NEWS FROM THE CORPORATE FINANCE TEAM
AT **ENSORS CHARTERED ACCOUNTANTS**

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SELLING A BUSINESS

BUSINESS SALES – the key factors to a successful exit

Your business is great, it would be a lucrative purchase for the right buyer who can take it forward and reap the benefits of future ownership and control. You know that's true, but how do you convince the buyer, which in turn helps you achieve the desired, higher, price for your business?

Continued overleaf ➤

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Making you more than just a number

Every business is different and whilst you know your business inside out there are potentially several aspects of your business that may make it hard to sell or may restrict the price a buyer is willing to pay because of perceived risks or uncertainty.

In this paper we will be looking at various barriers to business sale and assessing the impact these factors can have on the marketability of your business. Where you may view some factors as an asset it is possible for buyers to see risks, most business attributes have both positive and negative elements.

Mid-level management

Do you have a strong management team who will remain with the business and its new owners after your sale? Are they able to keep the business running, taking the pressure off your buyer, reassuring them the business will continue to be profitable in the future?

Where there is a lack of mid-level management it can create difficulties in finding the appropriate buyer for your business. If your involvement in operations is to cease following the sale, to maximise proceeds, you will need to be able to demonstrate to the buyer that they can run the business without your ongoing input.

It is possible that an industry competitor may see a business with no management costs after your departure as a lucrative addition to their current infrastructure. However, a lack of management team is likely to rule out private equity investors or buyers who are looking to expand into a new market as they will need the ongoing support of an experienced management team.

The in-situ management team can represent cost and inflexibility resulting in resistance to change, which may be seen as a disadvantage to some buyers, but generally a strong mid-level management team is seen as a positive attribute.

One question you could ask yourself is 'Who is the face of, and who operates the business?'. When you leave will there be anyone else there to maintain and run the business? If not, you may benefit from establishing some form of mid-level management.

Contracts and flexibility

Is your business totally flexible and able to adapt to every change in the market? Can you cut your costs or decline business where it meets your business needs or capacity issues with no penalty? This sounds like a useful attribute; however, such flexibility tends to mean there is no contract in place or such flexibility is available to both contract parties.

The risk of not having a contract in place, or working on 'gentlemen's agreements' is that, whilst you 'know' the business is good and is going to continue for as long as you want it, there is no reassurance to the buyer that the business will continue.

Where contracts with your customers help to establish ongoing trade, it is also important to ensure your supply side is supported with the correct level of certainty. Buyers often look for certainty in supply to ensure they can continue to operate and meet demands, however they will also want the flexibility to negotiate prices or change supplier, especially where a buyer may have increased purchasing power or are able to supply items themselves.

Lease agreements for business properties are an important consideration. If the lease is too long or restrictive it can impact upon buyers' perception of value, especially where they may have existing premises that could be used. However, where no lease is in place there is the risk that the business may be made homeless or unfavourable variations to the current arrangement may be forced upon the new owners. Each business is unique, as is each potential buyer.

Dependence on limited customers or suppliers

Does your business rely on one or two key customers or suppliers? Do you have a strong working relationship with these key customers and suppliers?

It can be useful to demonstrate a strong relationship with your customers and suppliers, however if you have a very limited number of customers or suppliers there is an element of risk of 'putting all of your eggs in one basket'. Conversely if you have no repeat customers or regular suppliers there is likely to be concern over the reliability of future activity.

There is no magic number of customer or suppliers, each business will have differing profiles however it is generally accepted that having only one or two customers presents a higher risk profile than having multiple customers.

Lack of forward planning and stagnation

The history of your business is key when a buyer is assessing the value they will be willing to pay for it. The underlying trends within the business provide guidance as to how the business may perform in future. A steadily growing business, with all other factors being equal, is expected to continue growing. A company with falling performance is, without further justification and explanation, going to be expected to continue falling.

It is important to be able to demonstrate that all your hard work over the years growing the business has not stopped in the run up to a sale. A buyer will want to know that you have continued to develop the business, as you would have done if you were not selling it, to maintain the growth or to address any 'short term' deterioration in performance you may have experienced.

The timing of any sale is therefore very important to obtaining the best price. Ideally you want to show consistent or increasing performance over recent years. If you are therefore considering retirement or other business interests in the near future, you may wish to market your business before you start to lose the passion that has historically driven the business forward.

Each business is unique and it can be difficult to tell when it's the right time to market your business, however, getting professional advice early will ensure you get the best possible price when the time comes to sell.

Complex structures

There are many legitimate business reasons for a company to operate within a group structure. These reasons could include the safeguarding of capital assets, the segregation of new business activities, or taxation planning to name just a few.

Whilst the structure of the business being sold should not prevent a sale, depending on the structure and the reasons for it you may need to be able to explain why the structure came about and how the structure will be dealt with in any sale agreement.

If you operate several businesses and you are only considering the sale of one part of the business it is important to be able to demonstrate a clear distinction between the different operations. A buyer will need to be able to clearly see what they are buying and how that business will operate when it is no longer part of your business operations.

It is also important to recognise where the structure may create the involvement of other parties in the negotiations. One example would be where a business operates from premises held within a pension fund.

Whilst you may view the premises as your pension fund, there is often a professional trustee to assist with the administration of the pension scheme and to ensure you do not fall foul of any legislation and potential tax charges in relation to the pension scheme.

Trading and non-commercial trading with associated companies

If your business operations contain transactions with other businesses under your control it is important to be able to demonstrate a clear distinction between the different operations when negotiating a sale.

Arm's length transactions between the different businesses will need to be quantified and an agreement may need to be reached about ongoing activity between the businesses after a sale has been completed. This may be important not only for your potential buyer but also for the future viability of your remaining businesses.

In some instances transactions may occur at non-commercial rates or may not even be recorded. For example, goods or services may be transferred at cost rather than at market rates, management time may be allocated on a percentage basis rather than at contracted consultancy rates, assets may be shared or occasionally used with no recharge or minimal cost allocation.

If you are selling all your business interests in one transaction these issues may present less of a challenge, however they will need to be understood to ensure the buyer can understand the business and value it appropriately. If you are selling only part of your overall business operation it is unlikely that these arrangements will be able to continue after a sale, or if they are to continue they will need to be carefully documented.

Poor records or lack of information

Are your records up to date? Can you identify and explain the 'story' behind your financial records? When you are selling your business, it is important to be able to clearly explain the operations of the business on both a commercial / operating level and at a financial level.

Depending on the type of potential buyer you are seeking they may need to obtain an understanding of the business from the daily operations right through to long term business development. Additionally, they will need to understand what the assets and liabilities of the company are as well understanding how the activity of the company has changed over recent years.

It is not uncommon to be asked a lot of questions about your business, for example:

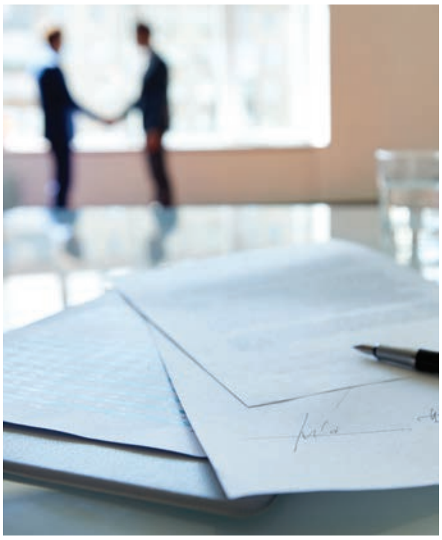
- Who are your main customers?
- How long have you supplied to them?
- What contracts are in place?
- How often do you have to requote for the work?
- What percentage of requoted work do you retain?

Any change in the level of activity is also likely to be questioned, for example:

- What is the reason for the increased turnover?
- Why has the gross margin changed from one year to another?
- Why have the overhead costs changed from one year to another?

These sorts of questions are usually raised during initial discussions or during due diligence. Due diligence is designed to allow the potential purchaser the opportunity to confirm and verify the business they are buying, therefore the information they request and questions they may ask can be numerous.

It may not be possible to answer all of the questions received due to record or system restrictions, however the more information that can be provided the more confident your potential purchaser should be about the transaction.



MEET THE TEAM

Our dedicated Corporate Finance team only work on a select number of projects providing the speed of response that is essential.

The team has experience across a wide range of industry sectors and sizes of business. We do not have a minimum or maximum deal size that we will advise on – we take each deal on its merits. We know the market and the people to help you complete the deal. Most importantly, we're approachable, friendly and down to earth, so you won't be swamped with jargon.

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"As we are due to complete on the sale of our business tomorrow I just wanted to thank you both for a sterling effort and extremely good advice and support all the way through. I know that you are being paid for this work but there is value received and value not received and this is definitely the former. It has been a long haul from our initial discussions about finding an investor, through the incorporation of the partnership, the management buy-out and now the conclusion with a sale of the company."

David Watson – Crown & Castle Hotel

"This was an extremely emotional and stressful period for my wife and myself. The Ensors team were 100% supportive from start to finish and provided the required information on time under considerable pressure, to meet the completion deadline."

Shaun Saddington – Hereward Car and Truck Components Limited

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