Investment Banking

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VIEWPOINT

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HELP!

SOMEONE WANTS TO BUY MY COMPANY

By Laura Kevghas

The phone rings unexpectedly one day, and on the other end is a CEO wondering if you would be willing to sit down and talk about selling your business. You may or may not discuss a purchase price. You may or may not commit to even a meeting, let alone an exchange of information. But nonetheless, that single unexpected phone call can touch off one of the most significant, emotional and time-consuming events in your life as a business owner: deciding whether to sell your company. The way you respond, both initially and in the weeks that follow, can have an impact on your company, your employees, and the value you can realize from the sale of your business.

For this article we asked experts in accounting, law and business consulting for advice on what to do when you receive this kind of phone call. Their suggestions – on everything from evaluating pricing, to managing proprietary information, to establishing a team of advisors, to performing due diligence on the buyer – can help you navigate the complexities of your unsolicited offer, and make the most of your opportunities, whether you decide to sell or not.

WHY THIS MATTERS:

- *Planning ahead can make the unexpected offer manageable*
- *Contemplating selling your business is the most significant and emotional decision you'll ever make*
- *Even considering an offer can affect your company, your employees and your family*

TOP TEN RULES FOR EVALUATING UNSOLICITED OFFERS

Though every company – and every deal – is different, we have found that there are a number of simple principles that can simplify the process of responding to an unsolicited offer and help you make the right decisions. Here are ten things to keep in mind when someone offers to buy your business.

RULE #1: DON'T WAIT UNTIL THE OFFER COMES TO PLAN YOUR RESPONSE

"Unsolicited offers can come at any time," says Tom Sherwin, founder of the consulting firm CEO Resources, Inc. "Ideally, CEOs should have a strategic plan in place before they get an offer." That plan doesn't have to be complicated, he adds. CEOs simply have to know whether they plan to continue to manage the business over the next three to five years, or whether they would be open to the possibility of a sale.

Linda Swerling, founder of Level II Solutions, adds that business owners should consider their personal, as well as financial, goals. "How long were they planning to work? What was their exit strategy for the business? All these things need to be written down," she says.

Sherwin says that he regularly meets with CEOs who maintain that they have no interest in selling their companies; yet it's often merely a question of price. "We play a game of 'what if' scenarios, usually over lunch," he says. "What if someone offered you 20% more than you think your company is worth? What about 50%? You end up constructing a game plan. Say, for instance, that you would consider offers above 25% of some benchmark. At 50% you would actively pursue a deal. And at 100% above the benchmark, you schedule a closing. Then you put that game plan away until the time comes."

RULE #2: KNOW WHAT YOUR COMPANY IS WORTH

Of course, you can't evaluate an offer without having a very good idea what your company is worth. Public companies learn their value every day when the market closes, but for private, closely-held companies, it may be worth spending the money required to get a good valuation at least every three to five years, Sherwin suggests.

Amy Mastrobattista, an attorney with the Boston law firm Ruberto, Israel & Weiner, says that the first stop should be your CPA, who can walk you through the most appropriate valuation techniques for your company and industry. "It's also not a bad idea to develop a relationship with an investment banker far in advance of any planned exit," she adds. "They can incorporate their knowledge of market conditions, recent transactions and prevailing multiples in your industry to give you a more accurate view of your company's value."

"To truly understand your company's worth, though, you need accurate and timely financial information," asserts Swerling. "Your current performance relative to last month, the year-earlier period and budget all influence the value of your company."

The integrity of your financial data is important, not just in understanding the value of your business, but in presenting it to outsiders, comments Margery Piercey, a CPA with the accounting firm Wolf & Company. "First impressions are important when you put financial statements in front of a potential buyer. And it can have an immediate impact on value if your financial statements aren't in order. You really need an accountant that's going to help you look behind those numbers to make sure they are presented in such a way that you're going to be maximizing the value, by ensuring you're in compliance with GAAP and industry-specific norms, while identifying any adjustments for owner-related expenses that won't continue post-closing."

RULE #3: PROTECT YOUR COMPANY'S PROPRIETARY INFORMATION

Very early on, potential buyers will often request extensive proprietary information about your company. It's important to provide information in stages – very little early in the process, and further information in pieces, only as you become comfortable that a transaction with this potential buyer is desired and likely.

FOR MORE INFORMATION ON SOME OF THESE TOPICS, PLEASE SEE:

- **VIEWPOINT 9 – A Valuation Primer**
- **VIEWPOINT 16 – Choosing The Right Investment Banker When Selling Your Middle Market Business**
- **VIEWPOINT 17 – Reduce Your Tax Bill By Millions On The Sale Of Your Business**
- **VIEWPOINT 18 – 338-H-What? How Deal Structure Can Increase (Or Decrease) The Sale Price of Your Business**
- **VIEWPOINT 29 – Beyond The Usual Suspects: Why Buyers Outside Your Industry May Pay More For Your Company**

However, Mastrobattista points out that "Before you share any information at all with a prospective purchaser, you need to have a good confidentiality agreement in place. This is the case even if the potential acquirer is not a competitor. You don't want your confidential business information to be used for any improper purpose, even if you think it's innocuous."

What issues are most critical in a P&S agreement is highly situational. Some issues that are of paramount importance in one transaction may have little significance in another.

Piercey concurs. "Usually in the early stages of getting to know your potential buyer, you are going to be disclosing a good deal of information," she says. "It's important that your attorney has put a strong confidentiality agreement in place to make sure you're properly protecting trade secrets, customer lists, and other things that contribute to the value of your company. That way, if the deal doesn't go through, you haven't given away some of these things of value."

RULE #4: KEEP IT QUIET

These negotiations should, in most cases, be kept confidential for as long as possible. "The impact on the employees of even considering a sale of a business can be very unsettling and actually can reduce the value of the business," says Piercey.

"Control of information is critical," adds Mastrobattista. "Rumors about your deal can affect not just employees, but customers, vendors and lenders. If the transaction falls through, it can even have a negative impact on your company's reputation, since people may assume there was something wrong with your business."

Mastrobattista advises CEOs to think carefully about who within the company needs to know the details of a transaction and to limit the access to this information to a small group of top managers for as long as possible.

RULE #5: PUT TOGETHER A TEAM OF EXPERTS

"Acquisitions take up a good deal of time – incremental time over what the CEO is already spending on the business," says Piercey. "Moreover, they require experience and insight that most CEOs don't have. As a result, it is critical that the CEO bring in people who are experienced in transactions: investment bankers, accountants, lawyers and tax advisors."

"You're only going to sell your business once, and it's a steep learning curve," cautions Sherwin. "Why would you try to do that yourself?" He advises seeking out experienced transaction professionals, people who specialize in M&A and work on multiple transactions every year. He recommends talking to other CEOs who have sold their businesses for referrals to investment bankers in your market.

Mastrobattista adds that you can often find these people by asking your current team of advisors. Your regular accountant, for instance, can usually recommend a tax specialist experienced in M&A transactions to augment his or her expertise. Your general counsel may know an M&A lawyer. "The best place to find good people is from good people," Mastrobattista says. "Talk to your trusted sources for business referrals and evaluate independently."

RULE #6: SCRUTINIZE DEAL STRUCTURE AND PROVISIONS CAREFULLY

Price is one key factor in a deal, but it's not the only one. "You and your team should look closely at the structure of the transaction," says Mastrobattista. "Is it cash? Is it notes? Is it stock? Are there hold-backs? Are there earn-outs?" There are tax implications to all of these different purchase price methods that a good tax advisor will help you evaluate. Each structure has different risk implications as well, with payment in seller notes or earn-outs increasing the risk that you won't receive the value you expected from the transaction.

RULE #7: THINK ABOUT OTHER POSSIBLE ACQUIRERS

"Just because one person is interested in buying your business doesn't mean you have to sell it to them," says Sherwin, adding that there may be multiple offers out there, in addition to the unsolicited one. For CEOs who are interested in pursuing a sale, he recommends widening the circle of potential buyers, not just approaching known competitors, but a larger circle of complementary, often larger potential buyers.

Unearthing these buyers may require an investment banker's help, Sherwin adds, and Mastrobattista concurs that their insight can be invaluable. "You need to look at the state of your company and of the market as a whole when you think about soliciting other offers," she says.

Deciding to widen the circle of potential buyers carries

By being alert to the meaning and importance of all portions of your P&S agreement, you can help ensure that you won't be in for unpleasant surprises once the ink on the document is dry.

with it the risk that the buyer who gave you the unsolicited offer may not wait for you to test the market. This is when an investment banker can be particularly helpful to determine if the offer on the table is pre-emptive enough to be worth accepting to the exclusion of other potential buyers.

Mastrobattista adds that bankers can tell you more about the market's appetite for deals like yours, but that ultimately, the transaction should be done on your timetable. "There's nothing worse than rushing a deal through, not understanding all the implications of price and market conditions, and then getting bitten in the end."

RULE #8: CHECK OUT THE BUYER CAREFULLY

CEOs should also scrutinize their potential buyers carefully. Sherwin says he is always astonished when a company owner agrees to a transaction without first verifying that the buyer can pay. "There are a lot of people out there who can't close," says Sherwin. Particularly in today's tight credit climate, you want to know that the buyer has the financial capacity to close the transaction.

RULE #9: PLAN YOUR POST-TRANSACTION ROLE CAREFULLY

You sell your company, and what then? Every one of our experts maintains that you should think carefully about what, if any, role you play in the acquired company.

If the transaction is structured to include an earn-out, you may wish to continue to run the business through the earn-out period to ensure that the maximum incentive payment is earned.

However, Swerling suggests that CEOs consider the implications of their shift from owners to employees, if they continue in the business. "You've been managing this business for years or decades. You've been doing everything your way, maybe with the support of some hand-picked managers. Now it's not yours anymore, and the company you built will change," she says.

RULE #10: DON'T BE AFRAID TO WALK AWAY

Given the intense and emotional nature of negotiating a sale, our final rule is perhaps the hardest to follow. If a transaction turns out not to be in the best interest of you or your company, you need to be willing to pull the plug. Not every deal is a good one. Sometimes even attractive transactions can turn sour over the course of negotiations, or as market conditions change. Even if you've spent months working on a transaction, it may still be better, at a certain point, to simply walk away.

UNSOLICITED DOESN'T HAVE TO MEAN UNANTICIPATED

Unsolicited offers happen more often than you think – and they can be a welcome wake-up call to business owners caught in the day-to-day details of running a company. Yet they shouldn't take you completely by surprise. Sound preparation for an unsolicited offer is good strategic planning.

By developing a strategy that says whether, when and for how much you would consider selling, by obtaining accurate valuations of your business on a regular basis, and by developing relationships with seasoned M&A advisors now, you can make sure that you maximize whatever opportunities come your way in the future.

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