FEBRUARY 2021 NEWSLETTER FOR BUYING OR SELLING BUSINESSES

THIS MONTH

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TRENDS AND OBSERVATIONS UPDATE

In the course of marketing a successful retail business, I noted an interesting trend – skilled professionals from Alberta looking to flee the Province and buy a business in the east, especially Ontario.

I interacted with engineers, accounting partners and other business owners all looking to avoid what they fear is a long term decline in the fortunes of Alberta. I hope this is not the case but it is certainly an opportunity for Ontario businesses.

It is impossible to open a newspaper or turn on a TV without hearing about COVID-19 but there is an abundance of qualified buyers in the market, and it is a great time to sell a business. In many sectors this demand is raising sale multiples noticeably. A surprise to me was the number of buyers who were open to multiple types of industries and business sectors – as long as the company was good, they were interested.

I have been helping an immigrant from India working as an engineer in Ontario, but anxious to buy a business, despite only having not received a Permanent Resident Card yet. There are lots of entrepreneurial immigrants choosing Ontario, great for us!

If you wish to sell your business and you or your name is viewed as the key to the business, be prepared to stay aboard for awhile during a transitional period. The most contentious negotiating item is often Seller tenure.

DEALING WITH WORKING CAPITAL IN A SALE

Working capital is the sum of your liquid assets (normally cash, receivables and inventory) and current liabilities (accounts payable).

First thing is to review these items and make sure :

- Only collectable receivables included
- Only non-obsolete or saleable inventory is included
- There are no undisclosed contingent or unrecorded liabilities

Once these accounts are normalized, we can see how much of the business value lies in working capital. The buyer will want as much as possible and the seller wants to give as little as possible.

If the business has solid cash flows and revenue numbers it will be easier to justify less working capital. One way to look at this, the buyer, after closing the purchase does not want to have to inject additional cash right away, that is just an addition to the purchase price that the buyer agreed to pay.

It is helpful to look at the business and how it generates working capital. After purchase there should be enough working capital so that the business continues to run smoothly, generating sufficient working capital to not require injections.

Each company will vary in this regard, some have very little working capital, and a great deal of goodwill. We will discuss goodwill in a later article.

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FEBRUARY 2021 NEWSLETTER FOR BUSINESS OWNERS OR BUYERS

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BUYING OR SELLING? CHOOSING YOUR TEAM

As an intermediary, or one who brokers a sale of a business, I would like to think I am indispensable, but that is not always the case. Depending on the circumstances, the seller may elect to use their lawyer, accountant or other resource to sell their business. Last year I has a client who decided that selling off inventory through industry channels was the most efficient approach.

In addition to an intermediary, there are other team members who can be critical to your success :

Accountants and bookkeepers – both are critical, and will help you generate the best quality disclosure possible. Make sure they know about the sale and enlist them to clean up your books and reporting package. If financials are critical and the company valuation is over $1,000,000 consider upgrading from Notice to a Review engagement.

Lawyers – make sure they have M&A experience and have the resources to respond in a timely manner when needed. I have worked on files with sole practitioners who, while fully competent to do the work, were tied up in court for days on estate and other general legal matters and could not respond to urgent matters properly.

Tax advice – Often wrapped up in accounting services but sometimes is an added resource – one example is a company with U.S. operations : My good friends at U.S. Tax IQ (www.ustaxiq.com) are often referred by accountants to help clients prepare for the cross-border impacts of M&A activity.

Business Valuators – Most have a CBV designation, and having a CBV do an analysis and value estimate may be very helpful in obtaining the best price and terms.

The important question is – who do normally confide in and whose advice to you trust the most? Keep them in the loop and run everything by them.

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KEY COMPONENTS OF A LETTER OF INTENT

The LOI is a staple in Business Brokerage in which the buyer outlines the key components of the offer. It is normally non-binding. Below is the architecture of a typical LOI for a small business:

Background/ recital – outlines who the Buyer is, the Buyer's understanding of the deal and who the Seller is;

Description of what is to be acquired – High level description of the what – assets? Shares?;

Consideration – Likely some cash but may be other things like assumption of liabilities. Also timing of payments and consideration in escrow details;

Purchase price adjustment at closing – Allows for adjustments for differences in benchmark working capital, revenues, long term debt etc;

First right of refusal – Could relate to purchase of leased premises if they become available;

Due Diligence - Deals with type and timing of investigation, access to records and physical assets, communication with suppliers, employees and customers; governed by confidentiality agreement to be drafted

Conduct in ordinary course – Seller agrees to continue normal operations and not make any unusual moves during due diligence;

Definitive Purchase agreement – Reference to a formal purchase agreement to be drafted after completion of due diligence, and recognition that the LOI is not a definitive agreement;

Integration of buyer into enterprise, employment agreements – Outline who, if any from Buyer will join Seller's operation and in what capacity (director, manager, employee). Reference to training by Seller, and if Seller is required to stay on for a period;

Expenses – Parties to cover their respective transaction expenses;

Public announcements – What each party can say, and restrictions on when and how;

Exclusivity – Seller to agrees to stop offering process and not solicit any further offers

Miscellaneous – Governed by laws under what jurisdiction, terms under which LOI may be amended, etc;

Closing conditions – Specifically what agreements, due diligence, and inquiries must be completed and what constitutes successful completion;

Non-binding – Confirmation that LOI does not form a binding contract except as previously provided.

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