SELLING A BUSINESS

WHAT TO EXPECT

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EBOOK SERIES

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Things to Know About Selling a Business

So many Owners want to sell their businesses.

Questions Start With

How do you get from an idea to reality? How do you get a good price? How do you find a Buyer? What does the process entail?

1. What Does a Buyer Want?

Buyers buy for many reasons. Perhaps they like your products, your IP, your factories, your distribution network, your cash flow. Perhaps you even know who you are trying to sell to?

They want the look and security of a GIC with 20% upside!

It is not always easy to get there, but entirely possible! But it does require planning, effort, patience and an ability to see the process through!

Remember too, that Buyers always feel as if they have lots of other options and that you could be hiding something, so expect them to spend a lot of time asking lots of questions and digging into all kinds of details with great scrutiny.

2. What Does a Seller Want?

Sellers typically sell for many reasons, being honest with yourself why you want to sell, will help you to structure the right kind of deal or find a Buyer that can provide what you are looking for.

Reasons Could Include

- I just want out.
- I want to advance my opportunities within a larger company.
- I want to take money off the table, but continue to work.
- I'm bored, I want some new challenges.
- Time to retire.
- I have a health issue.
- My partner and I are at odds and we need to buy each other out.

It may be that selling is not really what you want and that there might be some alternatives such as:

- Sale to your partner.
- Change of financing structure.

- A licensing deal.
- Hiring a CEO.
- Growing for another few years and then going to market.

All of which should be considered and at the end of the journey whatever you decide will be the right decision for you.

3. What to Do Before Looking for a Buyer?

Get Organized! Get Organized and Get More Organized

When you sell your house, it is super easy to hire a stager, place some furniture and paint a wall or plaster over a crack. Home buyers are emotional and rarely look beyond the surface. Also perhaps just one aspect of the house wins them over- the view, a nice kitchen etc.

Business Buyers are not even close. They are not emotional, they dig into every aspect of the business, often looking for faults or vulnerabilities perhaps more so than for features. They are always concerned that something is being overlooked or is not quite right. They don't have any emotional attachment to your baby! Furthermore, prospective Buyers are going to look for a minimum of 3 years of: history, tax returns, employee lists, products, inventory. You name it - they are going to dig into it.

Consequently selling requires that you structure your business in two key ways:

1. All your IP, corporate information, records, procedures and operating systems become refined, complete and accurate. Ideally you also have 3-5 years of solid historical financial data.

2. You as the Owner need to “work” yourself out of the business, such that there is a business to sell. A Buyer is buying the business NOT you! For an entrepreneurial Owner this is very difficult as we are typically hands on in every aspect of the business.

Reduce Business Debt

Realize that debt should either be paid off, or there should be a plan in place that reflects how this debt is being paid back. Trade credit and bank lines are critical to any business, but a Buyer will not be buying your debt. Typically they will as part of the agreement have a clause that requires all debt to be paid from the purchase price and expect that you leave a certain amount of money in the business to finance the short term operating expenses.

Consequently the more debt you can pay off, the more of the purchase price will be going to you. Secondly the lower the debt on your balance sheet the better your financials will look to potential buyers. Paying down debt can be hard, and might even require significant cost cutting and financial management protocols to achieve this. Frankly that discipline of managing debt and putting significant cost controls in place will be very valuable and will improve the profitability of your business, which improves your valuation!

Have Your Financial Information Correct and Ready

Prospective Buyers are going to need a “Coles Notes” version of the business to understand if they are interested in talking any further. This needs to be ready, so that as soon as a prospect shows interest you would be ready to respond. Time is of the essence. When someone shows an interest you need to be able to respond quickly and keep the process moving. A delay can also look like you are possibly hiding something and certainly a prospective Buyer will not wait around.

All information needs to be accurate and match exactly subsequent requests for information. Any variance could lead to a cancelled transaction, or worse a misrepresentation and liability for costs of the Buyers' due diligence.

Make sure that your financials are correctly stated, and that you are adhering to correct accounting principles. Revenues, expenses, inventory all need to be accurate and recorded according to GAAP accounting principles. Service contracts and prepayments need special attention to ensure accurate recording.

If you provide projections, then these too need to be solid and justified. There is a line between showing positive projections, unrealistic projections and being able to defend and explain your assumptions at some future date. Likewise during future conversations with the buyers presenting a too rosy picture relative to your current financials will open the questions: Why did you not execute on this? Why is there a gap between actual and potential? What are we missing? What else is being told that I should doubt? Is the Seller credible?

Identify Business Weaknesses and Challenges

Buyers are smart and likely will uncover all the real risks or minimally what they perceive to be business weaknesses at some point during the diligence process. At that time, these could depending on the nature of the weakness easily translate into reductions in the purchase price, vendor guarantees, or a failure to close the deal. Furthermore, an inability to fix the issue, or some attempt to cover the issue will be raise a huge concern with the Buyer. Again, either resulting in more work and questions for the Seller, or the Buyer getting cold feet and moving on.

It is important to be honest with yourself, before you engage with a buyer, at this stage, to figure out these issues, address them, and put solutions in place. One of the most overlooked issues is that of the role of the CEO and depth of the management team?. How integral is the Owner / CEO to the business? Can the business function without the Owner / CEO?

During the lead up to selling the business but before engaging a Buyer these weaknesses need to be identified and dealt with to ensure that the deal completes at the price agreed.

4. How Long Will It Take?

Given that as a Seller you will be expected to typically produce 3 years of solid historical information, it can take a while to get the business ready. A bad year does not always end the chances of selling, but could certainly be a major discount. Make sure there are good explanations for any significant change year over year in your financials.

Once organized the actual sale process can take from 8-12 months. It is very variable upon the buyers level of sophistication and your readiness. During this time you still need to keep your eye on the ball, run and grow the business to meet the forecasts you provided a year ago, make profits, service the needs of the Buyer, and keep things under wraps from your customers, competitors and most of your employees. Holding everything together while everything is moving along rapidly is going to be a major challenge! Having someone you can trust helping you is going to be very useful indeed.

5. What Is My Business Worth?

At the outset it would be useful to get a valuation or to do that yourself based on the sales of similar businesses. This could be a very valuable process. Use this as an opportunity to get your head into the game and understand what the business is actually worth. Ultimately a business is worth what a Buyer is prepared to pay, but having a good understanding of your value and position is important to not leaving money on the table. This is the largest and last sale you are ever going to make!

6. What Documents Do I Need to Show Prospective Buyers?

Typically there are two sets of documents, the initial being a generically worded high level overview. Since this document is going to be publicly shared and not subject to an NDA, this should be very generic, but contain sufficient details to interest a Buyer to look a bit further. This document is typically created together with the Selling consultant at the time of listing. Once the consultant has gathered some interest from a prospect and determined suitability they would then release the secondary document set / the initial vendor package.

The secondary set of documents typically includes:

- 3 yrs Income statements.
- Balance sheets.
- Cash Flow statements.
- Some kind of “business deck” to better explain the business.

These documents need to be accurate and correctly reflect the reality as they will become the basis under which a Buyer will issue a Letter of Intent and begin the due diligence process. Any variance here between what you present and what is found out to be the truth by the Buyer will result in a discount, failure to close, or if really bad, litigation for misrepresentation and Buyers costs of due diligence.

7. What Happens Next?

a) The Sales consultant will take the time to understand the business & Sellers needs, so that they are able to intelligently talk to prospective Buyers.

b) The Sales consultant will help you to gather the core documents and generate the basic Expression of Interest sell sheets as well as the secondary detailed document Confidential Information Memorandum - It is important to have this ready before starting to engage Buyers.

c) The Sales consultant will begin circulating the summary business documents to prospective Buyers. They will have conversations at a high level with a few prospective Buyers.

d) They will present these prospective people to the Seller and if the Seller agrees, enter into an NDA with each of the prospective Buyers. At this stage more detailed business information is released. Likely the Buyers and Sellers will also have a conversation/s and start to feel each other out. The prospective Buyer may well ask for some supplemental information, before committing any further.

e) A Buyer that becomes sufficiently interested in acquiring the business will thereafter issue a Letter of Intent, to acquire the business.

This would include the purchase price, various business terms, payment schedules and other Buyer considerations. Before signing this back it is highly advisable to have your lawyers review this and make sure that the document is acceptable to you. Once signed this will determine the details and terms of the final transaction.

8. Due Diligence Begins

This is where the Buyer gets to dig into every detail. All the homework that has been done in the past year/s really becomes critical at this stage. The preparation ensures that all the information is readily available, correct and can quickly be provided. There is no generic deal room set of documents. Each Buyer will put forward what it is that they would like to look at, further during the process as more information is uncovered they will likely make additional document requests.

The consultant will work with you to help identify what are likely to be the documents that will be required in your case, and ideally we will work to have the majority of these documents available ahead of time.

9. Confidentiality Matters

At all stages both before and during the process it is essential to treat this process with the utmost confidentiality.

It is imperative that you clients, competitors, suppliers/bankers and staff are unaware that the business is for sale and that you are engaging in a sales preparation process, until such time as it becomes appropriate to share that information.

Why?

a) Any client that finds out the business is being sold is quite likely to suspend doing business with you and or defer making any material purchases. Suddenly your projections, and financials will be negatively impacted and this will reduce your ability to sell.

b) A competitor (or their salesperson) will use this information to out-compete you and quite possibly spread rumours that you are having “financial issues” or something else detrimental to your ability to sell. You might not even know that this is happening until it is too late.

c) Suppliers and Bankers can also get anxious. They might want to review credit terms, renegotiate loans or any other aspect of their business terms. Once you have a deal in place or understand that the deal is going to close there will be time enough to involve them. Some banking and supplier agreements will require disclosure, don’t overlook that when preparing your deal room documents.

d) Junior and senior staff, even long term members of the management team (depending on the team), could become anxious as to their futures and this could cause them to start looking for other jobs, impacting your retention and therefore the Buyer perception. It could provide staff with information that they might unwittingly disclose to others. Again this could undermine your ability to sell. Once the deal is much closer to reality and or appropriate the necessary people can become involved.

There's no purpose in having to shake up what does not need to be shaken.

10. Next Steps and Bottom Line

Selling your business will take time, patience and organization. It can be both exciting and stressful.

To Summarize

a) Make the changes necessary to the business to actually be able to sell it and for a reasonable price.

b) Plan your current role and exit from the business so that the business is sellable.

c) Put in place the necessary legal and tax planning to deal with the outcome from the sale.

d) Engage a Sales consultant that you feel you can relate to, that is going to work on your behalf and help you through the process to ensure that you reach your goals.

11. Timeline of Events

4-6 Weeks Preparation

- 2 Weeks to gather the required information. The consultant will work with you to gather necessary information and to gain an understanding of the business (mostly client responsibility)

- 2 weeks for the consultant to compile the necessary Expression of Interest and Confidential Information Memorandum documents (mostly consultant responsibility)

- 1-2 weeks to review and finalize representations (joint responsibility)

1-3 Months for Soliciting Interest (duration is very variable)

- During this time the consultant will mostly be talking with prospects, answering questions, feeding more information.

- Most of the effort during this phase is the consultant working with prospects, trying to figure out who are serious and who are not, filtering and moving them along. Making sure that only serious prospective Buyers get to meet and talk with the Seller.

- The Seller may be required to provide ad-hoc ancillary reports (mostly should be accounting type data or answer a few questions).

- The Seller will most certainly be required to meet with prospective Buyers (1:1, duration and frequency is variable and will be based on seriousness of Buyer and comfort of the Seller).

Get a Letter of Intent (LOI) to Proceed

The prospective Buyer will issue a LOI. The Seller will be required to negotiate and accept the LOI terms (We would suggest legal review) The typical LOI would contain terms about the deal, payment schedules, vendor notes and post transaction employment / contracts, but it can have all kinds of terms and considerations that will form the basic terms of the future transaction.

Accepting an LOI is certainly a “go / no go point”. The Seller gets to make the final determination at this stage.

Diligence Process (This is a fairly intense period of 2-4 months)

- The Buyer will provide a list of expected items that they wish to review.

- The Seller will need to work diligently and expeditiously to respond and provide this information in a timely manner. Responses could be piecemeal over a few weeks. This for most sellers is the hardest part of the work required since there could be considerable asks, lots of documents to gather and create and lots of meetings to review and discuss.

- Depending on the answers to the above there could be further requests, conversations and meetings.

- Certainly the consultant can assist you during this period. But this is largely dependent on the information request, and what role the seller would like the consultant to play and what access to information would be provided to us.

Legal Process (Time required to read & review docs)

- Legal begins once Diligence completes and this typically lasts a 4-6 weeks or more. The variability depends on the legal complexity and detailed Seller & Buyer review of clauses and specific wording.

- Emotions could be running high at this point, so patience is required if you really want the deal to close!

Deal Done! Total elapsed time from start to end: 8-12 months but most of the Seller effort was during the diligence phase.

12. What to Look For In a Consultant

It is important that you feel you can relate to your consultant. There is going to be lots of interaction and involvement for the next 8-12 months.

A good Sales consultant will think like a Buyer. It may sound counter-intuitive, but you want the consultant to be critical and honest of your statements, budgets, documents and all submissions. So that when these are finally delivered to a prospective Buyer they have been through the “sniff test” and are likely to meet the needs of the Buyer.

A good consultant will likely have been in your shoes in the past and sold their own business. Meaning they are able to understand the process, the emotions you are feeling and can provide support as the process unfolds.

The next few months while exciting, are also potentially going to be quite stressful. You will need to keep running your business properly, while keeping everything confidential and at the same time delivering on the buyers needs and finally closing the deal.

At WarrenBDC we are here to help you, to take your side in the transaction and help you to achieve the outcome that you desire. We are patient, understanding and capable. Please visit www.warrenbdc.com

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