How to Sell a Business for Maximum Profit

When selling anything, it is important to focus more on the motivations of the buyer than those of you the seller. When selling your business you need to imagine what potential buyers might want to gain from an acquisition and make sure you give them what they want. We investigate this further in another article entitled *"Selling a Business; What Influences Your Prospect's Decision to Buy?"* and this is a part of what helps in maximising your profit gained from selling you business.

One of the key features of an M&A deal is the valuation process. One of the most common approaches is to offer a price based on a multiple of one of the key financial facts such as revenue, earnings before interest and tax (EBIT) or earnings before interest, tax, depreciation and amortisations (EBITDA).

Valuations based on revenue are not generally popular as revenue is only a measure of volume of business rather than the quality of the business as demonstrated by the earnings. You do of course have influence over the amount of earnings and this should be a key focus when preparing your company for sale, so here we will focus on earnings based valuations.

Whatever industry you are involved in there will be accepted norms, which may change over time, relating to the valuation multiples that will be used by prospective buyers. For example, a company in the IT sector which owns its own products could receive offers of 7-10 times earnings. A similar company without products but providing a people based service will attract a lower valuation of say 4-6 times earnings.

You also need to consider what is called the "quality of earnings". Consider two identical companies; the first has revenue of £10m and earnings of £1m (10%) and the second has revenue of £5m and earning of £1m (20%). The two companies will apparently attract the same valuation as they have exactly the same amount of earnings. However, the second company will be judged as being more valuable because a level of earnings at 20% effectively doubles the return on the investment required to complete the acquisition. The first company might be valued at 4 times earnings while the second might attract 5, 6 or even 7 times earnings.

With absolute earnings and the quality of earnings being so important to valuation, you need to do everything you can to genuinely and legitimately increase earnings. There is no point removing staff members from the payroll to increase earnings if those employees are crucial to the business. When the time comes to undertake due diligence, the buyer will quickly spot a change of this nature and trust, so critical to a successful transaction, will have been damaged.

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An ideal situation is that you give yourself 12-18 months to prepare/groom the company for sale. Part of the preparation will involve removing all unnecessary costs and demonstrating that the company can run effectively on the new cost base. When presenting your company for sale at the end of this 12-18 month period, you will be able to present the figures for a complete business year showing that it works with the lower cost base.

One area of "unnecessary cost" could involve the money paid by the principals to themselves and possibly to family members. I know a case where the wife of the main shareholder works in the business doing a job that would attract a salary of £20,000 for a "normal" employee but she receives £100,000 plus bonuses and a car fully expensed by the company. The company also pays for a gardener and a domestic cleaner for the home. In this scenario, you are paying something like £100,000 more than you, or an acquirer, would need to spend if the company was operating with normal employees. On a valuation of 5 times this will cost you £500,000 off the sale price! So clean up the finances before you start the sale process.

In addition to financial matters some other things to consider when preparing your company for sale are:

- Ensure the management team is strong enough for the selling process and transition to the new owner following completion.
- Straighten out all your company records
- Get audited statements from a respected firm
- Make sure all contracts and agreements are sound with; shareholders, employees, customers and suppliers. Also make sure product licenses are sound.
- Confront issues e.g. underfunded pension, labour disputes, pending legal proceedings and deal with them or prepare to disclose them to the buyer before the deal goes too far.

In summary, pretend you are doing the buying and make sure the buyer will see what you would want to see.

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