SELLING YOUR BUSINESS LATER: 5 MUST-DO'S NOW

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As seen in Forbes

Most entrepreneurs dream of one day selling their business and cashing in big. In reality, here's how most business owners will end up:

1. Dropping dead at their desks
2. Mumbling to the lamp at the nursing home, or
3. Just maybe, drinking daiquiris on the beach and watching their portfolios on their iPhones

Every business owner wants the umbrella drinks and the crashing waves. Most don't get it. Luck helps. Here are five key things you need to do now so that you can sell later.

#1 Clean Up Your Act

Many years ago, I represented some small retailers, including a woman who owned one dry cleaner and two cash registers. She used the first register during the day. Then, during the evening rush, she used the second one. She told the IRS absolutely nothing about that second cash register—not about the money that went in, not about the money that went out. I explained, "This is illegal." She explained, "I would not get out of bed in the morning and go to work if it wasn't for that second register." She thought she won that argument. But, she was incubating another big problem. Her homemade "duty-free zone" was killing her ability to sell her business. Her tax returns showed she qualified for food stamps. She had no legitimate financial statements that would ever impress a buyer.

Buyers aren't idiots. They dig into your business and investigate. If you're not paying your employees required overtime wages, buyers find out and ding the purchase price or walk away. If you own a car dealership and your repair crew has been pouring used oil in the backyard for years, you're failing the buyer's hazmat test. That oil doesn't just stain the grass. It steals your deal.

Many business owners believe they can fix problems right before they sell. **Inside Scoop:** By then, it's too late. You're not going to survive the buyer's due diligence by hurriedly Swiffering all your problems away. A smart buyer checks on what you have done for years.

Even if your misdeeds do escape immediate discovery, you need to promise—about a thousand times—that you haven't done anything wrong. And that can come back to haunt you. Recently, a large public German dialysis business, Fresenius SE, entered into a merger agreement to acquire Akorn Inc., a public generic drug maker. After the merger agreement was signed, but before closing, Fresenius discovered adverse information about Akorn, including evidence of misconduct in reporting drug testing data. Fresenius walked away, although Akorn fought it. Akorn's stock plunged when a court upheld Fresenius' right to walk away from the deal.

As Faulkner teaches, it's hard to escape your past. Even if you close and get your money, the buyer may discover a problem later and sue you.

Clean up your act well in advance of putting your business up for sale.

#2 Structure Your Business For A Sale

At every stage of your business, you need a legal structure that helps you sell. When starting out, many entrepreneurs are broke and in a rush. They recklessly ZOOM through the legal process.

Consider this unfortunate duo. They had built a sizable business. They had just received a great purchase offer and were referred to me. I took one look and ascertained "Problem el Biggo." When these new clients had long ago set up their business, they gave little thought to "later." Well, by the time they sat down with me, "later" was "now." And "now" they were "screwed." They had picked a C corporation for their business—good for many, just not them. Under the rules applicable to their business, 50% of the sale price would be lost to taxes. If my clients sold, they would have to pay other bills and would end up with almost nothing. They glumly limped away from the deal.

You have a lot of choices now about how you create your business and grow your company. You may need to make changes to address new taxes, laws and customs. Pay attention to the structure of your business—if you want to sell it.

#3 Create A Team

You may be the star of your business. But, buyers want more. It's the old "hit-by-the-electric-scooter" test. You get hit, there goes your business. If you hope to sell, build an executive team so your business can survive and thrive without you.

Sure, company culture and other warm-fuzzies matter. But, nothing says "stay and grow with me" quite like money. By providing equity stakes to your executives, you can create the opportunity for your team to earn great wealth. They're incentivized to stay and grow your business despite tough times and other opportunities. **Inside Scoop:** Buyers often insist that sellers reserve 10-15% of company ownership for employees to ensure that they have a significant stake in your business' success.

You can simply give stock—or alternatives, like phantom stock, options and stock appreciation rights. You can give similar stakes if you have a limited liability company or partnership. **Inside Scoop:** Don't underestimate the hassles involved. You need to invest a lot of time, money and concentration building a plan that works for your business. Don't overlook the benefits. A significant employee stake in your company checks a box for many purchasers and helps you grow in the first place.

#4 Build For Buyers

Buyers want a business that will reliably produce profits. Buyers also want those profits to increase every year. And many buyers want a business that they can grow and then flip in a few years for even more money. In short, buyers are willing to spend money if they are pretty sure they will make even more money.

But they're not going to take your word for it. You have to prove it.

Inside Scoop: Contracts—good contracts—are one of the best ways you can prove your future revenues. Unlike handshake deals and even a long track record of past sales, a good contract ensures your rights to future revenues. Recently, publicly traded Fiserv agreed to merge with First Data, another public company. Soon, Bank of America said it might terminate its long-term deal with First Data—which could hit First Data's revenues and might torpedo the merger with Fiserv. But, Fiserv expressed commitment to the deal because of First Data's contracts: "We did our diligence, including with respect to client contracts and any significant ongoing negotiations, and are comfortable with the business in a variety of outcomes." For now, apparently on the strength of those contracts, Fiserv is proceeding with the merger. You may have great relationships with your customers. You may feel sick about trying to replace handshakes with contracts, especially with long-standing customers. Do your best to get over it. Buyers pay top dollar when contracts ensure your future revenues.

#5 Protect Your Edge

A successful business—and any company that someone would pay a lot to buy—has a competitive advantage over its rivals. Think of Amazon's 2020 rollout of exclusive rights to all products on Earth and instantaneous teleportation-shipping. Intellectual property (IP) can provide that edge—from patents held by tech companies, to luxury fashion logos recognized worldwide on purses, caps and clothing, to copyrights held by multimillion-dollar gamer media companies. You may need to register trademarks, ensure copyright protection or even seek a patent. **Inside Scoop:** When you get a trademark, copyright or patent, the legal bills and hard work don't end—they often skyrocket. Now, you have to defend your rights against copycats and freeloaders. That means sending cease and desist letters and filing lawsuits. If you don't, you may lose your IP rights. That's why McDonald's goes after plenty of companies, from McMunchies to McCurry to McSleep.

Other companies seek to protect their competitive edge by preventing ex-employees from competing. **Inside Scoop:** It's getting tougher to use the same old noncompete agreements. In some places, they're illegal and, if you use them, you can be subject to fines, penalties and reimbursement of legal fees. For example, just last month, Washington state adopted a new law prohibiting noncompete agreements for employees that make less than $100,000 annually.

Still, companies use other measures to protect their businesses. When mega-biotech Amgen lost 19 salespeople to competitor, Kyprolis, Amgen did not sue its ex-employees for violating noncompetes or otherwise. Instead, the biotech behemoth sued Kyprolis for allegedly using Amgen's confidential information to hire Amgen's star salespeople.

Your competitive edge can be the deciding factor in a successful sale. Protect it.

With a lot of luck, hard work and planning, you can sell your business and end up on that beach. First round's on you.

ABOUT JACK GARSON

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Jack Garson's practice focuses on Real Estate, Construction and Business law. He serves as a legal advisor for numerous local, regional and national companies. In his role as legal counsel, Jack also serves as a strategic advisor and lead negotiator. Further, Jack provides guidance on the structure of complex transactions, the resolution of business disputes, the growth and sale of companies, and the management of issues such as liability and risk reduction, employment practices, and enhancing profitability.

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In the past two years, we've grown by 50% through expansions in New York City and, most recently, Charlotte, North Carolina. This growth has provided immense value to our clients and attorneys.

Wherever your industry, Offit Kurman is the better way to protect your business, preserve your family's wealth and resolve your most challenging legal conflicts. At Offit Kurman, we distinguish ourselves by our quality and breadth of legal services—as well as our unique operational structure, which encourages a culture of collaboration and entrepreneurialism. The same approach that makes our firm attractive to legal practitioners also gives clients access to experienced counsel in every area of the law.

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