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How to Maximize Your Price When Selling a Business

GUEST COLUMN

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You have worked hard to build your business. Maybe you would like to retire, maybe you need additional capital and resources to continue to compete, maybe the business has peaked and you believe it is time to get out, or maybe someone has made you an offer you just can't refuse (everybody hopes for this last one). Whatever your reason for selling your business, there are a few things you should do in order to prepare if you want to maximize your sales price.

Protect Your Intellectual Property: While entrepreneurs spend a substantial amount of time developing a unique idea, tradename, logo and brand, many fail to protect their intellectual property nationwide. If you are selling services or products in more than one state, you should obtain a federal trademark or service mark to protect your tradenames, brands and logos nationwide. If you fail to obtain a federal trademark or service mark, your tradenames, brands and logos may only qualify for protection in those areas where they are currently being used.

Additionally, you should adopt a formal policy to protect your proprietary information and trade secrets. Make sure that you have your employees, independent contractors, etc. execute confidentiality and non-solicitation agreements to protect your proprietary information (non-competition agreements for employees are prohibited in California, except under very limited circumstances). These policies should also be set forth in your employee manual in order to illustrate the importance you place on your proprietary information. Also, do not widely disseminate confidential information to your employees, restrict access to those on a need-to-know basis and use passwords. By putting together the proper internal systems to protect your proprietary information and coupling this with registering your intellectual property, you can help maximize the value of your business.

Remove the Skeletons From The Closet: Ultimately, everything reaches the light of day. Whether this occurs before the documents are executed (resulting in a reduction in purchase price) or after the documents are executed (resulting in an indemnification claim or a lawsuit), most buyers will pursue a seller for anything which causes damage to the business which the buyer did not know about prior to executing the final documents. Therefore, if you have taken some shortcuts to grow your business in order to save costs, etc., fix them, if possible, before you decide to sell.

Once a letter of intent is executed, the seller's leverage plummets and the buyer's leverage increases as the purchase price has now been locked into place. As a deal progresses and the buyer engages in due diligence, the purchase price can only be reduced. If the buyer finds things during due diligence which hinders the buyer's outlook for the business, the buyer will often demand a reduction in the purchase price or worse yet, kill the deal.

At this point in the transaction, as a seller, you are often times both emotionally and financially committed to the deal. As a result, it is tough to pull out of the deal and many sellers, confronted with this situation, often begrudgingly accept some form of a reduction in purchase price or modified terms. In order to prevent this from happening to you, either (1) remove the skeletons from the closet, or (2) have your advisors disclose the information early in the process, preferably before the execution of a letter of intent and during the bidding process, when the seller still has the most leverage and the buyer is most excited about the business.

Prepare Accurate Financial Statements: It is highly recommend that before the business is sold, you obtain at least 2 years of audited financials. Audited financials can help establish your credibility since an independent third party has reviewed and certified the accuracy of your financial records. If you plan on selling your business to a public company, it will help you maximize your purchase price since the buyer will not have to expend as many resources to comply with Sarbanes-Oxley.

If you cannot afford audited financials, we would suggest that you at least have them reviewed by your accountant. Additionally, you should talk to your accountant to make sure that you account for potential liabilities which may not be disclosed on your financial statements. For example, many small businesses do not accrue sick time and vacation time. This undisclosed liability oftentimes results in an immediate and unexpected reduction of purchase price if the buyer has not been made aware of the amount of this liability.

Negotiate Assignability Clauses: Many entrepreneurs do not appreciate the importance of a contract's "boilerplate" language; however, the boilerplate language can be very important when you sell your business. For example, if you enter into an asset agreement, one of the requirements of the asset agreement will be to obtain the consent of the other party to the assignment of the contract. If a contract has a non-assignment provision, the other party will have leverage over you and may potentially hold up the deal or reduce the sales price as a result of the potential risk that the contract may not be assignable.

Consult With Your Advisers Before Entering Into a Deal: It is important to work with your advisers closely before you enter into a transaction. They can help you find the right buyer as well as structure the transaction advantageously.

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