The truth in black & white about

# Preparing your business for sale

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**Introduction** Preparing your business for sale

# When considering a value event for your business there is far more to consider than choosing a quirky deal name or aiming to have at least 3 years trading history and a good profit trajectory to make the opportunity appear attractive to potential buyers.

**It can be a minefield of complex decisions, many of which will take you well outside of your comfort zone. Even as a seasoned business owner and entrepreneur, completing a deal can truly push you to your limits.**

There are many types of value events that your business could encounter (and many acronyms to accompany) from MBOs to MBI's, BIMBOs, fund raising, EMI share options, full sale and part disposal along with life changing considerations like non competes, post deal lock ins, deferred consideration and hierarchical ranking of debt, to name just a few.

For the purpose of this micro-report we are focusing on the business sale and grooming your business for sale scenario.

For many business owners selling your business is a once in a lifetime event, so you want to get it right, make informed decisions and maximise your chance of achieving your aspirational exit value.

Plenty of literature is out there on grooming your business for sale. All sources typically have a bias in that they are written by an advisor as bait piece content for clicks, in hope of you appointing them for an aspect of the deal's advisory team.

We hope you find this report a considered, independent opinion on some of more pertinent issues you can encounter and some useful hints and tips to help you prepare and guide you through the many stages of completing a transaction.

You may not be thinking of selling your business right now, but it's never too early to prepare your business for sale. We hope this candid report gives you some unique, first-hand advice on preparing your business for sale, whether that's now or in ten year's time.

The micro report is authored by Matt Smith, CEO of BDB, who prior to taking appointment at BDB worked across mergers and acquisitions, providing due diligence support for owner managed businesses to some of the most recognisable blue chip names on a global scale.

Matt has a unique experience and skillset to offer some candid thoughts and the memory of completing the 100% management buyout of BDB from the founding partners in the Summer of 2017 is still fresh in his mind.

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**Preparation**

# Start planning in advance – it takes a long time to sell your business. And it can often take as long getting your financials in order prior to the sale. The average sale takes just under a year to complete, so have your systems and teams in place to support the inevitable distraction to the business.

**It's never too soon to start planning your exit strategy. Even before you open your business for trading, many experienced entrepreneurs will tell you that you need to have a plan as to how and when you will cash in and move on. Although it may seem odd to pre-empt the end – and plan your departure as soon as you start – the ideal addendum to any good business plan should be a solid exit strategy.**

## Having your exit mapped out is all part of a good business plan.

A well thought-out exit strategy can help you to maximise the value you get and successfully market your business to potential buyers or investors.

Anyone who has started their own business will have an emotional bond that will never be felt by incoming investors. So, when it comes to parting company with your business, you need to ensure it is well-equipped to survive without you.

The skill is in knowing when to sell. If you hang on too long it may actually damage the business and reduce its value. And whilst the advice isn't always to the owner's liking, the person who had the idea and founded the firm can often be the wrong one to continue its growth.

Black & White
insight #1

**You get out what you put in when selling a business, so it pays to plan ahead – especially when it comes to your exit strategy.**

## It's a tough decision to hand over the keys, even if you know a new owner can potentially turn your small venture into a thriving company.

A founder preparing for a sale needs to make their business as attractive as possible.

You have to be clear and honest about why it is you are selling. Buyers will need to know – and they will find out. It's best to be upfront. After all, few sensible buyers will take on any venture that is counting down to its own demise.

## Owners also have to be realistic about when they will get the money.

It's typical for the selling founder to have a two- or three-year earn-out clause. So, they will have to remain working at the company to ensure the profit and growth forecasts are met. If they are not, then the agreed sale price drops and any potential earn out or deferred consideration may be reduced.

In reality many business owners are looking to succession plan in hope of selling to retire. The last thing you want is to be locked into working there after the sale. Preparation is therefore key, and the detailed planning needs to start early.

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insight #2

**The ambition of the idea may be greater than the ambition of the founder.**

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**Advisors**

# Selling a business might be the biggest deal an entrepreneur will ever do, so getting a good valuation is vital.

**Understandably, many entrepreneurs choose to use third parties to help them market and sell their business. But not all professional advisors are the same, so if you do use one to help sell your business, you should do so with great care.**

Most entrepreneurs won't have any experience selling a business, but you can bet the buyer will have bought before. The expertise a corporate financier can bring to the table to look after your interests in my experience is really worthwhile.

Of course, they come with a hefty price, but a good advisor is more than just a middleman. They can help you find a good suitor and walk you through what is an incredibly complicated and emotional process.

## As a result of the emotional drain, deal fatigue will hit you at some point.

Deal fatigue is a condition during a deal negotiation in which the involved parties begin to feel frustrated; helpless, as well as irritated; and fully exhausted and fed up. There tend to be feelings of resignation as negotiations drag on endlessly, causing the parties to lose hope of reaching an agreement.

Deal fatigue is an important issue and seasoned professionals can help you through this obstacle. Experienced intermediaries remind participants about the mutual advantages of the deal and the overall objectives of it if they are losing sight of the big picture and the major issues of the deal because they are getting stuck on unimportant details.

**Researching the advisor**
Whether or not you choose to engage an advisor depends on how confident you feel in your sales and negotiating skills. Particularly when you have built a business from nothing, putting its fate in an external third party's hands is a very personal decision.

If you do choose to go with a corporate finance advisor, it's essential you do your homework.

Advisors help to seal a sale, but entrepreneurs must look beyond the marketing literature and sales patter for the raw facts on the specific services the appointed advisor will provide. Hidden within the fine details are important decisions to make about any engagement, including extra fees/costs, termination rights, cooling-off periods and the obligations of both parties.

Black & White
insight #3

**Professional advisors can make selling a business totally painless, but you'll need to choose wisely to get the best possible deal.**

All of this needs to be fully understood before you sign on the dotted line. The track record of the deal advisor is of particular importance to any selling entrepreneur. They should be able to provide you with details of their previous work, specifically successful sales of companies similar to yours.

If possible, obtain references and seek recommendations from trusted sources prior to approaching any advisors.

For me the close rate of the advisor is a KPI I've always placed great importance on. Corporate Finance Advisors are famous for selling you the dream, the aspirational unicorn valuation that meets your wildest dreams and enables you to live the life you've always dreamt of.

Often the advisors are appointed on this basis i.e. who states they can achieve the highest sale price. Just like when selling a house, if an estate agent boasts an inflated valuation you are more likely to appoint them.

However, again just like with selling property the business is only worth what people are willing to pay and the advisor who manages expectations from the outset is far superior in my opinion.

Whilst it's a tough pill to initially swallow that perhaps your aspirational sales value isn't achievable, at least you enter the process with your eyes wide open and hopefully the eventual sales price you achieve shouldn't be a million miles away from the starting point.

If you think the advisor is too good to be true, then you're probably right. During the heat of battle your advisors are your corner men and when deal fatigue sets in…which it will, they are the guys to carry you over the finish line.

**Will I get the right price?**
There are various valuation methods when it comes to selling-up, but the simple fact is a business is only worth as much as someone will pay for it.

Advisors can use their market knowledge to fix a price tag to a company and argue a strong case with potential buyers.

Some entrepreneurs complain that advisors want to push prices down to close a deal. In some cases, this may be true, but in reality, what will best preserve price is demand. Let's be honest; if mid-process you feel that your advisor doesn't have your best interests at heart, you more than likely mis-appointed in the first place.

**Are they really representing my interests?**
Advisors will be the go-between for buyer and seller, helping to bring the two parties together. For entrepreneurs inexperienced in selling a business, this may be advantageous, with the advisor's fees more than paying for themselves with a successful negotiation and a great sale price.

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insight #4

**Appoint with qualified consideration but don't under any circumstances go against your gut instinct.**

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insight #5

**While balance sheets and perceptions are both important in the valuation of a company, the success of a sale usually comes down to one thing: price.**

**Valuation**

# Valuing a business has been described both as an art and a science. In truth, a great deal depends on perception. However, there are common fundamentals that will feature in most company valuations.

**The process begins by establishing the expected underlying profitability of a business at the time of valuation. This is followed by an assessment of the risk profile of the business to determine the appropriate cost of capital or multiple cost of capital to apply.**

The valuations of earnings are fundamental to this, and should be before interest, tax, depreciation and amortisation (EBITDA), enabling potential buyers to compare similar businesses without taking the individual structure into account.

A company's annual accounts are a year-end 'snapshot', but they don't illustrate your business profile during the year. A cash flow analysis of the past year and a forward projection are much more convincing.

In theory, a business is worth the present value of expected future cash flows, discounted by an appropriate rate. In practice, the value of a business in the market is based on a mix of quantitative and qualitative factors. I discuss in the next section how having a system that tracks your financials can really help with this side of sale.

Quantitative factors include historical performance, earnings multiples for similar public companies, recent sales of similar businesses and so on.

Qualitative factors include management strength, protection against competitors, monopoly, high barriers to entry, recurrent income and more.

Deal structures become more important when there is a gap between the seller and acquirers' perceptions of the value.

Mechanisms such as earn-outs can be used to bridge the gap by reassuring an acquirer that it won't pay for value that isn't delivered, while reassuring a seller that they are not leaving value behind.

Solid financial foundation: the market is the ultimate arbiter of a company's worth. Negotiating these can be tricky because they involve the allocation of risk, and an experienced adviser can make a huge difference.

Ultimately, the market is the driver of a company's worth. To get a proper feel for the value a company will achieve on a sale, conversations need to be initiated with prospective purchasers to gauge the level of interest.

Critically, if you can attract interest from one, or preferably multiple, overseas buyers, you may be able to achieve a significant premium to a textbook valuation. The reason is that overseas purchasers will frequently be prepared to pay a strategic premium to enter the UK or European market.

Japanese and Chinese buyers, for example, have been known to pay significantly higher prices for UK businesses relative to textbook valuation methodologies.

The competitiveness of the process, the prevailing market conditions, and the strategic need of the buyer will then influence how far beyond this formal or purely financial valuation an acquirer may be willing to consider stretching.

This is where a good adviser can maximise the likelihood and impact of these factors on the ultimate valuation of your business.

Then there is the value in the "eye of the beholder". Formal valuation methods aside, it is important to stand back to ask whether a willing buyer and seller would be prepared to transact at that value.

There is a science behind valuing a business, and valuation techniques such as discounted cash flow and market approach are at the heart of any process.

However, these methods should always be overlaid with a commercial sense check. An ability to stand back and determine where the true value lies is important; is it in the brand, the customer relationships, technology, know-how or something else?

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Systems

# Having a proven and respected business systems stack (both project management and finance) embedded in your organisation will not only make the due diligence process easier to complete but provide the advisors and suitor with comfort over the accuracy and reliability of the information being disclosed.

**From my time in professional services there was nothing worse than turning up to complete a piece of diligence to discover everything was maintained on manual spreadsheets with business plans frantically scribed into envelopes and individual sheets of A4.**

If you are serious about maximising value on any proposed exit, you need to take the systems your business chooses to implement equally seriously.

Running your business on a proven and respected system developed for your particular vertical brings many benefits. It instills credibility in your reporting and being supported by a 3rd party it removes over-dependence on any one staff member. It also provides the platform for many of the formal procedures that add value to the business, as it demonstrates to potential acquirers that operations run smoothly and consistently and new hires can be quickly integrated. These are all factors that make your business more attractive to a potential purchaser, increase its value and sweeten the appetite of acquiring parties. Crucially robust systems also provide consistency which is imperative when a potential suitor is looking to benchmark company performance and assess the future growth potential of the business. Historic performance and track records can only be quantified so much as the system and data sets allow.

**Predictability**
With business systems, you can produce the same products and services with the same level of consistency. Once you have created your systems and written down the sequential steps, your employees can follow the proper procedures consistently. You can monitor these processes and improve when necessary.

Systems can be implemented for sales, marketing operations, project management, employee training, etc. The people who benefit the most from having systems in place are your customers who know what to expect from your business and crucially this is what a potential acquirer will be keen to assess i.e. the level of potential disruption to the paying client / customer base post deal completion.

The quality of the systems in play can hugely help facilitate change and make the smooth transition in ownership far easier to accomplish.

Systems make a business predictable. So, when change impacts your business – which may often occur – then knowing what business systems need to be modified becomes easier. You will know the current work process and can predict how change should be handled while still maintaining your systems.

Business systems allow staff to focus on what they do best. Any time you are trying to complete a project with a specific deadline, you will want to avoid any problems that may develop. Implementing business systems that also best match the employee talent that is available to encourage the attraction and retention of key team members may also come under scrutiny. Allowing people with specific skills, knowledge, and abilities to focus on what they do best, as opposed to being laden with archaic business systems and spreadsheets where the risk of manual error or manipulation are heightened.

Black & White insight #6

**Business systems can create value way beyond the specific tasks they fulfil.**

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**Timing**

# Try to sell when you don't have to – this improves your bargaining position a great deal. If you have to sell, then your leverage is much reduced, and this will be reflected in the sale price.

**You have built up a successful business but, with your exit strategy in place, how do you know exactly when to cash in and move out? There are myriad reasons why an owner would want to sell their business. It could be that it's ripe for growth and needs someone new at the top, or that the risks no longer seem in proportion to the rewards.**

Personal circumstances may mean you're just too busy to run your own outfit, or, quite simply, you want to collect on all that work and time you've invested.

**If you are in control and have planned well ahead, a useful tip is to try to time your sale for the end of your financial year – it makes due diligence much easier and means all of your financials are up to date.**

Whatever the reason that drives an owner to seek a buyer, the big questions are the same: how can you ensure you get the best price? And is there a right time to sell?

I would argue there is never an ideal time to sell your business, and you will always be able to find an excuse as to why now isn't the right time. Whether it's a wobbly customer, increased staff turnover or, worse, a looming Brexit, all can be overcome with a ferocious drive to make things happen.

With uncertainty comes opportunity. It's your job to spin the perceived risks on their head and clearly articulate with tangible supporting evidence wherever possible why any downsides can be managed, or risks mitigated.

Ideally, your business should be on the up when you offer it for sale, with growing profits, reinvestment, employment opportunities and new markets, geographies or product lines.

If your business is suffering falling profits or other stresses, this is definitely not when you should look to sell, because it screams fire sale. If there is a loss of interest from founders or shareholders, or personal issues among the management team, a seasoned acquirer will very quickly pick up on that.

Black & White
insight #7

**Sell when you don't have to – this improves your negotiating power as you always have the option to walk away.**

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insight #8

**In many ways, selling a business is like selling a house. You either sell it in a good condition and get the best market price you can, or you sell it as a 'doer-upper' and declare that to potential buyers.**

### Due diligence

# A form of company health check, due diligence is an important part of preparing your business for sale.

**Due diligence is an essential process for prospective buyers of businesses. It's the best way to formally verify the company information provided to you, and it is the main way for investors to avoid burnt fingers on an over-eager acquisition.**

It is generally better to declare everything up front, and then it will be reflected in the price. Even when selling businesses that are healthy and robust, it will take time to ensure that the organisation is in a fit state for sale, requiring the help of accountants, lead sales advisory specialists and IT specialists to perform what is known as vendor due diligence.

In anticipation you or your advisory team will need to go through a process of business optimisation, producing a cohesive and documented business strategy, clear and healthy financials, detailed information on your people and plant, and finally confirmation that IT systems work and are up to date.

This information will need to be presented in an organised fashion and made available in a virtual or real data room, where potential buyers can view the information and cross-check it with their own due diligence.

In the case of the "doer-upper" business, the vendor still needs to prepare information, but prospective buyers may be more tolerant.

**More dos and don'ts about due diligence:**

## DO:

1. Bring the "housekeeping" up to date, formalising contracts, HR matters and other paperwork. This protects both buyer and seller from a range of expensive liabilities. And even if the sale falls through, tidying up the back end of your business is definitely time well spent.
2. Maintain open channels of communication with your advisers, accountants and lawyers, as well as the purchaser and its advisers. This will help to speed up the process and build the mutual trust and respect that helps a deal progress more smoothly.
3. Establish responsibilities for providing information in advance and provide all necessary information clearly and in good time, as a mess of facts and figures is a signal to any buyer that your house is far from in order.
4. Keep the business on top. It's easy to concentrate on a sale and neglect the day-to-day running of the business itself. Use your advisers to help manage the process so that you can concentrate on your day job.

## DON'T:

1. Spend too much time and money on detailed vendor due diligence. The purchaser is unlikely to rely on this alone and you will still need to spend time presenting the information in the manner required by the purchaser and its advisers.
2. Assume the deal is done before it is actually completed. Due diligence results can impact the price and the ultimate decision of whether or not to proceed.
3. Conceal any issues within the business until the latter part of the process. Be upfront, but ensure you provide this information in the clearest way, with supporting narrative and explanations.
4. Agree to changes to the contract too early into the due-diligence process. While one issue may lower the price, another detail later in the due-diligence process could offset that – by which point you've already lowered your valuation.

Black & White
insight #9

**The art of negotiation and selling are very close to one another. Whenever you are negotiating, you should also be subtly selling the benefits of your business.**

### The art of negotiation

# Negotiating a major deal can be a nerve-wracking experience for business owners.

**Once people believe you are valuable and worth having, they will pay more.**

When it comes to negotiations knowledge truly is power. Before a negotiation begins, entrepreneurs should research their potential acquirer as much as possible. Understanding the other party's sweet spots means you'll be able to push harder on some areas.

A little background research allows you to sell businesses for far higher valuations than one might have been thought possible. The more you can understand about the other side's business, the better.

Understanding their margins and what constitutes a profit is really important. If you are selling your business, then how much profit you're making isn't the most relevant factor – it's how much money they will make when they get it to their customers.

For those presenting and proposing deals, listening and responding is key. You should be listening with your eyes. Look for who you're making uncomfortable, or if you've hit a raw nerve. If someone asks a question and you have a good answer, then let it hang or delay before answering. People will fixate upon it and then, when you answer, it will have more impact.

## Negotiation is a trade-off and there doesn't have to be a loser.

Always trade and never give anything away for free. If they say: "There's no way we can pay any more," ask if they can pay faster.

You can end up in a good position by trading things which they didn't think could be traded. Private healthcare, company assets, subscriptions, access to ongoing management information. In isolation all are relatively minor, but when it comes to the throws of final negotiations each can help sweeten the deal for a seller, where all their costs are to be personally borne going forward as opposed to being company funded.

A successful negotiation means getting the right figure on the deal. It is vital that entrepreneurs decide what this is in advance of the meeting.

To do that, entrepreneurs must start at a point way beyond where they hope to finish. You need to push well past where you are comfortable with to end up where you want to be.

The other side needs to say: 'That's crazy".' But the advantage is that you will have put that figure into their minds.

Negotiations will involve figures and proposals going back and forth, as deal makers test one another's mettle. Stay humble, never be arrogant and most importantly keep the relationship going.

Having other partners in the background with whom you must occasionally confer can also useful. Never be the decision maker. Put some distance between yourself and the deal. Buy yourself some time by claiming the need to confer with business partners or advisors.

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### Conclusion

# Looping right back to the start of the report.

**The best advice I can offer from my collective experience working on, in and around corporate transactions is to start your preparation early, and most importantly remain humble and realistic in what value you hope to achieve for your company sale. Alongside cold feet / refusal to let go, greed and stubbornness have killed more deals on the verge of completion than I care to remember. And I can't stress enough how much having a system to track your finances and clients will help you in the long run.**

Selling a business is never going to be easy but approached in the right manner with the humility to take the right advice at the right time, the lifestyle you've always dreamed of may be closer than you think.

Good luck

Matt