Exiting on top

How to take advantage of the accelerating M&A market

PETER J. SMITH
Member
Semanoff Ormsby Greenberg & Torchia, LLC

(215) 887-4132
psmith@sogtlaw.com

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As the M&A market for small businesses continues to recover after the recession, now is the time for potential sellers to begin planning. After all, business owners who sell their business without a well-defined exit plan typically sell for too little.

"To maximize value, minimize cost and make for an efficient sale, the business owner must seriously review legal, financial and business operations before going to market," says Peter J. Smith, a member at Semanoff Ormsby Greenberg & Torchia, LLC. "Your lawyer, accountant and/or a good business consultant can help with this evaluation."

Smart Business spoke with Smith about the M&A market and how to create an effective exit plan strategy.

What are some indicators that the M&A market is heating up?

BizBuySell.com reports that sales of small businesses have for the first time reached pre-recession levels. We've seen this in our own practice as well with increased deal flow and increased multiples.

What is driving the increase?

A variety of factors: improving small business performance, increased capital availability, more add-on acquisitions for venture capital portfolio companies, more sellers who waited out the post-recession recovery in order to regain lost value, and more buyers willing to take on debt and risk to grow.

Currently, there are many potential sellers in the market with viable businesses. Many restructured during the recession, so expenses were reduced and their EBITDA and profits have now increased. At the same time, banks have relaxed underwriting criteria and are more willing to finance buyers who are interested in making strategic acquisitions. Finally, there is a lot of pent-up demand, both among small businesses that see acquisition as a way to grow, and venture capital firms that are looking to expand their holdings through add-on acquisitions that provide synergy with their existing portfolio.

According to a BizBuySell.com survey of brokers, the strong M&A market is expected to continue throughout 2014 and we see nothing on the horizon that should cause a decline in deal activity.

What should potential sellers be thinking about in this market?

They should be thinking about exit planning — How can I position my business for maximum value and a clean, quick sale? They should be reviewing their entire company from the perspective of a buyer. This is not how most business people usually view their companies.

What are some examples of things to consider when exit planning?

Among other things, the business owner should ask:

- Are financial systems and controls in place and adequate? Are financial statements presentable and in accordance with standard accounting principles? The business owner should consider having the financial statements reviewed or audited, if they are not already.
- Can the business owner identify the best ways to increase EBIDTA? This is the biggest driver of value in your business.
- Are employment agreements in place for key employees? Do all sales employees have non-competes?
- Do key customers and vendors have contracts? Is there any guarantee of recurring revenue?
- Does the business have title to all of its assets? Can it prove this in writing?
- Does the company have title to all of its intellectual property? Without contracts, this is unclear.
- Are all key contracts assignable? The business owner should know who can hold up their deal.
- Is the business qualified in all states in which it does business? Has it filed tax returns in all of the appropriate states?

How far in advance of an anticipated sale should exit planning occur?

The longer the lead time the better. Planning should occur at least a year in advance of going to market. Ideally, it would be two to three years before a sale as it's important to have the financial statements and tax returns in place as part of due diligence. ●