



The Exit Strategies Newsletter

The Two (2) Necessary Elements to Any Business Transfer

Owners who start to think about exiting their business often fancy the idea that someone else will certainly want to own their company after them. These owners look at the struggles that they faced to get the business up and running relative to the stability and lifestyle that they are living today. The natural thought that crosses these owner's minds is that another person or company would surely want to have ownership of this now stable business and gain access to the cash flow and opportunities that it presents. To these owners, we want to share the two (2) critical elements that are necessary components of any business transfer. Those two (2) elements are (1) someone who really wants to sell/exit the business, and (2) someone who really wants to buy / own the business after you. So, this newsletter examines these two (2) critical issues and what owners can understand to help make for a more successful transaction.

Why These Two (2) Elements Are Required

The reality of business exits is that there is a tremendous amount of complexity involved. History shows that in order to make it through these challenging levels of complexity there really needs to be two (2) highly motivated parties, one seller and one buyer. At the end of the day, negotiations

will center around what the future may or may not bring to the next owner. Many potential transactions fall apart at this stage in the transition. Therefore, it is often said that a 'good deal is struck when each party is equally unhappy with the final outcome'. In this context it is important to see that without some motivation pushing both the seller and the buyer, it becomes all too easy for either party to walk away from the negotiations that surround these transactions.

The Owner's / Seller's Mindset

As stated earlier, an owner will often believe that ownership of his business would be desirable to a number of potential buyers. For that reason, the owner feels as though he / she has a lot of leverage in the initial phase of the exit process. Many owners approach the potential transaction with a feeling that they need to negotiate from a position of strength in order to get the optimal result and showing any kind of weakness as to wanting or needing to sell will reduce their standing in the negotiations. There is a bit of truth to all of this.

However, the owner who does not truly understand why they are motivated to sell is likely to take too hard a line in the negotiations and resort to the notion that they are perfectly fine with life as it is and will reject the buyer's advances, creating a failed transaction. The owner who does not

really want to sell or exit is likely to not go the distance with the negotiations because they are not clear on why they are looking to transition ownership in the business to someone else.

Alternatively, the seller may hold out in the negotiations because they have an inflated expectation of the value of their business. In fact, this is the primary reason why most business exits fail. Therefore, if you know why you want to exit and you are committed to the process, it is really good idea to incorporate a realistic range of values in your exit planning process to avoid this trap.

The Buyer's Mindset

Now let's take a look at the buyer of a business. From the buyer's perspective, they don't know what they are going to find when they look to acquire a privately-held business. There are just as many risks in what they don't know about the business as there are in what they do know. Now, even though many of these risks can be mitigated through the legal agreements that are signed, the reality is that a buyer wants to see a 'clean' transaction because they are going to invest a tremendous amount of their resources into making a successful acquisition.

If the buyer is not ready to navigate the unknown and work with the exiting owner to understand all aspects of the business, then they too are likely to back away from the process midstream. Buyers need to want to own your business and you need to understand their motivations for doing so. You see, it's not just about the cash flow. Buyers have endless other motivations for wanting to purchase and own your business into the future. If you do not know why they are interested in owning your business as well as their level of commitment to the

process, then you need to dig further. You see, one of the most damaging things that can happen to a seller is that a buyer backs away at the last minute for unknown reasons. At these later stages in a transaction, the seller asks other buyers to go away as a transaction is pursued with your chosen buyer. Having that buyer back out of the process because they are not committed can have very negative consequences not only to the immediate transaction but, potentially to future transactions as well.

Determining the Motives of the Players

So, how do buyers know that an owner is ready to exit and how do owners know that buyers are committed to the process?

Well, an owner who has spent a few years preparing for the transaction demonstrates an intention to see the transaction go through smoothly. That owner has evaluated why they want to sell, what selling price is required for their lifestyle, whether that selling price is reasonable, and what they are going to do next. The company is ready for a new owner and the evidence is clear when a buyer arrives – we call this the 'exit planning process' and it improves the confidence that buyers have in the seller's motives and overall preparedness for the transaction.

So, how do sellers know that a buyer is truly interested in owning their business? Well, this one can be a bit more difficult because buyers will not always share all of their reasons. After all, if they really see that they can do more with your business than you can and they share all of it with you, then you may just try to do it yourself. Instead, a fall-back position may be to ask to interview other companies that the buyer has purchased to find out from the other exiting

owners how the process was handled. By interviewing the owners who have already exited you're likely to get an honest accounting of how your buyer conducts themselves through the process.

Concluding Thoughts

Having a seller who wants to exit and a buyer who wants to come into ownership really are two (2) critical elements of any transaction. Understanding the motivations of the buyer of your company will help you build your confidence not only in their ability and willingness to complete your transaction, but also in the future of your company in your new owner's hands.

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