Driving an Optimal Outcome When Selling a Business

by Manny Clark and Eric McCarthy

Selling a business is a rigorous, time-intensive, emotional, and costly process. Business sellers are often navigating this process for the first, and only, time. This guide is designed to help ready sellers with the sale process by positioning their business, collateral, and transaction team in a way that can help optimize the outcome for all parties involved.

To increase the probability of an optimal outcome, sellers must pay attention to the company's growth picture, the data room, the transaction team, and their own psychology.

Growth Picture

One of the keys to attaining a good outcome is to help create a growth picture for the buyer. Said differently, think about why you would be excited to continue owning your business (if you were not selling) and paint this picture for the buyer. Some of the more polished presentations we've seen include a seller-generated investment memorandum serving as an introduction to the opportunity.

An investment memo forces the management team to think about the business from the perspective of an investor; and further encourages thought clarity and consistent messaging when, eventually, negotiating with potential buyers. An investment memo should, at minimum, include a brief history of the company, the company's product offering, company culture and organizational layout, key company strengths, opportunities for improvement, growth opportunities, and risks that may hinder expected company growth. Detailed financial information should be included separately, but it is good practice to include high-level revenue and income figures in the investment memo (including any management forecasts).

We would note that many brokerages and intermediaries help compile a Confidential Investment Memorandum (CIM) to introduce the opportunity to potential investors. This is not the same as a written memorandum compiled by the management team. If sellers choose to write an investment memo, we would warn sellers not to get too wedded to the ideas that they generate. Buyers will likely do their own work and may come to different conclusions on certain items, the M&A process is a negotiation and reasonable parties can, and do, disagree.

Data Room

Outside of the growth picture, it is important to have a well-organized and collateralized data room. While the data room is an early step and is not sufficient to close a transaction, having a well-populated data room can streamline the sale process and reduce the amount of time to close. Recommended content includes:

Financials

- Three to five years of financial statements, including the balance sheet and income statement. A best practice is to have audited statements prepared on an accrual basis. Tax returns should also be included here.
- Financial forecasts and underlying assumptions
- Key performance indicators (KPIs) or other financial metrics that management tracks

Product

- Product or service overview
- Details on product plan or roadmap
- Supply chain overview detailing all suppliers in the value chain
- Include any supplier contracts, credit terms, pricing discounts, etc.

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Customer

- Customer breakdown and revenue by customer
- Customer aging and churn analysis
- Customer contracts and commentary on contract transferability
- Management Intelligence. This includes collateral related to your customer and can include ideal customer profiles (ICP), customer growth analysis, purchasing breakdowns, etc.

Marketing

- Go-to-market overview:
  - Include details on both outbound and inbound processes
  - A best practice is to include associated costs and KPIs
- Customer-facing marketing and product collateral

Company

- Articles of organization and proof of ownership; include any associated tax elections
- Organizational structure and chart
- Chart of employees and contractors with associated locations and salaries
- Employee benefit information
- Three years of board meeting materials, if applicable

Transaction Team

Having a transaction team in place is important. Strong transaction advisors are vital in helping sellers attain the best possible price and terms for the business, given a seller's goals and objectives. At a minimum, a transaction team should include:

- Business stakeholders who are required to approve the transaction
- A corporate transaction attorney who is experienced in the type of transaction being considered
- A corporate tax attorney or advisor who is experienced in the type of transaction being considered
- A financial advisor or investment banker who is experienced in advising on acquisitions

Intermediaries like business brokers and investment bankers can be important in packaging the business and marketing the company to qualified buyers. We see them involved in most deals. However, they are not strictly required to get a transaction done, especially if the seller already has relationships with potential buyers.

The transaction team may grow as a deal progresses and different issues arise.

Seller Psychology

A sale transaction can be a highly emotional process with ups and downs. Understanding this, it is important for sellers and buyers to manage their psychology to increase the probability of a successful outcome:

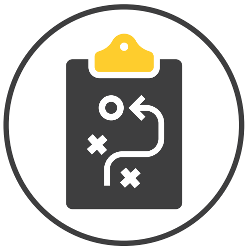
1. **Do not anchor yourself.** There is no shortage of opinions out there, most of them from unqualified parties. It is important for a seller not to anchor themselves to terms before they are negotiated—no matter how good or definite the opinion number sounds. Every deal is different, so it is important for a seller to consult with their transaction team on all terms and keep an open mind.

2. **Avoid mental math**. It is tempting to do back-of-the-envelope math when presented with, or targeting, a purchase price in order to get an estimated payout amount for the seller. This number typically becomes an anchor. The problem is that the calculated number is almost always wrong—often by a significant amount. It is important for a seller to consult their tax team to determine the estimated payout, given the dynamics of the seller's business and the structure of the deal being negotiated.

3. **Keep the faith**. This sounds cliche, but deal negotiations can be fraught—with distrust abound. In these moments, it is important to remember that all parties want the same thing—a successful transaction. Give your counterpart the benefit of the doubt and lean on your advisory team to avoid rash and biased decision-making when emotions are high.

Driving an optimal outcome when selling a business is an intentional activity that takes coordination, discipline, and patience. Being prepared with a ready growth picture, a robust data room, an experienced transaction team, and sound psychology is a great first step along the path.

9 Best Practices for Maximizing Sale Value



3+ years out…

1. Clarify the goals for your exit (e.g., retirement, obtaining a capital partner, etc.)
2. Get your company's "house" in order (accrual-based financial reporting, separating commingled assets/expenses, etc.)
3. Organize (and execute) your business's long-term growth strategy

12-9 months out…

4. Retain transaction advisors (investment banking, legal, tax, accounting)
5. Assemble your internal deal team
6. Gather and organize Company data that will help the buyer perform diligence (financials, product/service descriptions, marketing collateral, customer lists & contracts, HR, etc.)

6-3 months out…

7. Prepare and rehearse management presentations to potential buyers
8. Leverage your internal team and outside advisors to identify the buyer that helps you best achieve your initial goals
9. Continue to run the business efficiently. The sale process can become time-consuming, so it's important to balance both and not neglect the business.

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