Most entrepreneurs work their entire career to grow the value of their company. While they often earn a great living, a significant portion of their net worth is tied up in the business. One method of accessing that wealth is to sell all or part of their company.

Since selling a business is usually a once-in-a-lifetime event, entrepreneurs tend to have many questions about the process. Although every company is unique, there are common themes and frequently asked questions, which are summarized in this article.

Companies generally sell at a premium, if the previous few years have exhibited growth and the business is still strong.

IS THIS A GOOD TIME TO SELL?

The most important timing decision involves a seller's personal goals. If you are not ready to sell the business, the external environment is irrelevant. Once you have decided that both your financial and personal lifestyle goals point towards selling the company, then it is time to investigate the market environment.

Companies generally sell at a premium, if the previous few years have exhibited growth and the business is still strong. It is much more difficult to achieve a strong sales price if financial results have been declining or erratic.

The economy, in general, will influence cyclical industries like construction, and sales prices generally rise in good times and fall when the economy performs poorly. Buyers are more likely to pay strong prices for acquisitions when their profits are good and their stock price is up.

A long-term plan will ensure you are prepared to market the company in a time of strength, not weakness. Selling a business generally takes nine to 12 months, from the first meeting with your investment banker until the proceeds

Thoughtful preparation and planning are key to maximizing the value of your business. Any weaknesses in the business should be addressed well in advance of the sales process.

of sale are wired into your account. You want to be prepared to pull the trigger when the company is in growth mode, and the sector and economy are doing well.

HOW DO I PREPARE MY BUSINESS TO MAXIMIZE VALUE?

Thoughtful preparation and planning are key to maximizing the value of your business. Any weaknesses in the business should be addressed well in advance of the sales process.

If you think you will want to sell the business in three to five years, start preparing now. The terms "value drivers" and "value detractors" indicate the characteristics of your business that will be viewed as strengths and weaknesses by potential buyers. In general, they are the same characteristics that you look for in a strong business with a long-term focus. Value is enhanced by traits such as:

- Revenue and profitability growth
- Plans to address shifting markets and competitive pressures
- Technology and finance infrastructure
- Customer diversification
- Management depth
- Good working capital management
- Proprietary products or technologies
- Brand awareness/name recognition
- Up-to-date equipment and facilities that can accommodate growth

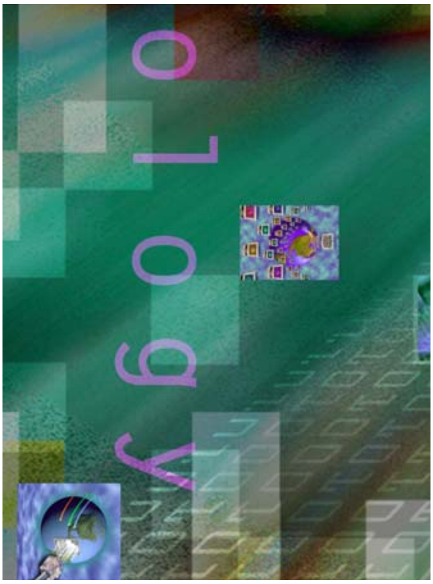
Conversely, negative results on these traits will detract from the value of the transaction.

External value drivers are those that are completely outside of the company's realm of influence but will still affect the value of the business enterprise such as:

- Market trends
- General economy
- Industry consolidation

Sophisticated buyers will ask the right questions to understand the true state of your company. If the value drivers/detractors are ignored by the business owner, they will surely be a focus of the potential buyer. The buyer will have to address your company's weaknesses by spending their own cash, which will affect the purchase price. If you are already a strong organization that is prepared for growth, you will be a better investment and command a higher price.

WHAT IS "PRIVATE EQUITY?" WOULD A FINANCIAL (PRIVATE EQUITY) BUYER/INVESTOR BE A GOOD FIT FOR MY COMPANY?



Private equity firms manage pools of invested money from private individuals, pension funds, insurance companies, endowments, and other investors. Private equity firms invest in companies using financial leverage, with the goal of growing the company, paying off its debt, and realizing a return far in excess of what traditional investments generate.

Private equity has grown immensely in popularity as an investment vehicle in the past five years. Due to the amount of funds available for investment (estimated at more than $100 billion), there is a great deal of competition for acquisitions of middle-market companies. In this unique environment, private equity purchasers are paying prices that are competitive with strategic (industry) buyers, and often pushing prices higher than would be possible, if only those strategic buyers were interested.

Private equity firms generally purchase majority stakes in companies, ranging from 51% to 100% of the equity. In general, private equity buyers want active management to remain with the company for at least two to three years after the transaction. The more active others are in running your company, the less emphasis will be put on you to remain with the company post-transaction. In general, the seller/owner will receive administrative and planning support from the private equity partner, which allows him or her to devote more time to the part of the business that he or she enjoys.

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Many entrepreneurs choose the opportunity to sell a large portion of the company to diversify their wealth, but still retain a significant percentage of equity so that they can participate in the upside as the company's success continues. Private equity buyers generally prefer to structure deals in this manner. When the company is sold for the second time (typically three to seven years later, and hopefully at a much higher value), the remaining equity is cashed-out in what is commonly referred to as "the second bite of the apple."

IF I WANT TO STAY, WILL THERE BE A PLACE FOR ME AT THE COMPANY AFTER A SALE? WHAT WILL MY LIFE BE LIKE WITH A "BOSS?"

The spectrum of buyers will range from large companies that have managers cued up to run the company after a transition period, to investors that want you to stay for three to five more years and continue to grow the company. Ideally, you will attract interest from a buyer whose post-transaction expectations match yours. However, flexibility on your part is always the best tool to secure the strongest financial deal. You can often maximize value by compromising your ideal transition.

Many entrepreneurs dread the idea of having a boss. After many years of controlling your own destiny, it is difficult to play second fiddle. Creating a new position, expanding into a new geography or purchasing a major piece of equipment may have been your unilateral decision before sale of your business. While you may have similar authority delegated from your new boss, it is more likely that some new rules will be put in place. With a strategic acquirer, you will likely be part of a large company and have to play by their rules and accept their corporate culture. The flip side is that you always have the freedom to move on, if you are not happy. With a private equity buyer, you will likely have a great degree of autonomy as long as things are going well. However, if sales and profits are suffering, you will certainly know that you have controlling shareholders to answer to.

The construction industry is a small world and many of the participants know each other.

It is always wise to speak with former business owners that have been acquired by your buyer. They will have excellent insight into what your life will be like as part of the organization post-close. Many entrepreneurs find long-term happiness partnering with their acquirers, but some need complete control to be happy. You should learn as much as you can about your acquirer, and be as honest as you can about yourself and your need and desire for control.

WILL MY CUSTOMERS AND COMPETITORS FIND OUT THAT MY BUSINESS IS FOR SALE?

The construction industry is a small world and many of the participants know each other. For this reason, most of our clients are concerned about confidentiality during the sales process.

There are certain measures that your investment banker should take to protect confidential information, including the identity of your company. First, your investment banker should not contact anyone without your approval. Second, your banker should have potential buyers sign confidentiality agreements before learning your identity or any significant details about your business.

However, there is always some risk that others will learn of your impending sale. While it can be minimized, risk of disclosure is one that you must unfortunately take in order to sell your company.

WHEN SHOULD I TELL MY EMPLOYEES? WILL MY EMPLOYEES LEAVE, IF THEY FIND OUT MY BUSINESS IS FOR SALE?

You can decide when to give employees knowledge of the transaction. Some sellers tell their top managers before the process even begins, and others wait until after the final sales agreements are signed. Business owners are seldom comfortable in making a pending transaction public. However, sometimes the downside of telling key employees is less problematic than the difficulty of completing the sale process without their knowledge. Often, key employees will be included in the process early, but other employees will not have any knowledge until late in the process or until after close.

> **Selling a business is typically a one-time event, with many facets to consider.**

By nature, most people are uncomfortable with change. Word of a pending sale does create an uncertainty for employees that will make many of them nervous about their future. However, in most cases, good employees will have greater opportunities after a sale as part of a larger organization. Also, in the case of a financial buyer, your employees will be valued since they helped create the success of the company. At an appropriate time, you can communicate to your key employees this fact. You can also emphasize that they will likely benefit from greater career opportunities as a result of the sale. Be as specific as possible without making guarantees that you are in no position to make.

Entrepreneurs spend many years building a business. Mistakes are made along the way. Lessons are learned, and eventually, business owners have an excellent grasp of their capabilities and their markets. Selling a business is typically a one-time event, with many facets to consider. It can seem a daunting event by even the most optimistic business people since it is a completely new endeavor and often outside their comfort zone. However, it has been done thousands of times, and countless entrepreneurs have dealt with the same difficult issues. At the conclusion, they reap the reward for decades of hard work building their business. ■

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MERGERS AND AQUISITIONS

Exit Options for Owners: A Checklist for Selling Your Company Internally

The recent strength of the U.S. commercial and institutional construction marketplace has provided a boost to the coffers of many contractors. Flush with these strong profits and record backlogs, many owners have begun to consider the next logical step — exiting their business through a sale or transfer. While the flurry of strategic and financial buyers who have emerged for construction companies in recent years has created mergers and acquisitions opportunities in our industry, the fact remains that the overwhelming majority of contractors (six out of 10) still cash out of their businesses through an internal sale to key employees or family. Whether you are contemplating an immediate internal transfer of your business or have the luxury of time to plan for such succession, this article lays out the key items to examine when considering a sale to key employees or family.

Align future ownership with future management responsibility.

The most successful internal sales occur between owners and those individuals who have a direct impact on the day-to-day operations and profitability of your firm. As an owner, you understand the direct correlation between ownership and accountability within a closely held firm — your plan should create and harness this powerful link for application to others.

Internal sales are much more likely to succeed when shared goals drive the process and transaction structure, rather than the other way around.

Goals and objectives come before structure and price.

Shared goals that are openly communicated among participating parties are critical. Ensure that the future owners of your business each have similar objectives with regard to managing operations, building equity, and distributing earnings. Once this foundation has been laid, your advisor can assist in selecting the right structure (ESOP, subchapter-S buyout, permanent joint venture etc.) to meet these needs. Do not try and fit your internal transfer process into an existing structure just because that is the method you are most familiar with. Internal sales are much more likely to succeed when shared goals drive the process and transaction structure, rather than the other way around.

Prepare for that which cannot be anticipated.

Just like in constructing any project, internal sale plans invariably encounter unanticipated bumps in the road — both bad and good. Bad jobs, bonding constraints, unforeseen market opportunities — none of these can be planned for but will likely occur during the course of your ownership transfer. Build flexibility into your plan to accommodate the necessary course corrections.

Profitability is critical.

Your employees likely do not have the financial resources available to purchase your company so most of the money will come from the future profits of the business. If your company is profitable, almost any internal transfer technique will work. If your company does not make money, ownership transition will not take place unless you are willing to give your company away.

Align strategic and ownership transition objectives.

Cautiously approach strategic initiatives with an eye towards your long-term ownership transition goals. A timely ownership transition will likely impose cash-flow constraints on your business that can limit strategic objectives. Before your transition plan begins, ensure that your strategic objectives align with your ownership transition objectives.

Company value is based on earnings and your exit timeframe.

The earnings capability of the business and your timeframe for exiting are far more important than any theoretical value of your business. You may value your company at $1 million, but this valuation is meaningless if there are not interested outside buyers and your employees are only able to pay you $500,000 over the timeframe you have set for the buyout.

Internal buyouts extend the length of your payments.

Financially, the difference between selling your company to a third party or selling to key employees is often a matter of the timing of the payments — internal buyouts take longer to achieve the same value. However, while value can be roughly equivalent between the two transactions, it is important to recognize that the extended timeframe associated with an internal sale also extends your personal liability as it relates to the company. Depending on your financial goals and the profitability of your company, a smooth internal transfer will likely take seven to 10 years.

Owners who choose to sell their companies to key employees or family have personal motives, which are frequently as compelling as their financial objectives. They may take pride in seeing their names remain on the door, giving their children or loyal employees a chance to own what they do, or in providing continuity of a unique corporate culture. The attractiveness of the internal sale process is that it offers owners a great deal of flexibility with regard to roles, responsibilities, compensation, and other deal components.

An internal sale to key employees or family can be a rewarding alternative for all parties. With the strength of the current construction economy, the climate has never been better for developing an internal ownership plan. ■

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