

\$39.00

**SELLING
YOUR
BUSINESS
IN
TODAY'S
MARKET**

r.a.cohen consulting
M&A experience when you need it most.

Bob Cohen and Sam Sacco operate R. A. Cohen Consulting, a trusted industry M&A advisory service. We have advised on more than 100 successful industry transactions.

Contact us at (416) 229-6462 or (910) 509-0691, respectively.

■ Table of Contents

Why Owners Sell.....	4
Preparing For a Sale	6
Why Deals Fail.....	7
The Letter of Intent	11
Continue to Mind the Store.....	15
Successful Strategies.....	17

SELLING YOUR BUSINESS IN TODAY'S MARKET

Many knowledgeable observers believe that the staffing industry is glutted with companies offering similar services, driving down operating margins with fierce competition to maintain some market share, and that many of these firms will have to merge to avoid extinction. We expect to see increased consolidations in future years, as smaller firms find they need to unite to maintain economic and market viability and very large firms feel the need to grow to remain globally competitive.

■ Why Owners Sell

Selling your business is an important decision because of its potentially far-reaching effects on your family, staff, customers, employees and yourself. Sellers rarely decide to put their business on the market on the spur of the moment. A great deal of thought and analysis usually precedes such a decision. Most owners have in mind one or more reasons for selling before they make the final decision, which include, but are not limited to:

- Creating an exit strategy for the shareholders because of failing health, burnout or a wish to retire.
- An unwillingness or inability to invest needed capital in the business.
- Cashing in by liquidating some or all of the value in the business.
- Lack of a suitable successor, but a desire to see the firm continue.
- Partnering with a larger firm to gain greater resources for growth and access to broader and more sophisticated programs and infrastructure.
- The opportunity to participate in managing a larger business, territory or sector.

Today's market environment for selling is very different from the market of just a few years ago. Some of the characteristics of the current marketplace are:

- An uncertain and less stable economy.
- Fewer publicly owned buyers, resulting in less use of stock as consideration in a purchase. In today's market, stock has little appeal for buyers or sellers. There's no question that sellers would prefer to receive cash rather than stock.

Not surprisingly in the current market, buyers prefer to offer cash rather than stock because they feel their stock is seriously undervalued.

- Fewer buyers overall, creating less competition for a seller's business.
- An increasing number of management buyouts. With little access to capital and low market valuations, management teams question the value of remaining public.
- More private firms buying, many for the first time, working with less flexible multiples, fewer human resources to devote to the purchase and less experience with the process.
- Lower multiples than at the peak of the feeding frenzy in 1996-98.
- Higher multiples than in most years before 1996. This is an important fact to keep in perspective. Many sellers today are thinking they'll just wait a little bit and get the outrageous 1996-98 multiples back again. We don't think that's realistic. Not to say we'll never see them again, but the market was too high for a while. Now it's a little too low, but it's important that people maintain a perspective that 3 to 5 times earnings is historically a reasonable multiple.
- More private equity money available to fund acquisitions. Most of these buyers are looking for firms with annual sales volume of at least \$20 million to \$30 million to serve as a platform for expansion.
- Almost 75% fewer completed transactions than at the peak in 1998.
- Longer transaction times – 50% longer than three years ago.
- An increase in single-suitor deals, leaving sellers less choice.
- Increased due diligence scrutiny of current profit performance by buyers.
- Bankers' and lenders' requirement that they sign off on every deal. Two or three years ago, bankers and lenders had more confidence in management. If they looked at a deal then, it was very cursory. Today, they're poring over the details with the potential buyer (the lende), asking why it's a good deal, how it will be integrated successfully into the buyer's company, what could go wrong and what contingency plans the buyer has to address those risks.
- Bargain hunters, who are often less realistic about valuation.

HOW MULTIPLES ARE DETERMINED

Multiples are determined by the market, not by buyers or sellers. Buyers or sellers can indicate what they think are appropriate multiples for transactions, but at the end of the day it depends on what the parties can agree on. Multiples are typically measured in three ways:

- EBIT (earnings before interest and taxes)
- EBITDA (the former, with the addition of depreciation and amortization, if any)
- EBT (earnings before taxes).

The multiple of that calculation is always an adjusted earnings figure. The basic thrust of adjustments is to normalize the expenses on a go-forward basis, e.g., if the owner's compensation (including cars, club memberships, travel not really necessary to the business, life insurance, etc.) was \$1 million, the market value to replace that owner's role might be only \$150,000. So we would adjust the owner's compensation figure by \$850,000 going forward.

The most significant factor that will influence the multiple is the sector the industry is in. It basically runs along skill lines, with some slight adjustment for supply and demand. For instance, lower-skilled light industrial workers will command a lower multiple range than office support workers, who will command a lower range than technical, IT, accounting, legal and other niches.

- Sellers not being current on market values.
- Buyers making more rational and strategic purchases. (In the end, this is good for all.)

The present market situation is not all negative, however. The good news is that since June 2001 more buyers with a clearer set of acquisition criteria and more latitude have entered the market, creating far more choices for sellers and more potential purchasers for each available firm.

Many current sellers already had planned to sell their businesses in 2001; however many other staffing firm sales today are being driven by flat or lower sales, squeezed margins, need for capital and diminished profitability.

■ Preparing for a Sale

How can you prepare your company to avoid the possibility of a fire sale? Timing is essential. Consider both the external economy and your firm's internal conditions when you are deciding whether to sell.

- A soft economy will have an adverse effect. Many prospective sellers have called us in the past few months saying they'd like to sell their business "but I understand that now may not be the best time to do it." It could be that it's the best time at the stage of growth their company is in, but it may not be best in terms of the state of the economy.
- Ensure that your financials are clean and clear, preferably audited or reviewed and easy for potential buyers to read. Most smaller firms (under \$10 million) only have compiled statements, unless their banks demand more. Ideally, these statements would include audited or reviewed financial statements such as income statements, a balance sheet, statement of cash flow, cash flow forecasts and pro forma income statements, supported by adequate notes to financial statements.
- Analyze the tax consequences of the sale. In a C corporation, if the owner sells the assets, money earned by the company is taxed twice: when it is earned and when it goes out to the shareholders. If an owner sells the stock of a C corporation, the money bypasses the company and goes directly to the owner; therefore, he only pay taxes once. In an S corporation, an LLC or an LLP, the owner can sell assets without any concern.
- Choose the correct method of valuing the business. Consult your M&A advisor.

- If your lease is up for renewal, make sure the new agreement is transferable in the event of the sale of your business. More than one deal has fallen through simply because a buyer could not secure satisfactory leasing arrangements from a landlord when the business was to change hands.
- Limit your attorney's participation to the legal aspects of the sale. The attorney's job is to protect you legally, not run the deal. Attorneys are more used to win/lose transactions than dealing with a prospective partner; some can set the wrong tone for negotiations.
- Strong, healthy companies will always be in high demand. If there is room for improvement in your firm, now is the time to make changes to preserve your future
- Keep up with trade industry journals that report on sale transactions. Make a note of these buyers, who they are, where they are and what they do. Many of these buyers are private firms and could be a good acquirer for your firm. Check out their web site, monitor how their other acquisitions are proceeding and then determine if they could be a candidate for you when you are ready to sell. You can determine how best to make contact at this point.

■ Why Deals Fail

Completing a sale of your business in today's market is a longer, more complicated and less certain process than ever before.

However it can still be very rewarding for sellers if they glean lessons from owners who have previously sold their companies.

There are many reasons why deals fail. Common reasons we see include:

- Unrealistic market valuations. An overpriced business, like a perfectly good but overpriced house, will sit on the market for so long that potential buyers will assume that something is wrong with it. If you are branded as having set an unrealistic value, it can drive away perfectly reasonable buyers because they don't want to go through the process of educating you, and it will be difficult if not impossible to get them back once they've walked away.
- Attempting to renegotiate the price or change the terms or meaning of terms after the initial agreement, effectively changing the deal. Be sure that you understand and are comfortable with both the price and the terms of the deal before you agree to them in the first place.
- Rigidity or arbitrary stubbornness about terms or struc-

ture. Buyers want sellers to be their partners going forward. They don't want to absorb all of the risk from day one, so they are very interested in earn-outs. A lot of owners initially aren't interested in earn-outs because they're leaving or being asked to leave and they feel they don't have any control over the earn-out, but buyers are saying, "If you don't believe in your business, how can I?" The reality today is that 99% of all transactions have an earn-out component. A buyer may say, "If we buy your business today for 100% cash, you've effectively shifted 100% of the risk overnight. Therefore, in terms of a risk:reward ratio, we're going to pay you much less." – perhaps below your perceived market value, so much so that you may not find the deal attractive. So they may say, "let's go forward together and share some of this risk. We'll give you 60% of the value we believe your business has in cash today and the remaining 40% over the next three years. If the business grows, you'll get more, and if it shrinks, then we both share in that shrinkage."

- Professional advisors attempting to function beyond their areas of expertise. Attorneys should protect you on legal aspects, financial advisors should give you tax advice and structure information, and the business advisor or M&A intermediary should advise you on the reasonableness of the offer, the terms and structure, etc. The M&A advisor is best suited to coordinating the disparate parts and professionals on both sides and affecting appropriate compromises.
- Landlords looking for a windfall. Typically, a buyer will want to take over the lease responsibilities of the seller. In most cases, the buyer's covenant is stronger than the seller's because it is a larger company, so from the landlord's perspective, he is getting a bigger, stronger, richer name added to the lease. It's reasonable for a landlord to charge a minimal amount for the administrative cost of affecting the change, but in some areas, depending on the real estate market at the time, landlords may ask for a \$5,000 or \$10,000 fee or an extension of the lease rather than a more appropriate \$50 to \$200.
- Not keeping bankers fully informed, particularly if they are owed money. They want to be sure they will be paid at the time of closing or whenever money changes hands. If the proceeds of the sale are insufficient to repay a bank, the banker will want to know how and when he will get the money owed. The loan agreement the owner signed when he took out the loan probably calls for him to advise the bank of any material change in the firm's assets

or stock, but many owners forget about this provision; the result is that the deal comes to a halt while the bank reviews the Purchase and Sale Agreement.

- Bottom-fishing buyers looking to steal a business. It's not worth the time or expense to try to negotiate with a buyer that makes an unrealistically low offer and will not increase it, if appropriate.
- Senior staff members holding an owner ransom. In a recent situation where an owner happened to hold the mortgage on an employee's house, the employee demanded that the owner pay off the \$186,000 mortgage to get the employee to go forward with the new company. That's an extreme example, but it's not unusual when an owner is insensitive to the effect of the sale on his employees. The seller has to remember that he is getting a lot of money from the deal, and senior employees in particular want to know what they're going to get out of it, such as a significant bonus in recognition of their role in helping to build the business or a stay bonus to help achieve an earn-out.
- Seller's spouse not committed to a deal. In many situations, the spouse (in the staffing industry, that's often the husband) is not very involved in the business and doesn't appreciate the mental and financial state that leads the owner to want to sell but instead urges the owner to "hang in there."
- Poor current financial results. One of the most important things knowledgeable M&A advisors do is present the seller's figures, no matter what they may be currently, in an acceptable and realistic form for the buyer to review. Nothing causes a buyer to lose confidence in a seller faster than inconsistent or unreliable numbers. Your results are what they are; if the worst is behind you, explain why.
- Unrealistic projections of future financial performance. Knowledgeable buyers are familiar with market conditions and aware of what reasonable future expectations should be for your business.
- Overly onerous sales, margin or profit levels required to achieve an earn-out. If there's an unrealistic earn-out, whether the seller will be there or not, and if for instance you have to increase the sales 40%, the margins 10% and the profit levels 15%, you're probably not going to make a lot of money on that. It would require exceptional off-the-chart performance to do so in this market. It will affect

CASE STUDIES

The examples that follow come from actual situations. Fortunately, they are avoidable for the most part.

The Greed Factor

Sometimes a seller is overly optimistic about his company's potential and begins to feel that he may be selling himself short on total consideration and the terms of payment. One seller under a Letter of Intent (LOI) became somewhat greedy during the buyer's due diligence process. At the time, the seller's sales were flat and he insisted that the closing be postponed to include another quarter of sales in the hope of enhancing the purchase price. We cautioned him about the possibility of losing his spot in the buyer's queue and the possibility, however remote it seemed at the time, that sales would remain flat.

But the seller was too optimistic. His sales fell, margins were squeezed and profits diminished significantly. Our ever-hopeful client said, "Let's wait another quarter." We know that a seller never wants to leave money on the table, and we caution against this as much as anything else, however it is often wise to play out the hand as dealt, because there is no assurance the next hand will be any better. In fact, this client's sales dropped again and he decided to go forward with the deal.

At this point, the buyer had a much bigger deal in its grasp and had put all other deals on hold. Our client became apprehensive because the terms the buyer had offered were so attractive that the offer was by far the best available to him. Now he had to wait for the

Continued on p. 10...

Continued from p. 9...

buyer to go forward.

Sadly, the client lost his priority in the buyer's queue. As the economy continued to weaken, more buyers decided to remain on the sidelines, and our seller had far fewer options than before. In the end, the client sold to the same buyer ten months after the last delay – for less cash, more stock and about the same total consideration, even though the seller's business was now up 20% over its earlier peak performance.

This owner was lucky to have averted a situation that could have had seriously deleterious effects on his family's financial security.

LESSON: Don't roll the dice when you have a good offer in hand.

Poor Advice from Professional Advisors

Sellers need professional advice. However the advice should be considered in view of the advisors' area of expertise. Attorneys should focus on legal issues and the legal meaning of the words contained in the agreement; the attorney's job is to protect the seller's legal interests.

Financial advisors and CPAs should focus on the financial and tax implications of the deal. Their job is to do whatever they legally can to lower the tax impact for the seller.

M&A advice is the responsibility of the intermediary hired to represent and counsel the seller on the merits of the transaction and to ensure that the price and terms are at market value or better and that the deal meets the stated objectives of the shareholders.

It is risky to accept advice, however well

Continued on p. 11...

the total value the you receives and your ability to compensate senior staff as you'd like to in order to encourage them to stay and help you achieve the objectives.

- Lack of attention to or ambivalence about the transaction. We commonly see this when the buyer's or seller's business starts to decline – the person is “away,” doesn't answer phone calls, etc. It's usually an indication of a more fundamental problem, resulting in inertia and delays, or the loss of the deal.
- Inexperienced buyers with poor internal communication. Many new buyers – private companies – don't have targeted M&A departments or business development departments focused on acquisitions. Consequently, the CEO, CFO and COO all may tend to have their hands in the process, looking at it from different aspects. This can result in a lack of coordination, with contradictory messages being sent to the sellers or their representatives, which creates confusion.
- Sellers' remorse, usually occurring just before the sale is completed.
- An inexperienced buyer trying to take all the risk out of a transaction.
- Unrealistic adjustments of certain expenses by the seller going forward. Typically, in addition to the cost of sales and SGA expenses, in M&A there's another section called adjustments. When we're adjusting earnings, that's when we see add-backs. An add-back is where the buyer determines what he would have to spend to replace the function the seller has eliminated. For example the seller may remove his own compensation and minimize his contributions to the business in an attempt to jack up the EBITDA, but the buyer will need to pay someone to perform those general management functions, so only the difference in cost should be adjusted.

Another seller may say he had a couple of top employees who were ineffective and actually cost the company money, but they've been fired, therefore that expense should be deleted going forward. That may or may not be realistic.

Or a seller may say he had a dot-com client go out of business, leaving him with a large amount of bad debt, but he's not going to deal with that kind of firm again so that expense should be deleted. If the firm's bad debts have been running at half a percent of sales, which is

about the industry average, and they shoot up in one year to 2% to 3% because of specific, identifiable customers that went out of business, then yes, there might be some justification for that add-back. But ordinarily, if the bad debt goes up to 0.75% or even 1%, how does the buyer know that's not just a lack of good internal controls on issuing credit?

The rule is: When adjusting your earnings, keep your add-backs of expenses realistic.

■ The Letter of Intent

Signing an LOI is an important initial commitment between a buyer and a seller. While LOI's are typically non-binding documents, they do form the basis of the Definitive Purchase Agreement, which, when executed, is a contract binding all parties to the agreement.

Some of the areas that an LOI addresses include the purchase price, the terms and structure of the transaction, and the currency to be used in the transaction.

There are only four types of currency that can be used in any transaction:

- Cash on closing.
- Notes – unconditional promises of payment at some time in the future, e.g., \$100,000 on the first anniversary and \$100,000 on the second anniversary, at 6% interest per annum. Regardless of whether the business goes to heck in a hand basket or skyrockets, the seller gets the predetermined amount.
- Stock.
- Earn-outs – contingent future payments, contingent on performance metrics that are determined at the time of the transaction. They may be based on generating a certain level of sales, gross margin dollars or bottom line profits over a period of years. If the agreed-upon level is achieved, the seller earns the amount specified during that period. In a typical earn-out the buyer might say, "If you generate the same gross margin dollars as you did in the first year after closing, I will pay you \$1 million. If you're 10% below that, I'll pay you 10% less."

Typically, the seller can get more or less than the stipulated amount. A buyer can say, "If the gain is less than 50% [or 75% or whatever the buyer has factored in], you get

Continued from p. 10...

meaning, from advisors trying to operate outside their primary area of expertise. A seller we dealt with decided, based on advice from three well-meaning but uninformed advisors, that his business was much more valuable than the market indicated.

These advisors were an attorney, a CPA and a relative with an MBA. All three wished only to help the seller; however, among them, they had participated in only a single business sale: that of a neighborhood florist shop to the owner's son-in-law. None had ever participated in the sale of a service firm.

At a scheduled meeting with the potential buyer, who had flown in specifically for the meeting, this trio descended on him like a ton of bricks. The original agenda, scheduled to explain the terms of the buyers' offer, was ignored while the advisors told the buyer why the seller's business was worth far more than he had offered. The seller's advisors used many colorful charts and graphs to justify their views. However, the presentation had nothing to do with the circumstances of the seller's business.

The buyer showed great restraint. Although offended by the new agenda, the buyer was an M&A veteran who stayed clearly focused on the big picture and listened patiently. Eventually the seller, upon understanding how close he had come to losing a great deal, took control of the situation, and the deal was completed.

LESSON: It is your responsibility to control your professional advisors and be sure that they understand that your objective is to complete the deal. Remember, "Experts advise, but owners decide."

nothing,” or he can cap the earn-out gain at 125%, but some just let it run according to the amount gained. A few years ago it was like a cliff; either you got the agreed-upon increase or you didn't, and you were paid or not as a result. In the last few years we've been able to convince buyers that it's to their advantage to use a graduated scale so as not to discourage sellers' initiative.

Other areas covered by the LOI are:

- A proposed closing date, or the maximum number of days until closing – typically 90 to 120 days.
- A description of what is to be acquired: stock (which is the entire company, lock, stock and barrel or some portion thereof) or (more commonly) selected assets, which may include the fixed assets used in the business, goodwill, customer lists and other items such as the balance sheet, current assets and current liabilities (including accounts receivable, current government remittances and taxes due, typically as of the closing date).

Usually, buyers don't take the cash or securities that belong to the owners and they won't take any of the owner's long-term bank debt. Some leave the balance sheet completely alone and just purchase the stream of earnings, i.e., the tools, equipment and materials required to generate sales and profits – customer lists, desks and chairs, phones and computers, etc. They're buying it as a going concern.

The type of corporation the seller is functioning under often dictates whether he wants to sell stock or assets. Most times buyers prefer to buy assets because there's less due diligence – they're not buying everything hook, line and sinker so they don't have to worry about the seller's unknown or undisclosed liabilities.

- A Confidentiality Clause, which will survive the LOI. Typically, a standard confidentiality clause or a non-disclosure agreement will indicate for a period of time, up to indefinitely, that any information the buyer learns as a result of the evaluation process will be used only for the purpose of making the investment or acquisition and not for market purposes. The seller agrees not to divulge the information to anybody, call on the seller's clients, try to hire the seller's employees, and vice versa. So even if the deal collapses at the LOI stage, there is still protection.
- An Exclusivity or No-Shop Provision forbidding the seller

or its representatives from discussing a possible transaction with anyone other than the (LOI) buyer until the agreement terminates.

- A No Public Announcement Clause in which both parties agree not to disclose any details about the transaction (unless required by law) until its conclusion.
- A Preservation of Business Clause in which the seller agrees to continue to conduct business in his accustomed manner and to use his best efforts to maintain customers, margins, staff and employees.
- An Expenses Clause indicating that each party will bear its own costs to complete the transaction.
- An Access Clause permitting the buyer reasonable access to the business premises and/or business information to assist in conducting due diligence. The term “Buyer” refers to the entire corporate entity, including accounting staff, audit people, some of its operational people, and sometimes outside auditors hired for the transaction. (The Big Five accounting firms do very well with private buyers because they coerce banks into making their reviews a necessary part of the lending process. The cost is absorbed by the buyer but is reflected in the pricing, as are M&A fees.)
- A Jurisdiction Clause indicating the location of the prevailing law under which the agreement is to be adjudicated, if necessary. Typically the location will be in the State/County/Province where the buyer is based.

Letters of Intent may address the following additional items:

- A list of assets/liabilities specifically included or excluded. Items included might be current accounts receivable (sometimes defined as “outstanding no more than 60 days”), items excluded might be paying off long-term bank debt. This only pertains to an asset deal; in a stock deal, you get the good, the bad and the ugly. In a stock deal there’s a benefit to the buyer because there’s usually equity on the balance sheet: retained earnings or surpluses in an S corporation that they call their “triple A (AAA) accounts.” In other words, if you were to pay off all of the liabilities and collect all of the assets, you would typically be left with a surplus of money. That’s an advantage to the buyer for all of their trouble, and sometimes it is reflected in the purchase price.
- A clause contingent on the buyer obtaining Employment Agreements and/or Non-Compete Agreements for key employees of the seller.

- Proposed employment terms for key personnel the buyer wishes to retain.
- Definitions of Gross Margin and/or EBITDA, if appropriate.
- Finally, given the investment of time and resources, some buyers may include a Break-Up Fee clause, in the event the seller decides not to go through with the deal, even though he signed the LOI with the intent of selling. The break-up fee can be a nominal amount or a more significant (punitive) amount ranging anywhere from \$10,000 to hundreds of thousands of dollars. It usually depends on the size of the transaction.

Many of these clauses are designed to clarify certain issues and items for both buyer and seller before they embark on a costly due diligence process. Buyers view an LOI as an inducement to them to expend the significant resources required to conduct due diligence and to prepare the many legal documents required to complete the transaction.

Typically, due diligence is a multi-part task. It should be conducted in a way that protects the seller from unnecessary or premature disclosure to his staff and limits the resources expended by both parties until the likelihood a deal is fairly certain.

A letter of intent is generally contingent upon the following terms and conditions:

- The signing of a Definitive Purchase Agreement containing the usual Representations and Warranties for agreements for transactions of this type. In the staffing industry, those representations and warranties might include: “To the best of your knowledge, all employees have been paid; all workers compensation claims settled; there are no outstanding liens or litigation against the business; the financial picture of the company is as it has been presented; and there has been no material change in the business, the customer base or the employee base since the LOI.”
- A satisfactory due diligence examination by the buyer.
- Approval of the transaction by the buyer’s board of directors.
- Sometimes, approval of satisfactory lending arrangements by the buyer, who may say the LOI, is subject to his obtaining satisfactory financing for the deal.
- Sometimes, satisfactory transfer or cancellation of leased premises.

At times a buyer will be content to begin negotiations with a Term Sheet. This is a less all-encompassing document that, as its name implies, purports to identify the key terms of the deal. It most often focuses on purchase price, terms and structure, currency to be used, and what is being purchased.

Term Sheets are most often used when a deal is expected to be very large and complex and the buyer wants to be sure there is agreement on the basic elements of the deal before drawing up an LOI. Perhaps surprisingly, if the opposite set of circumstances exists – that is, if a deal is expected to be very simple or imminent, some buyers will prepare a simple Term Sheet then go right to the Definitive Purchase Agreement. Often it is just a question of what makes sense for the proposed transaction.

As you can imagine, since there are no firm rules as to what comprises an LOI or a Term Sheet, the details provided in this document will depend on the individual seller and buyer.

At this stage, the Term Sheet or LOI is non-binding for both parties. But it is important to keep in mind that the document will be referred to and relied on in preparing the Purchase Agreement and other important documents. An LOI is always a compromise document that tries to balance the interests of both buyer and seller, and your wishes need to be heard. Be sure to negotiate or have your representatives negotiate to include all items of importance to you. Due diligence is a two-way street.

Settling basic terms is one of the most valuable aspects of the LOI. If you take issue with any of the items mentioned, this is the time to address it. If you can't agree at the LOI stage, proceed only if you can live with the issue as is. If an item is a deal breaker, it's best to cut your losses and move on. Selling your business is too important to leave to chance.

■ Continue to Mind the Store

The decision to sell your business is one of the most significant issues you can face, because the implications for you and your family can be extremely far-reaching. Since most of us only do this once in a lifetime, it's important to do it right. And in the present economic environment, it is particularly important to continue to manage your business aggressively until the transaction closes and beyond.

Many elements go into making a solid deal. These include price, terms, deal structure; strategic and cultural fit; future career opportunities for you and your staff; negotiating a Letter of Intent, Employment, Non-compete, Purchase and Sale Agreements and many other issues. However, the focus here is on what happens to the business from the time you decide to

put your company on the market until the sale has been consummated.

The selling process is a precarious time for your business. It is riskiest after you have executed an LOI because, at that point, many owners feel that, for all intents and purposes, they have sold the business and merely need to wait for the buyer to conduct due diligence and for the respective legal advisors to word-smith the various agreements. In many cases, the seller has moved on mentally and is thinking about the post-sale future. As a result, the business can suffer, and the deal can fall through.

During this past year, we have seen firms sign an LOI only to find their sales declining dramatically. This cannot be attributed simply to owners neglecting their marketing; it has been a very challenging market for many staffing and professional services firms. However, the post-LOI period is a critical time for owners to re-double their sales efforts so buyers are not frightened off by declining sales, lower margins or lower operating profits. Both buyer and seller negotiate the price and terms of the LOI. Even though that may have been negotiated under earlier, possibly better market conditions, it is still the seller's responsibility to do his best to maintain the business in the same or improved condition.

For many years, staffing firms' metrics often improved after the initial valuation, and sellers wanted to re-price the deal to reflect this increase in value. Now the tables are turned a bit. Buyers are concerned that downward trends may continue and they fear seriously overpaying for a firm that no longer appears to offer market value comparable to similar firms. Sometimes these concerns slow the transaction process to a crawl, with both sides wanting to see better results before moving ahead.

In spite of continual reminders that "a deal is not done until it's done," and that it isn't done until all the necessary documents are signed and the purchaser's funds have been wired successfully to the seller's bank account, an owner may forget to tend to the business as closely as he did when he was building it. As a result, sales drop, margins slip, and the pipeline for new business dries up at the very time the buyer most needs to take care of his business.

It is essential that you, the seller, continue to oversee your business properly because:

- You still own it, and you may continue to own it beyond the planned closing date.
- A buyer will get jittery if business is slipping, which will become apparent during due diligence.
- Most purchases today have an earn-out as a significant

part of the transaction terms. You don't want to put yourself behind the eight ball and leave money that you deserve on the table.

- Staff will become demoralized if they sense that you've already "checked out."
- Declining performance may lead to a reduction in the offer price.
- If you lose the current buyer for any reason, you'll have to begin the selling process all over again.
- It's just good business, and it's still your business.

■ Successful Strategies

Many business owners are very disciplined and diligent about watching their metrics while they are building their business. In fact, it is generally because they have been taking care of business that their company is an attractive acquisition target for buyers.

Selling a business generally takes several months from beginning to end. Use this time to your advantage. Don't stop doing all those little things that have made your business a success for so many years. Maintain your focus. It will pay off for you.

If you plan to sell in the near future, start now to:

- Evaluate the performance of each staff member and stay close to your key employees, re-recruiting them to ensure that they are comfortable and committed to your business. This is a time of great vulnerability for your staff. They are concerned that things are going on that they are not privy to or haven't any control over. The stronger they are, the faster they will seek out alternatives if you are unable to reassure them about their future. Strong performers always have more options and opportunities than weaker or less experienced staff.
- Weed out poor performers and malcontents. This is something we tend to feel we do all the time, but there may be room for improvement. Poor performers can lower the standard for an entire office. Malcontents are at best a distraction and at worst a cancer eating away at your firm's morale and productivity.
- Determine whether you can increase sales by enhanced selling, advertising or recruiting efforts, and then do so. The old maxim about not cutting back in tough times on items or practices that can improve your business is sound, provided you will benefit through an increase in orders or candidates.

- Evaluate the profitability of each client's effect on your margins, wear and tear on internal staff, timeliness of payment and other costs of maintaining that client. Not all clients are created equal. Some large-volume accounts are poorly supervised and offer limited feedback on your workers. Others can demand far too much of your staff's time, particularly those who offer only short-term assignments that require frequent dispatching calls. Some clients pay faster than others. Some have lower margins. These areas are all worth examining.
- Increase margins where possible, particularly if you have differentiated your firm through added value, better service and by staying close to your customer. If you are delivering Rolls Royce service, you can't stay in business if clients are only willing to pay Chevy prices. Determine who you are and what segment of the market you are geared to serve. If your staff is accustomed to providing a high level of service, they will continue to do so even if you lower your prices to match a competitor or a customer's demand. Although doing so may be good for your reputation, it can be bad for your bottom line.
- Broaden your customer base when practical to reduce or eliminate your dependence on only a few accounts. Ideally, you want to work toward having no client represent more than 10% of your annual volume.
- Monitor credit and collections closely. This area is often overlooked during the pre-closing phase of a sale. Continue to focus on credit and collections. It's your money!
- Review all non-essential expenses and deciding which ones you can eliminate without adversely affecting business performance. Don't ignore long-term payoffs, particularly if you may decide to retain the business, but if you don't have to make an expenditure and it won't give you a return within 12 months, you will probably lose most of the resources you invest.
- Clear up any outstanding legal or insurance matters. Buyers are often concerned with outstanding legal matters because of their potential for distraction from business. Clear your books as much as you can.
- Maintain advertising and promotional activities when possible. You will benefit both short- and long-term. If you curtail these activities, you may find yourself trying to achieve your earn-out objectives from a standing start. Maintain momentum in your programs; just don't go overboard.

- Maintain up-to-date and clean books. You will rely on your financial reporting process for critical business performance information during the selling process. It's vitally important to make certain that your numbers are reliable, timely and credible.

While much of this advice seems like normal everyday good business, continuing these practices during the excitement and euphoria of selling your business can be a challenge. The issue isn't knowing what to do; it's doing it, and it's all in your capable hands.

r.a.cohen consulting
M & A experience when you need it most.

1827 Pembroke Jones Drive • Wilmington, NC 28405
(910) 509-0691 • Fax: (910) 509-0692