Selling your business

What you need to know

The **independent, entrepreneurial approach to deal making**

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Introduction

- This guide provides answers to some of the key questions which should be considered when selling a business. It also sets out the main steps in a sale process and highlights some of the common issues which can arise.
- Whilst this guide sets out a typical sale process, every business is different and each sale process should be tailored to the specific requirements of the vendors and the market in which the business operates.
- A sale process is typically time consuming and complex, and can be an emotional rollercoaster. During the process it is critical that the business itself continues to perform well, and as such it is important to receive advice from experienced professionals in order to help you spread the burden and provide an independent perspective.
- Momentum has an excellent track record of successfully selling businesses through running well prepared and well controlled processes, allowing management to focus on doing what they do best – running the business.

Why are companies sold?

There are a number of factors which can trigger a company sale:

Owner retirement

A business owner looking to retire, but with no clear plan for succession, may wish to sell in order to realise the value in the company that they have built.

Private equity exit

After investing in a management buyout, or providing development capital, a private equity institution will generally seek to realise capital gain within three to five years.

Disposal of a non-core operation

As businesses grow and develop, certain areas can become "non-core", diverting management time and resources away from the main strategic direction of the business. The sale of a non-core business allows management to focus the group strategy and allows capital to be redeployed or released back to shareholders.

Unsolicited offer

A growing, successful business will often receive unsolicited offers from a range of trade and financial purchasers, triggering a shareholder discussion around exit.

Shareholder conflict

In a business where shareholders' objectives or views conflict with one another, the best solution could possibly be to sell the business so that all shareholders can use their capital as they wish, or for one or more of the shareholders to be bought out.

Expansion and investment required

A growing business may reach the point where it needs the support and investment from a larger group or funder to provide the expertise, knowledge and resources to fully exploit its opportunities.

Financial distress

External factors may cause fundamentally sound businesses to undergo periods of financial stress if the current shareholders do not have sufficient flexibility of capital resources to see the business through these periods. The sale of the business may represent the best solution for the shareholders, employees and customers.

What is important to a vendor?

Every vendor will have their own set of objectives when selling their business. Below is a list of the more common factors that are important to a vendor when considering the sale of their business:

Which of these are important to you?

- **Sale proceeds**
- **Commercial conditions of the deal**
- **Timing**
- **Partial sale or full disposal**
- **Loyalty to employees**
- **Shareholder agendas**
- **Differing management aspirations**
- **Future direction of the business**

A good corporate finance adviser will ensure that your objectives are met, whilst protecting your interests, preventing any damage to the ongoing business and managing the timing of the deal.

When is the right time to sell?

The ideal time to sell a company is when it can demonstrate the following attributes:

Successful track record	The historical financial performance of the business is a significant factor in determining an acquirer's valuation of the business. It is considerably easier for a company with a consistent track record to justify its future growth prospects.
Good future prospects	An acquirer is buying the business for its future prospects and the cash and profits that the business will generate. In addition the level of visibility of profits is usually an important factor. Securing a major contract is often an ideal springboard from which to launch a sale process.
Management Team	Regardless of whether the shareholders will remain in the business, the quality of the management team is nearly always important. They will often have an important part to play in the process (e.g. helping to answer the majority of questions during the due diligence process) as well as potentially being required to run the business after the transaction.
Purchaser landscape	Premium prices are typically paid when there is strong competition between purchasers to acquire the business. As such careful positioning of the company to maximise the number of seriously interested parties is an important part of the pre-sale preparation.

The most successful disposals result from **positioning a business in the right place at the right time**

What are the exit alternatives?

There are a number of ways for owners to exit their businesses:

Trade sale	The business is sold to an existing trade purchaser either in the same market or a buyer who wishes to enter the market.
Financial institution purchase	A private equity house or bank purchases the business, usually backing existing (MBO) or new (MBI) management, typically with a view to selling the business in 3-5 years.
Cash out or recapitalisation	The owner takes out part of their equity but retains an on-going stake in the business often alongside management, funded by a bank or private equity house.
Flotation (IPO)	Some or all of the owners value is floated on a UK or overseas public market. This is typically a less clear exit route as management will be expected to continue and potentially to invest, and existing shareholders are often subject to "lock in" periods during which they are not able to sell shares in the listed business and hence realise cash.

In deciding on the best exit strategy for a particular owner it is **essential to identify what the shareholders are trying to achieve**.

Other considerations

Other considerations include:

Partial sale vs. full disposal?

A partial sale would be attractive to an owner looking to realise some of the value of their business without giving up control. A partial sale typically involves selling a minority stake but could involve disposing of a division or selling a subsidiary. A full disposal attracts a control premium from acquirers.

Sale of assets vs. shares?

The vendor can dispose of either assets or shares. The tax treatment of the two options differs and this has to be considered carefully, with the help of a tax adviser. The acquirer may also have a strong preference for buying either assets or shares and some flexibility may therefore be needed in order to satisfy both parties.

How to sell: auction vs. preferred bidder?

Typically an auction process involving several bidders will elicit a higher offer than dealing with a single preferred bidder. Vendors may have other non-value considerations (confidentiality, future investment, time scales) which a single bidder may be able to accommodate whilst still meeting value criteria. In addition, an acquirer may actually be prepared to pay a strategic premium simply to avoid the business being auctioned.

What does the sale process look like?

1. Preparation / grooming for sale
2. Strategy and packaging
3. Marketing
4. Evaluation of offers
5. Due diligence
6. Completion

Months/ potentially years

4-6 months

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Stage 1 – Preparation / grooming for sale

1. Preparation / grooming for sale
2. Strategy and packaging
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- The objective of this stage is to ensure that the business is optimally positioned for sale, and that any key issues that could affect value are addressed well in advance, e.g. property considerations, environmental issues, pensions or employees.
- It is also important to consider the vendors objectives with regard to:
  - Valuation
  - Structure
  - Timing
- This is also an ideal stage to:
  - Review management structure and the strength of second tier management.
  - Perform tax planning.
  - Conduct research and evaluation of potential purchasers.

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Stage 2 – Strategy and packaging

1. Preparation / grooming for sale
2. **Strategy and packaging**
3. Marketing
4. Evaluation of offers
5. Due diligence
6. Completion

- Refine potential purchasers list, considering the following:
  - How many purchasers to be approached.
  - Whether financial buyers should also be approached.
- Prepare Confidential Information Memorandum and related marketing materials.
- Finalise contact strategy for each potential purchaser, to ensure that each approach is tailored to generate the maximum possible interest.

Stage 3 - Marketing

1 Preparation / grooming for sale

2 Strategy and packaging

3 **Marketing**

4 Evaluation of offers

5 Due diligence

6 Completion

- Make contact with potential purchasers.
- Put Confidentiality Agreements in place.
- Information Memorandum sent to purchasers.
- It is important that a competitive bidding environment is created at this stage. Competitive tension is the key to maximising price and keeping the process running to timetable.
- Receipt of indicative offers in writing.

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Stage 4 – Evaluation of offers

1. Preparation / grooming for sale
2. Strategy and packaging
3. Marketing
4. **Evaluation of offers**
5. Due diligence
6. Completion

- Indicative offers typically take the following form:
  - Price to be paid
  - Form of consideration
  - Method of funding the transaction
  - Details of any deferred consideration
  - Approach to due diligence (what due diligence will be required - financial, commercial, environmental, other)
  - Timetable to completion
  - Any conditions attaching to the offer, e.g. shareholder approvals required
- A number of potential purchasers will be then be invited into a second round to meet the management team before submitting final offers.

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Stage 5 – Due diligence

1 Preparation / grooming for sale

2 Strategy and packaging

3 Marketing

4 Evaluation of offers

5 **Due diligence**

6 Completion

- Following the receipt of final offers a preferred purchaser will be selected to enter a period of exclusivity where they will conduct due diligence.
- The preferred purchaser will typically appoint a number of professional firms to undertake due diligence on the business being sold. Due diligence may take many forms and will depend on the business. Common types of due diligence include:
  - Financial (including taxation)
  - Commercial
  - Legal (including pensions)
  - Environmental
  - Management and employees
- Your financial advisers will coordinate this due diligence process to ensure that it runs as smoothly as possible and minimises, as far as possible, management time and effort.

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Stage 6 - Completion

1 Preparation / grooming for sale

2 Strategy and packaging

3 Marketing

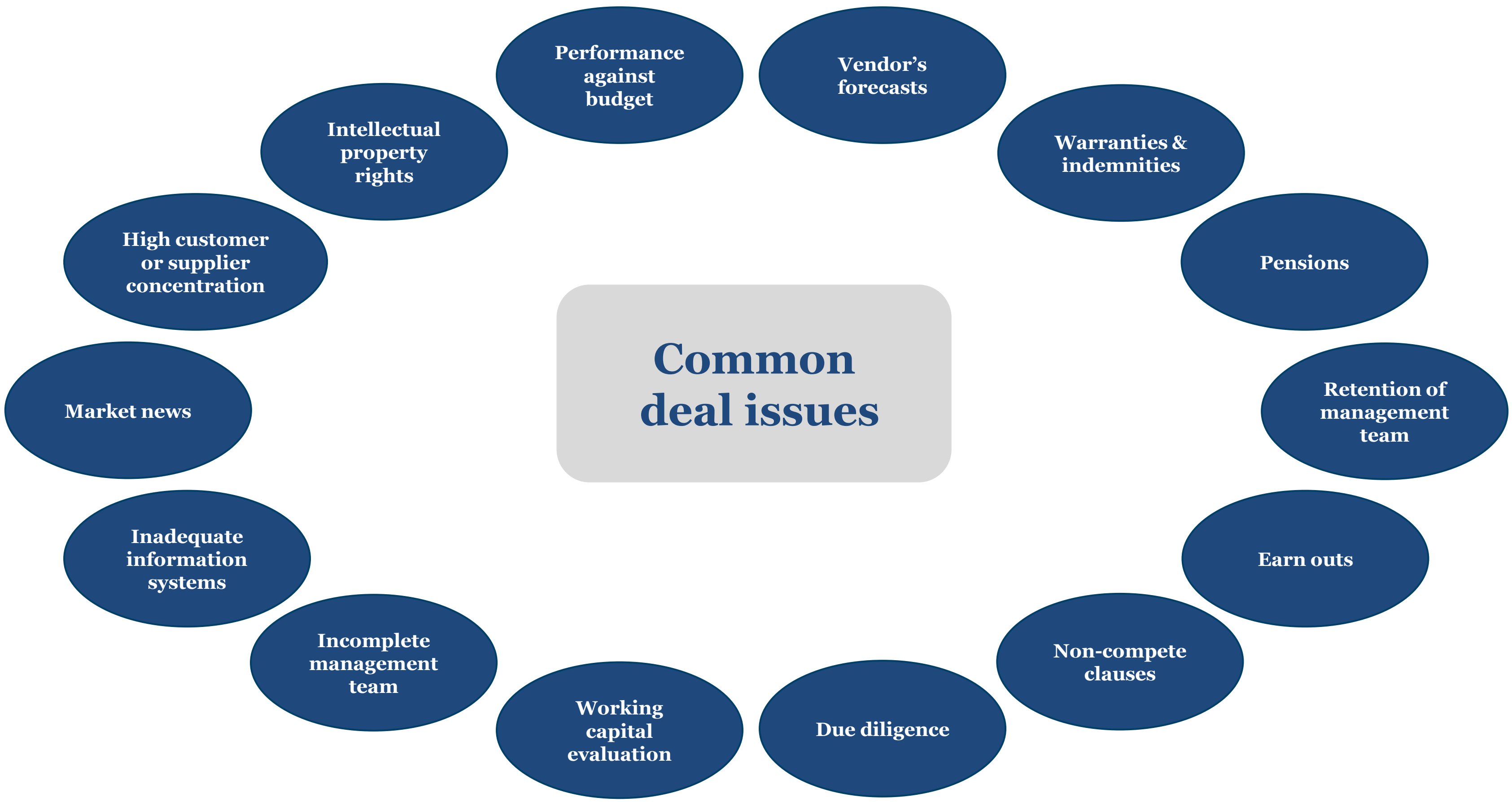
4 Evaluation of offers

5 Due diligence

6 Completion

- The key legal documents will be drafted and negotiated by your legal advisers. Your financial advisor will be involved in the negotiation of the commercial aspects of these documents.
- The principal legal document for the vendor is the Sale and Purchase Agreement ("SPA"). The key points for negotiation in the SPA often centre around the nature and extent of the warranties and indemnities to be provided by the sellers to the purchaser, completion accounts or locked box mechanism, deferred consideration clauses and non-compete clauses.
- Another important legal document is the Disclosure Letter in which the vendor discloses certain matters to acquirers which then cannot be considered in any warranty dispute.

What are the typical deal issues?



These are just some of the issues which typically arise in the sale of a business. A well planned process and **a good team of professional advisers will identify and deal with these issues before they cause significant problems**.

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The role of the financial adviser

The financial adviser (also known as the lead adviser) typically takes the coordinating and advisory role for the entire transaction. Whilst this will include specific advice on the financial aspects of the transaction, the role is typically much broader and will include advice on the wider commercial aspects of the deal and also coordination of the other professionals working on the deal.

Some of the specific aspects of the role include:

- Understanding the objectives of the shareholders and other significant stakeholders
- Identification of potential deal issues and creation of strategy for resolving them
- Assistance with grooming the business for sale
- In-depth research of potential purchasers
- Preparation of succinct and powerful marketing materials (potentially including an Information Memorandum)
- Negotiating and structuring the deal
- Project management of the entire deal process

The role can be summed up as making sure that:

- The right deal is secured for the vendor; and
- It happens on time

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