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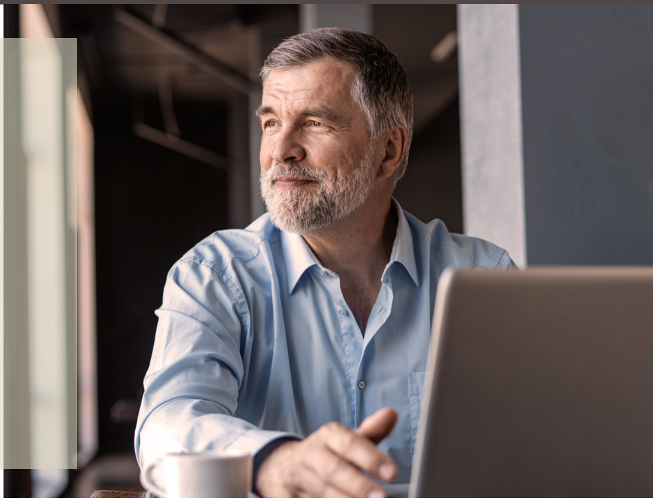
Issues that Derail the Sale of a Business and How to Avoid Them



You're selling your business, the culmination of your hard work, talent and vision. Closing the transaction will enable you to accomplish the goals you have for yourself and loved ones. You've spent a lot of time preparing for this milestone — but is there anything else you can do to ensure the process is smooth and successful?

One important step you can take is to understand common pitfalls ahead of time. It is not uncommon for business transactions to fall through — sometimes after months of negotiations — for reasons that can often be avoided with foresight and advance planning.

Here are some common issues that tend to derail transactions and how to prevent them.

Common Reasons Transactions Fail

01 | Family conflict: Family businesses often serve a variety of purposes for different family members — ranging, for example, from a source of income and perks (e.g., company car, memberships, etc.) to providing a sense of meaning and self-worth. When it comes time to consider selling the business, this can lead to disagreements on whether to sell, and under what terms, evoking intense emotions and surfacing complicated family dynamics. This can derail the sale and, more importantly, cause lasting disagreements within the family.

02 | Underdeveloped management team: If you haven't identified and mentored the right successors, your buyer may conclude that too much of your company's value is tied up in you running it, leading them to significantly discount the offer price or even walk away.

03 | Problematic financials: Inadequacies or errors found in your financial controls, reporting or forecasts could cause your buyer to lower the offer price to an unacceptable level. Sources of these issues take many forms, including poor cash flow or expense management, lofty assumptions, or poor accounting practices.

04 | Risky concentration of customers or vendors: If your sales are too concentrated in too few customers, the buyer may not be willing to accept the risk associated with losing those customers. Same with vendors. If your business relies too heavily on one vendor, the buyer may not want to accept the risks associated with that vendor and determine that replicating your business model without that vendor would be too difficult.

05 | Unrealistic price expectations: Your business is likely a big part of your identity. You've worked hard to build it, and the conviction you have in its potential is part of what's made you successful at running it. But this same passion may lead you to overestimate its worth in the eyes of a buyer. Not having a realistic sense of what your company is worth in the marketplace could cause you to prematurely reject — and even get insulted by — valuations derived from the due diligence process, causing the deal to fall part.

How to Avoid Deal Breakers

Fortunately, the probability of a failed transaction can be substantially reduced with a few best practices. These include:

Implement regular family communication: Business owners are usually laser-focused on running their business with little time to proactively prepare for the sales process and its implications for the various family members involved. However, family conflict can be avoided by making time to adopt formal governance and communication processes — guidelines for how family members participate in, receive details about and discuss the business. This can include monthly or quarterly meetings, which are usually not only healthy for the family but also for the business.

Invest time in developing your management team: If you haven't already, identify successors to train for key management positions and consider putting certain retention incentives in place (e.g., employment agreements and retention bonuses) to help financially motivate them to stay and ensure a smooth transition when the company is sold.

Conduct your own due diligence: Put yourself in the buyer's shoes and conduct due diligence on your own company with an objective eye toward stress-testing the financial, operational, legal, and strategic data and practices you have in place. This can help you anticipate buyer questions and concerns and, at a minimum, be better prepared with answers. You may even be able to implement improved practices and processes ahead of the buyer's due diligence.

Value your business ahead of due diligence: As part of, or in addition to, performing your own due diligence, seeking an objective third-party valuation for your company can help ground your expectations or even help you determine that you're not ready to sell at the price you would currently be likely to receive. It's much better to discover this on your own rather than after months of due diligence and negotiations with an interested buyer. This could include seeking a full certified business valuation — one that adheres to the Uniform Standards of Professional Appraisal Practice (USPAP) guidelines — but it doesn't necessarily have to. For example, BizEquity, a patented, online business valuation service, offers a solution that is between full-blown certified appraisals and back-of-the-envelope calculations.

Understand your personal spending goals and potential tax liabilities: Identify your financial priorities (e.g., lifestyle spending, major purchases, support for your family) and then understand what sales price (net of taxes) would be necessary to support them. Then you have an understanding — ahead of due diligence — of what valuation is needed to support your goals, or if you need to reprioritize your goals and/or delay the sale of your business until a higher price can be achieved. Or, better yet, you may even realize that you will have an unexpected surplus of wealth that you can begin planning for now.

Find the right advisors: You are busy running your business. Find the right financial, business, tax and legal team to support you with all of the above practices. Your role is leading your company — let other people with the benefit of experience handling many successful sales guide you on the other pieces. Given our focus on serving business owners and our established partnerships with investment banks, attorneys, accountants and valuation solutions such as BizEquity, we can help coordinate this team. Please reach out to us for help.

DISCLOSURES