

What's So Hard About Selling a Business?

Commitment Verification

Selling a business is an emotional and tedious process for most people. You poured your heart and soul into your business for so many years and yet no one seems to view the value as you do. Backing out in the middle of the process can hurt your business.

Are you sure you (including your spouse/partners/family/shareholders) are totally committed to selling your business? Who should be on the negotiating team and how will the decisions be made when shareholders or partners can't agree?

Do you really need to sell or are you trying to solve another problem by selling?

Timing

Is it the right time to sell? Have you been preparing to sell? Could you get better price and terms by making some changes? How is the market?

How long does it take to sell a business? Do you know that some businesses have been on the market for more than 2-3 years and have gone through 2-3 different advisors?

Properly planned, prepared and priced business should take about 6-18 months to sell.

Valuation

Can a cardio surgeon successfully perform a heart surgery without a thorough diagnosis?

Getting a professional valuation done before deciding to sell may save you lots of time, money and grief because the market may not be willing to pay what you expected. Privately held companies are valued much lower than publicly traded companies, mainly due to higher risk and lower liquidity.

What are the advantages and disadvantages of using multiples of historical Revenue, EBITDA or Earnings? What are the advantages and disadvantages in using the Discounted Future Cash Flow method? What are the impacts of qualities of revenues, cash flow, customer relationships, tangible assets, brand equity, intellectual properties, employee base, channel relationships and other variables on the multiples or capitalization/discount rates applied in valuation?

The valuation may uncover hidden values and provide useful negotiating tools. The valuator can identify weaknesses to be improved and identify the value drivers that will maximize the sale value. The better-prepared party with more comprehensive information will have an edge over the less-prepared party in negotiation.

Tax Matters

How much do you get to keep after tax? Would it help to know what your tax position is so that you don't sign an agreement that is disadvantageous to your net proceeds? Should you sell shares or assets? Do you qualify for the enhanced capital gains deduction? Could you "purify" your company to be eligible as a qualified small business corporation? Does it matter whether the buyer is a publicly traded company? What about the GST/HST, Land Transfer Tax and Sales Tax, etc.?

Legal Matters

Are there any restrictions on selling, such as shareholders' approval or first right of refusal? Do you need to address the issues of employee benefits, employee share options and severance arrangements? Do you have any contracts that require third party consent on sale or change of

control (e.g. landlord or bank)? Will there be any regulatory requirements under the Securities Act, Investment Canada Act or Competition Act? Have you consulted your lawyer on what representations and warranties you are prepared to give? Do all shareholders or partners agree on the representations and warranties?

Employees

What will happen to employees after the sale? When should you tell them? What if key employees leave before the sale? Will the leak damage employee morale and customer loyalty? What are your options when a buyer requests certain employees be terminated before the closing? What are the implications?

Liabilities

Are there any issues that may kill the deal at the last minute? Have you reviewed your environmental, litigation, tax and product warranty obligations, etc.?

Capital Expenditures

What has to be done to maintain the business and what can be deferred? Will any of the capital expenditures pay off in time?

Keeping It Up

Can you keep up the business while spending time on the sale process? What can you do to make sure your sales and gross margin do not decline? Do you expect to lose any major customers in the near future? Declining sales will put a damper on selling your business and losing a major customer will kill a deal.

Professionals

Do you have the time and the know-how to sell on your own or should you hire professionals? Do you know which professionals are needed and when? Many sellers bring in their advisors too late. What roles do a valuator, lawyer and tax accountant play? What are the costs of each professional? The fees may be fixed, contingency based, hourly based or a combination. Most professional firms require a retainer.

Value Enhancement

How much will fine-tuning and upgrading your business increase the value? Do you have a management information system (MIS) that generates timely, accurate and useful information? Do you have an accurate costing system that tracks profitability by product line and by customer? Do you have capable managers that will stay and work with new ownership? Do you have any redundant assets that do not contribute to value? Do you need to remove shareholder payables, personal properties and non-operating payables?

Housekeeping

Is your corporate house in order? Is your business in tip-top shape – physical appearance, information, documentation and regulatory compliance? Does your business give the impression of a well-run business? Do you have deficiencies that a buyer might use to negotiate? Could you dispose excess or obsolete inventories? Could you collect accounts receivables and keep them current? Could you lower the working capital requirement?

Normalization (Adjusting for Unusual/Unnecessary Items)

Do you have excessive salaries, bonuses, perks and one-time expenditures etc. that should be adjusted for? Can you justify all adjustment items in your normalized statements?

Expectation & Pricing

The final price will vary depending on the number of buyers, buyer motivation, buyer type, vendor financing, earn-out, management contract, representations and warranties. Is your expectation in line with the market? What would you do if no one submits an offer that is anywhere close to your expectation?

Asking Price

Should you quote an asking price or not? How do you avoid over pricing or under pricing? Can you get someone to submit an offer without an asking price? What would you do if the market conditions and company circumstances change (e.g. substantial increase/decrease in sales)?

Sale Process

Will the auction approach be better? How do you get multiple offers to have buyers compete against each other? What if no one bids?

Packaging

What should be included in the information package - History, Industry, Market, Economy, Products, Customers, Management, Facilities, Financials and Future Outlook? When should the sensitive/competitive (customer names or intellectual property) information be released?

Buyers

Who would be the logical buyers and why? What are the differences between the strategic buyer, synergistic buyer, financial buyer and job buyer? How should you approach them? Is there some strategic fit, synergy or growth opportunity? Do you know the buyer's position and motivation? Can you quantify the synergy effect to estimate the buyer's price? Can the buyer take advantage of weaknesses in your business?

Qualifying

How do you screen out the tire-kickers? Did you know that 90% of inquiries are from unqualified prospects? Do they have sufficient cash or have financing in place? Do they have a focused acquisition plan? Do they have the background or capability to operate the business? Have they bought a business in the past? Why do they want to buy your business?

Confidentiality

How do you let the right buyer know you are selling while protecting confidentiality? Have you got everyone to sign a Confidentiality Agreement before releasing information? Does the agreement contain all provisions that prevent prospects from damaging your business? Have you creatively sanitized or camouflaged your marketing material? Are you keeping track of all the packages given out and details of all people that received information? Are you ensuring the return of all information if they abort? When should you release sensitive/competitive information?

Integrity

Are you being clear and straightforward about the business and reasons for selling? Is the buyer being same? Credibility can be lost quickly after a couple of surprises. Have you developed mutual respect and trust with the buyer that will be fundamental in completing the deal?

Being Current

Do you know what's going on in your industry and can you present your business in a positive light? Can you defend the negatives that the buyer will try to use for negotiation?

Practice

Have you prepared for buyers' questions - past performance in sales, gross margins, wages, expenses, capital expenditures, sales breakdowns, obsolete inventory and monthly operating variances, etc.?

LOI – Letter of Intent

Should you consult your lawyer and tax specialist before signing back on the LOI? Do you think you can reopen the discussion on terms already agreed in your LOI if you find out later that you made a mistake? Do you know if it is truly non-binding? Should you ask for a deposit? How much? Should you ask for a break fee? Should you address the price allocation if it is an asset sale? How much detail should you address at this stage?

Continuity

How long are you willing to stay after the sale? How important is your stay, after the closing, to the business? What if you can't get along with new owners?

Consideration

Buyers seldom pay all cash in private company transactions. Are you prepared for offers with vendor financing, earn-out, a consulting fee, management/employment contracts, common shares, preferred shares and other combinations? What should be your remuneration if you decide to stay on? What are the tax implications?

Earn-out

Earn-out is a form of consideration based on future performance of the business. Should you agree to an earn-out? Should it be based on the sale, gross margin or something else? Should it be three years or longer? What are the tax implications? The earn-out provision usually takes time to be negotiated, can be subject to disputes after the closing and thus needs to be carefully crafted.

Vendor Financing

Will any one buy without vendor financing? How much are you willing to finance and at what terms? What kind of security or collateral should you ask for?

Exclusivity

Should you give any prospective buyer an exclusive period that forbids you from marketing the business or accepting another offer?

Negotiation

Are you clear on what's being sold? What are the excluded assets and liabilities? What should you concede on and what should you be firm on? Have you read and understood every detail of the agreement, especially the representations and warranties? Have you calculated the risks and potential consequences of representations and warranties?

Insurance

What happens if the buyer dies or becomes disabled before paying off your note? How do you protect yourself from these possible events?

Final Agreement

Some of the issues to be addressed are: collection of receivables, undisclosed liabilities, minimum level of equity and working capital at closing, audited statements, costs, covenants, representations, warranties and indemnities.

Representations & Warranties

"Reps & Warranties" is about disclosing information and risk allocation. Without certain representations and warranties, buyers will not buy your business. But many representations and warranties are up for negotiation and qualification and a competent transaction lawyer will be valuable in making those decisions. What's the difference between "to my knowledge" and "to the best of my knowledge"? What should be the time limit (e.g. 3 years after closing)?

Other Agreements

What should be considered in non-compete agreements, real estate lease agreement, employment/consulting contracts and vendor financing agreements?