M&A Preparation Tips for Businesses: Part 2 (Sellers Guide)

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Note: This the second piece of a two-part alert on mergers and acquisitions. Recently, CPBJ asked and our partners Paul Mattaini and Jeremy Frey answered questions on M&A, both from the buyers' and sellers' points of view. The reporter then used pieces of those answers in two separate articles. But we wanted to show people everything that was asked and answered in case it can help those in the M&A stage of their business. In Part 1, Mattaini answered questions from the buyers' perspective. You can read it here. Both articles appear in CPBJ's recent M&A in the Midstate supplement. If you have any questions on anything in these answers, please contact Paul Mattaini, Jeremy Frey or anyone in our Mergers & Acquisitions group.

Jeremy Frey, chair of the Barley Snyder Business Practice Group, answered questions for the article, "House in Order," a guide for owners getting ready to sell their business.

Central Penn Business Journal: How can you make your company more attractive to a potential buyer?

Jeremy Frey: One of the keys is to have the appropriate financial statements ready. Buyers generally require three years of financial information, including statements audited or reviewed by an outside accounting firm rather than internally-prepared statements. If you have not started this process and plan on selling your business in the next few years, it would be advisable to begin the financial statement process sooner than later. In addition, make sure that financial reporting systems are in place so you can produce data and reports that are likely to be requested by potential buyers.

CPBJ: Is there a "right time" to put your business on the market?

JF: There are many factors at play here and it really depends on the owner's desire. If the desire is simply to maximize the sale price, then the company's results will obviously play a huge role in this. But if the owner is simply looking to get out of the business in the near future, this may be less important. I've even seen situations where companies have sold because they recognized the market or their industry were changing and they wanted to get out before the change occurred. So it really depends on a case by case basis.

CPBJ: Conversely, is there a "wrong time"?

JF: The same factors that are at play in the "right time" analysis are at play here. But probably the worst time to sell would be when the financial results are not representative of what would lead to an acceptable valuation. In other words, a seller may think (and may even be right) that the company is worth a certain value. But if the financial results do not support this, it will be difficult to get this value.

CPBJ: How important is company culture in the merger process?

JF: Interesting question. This can be critical to the success of the business afterwards. If the culture appears to be poor or incompatible, this could pose significant challenges to the post-closing operations. Merging two cultures can be a challenge and it takes great leadership to accomplish this in most cases. An analysis of the company cultures prior to the deal is important so that the leadership team is prepared for this after the closing. But from the seller side, it is not as critical unless the seller is worried about the future of the seller's existing workforce. In that case, the seller may want to do some of its own due diligence into the culture of the buyer. But I can say this rarely happens though.

CPBJ: What should a seller look for during the due diligence phase?

JF: The seller should be prepared for the due diligence process by having its records in order. We have a typical due diligence checklist we like to review with clients so they can be prepared for this. They may also want to do a sale side quality of earnings report.

CPBJ: What are the red flags that make you say you shouldn't go through with a deal?

JF: On the sell side, I would say there are fewer. Ultimately the seller wants to get paid for the business and have as few liabilities or responsibilities as possible after the closing. So if the purchase price is deferred over time, or if the seller is asked to retain some liabilities after the closing, these could both result in a seller rejecting a deal. As some sellers approach the closing, they start to get uncomfortable about the social issues related to the future of their employees, their legacy and just the change of no longer owning something that has been such a huge part of their life.

CPBJ: On the other hand, what are some things you look for that make you think a company should go through with it?

JF: If the price and timing are right, the seller usually feels good about proceeding with the deal.

CBPJ: What kind of protections need to be in place to protect yourself if you decide to sell?

JF: The first protection is to get as much money as possible at closing. We caution our sellers that they should be prepared to proceed without any of their deferred money if they choose to defer a portion of the price. Unexpected things happen post-closing and unless you receive the money at the closing, you are never guaranteed to receive your money. We also build protections into the purchase agreement. That is where the buyer will typically try to obtain some protections from the seller and we try to limit the obligations of the seller. Lately it has also become more and more common in larger transactions for sellers to obtain representations and warranties insurance. This allows the seller, in exchange for the payment of an insurance premium, to have some additional comfort that they will be protected from most post-closing claims related to the purchase agreement. Depending on the deal, this feature can provide some additional comfort to the seller.

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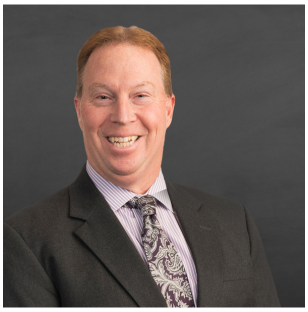

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