The M&A Files

Steve Monnington of Mayfield Media Strategies presents a step by step guide to selling your business.

1) Before you decide to sell

In a small company it is normal to make major decisions quickly. However, the results of these decisions can have a major impact on the value of your business when you finally decide to sell or could even make it unsellable. As soon as you establish your business you must consider every major decision, especially if they involve other partners or associations, in the context of how they will look to a purchaser and you MUST make sure that everything is documented legally.

We have been involved with a business that created a complex portfolio that proved too complicated for potential purchasers. As well as their main exhibition which was owned 100%, they had acquired a minority stake in a related but semi-competitive event. There was also a management contract for some more shows, a 50% stake in a publishing company and a travel agency that had been set up to capture the exhibitors travel and accommodation spend.

The publishing business couldn't be sold without the approval of the joint venture partner (which was only given on the proviso that they received more for their 50% than any purchaser would offer) and there was no control over the minority owned exhibition. Management contracts are never valued as highly as owned events because of the risk of non –renewal. The travel agency was a no-go area for potential purchasers.

You must create a logical uncomplicated structure and put non-core business into a separate company. Very few purchasers are interested in non-exhibition or non-publishing business.

If you have both trade and consumer shows, you need to consider that very few purchasers are interested in both, so structure your business so that different parts can be sold off if necessary. Even if you create more than one trade show and you think you may sell them at different times you should also put them in separate companies otherwise you will pay more tax than you need to.

2) Effective management tools and sensible agreements

Effective management tools should be part of any exhibition company regardless of whether or not the business is for sale. However, they do demonstrate to a potential purchaser that you have a well run business and it makes it easier for them to review the likelihood of meeting the forecast revenue for the next show.

Sales Graphs should track cumulative contracted sales revenue on a week by week basis and should show the current year and at least two historic years. If you don't have these graphs in place when to decide to sell your business it is worth going back through the records to recreate them as the graphs provide an immediate visual overview of the year on year growth.

Exhibitor retention rate analysis should track the same years as the sales graphs and in particular should analysis the trend in the stand size and revenue spend of the top twenty exhibitors. It is always advisable to have the key exhibitors contracted for the following year before you approach potential purchasers.

It is vital that agreements provide security for the next show but have flexibility beyond this. Venue contracts should be firm for the next show but with provisional dates for future years. It is important not to sign a multi-year contract as the purchaser may wish to move the show, for example to co-locate it with one of their own events. Supplier contracts must also be short term as the purchaser will want to use his own suppliers if he can gain some economies of scale.

Association support is the one exception to this rule as barriers to entry for competitive events are low and exclusive long term association support is the most effective way of raising the bar.

3) When is the best time to sell?

Timing is a critical factor in a successful sale and given the annual or biennial nature of exhibitions, this requires very careful planning.

MMS often get calls from organisers who want to sell one or more non-core products. Often non-core is code for “it’s now slipped into a loss-making position and we need to get rid of it quickly”.

There is often a strong reluctance to sell an exhibition while it is still generating good profits. However, if a top price is to be achieved it is essential to leave some good growth for the purchaser. So the optimum time in the cycle to sell is when the show is well-established in its sector but hasn’t yet reached the peak of its growth curve.

Once the decision to sell has been made, the next decision is whether to sell before or after the show. Our experience is that the best time to start the sale process is about 2 months before the next edition. At this stage, the forecast revenue should be strongly underpinned by contracted sales. We generally advise our clients to sell just after the show takes place and to invite potential purchasers to see what they might be buying. This is an essential part of their due diligence.

A strong attendance and a good re-sign at the show for next year creates a great momentum for sale. Selling after the show rather than before also means that the seller will keep this year’s profit.

However, some potential purchasers may have a strong preference to acquire just before the show takes place in order that they can announce the new ownership before or during and to use the show to cement key relationships. Starting the sale process 2 months before the show still gives enough time to complete the transaction early if necessary.

4) Preparing the Information Memorandum

The Information Memorandum is as important to the sale process as your marketing materials are to the success of the event you are selling. However the IM must be factual and succinct as potential purchasers are turned off by marketing language and don't like the feeling that they are being "pitched to".

The main purpose of the IM is to provide enough information for purchasers to make a realistic offer and it should provide the history of the event, a snapshot of the current situation and a vision of the future. It should incorporate three years historic financial information, the current year's budget or forecast and a forecast for the following year together with the assumptions behind the forecast growth.

You should avoid the temptation to produce an "acquisition forecast". This is a tactic that is well known to potential purchasers and manifests itself as a forecast for dramatic growth for no discernable reason after many years of flat revenue and profits. This destroys any credibility that the rest of the IM may have.

The other purpose of the IM is to protect the seller from the purchaser re-negotiating the price once they carry out their due diligence exercise and find problems that they weren't aware of. It is important to use the IM to highlight anything that may be an issue to the purchaser. Purchasers like honesty above all else and bad or difficult news is best dealt with at the start.

Many sellers are wary of providing too much information to purchasers who are existing or potential competitors and it is important to strike the right balance. No-one wants to be bombarded with a massive amount of detail. The IM for a single show should be no more than 7 or 8 pages incorporating event focus, financials, association support, key agreements, up to date sales graph, competitive analysis and prospects for future growth.

5) Valuation and Price Negotiation

It may sound a bit corny to say that a business is worth what someone will pay for it but this has never been truer on a recent transaction where the offers ranged from £750,000 to £2.6m. Companies have different methods of valuation and certain buyers may be prepared to pay more if the exhibition is particularly strategic for them.

Most buyers ask for price guidance but they only want to know this so that they don't pay more than the seller is expecting to receive. It is important to let the buyers value the business, knowing that they won't make their best offer straight off. However it provides a good starting point for negotiation.

You will hopefully receive more than one offer for your business and you shouldn't worry about keeping potential purchasers waiting (obviously not for too long) while you assess and negotiate the different offers. However you should be open and honest about the situation so that everyone knows where they stand.

You should also use an intermediary for the negotiation. Buyers are very good at reading emotions and a dispassionate approach could mean a higher achieved price. Using a third party in this way will also give you more time to reflect and to consider the best way to respond without being pressured into an immediate reaction.

Selling after a show rather than before allows you to keep the profits of the show and to base the price on (hopefully) a higher profit than the previous edition. It is often effective as a final negotiation to include an element of earnout – an amount to be paid on future performance. However, unless you are continuing to be in control of the show this shouldn't be a large proportion of the total price.

6) Preparing for Due Diligence

You've prepared an Information Memorandum, had a meeting with a few potential buyers and negotiated a price that you're happy with. Now the hard work starts.

If an acquisition is likely to become derailed it is during the due diligence process. There are usually three parts to the due diligence process. Commercial – which may well include interviews with exhibitors, Financial – which will pretty much involve an audit of your financial results and Legal – to ensure that you actually own the assets you are selling.

Be prepared for your business to be investigated with a fine toothcomb. If the potential purchaser senses any reluctance or resistance to providing information on the business they will become suspicious. However you must ensure that you review the types of questions that the purchaser intends to ask your exhibitors and you shouldn't be afraid of vetoing anything you consider is particularly sensitive. It is also advisable to present these interviews as a customer care survey being carried out on your behalf.

If you have nothing to hide you should provide all the information the purchaser asks for. If there are some problems lurking in the darkness it is essential that you disclose these right at the start as your purchaser will become aware of them one way or another. Most issues are not so critical that they will stop the purchaser acquiring the business, but if problems are discovered by the due diligence process and it is clear that you are aware of them, this will lead to a loss of confidence and the purchaser will start to wonder what else they have missed that you're not telling them about.

The key to a smooth due diligence process is comprehensive, well prepared and well presented documentation.

7) The Legal Process

For the buyer and seller, the legal agreements are the most boring part of the acquisition process but the negotiation of these is another area where it can fail. When choosing a lawyer, don't automatically engage the firm who have acted for you for the last 20 years, especially if they don't have any M&A experience. If you work with a firm with a good track record in acquisition work the process will be much smoother.

Legal agreements are not rocket science but sometimes a pedantic lawyer can make them seem overly complicated so choose someone who has a pragmatic approach and can focus on the issues that really matter.

Once you have agreed the deal with the purchaser, the first document will be the Letter of Intent or Heads of Agreement. You should engage your lawyer right at the start of the process so that they can have some input into this document as it will form the basis of the main legal agreements.

The main agreement will be a Share Purchase Agreement (SPA) or Asset Purchase Agreement if you are selling assets rather than shares. If you are selling less than 100% of the company there will also be a Shareholders Agreement which governs the way the company will be run by you and your purchaser.

Apart from the calculation of the price to be paid, the most crucial part of the SPA is the Warranties. This is the purchasers insurance policy that you are selling something you actually own and that there is nothing sinister that will crawl out of the woodwork. Purchasers become very suspicious if sellers argue too much on the warranties, wondering what they have to hide. Always be open, honest and disclose anything that you think the purchaser needs to know.

It is very rare to have a claim under the Warranties but this is the area where lawyers lock horns and where the process can be de-railed. So, be careful but pragmatic and always keep your lawyer under control. Remember that, although it is his job to protect you, you are the client.

8) Why deals go wrong

Throughout this series we have seen that the key factors for a successful sale of your business are having a great exhibition to sell, being well prepared with the right documentation and being open and honest during the process. All of this seems obvious but I am constantly surprised at the problems we come across during the sale process. Some of the examples below resulted in the purchaser pulling out of the deal whilst with some we were able to keep the sale on track.

The misleading Information Memorandum – The accuracy of the IM is always tested during due diligence and material inaccuracies will be discovered. One business we sold ran a show outside the UK and the owner decided to translate the Euro revenue into sterling at the closing rate rather than the average rate for the year because it gave a higher sterling figure. This was picked up by the purchaser and the deal was re-negotiated

Inadequate key agreements – It is vital that all contracts are as watertight as possible**.** One show we sold was founded by the seller but was effectively created in conjunction with a colleague who handled most of the sales and marketing functions.

During the sale process it emerged that the partner felt he was entitled to 50% of the show even though he had no formal shareholding. His contract didn't include a non-competition clause and because of his links to the sector this was something the purchaser insisted on. In order to get the partners agreement to this, it was inevitable that he was given a share of the proceeds and this long internal negotiation severely tested the patience of the purchaser.

IPR (non) ownership – Rightful ownership of the business you are selling is obviously fundamental but this isn't always clearly defined when an association or a publication are involved in the initial launch. Therefore it is vital to ensure that you don't only own the exhibition but also the name of the exhibition. You should trademark the name if you can.

One exhibition we sold had the same name as the supporting publication. Part way through the sale process the owners of the publication applied for ownership of the trademark for exhibition use. As the support of the magazine was renegotiated on a yearly basis, it meant that if the support agreement was cancelled, the exhibition could no longer use the name.

Disagreement over non-competition agreements – It is perfectly reasonable for the purchaser to expect the seller not to compete with the business they have just acquired.. When the seller argues vociferously against the length of a non-competition agreement (usually around 3 years) and insists on limiting it to 12 months, the purchaser is bound to question the seller's motives.

Sellers will never win this argument as it is just too risky for the purchaser, so accept the non-compete as put forward otherwise the purchaser will pull out.

Negative commercial due diligence – As part of the due diligence process, many purchasers will interview existing exhibitors and will also want to talk to "lapsed" exhibitors to understand why they no longer want to support the show. One of the most compelling pieces of due diligence data is how well regarded the seller is among his exhibitor community.

The flipside of this is that, no matter how good a show you have, if you don't provide good customer service it will inevitably come through as a negative in the due diligence process.

Renegotiation – The purpose of the Heads of Agreement are to agree the key parameters of the deal so that there are no surprises when the main contracts are negotiated. This means that the purchaser expects the seller to stick to the broad financial terms already agreed (and vice versa). Most deals conclude as initially agreed, but sometimes the seller decides to renegotiate on the basis that, if the purchaser agreed to the terms, he should have asked for a higher price.

We had one client who constantly found new ways to try and increase the price. We lost one purchaser because of this and it wasn't any easier to control our client the second time around. We eventually signed the contract and I breathed a sigh of relief. Over a drink to celebrate my client turned to me and said "of course you do realise that Clause 6 will never work and will need to be renegotiated..."

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