The BHP guide to selling your business

BHP Corporate Finance

About BHP

BHP is a UK Top 40 advisory firm, with specialist teams to support all of your financial needs.

Our multi-award winning Corporate Finance team offers strategic advice and practical support across a wide spectrum of areas including:

- Strategic options and exit planning
- Company sales
- Company acquisitions
- Management buy-outs and buy-ins
- Private equity
- Debt fundraisings.

We provide our clients with exceptional advice and our partners remain actively involved in transactions throughout the process. We understand that choosing your advisor is a very personal decision and that you entrust specific individuals to advise you on what will likely be a life changing transaction. We therefore don't have separate sales and execution teams. The team you meet from the outset will be the team that works with you hand in hand towards a successful completion.

In today's global environment we also recognise that businesses need to be able to transact on an international basis. As part of Translink Corporate Finance, one of the world's largest mid market M&A advisory groups, our ability to advise on cross border transactions is underpinned by a team of more than 600 experts across 30 different countries. However, no matter where our clients transact, all our assignments are led by your local BHP Corporate Finance team. This ensures that delivery of the deal always remains with the individuals you have appointed.

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Background

Reasons for sale

We understand that owning a business can feel like a very lonely place and that often there can be conflicting emotions when considering the future of the business. Reasons why our clients consider a sale are many and varied but often include:

- Receiving an unsolicited approach for the business
- Retirement of one or more of the directors
- Health, personal or family issues
- Lack of a management team capable of taking on increased responsibility and the running of the company
- Desire to extract some of the value built up in the company
- Concern over the proportion of family wealth tied in to a single asset.

Consider your options

In all these cases a sale may well be the right solution but equally there are alternatives that should be considered before you embark on a sale process.

These options may include:

- The sale of the company to a management buy-out (MBO) or management buy-in (MBI) team (funding for which is likely to be available from a variety of sources)
- Extracting value from the business in a tax efficient way, whilst maintaining management control (again, this may involve raising external finance to fund such a deal)
- The buy-back of shares by the company from a director who wishes to retire
- A flotation on a public market such as the Alternative Investment Market or the London Stock Exchange (although this is unlikely to provide an exit for shareholders in the short term).

Commencing a sales process is a very big decision for business owners. It is extremely important that you take time, in advance of committing to a sale process, to consider your motivations for exploring a sale and what the alternatives might be.

For shareholders who conclude that a sale is the right course of action, the next thing to be clear on is what your ideal outcome from such a process is. In many cases the single most important factor is a desire to maximise the proceeds from a sale.

Whilst we are experts at helping clients achieve this, we recognise that having built a company, often over a period of many years, there will be a number of other softer factors that are also important to shareholders such as:

- Can the buyer help the company to achieve its full potential and continue to prosper going forward?
- What are the future plans for the company?
- Will the staff keep their jobs and will offices/sites be closed?
- Will the brand/family name be retained?
- Is the potential buyer someone the shareholders trust and respect?
- Are there commercial reasons not to speak to certain potential buyers?

We also recognise that some shareholders may have differing opinions and we can help you to agree a way forward which takes all these views into account.

Sale process overview

Whilst every sales process is different, there are common themes to each process and these can broadly be split into three stages: planning and preparation, marketing, due diligence and legal completion.

The principal objective of the first two stages is to maximise the value of the offers received for the business. The third phase is generally concerned with preserving the value of those offers through due diligence and ensuring that the deal is managed to completion in a timely manner with minimal disruption to the business.

Whilst some deals can happen very quickly, a typical process may take between 6 to 12 months to complete. The wide range in time frames is normally caused by the length of time the shareholders wish to spend on the preparatory stage. From the point that the marketing of the business commences a sale can typically be concluded within 6 months.

Appoint an expert

Most shareholders only sell their business once and have little or no experience of selling a company. An expert advisor will not only help shareholders to maximise their chances of getting the best possible offer for the company but will also help to ensure that the deal is successfully completed on the terms outlined in the offer letter.

The relationship between an advisor and the shareholders will involve the parties spending a lot of time together and so it is critical shareholders find someone who will not only do a great job, but also someone they feel they can have a close personal relationship with. A sales process can be a roller coaster of emotions at points and a good advisor will be invaluable in helping you through these times.

What to expect from a corporate finance advisor

A fundamental part of the role of a corporate finance (CF) advisor is to project manage the whole sale process from start to finish, coordinating all other advisors and leading the process through to a successful conclusion. This will allow you to focus on an absolutely critical element of any successful sales process – ensuring the business continues to perform well. If the performance of the company dips during this process, it can have a negative drag on the proceeds received and/or the appetite of a potential purchaser to conclude a sale.

In addition to this a CF advisor will help the shareholders to:

- Identify a list of potential buyers, usually on a world-wide basis, using their buyer research expertise
- Produce robust financial forecasts
- Produce a high quality information memorandum that can be provided to interested parties and which will highlight the key attractions of the company
- Lead negotiations with bidders to obtain the highest possible price with attractive associated key commercial terms.

Agreeing a deal in principle is typically only the start of negotiations. Throughout the deal process there will be numerous points at which value can be eroded. A key element of the role of your CF advisor is to help you strategically handle the disclosure of information and work closely with your legal advisors to ensure your ultimate proceeds are not eroded through commerical points of detail in the legal contracts.

There are common themes to each process and these can broadly be split into three stages:

- Planning and preparation
- Marketing
- Due diligence and legal completion.

Planning and preparation

Preparing your company for a sale

High quality preparation is very important. It can significantly improve both the likelihood of a sale completing successfully and the total price achieved being maximised.

Typically the preparation phase will focus on matters such as:

- Ensuring that budgets/forecasts are achievable and met
- Ensuring that the management team remaining with the business post sale is sufficiently strong
- Identifying all one off and exceptional costs
- Identifying all "owners' costs"
- Considering how the timing of capital expenditure plans will impact the future financial performance and cash/debt position of the company
- Reviewing the working capital cycle for opportunities to generate additional cash proceeds
- Considering whether there is sound commercial rationale for implementing cost saving initiatives
- Ensuring that the company's statutory and tax affairs are up to date and filed with the relevant authorities
- Considering the potential sale when negotiating key contracts with suppliers and customers
- Considering break clauses on any rental properties which may not be required by future purchasers
- Considering extraction of property assets from the company tax efficiently
- Reviewing the tax position of all the individual shareholders.

Undertaking a strategic review at least 12 months in advance of starting the sales process will identify a number of factors, including those listed above, which should enhance the ultimate valuation of the company.

Identifying purchasers

A fundamental aspect of maximising value is to identify and engage with potential purchasers who have the greatest strategic imperative to acquire the company. A strong rationale for acquiring the business should in theory lead to a more compelling reason to offer a higher price.

When identifying potential purchasers, factors that may need to be considered include:

- Competitors for whom the acquisition would enhance their market position or prevent a new or existing competitor becoming a greater threat
- Complementary products or services where the product offering of the vendor company would allow product diversification that otherwise may not be possible
- Suppliers seeking to secure a route to market for their existing products
- The ability for the acquisition to fill a geographical gap in the acquiror's existing business
- The ability of the potential acquiror to accelerate growth opportunities through its existing relationships / distribution network.

It is often the case that potential acquirors are located overseas and so it is essential that detailed research is undertaken on a world-wide basis to ensure a high quality list of prospective buyers.


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It is also essential to consider the financial resources of the potential purchasers to understand their capacity to deliver a transaction. Whilst past acquisition activity can be a positive indicator here, it is important not to make presumptions. Things can change rapidly in business and often events are happening that are deliberately not in the public domain.

Your CF advisor should have early stage no name conversations with potential buyers to ascertain as much information as possible about their current position before any confidential information is provided.

Valuation

If you were to ask a panel of experts to value a business, the chances are they will all come up with slightly different numbers as valuation is not a precise science. That said, there will be a number of common factors that will have a material impact on their opinion:

- The current and forecast maintainable profits and cash flow of the company (historical profits are less important but will also be considered)
- The visibility of future revenues and the strength of any contractual relationships
- The dependency on a single or a small number of customers and/or suppliers
- The uniqueness of the opportunity
- The barriers to entry preventing the business model being quickly and easily replicated organically
- The strength of the management team that will be remaining with the business, post deal
- The perceived risk, in the eyes of one or more of the potential purchasers, of someone else acquiring the company
- The period of time in which the acquiror can realistically expect to recover its cost of investment
- The availability of bank debt to finance the acquisition.

Your CF advisors should be happy to give you their view on valuation and it is normal then to agree a fee arrangement with them that incentivises them to exceed those initial expectations.

Ultimately the value achieved will come down to a wide range of factors, some of which will be outside the control of the vendors and their advisors. Running a highly professional process, which creates a real or perceived competitive bidding situation, should maximise the chances of receiving the highest possible offer.


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Marketing

Confidentiality

The process of selling a business will inevitably require the release of sensitive commercial information. Care must therefore be taken to preserve confidentiality and to carefully control the conditions and timing of when such information is released.

This control commences when deciding on the number and specific names of parties to approach. Once a list of names (and sometimes this may even be a single party) has been agreed with you then the process should be controlled through:

- Ensuring all potential purchasers enter into a legally binding non-disclosure agreement
- Restricting the information contained in the information memorandum
- Providing further information requested by potential purchasers only as and when it is deemed appropriate.

Sometimes a company may have already received an offer or approach before a CF advisor is appointed. In these circumstances, it is very important to discuss with the advisor whether additional potential purchasers should be approached.

Information memorandum

The information memorandum is the key document in the sales process, which is why a high quality information memorandum that provides the reader with a good understanding of the business and a compelling reason to explore the opportunity in more depth is therefore critical. The main objective of this document should be to create sufficient interest with potential purchasers for them to want to meet with the company.

A well crafted information memorandum should strike a balance of presenting the business in the best light possible whilst avoiding making claims which cannot be later substantiated and therefore undermine credibility in the eyes of the purchaser. A high quality information memorandum will also provide the impression that a professional and competitive process is being run.

Meetings with potential purchasers

To preserve confidentiality, preliminary meetings with interested purchasers are normally held off-site away from the business. They provide potential buyers with an opportunity to meet the vendors (and sometimes the senior management team) and build on their understanding of the opportunity from the information memorandum.

For vendors, it allows them to assess whether the potential purchaser is someone they would be comfortable to do a deal with. Matters to consider include how the company would fit within the purchaser's business, shared values, personal chemistry and whether the potential purchaser is someone the management team remaining with the business could work with. This meeting will also give the CF advisor a chance to gauge the interest in the opportunity and discuss the process should matters proceed forward.

On-site visits

Depending on the type of business, vendors should normally be prepared to allow pre-qualified buyers to undertake a brief accompanied tour of their facilities. Particularly in the manufacturing or engineering sectors, purchasers are often reticent about making a written offer without having physically seen the company's key operations. Notwithstanding this, access needs to be carefully controlled including giving advance thought as to the reasons for the visit. Some potential purchasers may actually be known to your employees already, so this will also need considering.

Indicative offers

At this stage, purchasers should have a sufficient understanding of the company to enable them to submit a written indicative offer, setting out:

- The price
- The form of consideration
- Details of any deferred consideration
- Details of any earn-out
- Key assumptions and conditions underpinning the offer
- Any approvals required to be able to complete a deal
- Proposed due diligence
- Names of advisors
- A proposed timetable with key milestones.

Each offer should be carefully reviewed by the vendors and their advisors. It is important that any areas of ambiguity are clarified and further explanations sought where insufficient detail has been provided. Following the review of offers, it may be decided that there is a preferred purchaser.

In the event of multiple offers being attracted, further information may be provided before these parties are invited to make a “best and final offer” by a specified deadline.

In ultimately choosing the preferred purchaser, the decision may not be based purely on price and other considerations may include:

- Structure of the offer
- Future plans for the company
- Views of the senior management team
- Cultural fit with the purchaser
- Extent of due diligence investigations
- Reliance on third parties (such as funders) which might impact timetable and/or deliverability.

Negotiating heads of terms

On receipt of final offers, a headline price and other key commercial terms will need to be agreed. This may involve approaching one of the parties and giving them an opportunity to match another offer.

At this point detailed heads of agreement will be agreed. It is common practice for the advisors to lead these discussions so as to enable vendors to distance themselves from any contentious aspect of the negotiations. This can be particularly helpful if the vendors later want to concede a point or may need to work closely with the buyers going forward.

The output of these negotiations should be recorded in heads of terms or more simply “heads”. Heads are a written document which sets out the key commercial terms of the proposed transaction.

Heads are signed by all parties and are, in most respects, not intended to be legally binding. Exceptions where they are legally binding often include exclusivity periods and confidentiality. Notwithstanding this non-binding nature, it is important that any key points of principle are carefully considered as subsequently seeking to renegotiate a position agreed in the heads will at best delay completion and at worst cause the transaction to abort.

Due diligence and legal completion

Due diligence

Having agreed heads of terms, the purchaser will wish to undertake due diligence investigations to confirm both the assumptions it has made in making its offer and to identify any material matters that have not been disclosed by the vendors.

Due diligence may be undertaken internally by the purchaser's own deal team but it is usual for at least part of the process to involve third party advisors appointed by the purchaser.

Typical areas of focus for due diligence would include, but not be limited to:

- Historical and forecast financial performance
- Valuation and condition of property and plant and machinery
- Taxation
- Customer, supplier and employee contracts
- Intellectual property rights.

Depending on the potential purchaser's knowledge of the market, they may also wish to undertake some commercial due diligence. Environmental and health and safety issues may also be the subject of separate due diligence depending on the activities of the company. Whilst due diligence may require the purchaser and its advisors spending some time at the company's premises, it is normal for as much work as possible to be carried out off-site and is likely to involve the use of an electronic data room.

The due diligence process must be carefully controlled by the vendors' advisors in order to protect against it being used as an excuse for renegotiating the deal or potentially withdrawing from the process.

Legal negotiations

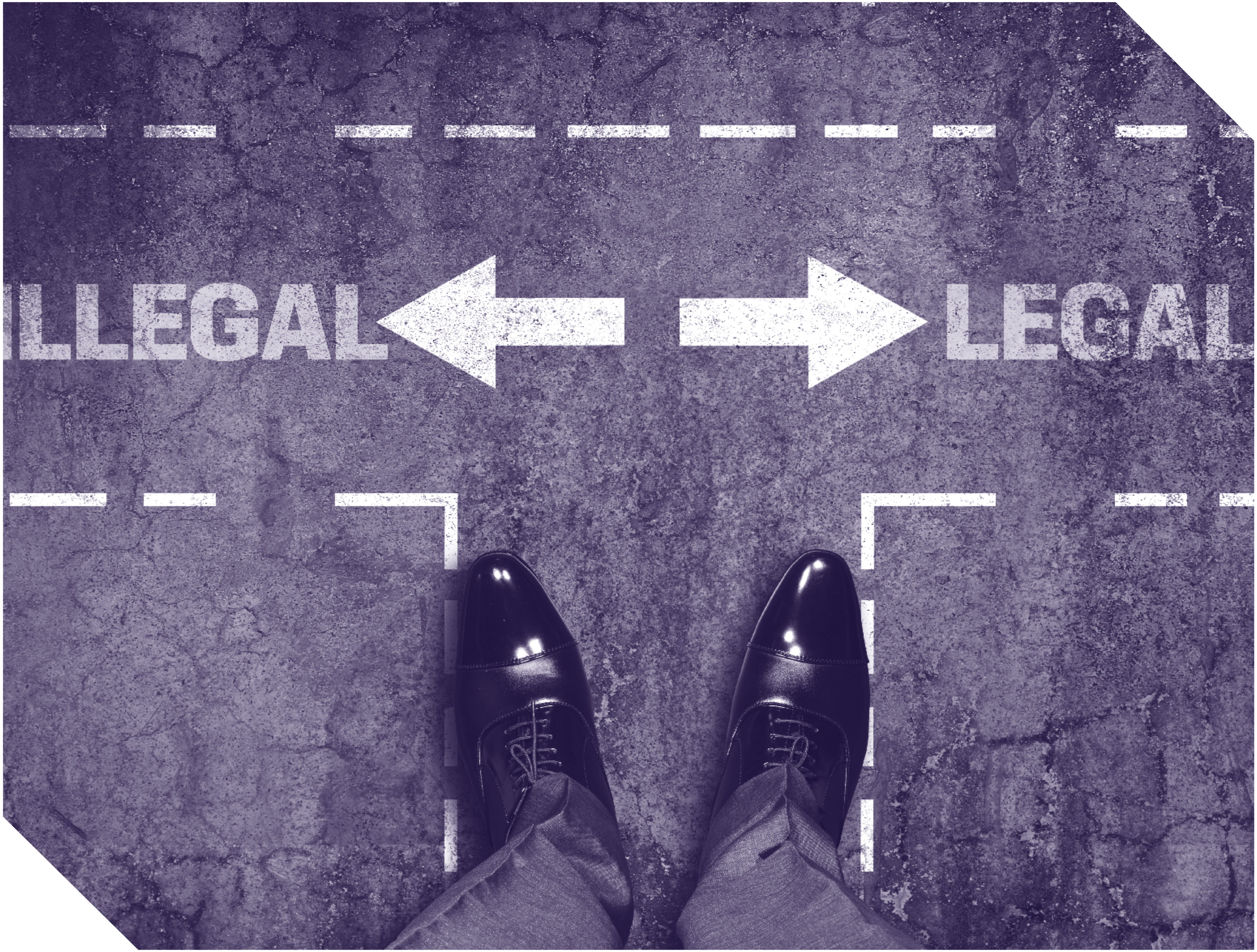
In parallel with the due diligence investigations, the purchaser's lawyers will prepare a first draft of the legal documentation. The principal document is the sale and purchase agreement or 'SPA'. The SPA builds on the commercial points agreed in the heads of terms but unlike the heads, it is a legally binding agreement. Typically a SPA will include:

- The detailed terms of the transaction
- Restrictive covenants/non-compete undertakings from the vendors
- Warranties, a tax covenant and possibly indemnities in favour of the purchaser.

It is vital that you obtain expert advice from a lawyer who is experienced in company sales and has an appropriate level of resource to be able to respond to the purchaser's questions in a timely manner. An experienced lawyer will also be able to advise you on what undertakings are reasonable to give to a purchaser and thereby protect the value of the sale proceeds post completion.

Negotiation of the legal documentation will typically take around four to six weeks. It is however a misconception to think that once heads are signed, lawyers can simply get on with drafting the documents. This is not the case as there is often substantial value to be won and lost in this phase of the transaction. It is therefore vital that your CF advisors remain closely involved working hand in hand with the lawyers throughout.

The due diligence process must be carefully controlled in order to protect against it being used as an excuse for renegotiating the deal or potentially withdrawing from the process.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Completing the deal

This is the time for everyone to celebrate the successful conclusion of the transaction. A process that may have lasted several months typically finishes with a flurry of paperwork signing and a glass of champagne in the lawyer's office.

Whilst no two transactions are the same, in our experience there are typically a number of key features that will have led to a successful sale:

- Starting out with firm foundations – plan thoroughly for the sale. Typically most business owners only sell once, so make sure you maximise your chances of success with diligent preparation
- Thoroughly researching the buyer population to identify the strategic purchasers. Often these may be overseas
- Structuring the sale to create a sense of competitive tension between bidders
- Retaining credibility throughout the sale process by ensuring that information provided to purchasers is timely and robust, and the performance of the business remains on track
- Controlling the timetable and process but retaining flexibility to adapt as circumstances develop
- Working as a team. Selling a business will inevitably be a demanding, and at times, an emotionally draining process. Make sure you work with a team of experienced advisors who not only understand your business but are on hand 24/7 to provide guidance and support.

BHP Corporate Finance

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