



## A business succession checklist.

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The life cycle of a closely held business can be compared to that of your typical family home. When you are considering the purchase of a home you analyze location, price, size, current mortgage rates and the overall appeal of the home. You have a title search done, radon and termite inspections, and some local authority walks through to make sure the home is structurally sound. The day before you move in the house is immaculate and there are few, if any, apparent problems. The kids haven't put holes in the walls or stained the carpet, the car hasn't leaked oil all over the garage floor, you haven't been late on a mortgage payment, and you haven't discovered as of yet that the neighbor's teenage boy is in a very loud rock band that practices from midnight to three in the morning every other night. Then the joy of home ownership begins - large amounts of debt, landscaping, maintenance, improvements, yard work, etc. But the home serves its purpose - you raise your family there, make a lot of fond memories and build good relationships with neighbors. Then the day comes when you decide to sell your home. You want to get the best price you can for the home. Prior to putting your home on the market you'll make repairs, remove twenty years of clutter, rearrange the furniture, collect all records of improvements made, and try to make it as appealing as possible to a potential buyer.

A business is very similar. Before starting the business the founders analyze location, start-up costs, interest rates, and the overall appeal (potential for earning a profit.) Decisions are made on business structure (C corp., S corp., partnership, etc.), employees are interviewed, shareholder agreements are drafted, etc. The day before you open for business the office is clean, no employees have quit, no customers have sued you, you aren't late paying any suppliers and you haven't discovered as of yet that the "art studio" that is renting the location beside you is really a 24 hour tattoo parlor. Then the joy of owning a business begins - large amounts of debt, maintenance, employee turnover, balance sheets and income statements and many, many working weekends. But the business serves its purpose - you earn enough money to raise a

family, make a lot of fond memories and build good relationships with employees and peers. Then the day comes when you decide to retire and sell the business. You want to get the best price for the business that you can. With all of the planning that went into starting and operating the business, many owners fail to create an effective plan for creating value in the business prior to transferring ownership.

Just as you cleaned house before you put your home on the market, business owners need to "clean house" before putting their business on the market. They need to put themselves in the shoes of a potential buyer. What would a potential buyer (and the potential buyer's counsel) want to see when they inspect your business? Just like the sale of a home, the sale of a business often involves negotiation. Having your "house" in order creates leverage in these negotiations and can have a substantial effect on the amount a willing buyer will pay.

While all businesses are unique, the following list is a sample pre-sale due diligence checklist a potential buyer may go through. Owners should consider the availability of documentation and whether or not improvements can be made in any of these areas prior to the potential buyer's inspection.

## Business Operations and Property Information


- Description of business operations, products, diversity of products, pricing, sales volume, trademarks, copyrights and patents, trade secrets, etc.
- Operating facilities, descriptions, layout, maintenance costs, access to facilities, need for additional facilities, facilities that are under-utilized, potential for expansion, lease and rental agreements, zoning and building code restrictions.
- List of machinery, plant equipment, vehicles, and any other assets necessary for production - include age of property, maintenance costs, insurance coverage, need for additional equipment.
- Real estate - include copies of leases, rental agreements, description of property, zoning information, restrictions and easements, insurance coverage, taxes, cost of maintenance and utilities, advantages or disadvantages of location.
- List of top competitors, competitive advantages and disadvantages, market share.
- List of top customers, diversity of customers, revenue generated by these customers as a dollar amount and percentage of total revenue, special considerations for these customers.
- Marketing and advertising efforts, cost / benefit analysis, results.
- Business licenses and permits required to operate, effective dates and termination dates, method of obtaining.
- Documented history of sales activity.
- Research and new product development efforts.
- Distribution methods.
- Information systems capacity, software and hardware, record keeping systems, need for special training to operate.
- Written business plan with forecasting.
- Trade associations, involvement and activity.
- Press releases issued by the company in the past three years.

## Financial Information

- Historical financial statements (with notes, audits, etc.) for the past five years.
- Income tax returns for the last five years.
- Projected financial and cash flow statements for the next five years (with explanations of assumptions).
- Schedule of bad debt, write-offs, aged trade accounts receivable.
- Inventory, valuation method, finished or work in progress, costs associated with inventory, location, control methods, source of supply (with list of possible alternative sources should supply be cut off), contracts and notable dealings with suppliers.
- Schedule of notes and loans payable for the past three years (with copies of agreements), lines of available credit, personal guarantees and indemnification arrangements, etc.
- Financial information by product line - revenue and gross profit.
- Description of accounting policies.

## Employee Information

- Organizational chart with a list of key employees, compensation, job duties, education and unique skill sets, golden-handcuff agreements, potential successors, stock or stock options granted, etc.
- Census of employees, compensation, job duties, full or part-time, cost of benefits, employee turnover experience, records of performance reviews (including terminated employees), records of outside consultants with copies of employment agreements.
- Details of any employment agreements entered into.
- Company employment policies (employee handbook).
- Qualified and nonqualified retirement plan information, administrative costs, account balances, copies of 5500's and DOL letters, trust documents, summary plan descriptions, etc.
- Benefit information, medical, dental, vision, sick-pay, life and disability - include summaries, cost and experience and claim information.

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- Key man life insurance policy information, include reasoning for amount purchased
  - Pending employment issues, controversies, litigations, union or non-union, EEO and ADA claims, OSHA compliance, etc.
  - Availability of local competent skilled employees for hiring.

### **Other**

- Product liability - open claims and closed claims for past two years, required product standards (government, etc.), customer complaints, warning labels, safety instructions, and warranties.
- Other claims, judgments or court orders against the company, officers, directors, legal costs associated with litigation.
- Toxic substances used.
- Method and availability of waste disposal.

**This list is not an all encompassing list of the items a business owner needs to consider prior to presenting their business to a potential buyer. There may be other items that you should consider obtaining, reviewing and improving upon depending on the nature of your business. This article assumes you are looking for the maximum value in a sale to an outside third party when in many instances it may be best to reduce the value of your business (topic for another article.) As you can see by the scope of this list, it will take time and effort to go through this process in order to present your business in the best light. However, if you take the time and effort in these areas, you will be well positioned to substantiate the maximum selling price for your business interests.**