Preparing Your Company for Investors or a Sale

by David T. Thibodeau

The past 18 months have been tremendous for acquisitions in the health and nutrition sector. The most recent sale of Schiff Nutrition to Reckitt Benckiser (announced in December 2012) was nothing short of astonishing and, up to now, the pinnacle of an exciting and lucrative merger and acquisition (M&A) cycle.

You, like many others in our industry, were sipping eggnog during the holiday wondering, "Is this the time to bring in investment capital, or perhaps take some chips off the table and maybe even sell my company outright or merge with another?" I offer a note of caution in all of this euphoria. At this point in the M&A cycle, both owners and buyers/investors can get overzealous, with owners thinking their company should be valued at the same multiples as the most notable transactions, and buyers/investors thinking if they don't jump in now, they will miss the opportunity.

Take advantage of the cycle, but do not tie your valuation expectations to blockbuster transactions. You can improve your opportunity to get the most value for your company by being prepared for the process.

First impressions are critical for the management team, employees, operations, physical plant, legal/regulatory issues and, especially, financials. Step back and take a critical look at each of these areas like it's the first time you are seeing them and/or seeing them through the eyes of another. Having an outside advisor guide you through this process can be beneficial.

Pick the Internal Team Carefully

The transaction process can be arduous and time consuming. A team captain from management can coordinate the process both internally and with external advisors. Although it would be preferable for this person to have transaction experience, most often companies (particularly smaller companies) do not have that type of experience on-staff. Oftentimes, it is the president or CFO who runs the process internally. In all cases, it should be someone with good knowledge of all aspects of the business.

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Pick the External Team Even More Carefully

A good "deal" lawyer and an experienced financial advisor usually mean the difference between getting a deal done or not. Your college buddy who is a real estate lawyer is not the right guy. Significant nuisances are inherent in investment agreements, purchase and sale documents or merger agreements; if not negotiated properly, these details can lead to significant liability on the seller's part. A good "deal" lawyer knows where to push and when to step back. The key is to minimize seller risk, but in reality, the risk is there.

Corporate Document Housekeeping

In the day-to-day demands of our business, good corporate document housekeeping can suffer. The time to become aware of any potential issues is not when the potential buyer's army of advisors is combing through every contract. Get organized upfront. If documents are missing, incomplete or disorganized, the potential buyer/investor goes on high alert and will scrutinize everything even more thoroughly.

Present Clear, Concise Financial Statements

Presenting financial statements in a transaction/due-diligence process is like peeling back an onion. You start by supplying summary financials for the last three to five years, and summary forecasts for the next five years. As a buyer/investor moves deeper into the process, they will want much more detail. Organize corporate documents upfront, and make sure all key/appropriate management team members are on the same page to explain both positive and negative variances.

Many companies in our space are owner-operated and either Subchapter S Corps or LLCs. Oftentimes, certain owner expenses run through the company that may be legal from a tax standpoint, but are not typical in a "professionally" managed company. It is to your advantage to identify all of these expenses and present an "adjusted" income or EBITDA. I caution you to be realistic on add-backs, particularly in the area of salaries adjusted to market rates, not below. You and your advisors will have to defend each add-back, and if they are not reasonable, you will lose their value and another degree of buyer confidence in your company.

Identify Potential Value Detractors, Red Flags or Deal-Killers

This is an important exercise that many companies don't go through prior to inviting a potential buyer/investor to scrutinize one's business. The time to discuss internally and to agree on a game plan is before a buyer/investor comes in. Along with appropriate advisors, bankers, lawyers, accountants and the management team, look at your business critically and identify the issues. This is not a time to be timid. Of course, many other components are involved in a transaction. However, these five tips will get you well on your way. Remember, prepare, prepare and prepare, and you will be rewarded with a higher valuation and a smoother process. ■

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