

# Selling a business

**Selling a business is often the culmination of years of work. It can be a difficult, emotional and time-consuming task. It is not something that many managers or owners do more than once. You have to get it right first time.**

This briefing outlines:

- The advice you will need.
- Grooming the business for sale.
- The sale process.
- Negotiation tips.

## 1 The decision to sell

### 1.1 Plan ahead.

- Think about the possible sale of your business several years before you intend to start the sale process. Good planning helps you maximise the value you draw from a sale.
- Consider other ways of exiting from the business. Would they give better results? You may be unable to find a buyer so you should look at options such as a management buy-out or passing the business on to a family member. See **Planning your exit from your business**.

### 1.2 Be clear about your **reasons** for selling.

- Common reasons include making as much money as possible, protecting your financial future, moving to something new, retirement or ill health.
- You may feel the business and staff have better prospects under a new owner.

**1.3 Write down your specific objectives.** These might include:

- Sell by a given date.
- Sell at a target price, or at least at a fixed reserve price.
- Receive immediate payment in cash of at least a certain amount.
- Continue (or not) to be involved in the running of the business.
- Secure the jobs of your employees.
- Minimise personal tax liabilities.

Your objectives will influence the way you sell and who you try to sell to.

### 1.4 Pick the right **time**.

- Consider the economic cycle.

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- Sell before your market declines.
- Consider any forthcoming tax changes. Will they affect you or the buyer?

For those who sell a business out of choice, rather than necessity, a common mistake is to sell too early. Spend the necessary time building up stability and profitability (see **3**).

## 2 Getting the right advice

Choose advisers who specialise in selling businesses.

### 2.1 Good advisers can fill many **roles**, such as:

- Boosting your credibility and making negotiations go smoothly.
- Providing a realistic business valuation.
- Approaching potential buyers without revealing your identity.
- Widening the list of possible buyers.
- Allowing you to run the business while they concentrate on selling it.

### 2.2 Consider using a **combination** of advisers to cover all aspects of selling.

- A corporate finance adviser can help groom the business (see **3**), identify buyers, and write the Sales Memorandum (see **4**).
- A non-executive director can offer objective advice and support.
- A corporate lawyer can draft and negotiate the Sale Agreement.
- A tax accountant (or lawyer) can minimise your tax liabilities.
- Specialists can accurately value assets.

### 2.3 Agree a clear **fee** structure. There are three main ways of charging fees:

- An hourly rate. Obtain an estimate of how many hours' work is required. Agree an upper limit, and the timing of interim fee statements.
- A fixed rate for a certain piece of work (eg drawing up the Sales Memorandum).
- A contingency fee dependent upon success and the eventual sale price.

### 2.4 Divide **responsibilities** between advisers.

- The instruction and fee basis for each adviser should be clear and in writing.
- Avoid overlapping responsibilities, but seek second opinions on important issues.
- Agree the lines of communication and make sure each party knows its responsibilities for dealing with enquiries. Get key items of advice confirmed in writing.

## 3 Grooming the business

Showing the business in the best light is a crucial factor in gaining the best possible price.

### 3.1 Create a good **financial record**.

- Concentrate on short-term results.
- Try to show a stable financial pattern through the year. Delay or bring forward major purchases to help achieve this.
- Be realistic when using depreciation figures or the timing of income in your accounts. Provisions for bad debt and old stock should also be realistic.
- Sell under-used equipment and property.
- Improve your working capital position, by good stock management and tighter credit control (see **Credit control**).

### 3.2 Make sure management **information systems** are working smoothly.

- Buyers will want information quickly.
- You need to show that the business is under control.
- Ensure the information is accurate. A buyer's confidence will be undermined by errors.

### 3.3 Present the **assets** in good condition.

- Premises and equipment should look well maintained.
- Stock should be neat and orderly.

### 3.4 Make the business **less risky** from the buyer's point of view.

- Turn informal deals with suppliers and customers into formal contracts.
- Establish sensible incentive schemes to encourage key employees to remain with the business (see **Incentive pay**).
- Reduce dependence on a few large customers or a single source of supply.
- Tie up any loose ends. If your tenancy agreement is due to expire soon, make sure the landlord will agree a new one.

There are many ways to make a business shine, so it is always worth discussing with your adviser or non-executive directors.

## 4 Sales Memorandum

The Sales Memorandum is the initial marketing document sent to interested parties. It is written jointly by the management and your corporate adviser. It should:

### 4.1 Make the business sound **attractive**.

“Look for a premium purchaser — one who will pay over the odds because your business fills a gap in his or her portfolio.”  
**Nick Brown,**  
**Solomon Hare**  
**Corporate**  
**Finance**

**4.2** Be a source of hard **information** for buyers.

**4.3** Show that the business can be **improved**.

- This is particularly important when the buyer plans to be a hands-on manager.

Keep detailed confidential information out of a Sales Memorandum. This can be shown later to serious buyers.

## 5 Marketing the business

Marketing your business falls into six stages.

**5.1 Find** potential buyers, such as:

- Competitors, suppliers or customers.
- New market entrants, including foreign companies.
- Your own management (a buyout) or another management team (a buyin).
- Financial investment companies.

### Getting your price

Once you have received opening offers, start the bargaining process.

**A** Set a **price**.

- Decide what valuation you are likely to get (see **Valuing a business**).
- Reject buyers who are significantly below this level.

**B** Coax the remaining buyers into **closer contact**, keeping them well informed.

- Offer them access to selected members of your team.
- Distribute positive business data, before the buyers ask for it.
- Be ready to counter negative information.
- Be open and transparent.

**C** Spur buyers into action. Ask for **final offers**.

- Tell them how much to raise their offers.
- Consistently emphasise the future business opportunities.
- Make it clear that other buyers are also seriously interested in the business.

Setting and holding out for a high price usually pays off. Potential buyers will gain an impression of genuine self-confidence.

**5.2 List** possible buyers.

- This should involve no more than 30 names, divided into an A and a B list. Only use the B list if the A list does not produce results.

**5.3 Approach** the possible buyers to see if they are interested.

- Keep your own business anonymous by using an adviser.
- It is usual to approach a business through its adviser (eg the auditor), unless you have a better contact. The adviser can direct you to the appropriate person. If the business is run by an owner-manager, approach the individual directly.
- Use the phone, or a one-page letter.

**5.4** Ask your legal adviser to draw up a short **confidentiality** agreement for interested buyers to sign.

**5.5** Send out the **Sales Memorandum** with:

- An outline of the sale timetable.
- Details of where and when you would like to meet buyers.
- A request for opening offers.

**5.6** After receiving offers, draw up a **shortlist** of buyers.

- Reject buyers without the finance to make the purchase.

The process of meeting buyers can disrupt your business. Balance the access you give buyers with maintaining confidentiality and productivity.

## 6 Weighing up the offers

There are many ways of paying for and taking over a business. You will need to weigh up what is on offer.

The most important things to consider are:

**6.1** Can the buyer really **pay** for the business?

- However good an offer may sound, unless it is properly financed, it is worthless.
- Buyers must have the right approvals (eg from the board or from shareholders).

**6.2** What **form** will payment take?

- Cash payment up front is the safest option but may also be the least tax efficient.

“Selling a business is a very distracting process for management. Be careful not to take your eye off the ball, or the performance of your business could deteriorate at the exact moment when the buyer is examining it.”

**Brian Hayden,  
Hayden  
Associates**

“For a seller, the giving of warranties and indemnities is arguably the most important issue of all, because they can come back and haunt you.”

**Jeremy Ticktum,  
Shranks solicitors**

- If deferred cash payment is offered, establish whether it is guaranteed. It may be in the form of earn-outs which are linked to future sales or profits. In a situation where payments are reliant on the future performance of the business, make sure you retain some form of management control to enable performance targets to be met. Otherwise, you may receive less than you are entitled to.
- A share swap is only comparable to a cash payment if the shares you receive are in a quoted company. Shares in an unquoted company may be hard to value and difficult to sell.

### 6.3 What will your **responsibilities and liabilities** be?

- You may be asked — or required — to remain involved in the business. But remember you will no longer be in control.
- You will probably be tied to warranties and indemnities for a year or more.

### 6.4 How will the business be run in **future**?

- What expansion or sales plans does the buyer have? Will any parts of the business be sold off?
- How will the deal affect employees? Will anyone be made redundant?

### 6.5 How **long** will completion of the sale take?

- Industry and accounting due diligence must be completed. This may include an accountant's report. The accountant's remit will be to verify the key management information and to identify potential problems for the buyer.
- Legal due diligence may take up more time — sometimes several months.

## 7 Choosing a buyer

You should now finalise sale terms.

- 7.1** Be sure you fully **understand** all offers eg any warranties or indemnities you will have to provide.
- 7.2** **Play off** one party against another so that they raise their offers.
- Be prepared to bluff. The buyers will negotiate, but are unlikely to pull out.
- 7.3** **Choose** the buyer you want to sell to.
- Discuss the deal only with this candidate.

- Do not try to negotiate better terms at this stage, as this would destroy any trust that is developing between you and the buyer. A good working relationship is important. Your goal now is to complete the deal without any hiccups.

### 7.4 Quickly agree **Heads of Terms** with the buyer. This is a signed agreement setting out the deal's chief points.

Parts may be legally binding. For example:

- An exclusivity period during which the seller cannot negotiate with anyone else.
  - Payment of the buyer's (or your) costs.
- 7.5** **Tell** other potential buyers that you have signed a Heads of Terms with the buyer.

- Keep at least one other buyer interested, as a back-up.

## 8 Completing the deal

The buyer's offer will be subject to further due diligence and to the detailed sale agreement. Provided that this due diligence is trouble-free, and neither party has any surprises up its sleeve, the sale should now be relatively safe.

### 8.1 The **further due diligence** usually involves the buyer's accountants and lawyers.

- The accountants will want to look at every aspect of the finances of the business.
- The lawyers will want to check that your business has full legal ownership of all key assets (eg property deeds and licensing contracts). They will also want to look at the legal relationships with customers, suppliers and employees. Many legal issues are covered by warranties and indemnities that you, as a vendor, will almost certainly be asked to sign. Read these carefully — they can be far reaching.

### 8.2 **Certain** members of your staff (eg Finance Director or Company Secretary) may have to be involved early on in the due diligence process.

- Be mindful of the feelings of your employees, especially when communicating your plans, as you may run the risk of losing key members of staff if they fear their jobs may be in jeopardy.
- Carefully consider who you tell and when you tell them.

### 8.3 Finalise the **sale and purchase** agreement.

### Expert contributors

Thanks to **Brian Hayden** (Hayden Associates, 07785 532266); **Paddy MccGwire** (Cobalt Corporate Finance, 020 7491 1271).

### Further help

There are other Directors' Briefing titles that can help you. These briefings are referred to in the text by name, such as **Planning your exit from your business** and **Credit control**.

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