

M&A Market is Still Hot—For Now

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The M&A market has been booming, with the last five years moving at a head-spinning pace. COVID-19 may have momentarily dampened the market, but the fourth quarter of 2020 rebounded to be the strongest quarter in recent memory. 2021 is setting up to look even stronger, but all good things come to an end. Eventually.

Given all the uncertainty—interest rates, tax rates, political climate...the list goes on—if you are thinking of selling your business, now is probably the time. Advisors will often advise to plan well in advance of a business sale, however, if opportunity is knocking, there are still some things you can do to make a meaningful difference in the price and salability of your business.

Reverse Due Diligence

As M&A counsel, I advise clients on the front end that there is always one “thing” (sometimes there are many “things”!) that plagues a deal. Part of my job is to flush that “thing” out as soon as possible so we can manage it proactively. Even better though is to understand what your “thing” might be going into the deal.

Understanding what buyers will identify as a problem or concern in your deal at the earliest convenience—ideally before the buyer is even at the table—gives you the most control to make those concerns non-issues.

Reverse due diligence is the process of having your counsel review standard due diligence items requested in M&A transactions. Due diligence covers areas such as:

- Corporate Documents
- Ownership of IP
- Environmental Issues
- Assignability of Contracts
- Classification of Employees

Say, for example, the value of your business is heavily dependent on its customer contracts, but those contracts are not assignable without consent. You may not be able to fix contracts you have already signed, but you can change your

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template or negotiate future contracts so they can be assigned to a buyer in an M&A transaction. If corporate records do not match current ownership, or are nonexistent or messy, cleaning up records is time well spent. First impressions matter and disorganized corporate records can color the way a buyer views your business. Tackling environmental issues head on can prevent delays and quantify any potential issues. Knowledge is power in negotiation.

Talk about Risk Allocation

Post-closing indemnity is one of the most negotiated aspect of every transactions. Sellers should talk with counsel about what the market has established as reasonable risk allocation for a particular type of transaction. There are statistics put out by the American Bar Association that can tell you what an average basket and cap is in a health care transaction, for example. This information should be used going into the negotiation, instead of at the back end. Try to hammer out baskets, caps, fundamental representations, and the like at Letter of Intent stage. This strategy may not work with all buyers, but when it does, the purchase agreement negotiation is quicker and smoother, meaning you get your money sooner.

Preserve Value

In addition to reverse due diligence to flush out issues and “fix” problems, there are some relatively simple steps you can take to actually enhance the value and salability of your business:

- Increase EBITDA and explore add-backs to the profits of the business for expenses a buyer would not continue
- Reduce working capital
- Lock in management team and other key employees
- Reduce long-term contractual obligations/buy-outs
- Clean up financials

Line up your team

Buyers can identify an educated and committed Seller by the team they assemble around them. It is essential to have an experienced M&A team around you, including (but not limited to!) legal counsel, CPA, and financial advisor. An experienced team will translate into improved economic consequences, less risk, and a smooth closing. A buyer’s counsel will spot an inexperienced advisor a mile away. And, they’ll negotiate accordingly.

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