

Boston Business Journal

March 14-20, 2008

Some important do's and don'ts in selling a business

Selling your company? There are critical decisions to be made at each stage of the sale process, particularly early on. Avoiding pitfalls at each stage of the process is essential in maximizing value and ensuring a smooth transaction.

Here are some suggestions for sellers:

1. Prepare the business for sale when an M&A exit seems likely. Engage your lawyers early in the process to identify problem areas and fix them. Anticipate the buyer's due diligence request. Have your lawyer prepare a buyer's "due diligence checklist" and populate an online data room with all required responsive material. Making it easier for the buyer facilitates more and quicker bids.

2. Hire an investment banker. In all but the smallest transactions, it is my experience that investment bankers are well worth their fees (which are high — even by lawyer standards). Investment banks have their finger on the market. The last thing you want to do is sell yourself short.

3. Negotiate the investment bank engagement letter. These agreements are negotiable, up to a point. Pay particular attention to the fee structure. Suggest a modest fee for a modest result and a significantly greater fee for getting a great deal. Be certain you can get out of the engagement if the bankers perform poorly.

4. Fight for all of the key terms that you can at the letter-of-intent stage. Buyers and sellers are always extremely anxious to cut a deal and do a simple letter of intent. But this is the crucial time to rock the boat if you are the seller because sellers tend to lose their leverage once the letter of intent is signed. Word leaks out to employees, customers and suppliers that you are sell-



INSIDER VIEW

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Ed
Miller

ing your company, and it's hard to retreat from that. Here are some key points to raise at the letter of intent stage:

- Understand the purchase price calculation. The "real price" is the price the buyer will pay per share of your stock. In getting from the aggregate purchase price for the business to the price per share, do you include unvested stock options? Do you add back the exercise price of options under the "treasury stock method"? Do you exclude out-of-the-money options?

- Avoid purchase price adjustments and earnouts if you can. Purchase price adjustments that tie to changes in net worth or balance sheet items may seem innocuous, but they invite claims that your books were not maintained in accordance generally accepted accounting principles. Earnouts that adjust the price based on post-closing performance seem appealing but are an invitation to litigation — the buyer's and seller's interests in how the business is run after the closing inevitably are in conflict.

- Liquidity issues. Worry about liquidity if you are getting paid in stock. Whatever you do, don't get "restricted stock" in a taxable deal.

- Ancillary agreements. If there are to be noncompete agreements or employment agreements, know early who is going to have to sign them and an outline of what is

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- Indemnification. What do you ask for to limit the buyer's post-closing remedies against the sellers?

- Limit the amount of time that the representations in the definitive agreement survive to one year or less.

- Get a small escrow. More importantly, try to limit the indemnification to the escrow, even at the price of a larger escrow. This may be the most important seller provision of all.

- If the acquisition consideration is wholly or partly buyer stock, consider providing that indemnification claims can be paid back in buyer's stock valued at the time of the closing. Even better, insist that the sellers can at any time substitute cash for the shares in escrow valued at that fixed price or can pay valid claims in cash at their option.

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ED MILLER is a partner at Sullivan & Worcester in Boston and is the author of "Mergers & Acquisitions: A Step-by-Step Legal and Practical Guide" and "Lifecycle of a Technology Company: Step-by-Step Legal Background and Practical Guide from Startup to Sale."