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Serving owners of small and mid-size businesses since 1980

WHITE PAPER

Selling Your Business
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It is often said that owning a business is like owning a boat: the two happiest days in your life are the day you buy it and the day you sell it. Whether you agree or not, selling a business is a complicated process that requires patience and perseverance. But to maximize your return, your business deserves the widest possible exposure to prospective buyers and the focused efforts of an experienced intermediary. This paper outlines the process involved in a typical transaction.

The Best Time to Sell

If you are considering selling your business but are concerned about optimizing the timing of the sale, keep in mind that a typical transaction requires 6 - 12 months to complete. Delaying a decision to sell means that you are taking a risk regarding future economic and market conditions, including interest rates and capital gains tax rates. The best time to sell is when business conditions are stable or improving, thereby leaving several good years in a business cycle to the new owner. This creates a win/win situation for both you and the buyer.

On the other hand, if you wait until too late in a business cycle, your selling price will be lower, with the increased risk that your buyer may fail. Since most transactions involve some seller financing in the form of notes, consulting agreements or a covenant not to compete, your future payment stream may be jeopardized. Therefore, if you are planning to sell your business, act while business is good, not when business is declining.

Preparing Your Business for Sale

In some respects, selling a business is similar to selling your home, in that you want to present the best possible “face” to prospective buyers. Just as you would fix up your home for sale – painting inside and out, cleaning closets, removing clutter, new landscaping, etc. – the same applies to the sale of a business.

The first place to start is to make sure your accounting books and records are in order. Many a deal has been killed during the due diligence process due to poor record keeping and accounting practices. Having at least three years of audited financial statements by an outside CPA is the ideal situation, but most smaller businesses choose not to incur the expense of a formal audit. As part of our services, ASI can review your accounting procedures and recommend what you should do to prepare your business for sale. For example, in some cases, it may be necessary to hire an experienced controller or VP Finance to augment your existing accounting staff. In other cases, a temporary financial consultant may be sufficient.

While the condition of your accounting records is critical in preparing for a sale, there are other factors to consider as well. Some examples: Do you have any pending litigation? If so, try to resolve the matter before putting your business on the market. Do you have any glaring holes in your management team? If your production manager or any other key employee just quit, be sure to hire a replacement as soon as possible. Does your mother in law keep your books? You may want to consider hiring non-family members for key positions who would be willing to remain with the business after the ownership change. Is your inventory clean? Now is the time to get rid of your obsolete inventory, as a buyer will only purchase inventory that is current and saleable.

Finally, don't overlook the "window dressing" items in preparing for the prospective buyer's visit to your premises. This is a good time to clean the carpets and windows, paint the walls, get rid of the clutter in the shop, and ask you employees to straighten out the messes on their desks. Always keep in mind the value of a good first impression!

Now that you've gotten your business ready to sell, here is a general outline of the process that ASI follows when engaged to sell a Client company:

The Initial Consultation

The first meeting at a prospective client's office is to get more acquainted with the business. After signing a mutual Confidentiality Agreement, we ask for support material (sales and marketing information, financial data, and tax returns) for preparing an informal valuation estimate. This non-binding estimate (usually in the form of a valuation range) is to insure that your expectations as the seller are in line with our own professional appraisal of the company and current market conditions.

If you agree with our valuation estimate, we then enter into a Representation Agreement that outlines the scope of our work and the fees involved. While we normally require a modest retainer, the vast majority of our compensation is in the form of a "success fee" paid at the completion of the transaction.

Finding the Right Buyer

Once we begin an active engagement, our first task is to prepare an Offering Memorandum. The Offering Memorandum ("OM") is like a prospectus, in that it describes your business, the industry, the market, the technology, production capabilities, facilities, key personnel, and financial data for the past 3 - 5 years. The financial data in the OM is usually "recast" to exclude personal items that you may have charged to the business, such as excess officer salaries, automobiles, personal travel, club memberships, etc., as well as any extraordinary one-time expenses not considered to be in the normal course of business. The recast data is intended to give a prospective buyer a better picture of the earning power of the business if it were operated as an independent subsidiary of a public company.

During our second meeting with you, we begin to compile a list of prospective buyers. This list will be as extensive as possible, including firms both within and outside your industry. The list may include, but would not be limited to, major suppliers, major customers, competitors, as well as other strategic and financial buyers. These companies would be identified based on your input as well as through the use of various industry databases that ASI regularly uses in this process.

Once the initial prospect list has been compiled and approved, we then send a personal letter to the CEO of each target company. This letter typically contains a one-page summary of the Client's business, but without any names or other means of identifying your company. It is intended simply to peak the interest of a prospective buyer who must then return a signed non-disclosure agreement (NDA) in order to receive a copy of the Offering Memorandum. All materials sent, including the initial mailing package and the OM, are personally reviewed and approved by you before mailing.

Following an initial mailing, we normally receive a number of requests for the OM. After receipt of a signed NDA, the OM will then be sent to the prospect by email or overnight courier. We will typically follow up after a day or two to make sure the intended recipient received the package, and then again in a week or two for further follow up. In most cases, the prospective buyer will have some questions and comments that will give us an indication of his or her level of interest. At the same time, we will be gathering information to make an assessment of the buyer's financial capabilities.

If the prospective buyer is acceptable, appears to be financially qualified and is interested in seeing the business, we will then arrange a face-to-face meeting at your office. This is an opportunity for the buyer to "kick the tires" and get a better feel for your business. It is not uncommon for a team of people from the prospective buyer to attend this meeting (e.g., someone from finance, manufacturing, engineering and corporate development).

Negotiating the Deal

If the initial meeting is successful and the buyer is interested in pursuing a transaction, the buyer is asked to prepare a Letter of Intent (LOI). While not a binding Purchase Agreement, the LOI is a key document in the process as it provides an outline of the main terms and conditions of the offer. There is typically a considerable amount of negotiation during the preparation of the LOI. Having been involved in hundreds of transactions, ASI is particularly experienced in dealing with these negotiations. Frequently, a client will also involve their corporate attorney at this point.

Due Diligence

Once the LOI has been received and accepted, the buyer's due diligence process begins, which may take anywhere from 30 – 90 days. This usually involves a detailed review of your organization and verification of your financial, marketing, and operational data. During this period, a Definitive Purchase Agreement is drafted which contains the legal details of the transaction, including representations and warranties of both buyer and seller. The buyer's attorney typically prepares the Purchase Agreement and the seller's attorney reviews and comments on the contract. ASI assists the seller's attorney and tries to keep the parties focused on the transaction.

On the Closing Date, the Purchase Agreement and other closing documents are signed by both parties, followed by a transfer of funds to an escrow agent. Once both parties agree that the documentation is complete, the escrow agent releases the funds to the seller.

Some General Comments

During the entire process, ASI never mentions a “selling price” for the business. In ASI’s experience, it is always better to let the buyer make the first move toward a valuation. In many cases a buyer will have their own reasons for wanting to purchase the business that may not be obvious to the seller. In such cases, a strategic buyer may be willing to offer a much higher valuation than a financial buyer.

ASI goes to great lengths to insure confidentiality during the entire process. Your company identity is never revealed without permission, and we use the utmost discretion when dealing with company employees who may not be aware of plans to sell the business. In all material prepared and distributed by ASI, your company is identified only by a six digit number.

As our client, you are in control of the entire process in terms of who is contacted, who is sent an Offering Memorandum, and who is invited for a company visit. As mentioned, you must approve each phase of the transaction before we proceed.

While ASI cannot officially offer legal and accounting advice, we have CPAs and attorneys on our staff that can identify key legal and accounting issues that deserve further investigation. ASI can also assist in arranging external financing that is sometimes required to complete a transaction.

The sale of a business is an important event in the life of any business owner; however, it need not be traumatic. The professionals at ASI are trained to guide you through the entire process and negotiate the best possible price and terms for your business. For further information about the services offered by ASI, please call us or visit our Website at www.asiinvbank.com.