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Pre-transaction planning and business readiness

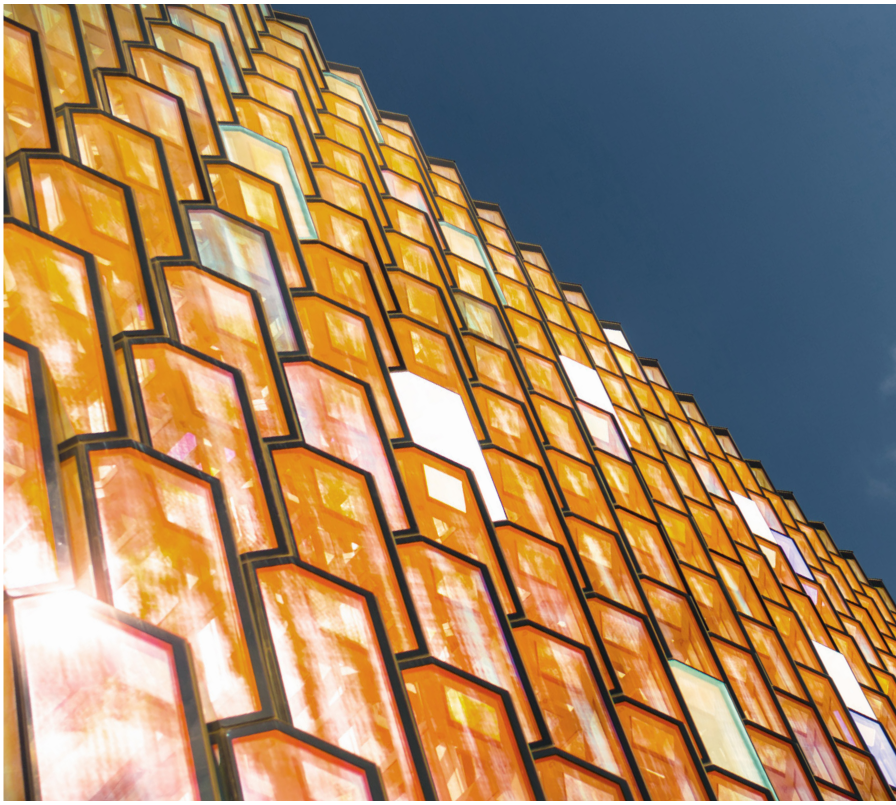
Key considerations for privately owned businesses

Introduction

Planning for a business transaction, transition of ownership, outside capital raise or liquidity event can be an exciting, albeit potentially overwhelming, time for a business owner. Putting together a thoughtful execution plan and preparing the business well in advance can make a big difference when it comes time for the transaction.

Regardless of the path chosen—generational transfer, third-party sale, infusion of growth capital or sale to an employee stock ownership plan (ESOP)—the 18- to 36-month period prior to a transaction provides a critical window to assess the overall state of the business, get the financial house in order and address potential risks. Harmonizing the corporate balance sheet with the shareholders' balance sheet optimizes wealth accretion and tax savings no matter the outcome selected.

In this guide, we've highlighted key topics that can help you shape your approach to selling your business or preparing for a transaction or liquidity event.



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Pre-transaction planning and business readiness best practices

Each business and prospective transaction will have unique characteristics. The topics, considerations and best practices outlined below are a common framework for leaders contemplating a transition or liquidity event in their business.

Financial quality

Companies with high-quality financial information and controls often command a higher valuation.

Best practices:

- Maintain accurate and detailed financial records using consistent accounting practices over time.
- Develop realistic financial forecasts with appropriate supporting documentation.
- Assess when to move to annual audited financial statements and whether to get a quality-of-earnings analysis to enhance financial transparency, reporting and leverage for operational efficiency.

Balance sheet

Critically assess the balance sheet to ensure operating activities of the business are financed efficiently.

Best practices:

- Evaluate opportunities to pay down debt and assess current inventory and account receivables levels against industry standards.
- Find ways to improve the cash-collection cycle and other free cash flow generating activities.

Operational efficiency

Inefficiencies in business operations can strain resources, limit revenue-generating activities and hurt business valuation in a transaction.

Best practices:

- Review core business processes to identify opportunities for improvement.
- Assess and implement cost-effective solutions like technology, automation and controls.

Business risks

Proactively identify and mitigate business risks before a transaction. Enhancing risk oversight strategies can reduce their impact on performance and facilitate confirmatory due diligence.

Best practices:

- Identify the differentiating factors of your business, and how you mitigate risks to ensure downside protection.
- Prepare thoughtful responses or solutions to potential buyers' concerns about business risks, including client concentration, external events, technology and more.

Governance

You may decide to monetize all or a portion of the business, or transfer it to employees or to the next generation. Creating a formal board of directors helps professionalize the business, provide management with oversight and give guidance to your children.

Best practices:

- Consider adding outside directors who bring additional perspective and transaction experience. Outside directors can also help minimize perceived conflicts of interest, such as setting compensation for family members.
- Alternatively, consider an advisory committee of disinterested members. The committee can provide guidance to the board on specific topics, such as operational efficiencies, transactional expertise, financial improvement and fiduciary best practices.

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Transaction advisors

Assembling a reliable team can help you keep the process moving smoothly and ensure that all parties are aligned and focused on your long-term success.

Best practices:

- Start the process with a team of coordinated specialists.
- Consider including the following on your team: an M&A advisor, a corporate attorney, a trust and estate attorney, an accountant and a personal banker.

Succession planning

Buyers are often interested in the strength and continuity of the existing management team. A cohesive succession plan is a valuable asset for prospective buyers.

Best practices:

- If retaining the business multi-generationally, consider making a wealth transfer plan that incorporates the latest tax planning.
- Consider key management roles and how those might be replaced, upgraded or eliminated as you grow or move through a transaction.
- Consider retention plans to protect sensitive information, align incentives and provide security to key personnel through the sales process.
- Consider implementing a "double-trigger" acceleration of equity grants, which can help retain key personnel and align everyone's interests, including those of future family owners.

Personal estate planning

Properly implementing a pre-transaction plan ahead of a business transaction may lead to significant wealth transfer benefits and support post-transaction goals.

Best practices:

- Consult with your Private Baker to update your wealth plan and discuss the impact of a transaction on personal goals.
- Talk to your trust and estate attorney to identify and implement wealth-transfer strategies. These strategies may be even more tax-efficient if you transfer interests in a private company, as those shares may receive discounts due to their lack of control and marketability.
- Consider moving assets off your balance sheet in a tax-advantaged manner. This has the potential to turn a good sale into a great one and doesn't require any additional sales proceeds.

Private Business Advisory Solutions

Effective pre-transaction planning and structuring can start as early as 36 months before the transaction. At J.P. Morgan, we have a range of experts to assist throughout the process and a specialized team to help you bridge the intersection between your business and personal wealth goals. We bring an objective and long-term perspective to provide you with the advice and capital that you need to support an upcoming growth opportunity, complex transaction or governance decision.

To learn more, connect with a banker.

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