Preparation for Selling A Firm

Entrepreneurs invest a great deal of time and money into growing their private business into a successful enterprise. As retirement nears, the sale of the company often provides the nest-egg that will provide income for retirement, as well as an estate that may be passed down to their children or other representatives. Obtaining the best possible offer is important for providing this security. It is essential that the owner prepare their company for sale, ideally well in advance of the actual transaction. Enacting these improvements may increase the number of potential acquirers or may increase the ultimate price of the sale.

Acquiring firms will be most interested in firms that have exhibited growth in the previous years, have established operations and well-maintained facilities, maintain a strong credit rating with few late or uncollectible accounts payable, have a diverse group of suppliers and customers, and have reasonable inventory with low levels of obsolescence or spoilage. Actions taken by owners to establish or enhance these characteristics will improve the attractiveness of the firm.

Steady and increasing revenues as well as increasing profitability are strongly desired by an acquiring firm. Strong cash flows may be needed to repay debt used in the acquisition, and public acquirers may only seek target companies that can increase the acquirer's earnings per share (EPS). Owners should ideally sell their company after several periods of growth, or when the company is nearing maturity. If the company has recently had poor financial performance, the owner should consider waiting until the firm's performance improves.

Improving the appearance and modernity of the firm is an important first step in this process. Simple improvements such as repainting the facility, upgrading or replacing outdated machinery, or upgrading computer systems will create an impression that the operation is professionally run. Acquirers are more interested in firms where the facilities have been well-maintained, because this will require less expenditure by them after the transaction is completed. Additionally, a well-maintained and clear workplace also enhances the perception of safety in the workplace.

Diversifying the company's operations may also be beneficial to the firm. Should your company have opportunities to add additional profitable lines of production, add customers in a different sector or geographic location, or improve the existing product line, these actions may improve the overall perception of the firm. Establishing a diverse product line increases the likelihood that your company produces a product desirable to an acquirer and reduces the risk that a market change will negatively affect the firm. Additionally, it is beneficial to begin these operations several years before a sale, to enable your company to gain experience. Adding customers in a different geographic segment or industry also reduces the risk of economic downturn, and also may provide entry for an acquirer into a desired market. Further, having an established and diverse group of suppliers is also important to ensure access to needed raw materials.

Effective financial management can also add value to the firm. Timely payment of payables signals the favorable financial health of the firm while ensuring good supplier relations and reducing the likelihood of claims made against the company. Additionally, timely receipt of receivables by the company signals the health of customers and improves the valuation of these accounts at the date of sale. The firm should also address any lingering or questionable debt on the balance sheet. Frequently, firm secrets should be patented or be in the process of seeking patent and trademark protection. The financial statements of the firm should be reviewed at least quarterly and should be audited by a professional accounting firm. Audited financial statements indicate that the owner is serious about selling the company, create trust in the reliability of the company's finances, and may be required by the acquiring firm. Preferred or not, audited financials may not be possible unless the company has developed the financial and accounting systems necessary for this type of investigation of financial condition. In those situations, reviewed rather than compiled financials are preferred.

Solid management can create additional value in a transaction. Often, management is retained by the acquiring firm to continue to run the company or help transition the company to new management. Additionally, good managers may be transplanted to other operations in the acquiring firm. If the firm employs relatives or family members on the payroll, it should consider the pros and cons during the acquisition period. Lastly, smaller private companies often do not have officers such as a chief financial officer or chief operating officer, but are likely to be desired by an acquirer. By installing these officers prior to the sale, this will allow management to gain experience in managing the firm. These positions are likely to be filled by the acquirer after the transaction, and filling them prior to the sale will allow the owner greater control in selecting the desired candidate for the position.

Weaknesses in the company may be strengthened by an acquisition of another company. For example, another firm may be purchased because it generates strong fourth quarter revenues, a normally slow time for the company. The firm may be better positioned for sale with a strategic acquisition for the same reasons mentioned before. However, by completing the transaction prior to sale, the acquired firm will be better integrated into the operations of your company, and your company is more likely to benefit from the synergies of an acquisition that often take significant time to materialize.

These changes may improve the attractiveness of the firm, and may also increase productivity if a transaction is not undertaken. Owners should consider enacting the changes they feel appropriate well in advance of the anticipated sale. These suggestions are not ideal for every firm; the owner of each private firm should only undertake the improvements that they feel will be effective in their individual case. Additionally, owners interested in pursuing a sale should seek qualified legal, accounting, and investment banking advice to determine if a sale is appropriate and how best to prepare the company for sale.

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