White Paper: Selling Your Company Vs. Selling Your House

Getting your company ready to sell is both like and unlike selling your house. When you sell your house, you make it look as nice as possible by performing touch-up painting, maybe replacing a worn carpet, or replacing windows that may have lost their seal. These are all “cosmetic” improvements.

When you sell your business, you should take care of as many “cosmetic” improvements as are necessary to have the business “show” as well as it can. Buyers are more interested in companies they can grow with minimal CAPEX or Capital Expenditures required post acquisition.

Sometimes a house needs “infrastructure” help, like foundation leveling. However, this does more to keep the price of the house equal to comp’s. Think of it this way, the less the buyer of a house or a business perceives they have to spend, the more they will pay you!

Here are the Top 10 ways to increase your company’s Enterprise Value:

1. Get your financials in order

- **Why?** Buyers will perform due diligence on your financial records to determine how much assurance they can place on them. When buyers find “issues” in the financials, they ascribe the types and volumes of issues to risk. The higher the risk (meaning more investment on their part to mitigate the risks), the lower the selling price. To the extent there are questions/concerns, buyers will use these “red flags” to negotiate a lower sale price or delay payments to you.

- **What to do:** Have a review that will simulate the due diligence process, identifying all of the red flags that will pop out during due diligence. Red flags are essentially discrepancies or “vague” areas of your financials where sub-ledgers do not readily and apparently tie to the General ledger or where there are large balances that do reconcile to a detailed schedule. Have someone perform a “GAAP Review” to identify all of the issues that will potentially come up at the closing table and possibly be used to reduce the sale price or delay your payment. Then, correct or mitigate the issue immediately, even if you are not closing for several months.

- **Benefit to you:** Maintain and/or increase the sales price. Having clean financials gives buyers confidence in the numbers, which can lead to a higher sales price.

2. **Prepare for Due Diligence.**

- **Why?** Buyers use time (elapsed time) in the deal process as a negotiating tactic. The more prepared you are for due diligence, the less time it will take to close. The less responsive you are to their requests for information, the more time it takes to close, the higher the probability your original price gets “discounted” by the buyer.

- **What to do:** Have someone who is very familiar with the due diligence process collect and organize the data you will need to present to a buyer. Today, many use online data rooms for this, so that access is easy and immediate while controlled for confidentiality. Also, you can control when certain documents are released based on how far along you are in the process. For example, you can place a top ten customer list in the data room, but not release it until terms and conditions are finalized.

- **Benefit to you:** Closing on time and getting paid on time.

3. **Have a plan for growth, and execute on the plan.**

- **Why?** Because buyers are not purchasing your company to operate “as is”. They want to increase the return on investment, and will look for companies that have demonstrated reasonable growth of at least 10% over the, (TTM), trailing twelve months.

- **What to do:** You need a documented plan and you need to manage to that plan. Don't know where that growth will come from? Your sell-side intermediary can help you with this. Executing against a plan demonstrates you and your employee's ability to plan strategically and execute on a day to day basis. The budget and forecast will become a significant part of this plan.

- **Benefit to you:** Buyers will give more credence to projections (and thus a higher sales price) if you have demonstrated the ability to plan and execute effectively.

4. **Prepare a budget and forecast, then live it.**

- **Why?** Because having targets in writing is motivational to most people, and you need everyone on your team pulling in the same direction. Buyers are looking to see how well managed the company is, and whether its management team can work together and achieve reasonable results. To the extent that the forecast is documented and you show that you met or exceeded forecast, the buyer will ascribe less risk to continuity and likely offer a higher price. Having a budget will also help move your company to its highest performing potential, which will have a direct effect on the bottom line and the selling price.

- **What to do:** Prepare a detailed forecast (including detail at the revenue driver level) and monthly budget and manage to the numbers every month.

- **Benefit to you:** Better internal accountability and a higher selling price

5. **Maximize revenue and profit to the business.**

- **Why?** The higher your EBITDA, generally, the more you will make on the sale of your business.

- **What to do:** Get help. Get help. You are not in a position to be expected to know what is best to be done in all aspects of the business to maximize your profit and

EBITDA in advance of a sale. Your sell-side intermediary will be instrumental in helping you plan and execute a list of "projects" to ensure that you hit forecast targets/budgets and maximize your return during the go-to-market period. These projects include things like streamlining your operations to reduce unnecessary staff, eliminating unnecessary and non-business operational costs, expanding markets/industries to include secondary and tertiary uses of your products, etc. Your sell-side intermediary will also help you make capital expenditure decisions during this critical time, so that you can be assured of getting a return out of each dollar you spend.

- **Benefit to you:** Every dollar you add to the bottom line can have a "multiple" effect on value, meaning a higher sales price. Yes, buyers use multiples in their conversations about deals, but multiples are NOT their primary method of pricing. Rather, multiples are figured AFTER their calculations are made.

6. **Develop a second level of capable management.**

- **Why?** Buyers know that you will be leaving the company. They are concerned about sustainability and continuity of the business at previous levels and higher. To the extent that you have a competent management team that can carry on in your absence, buyers will deem the purchase less risky (meaning less investment on their part), and therefore pay more for your business.

- **What to do:** Document the value-add that you provide the business. It may be sales, customer service, bookkeeping, or product innovation. Determine what skill is necessary to replace your contribution, and then find/hire that skill if it does not exist in the company. This point takes time; start now on fully developing your second level of management.

- **Benefit to you:** Less risk ascribed to the sustainability of the company, which translates into a higher price or better terms and conditions.

7. **Document what people do.**

- **Why?** Titles don't always convey the reality of a position in a company. Buyers want to know who does what, and in what combination, so that they can make assumptions about staffing levels in their calculations. Quite often, in small companies, one person may hold the job of 2 or more people. This needs to be clearly communicated to buyers.

- **What to do:** Document job descriptions for each of the top 2 or 3 layers of management and the supervisory level. Include key skills and attributes, certifications, degree or license requirements, etc. Also, consider developing and implementing Employment Agreements that transfer to the new owners in order to keep key players on board well beyond the sale.

- **Benefit to you:** Buyers will make assumptions about replacing or adding to staff once the sale is closed. To the extent that positions and skills are documented and key players have employment agreements in place, the buyer will lower their "additional cost" assumptions, meaning a higher sale price to you.

8. Simplify the "family relationships" in the business.

- **Why?** Buyers don't trust family members working in the business for the most part, especially if they will be receiving a portion of the sale. Quite often they disappear after the sale, even though they indicate they will stick around for a while.

- **What to do:** For non-key employee friends/family members, attempt to move them on to their next successful venture before closing, and make sure that their positions can be performed by someone else. For key employees, get an Employment Agreement in place.

- **Benefit to you:** Peace of mind that friends and relatives will be taken care of and not at the mercy of a new, unrelated buyer. Also, this can have a positive effect on sale price, primarily in not lowering it rather than raising it.

9. **Diversify your customer and supplier base.**

    - **Why?** Concentration in either customers or key suppliers is a big red flag to potential buyers, especially when that concentration is based on a relationship between the customer/supplier and the current owner, who will eventually leave.

    - **What to do:** Identify concentration issues and either get long-term contracts in place, or work to find additional customers/suppliers to reduce concentration. This is easier said than done and takes time, and is generally easier to do with suppliers than customers.

    - **Benefit to you:** Less risk in the business, translating into maintaining or increasing your final sale price. Some buyers will not even look at companies with significant customer concentration issues.

10. **Keep your customers happy.**

    - **Why?** Buyers will investigate whether customers are happy with the products and services they receive from the target company. This gives them an idea of how loyal the customers will be during an ownership transition. Unhappy customers translate into risk, which leads to a lower selling price.

    - **What to do:** If you haven't surveyed your customers recently, do so. The key question to ask is "On a scale of 1 to 10, how likely are you to refer our company to a friend or colleague?" The answers to this one question will tell you most everything you need to know about overall customer satisfaction. Subtract the percentage of those that score you 1-6 from the percent that score you 9-10, and you will know your Net Promoter Score (Fred Reichheld, *The Ultimate Question*).

    - **Benefit to you:** Buyers will see a very loyal customer base that is founded upon confidence and reliability in your products and services rather than any one individual, ultimately leading to a higher sale price. Seem daunting? It can be. Starting early, and getting the advice of an experienced sell- side intermediary (M&A advisor), an accountant, and a competent transaction attorney (usually

NOT your family attorney; transactions are dramatically different from trusts and wills) will provide extremely valuable insight and your return on investment in these professionals will be realized at the closing table.

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