Selling Your Business: 12 Mistakes to Avoid

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Business owners who run their own companies make huge investments of time, money, and expertise to make their businesses successful and should be able to reap the maximum reward when they sell their businesses. In over 25 years advising owner-managed businesses, I have found that to do so, sellers of such businesses, both large and small, must avoid these mistakes:

1. **Not considering tax advantages.** There are significant tax advantages available to vendors of shares in certain types of incorporated businesses. The ability to multiply this preferential tax treatment by involving the owner-manager's family members should be explored and if appropriate, put in place years before a possible third-party sale. This may entail estate freezes, holding companies, and family trusts. The corporate records of the business should be kept current and accurate throughout these transactions.

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2. **Not making goodwill an asset of the business before selling.** Goodwill, the intangible contribution of reputation, customer loyalty, business relationships, etc., is often vested solely in the owner-manager who is selling. When the owner-manager is gone, there is no goodwill to sell. The goodwill must be made an asset of the business and become part of its core infrastructure by putting in place formal processes such as business agreements and contracts that will have a value when the business is sold.
3. **Not looking at your business through a buyer's eyes.** Owner-managers focus on running their businesses. A buyer will look at a business to identify its soft spots and then use them to negotiate a reduction in the purchase price. Such soft spots should be identified well in advance of any possible sale by the owner-manager's legal, financial, tax, and accounting advisors and then addressed or minimized as much as possible.
4. **Not securing your business' intellectual property.** The business' brand, the names it trades under, and its logo should all be protected by trademark registrations so that they have value in the sale.
5. **Not having written employment agreements with key employees.** The legal relationship of the business with its key employees should be documented in written employment agreements containing, where appropriate, enforceable provisions preventing departing employees from competing or soliciting clients of the business.
6. **Not completing due diligence on a would-be buyer.** A seller should always investigate would-be buyers, confirming that they are who they purport to be and that they have the financial wherewithal to complete the proposed transaction.
7. **Not having a confidentiality agreement in place before disclosing confidential information.** It is essential to enter into a legally enforceable confidentiality agreement with the potential buyer before disclosing any financial or other confidential information about the business. Without such an agreement in place, the potential buyer may be able to use the information to the disadvantage of the seller.
8. **Not signing a letter of intent before negotiating a formal sale agreement.** Once the confidentiality agreement is in place, the key business terms should be set out in a letter of intent or memorandum of understanding and signed by both parties. The letter of intent protects both parties and provides safeguards during the negotiation of a formal sale agreement.
9. **Not negotiating a non-refundable deposit.** The letter of intent should require a non-refundable deposit to cover the seller's expenses should the deal fall through, since the seller will likely be restricted from being able to pursue other sale opportunities while negotiating with one buyer. The deposit is sometimes known as a termination fee.
10. **Not taking adequate security for financing the purchase price.** A seller who finances a portion of the purchase price is making a loan to the buyer and must therefore think like a bank, which would consider obtaining personal guarantees, sworn net-worth statements, mortgages on real property, letters of credit and security on personal property from both the buyer and the individuals and entities with which it is affiliated.
11. **Not capping potential liability.** Things can go wrong in any transaction. Sellers should limit their possible exposure by ensuring that the sale agreement includes a cap on any potential liability the seller might face under the agreement.
12. **Not including a "deductible" provision in the sale agreement.** After closing, a buyer may bring a claim against the seller for compensation for damages the buyer may claim to have suffered on account of the seller's breach of a representation or warranty. To reduce the likelihood of a claim, the seller should negotiate a provision in the sale agreement requiring the buyer's loss to be over a certain minimum amount before any such claim can be brought against the seller.

Mistakes like these can be avoided by seeking and following professional advice well in advance of a sale and throughout the sale process. Lawrences has decades of experience in providing this kind of advice.

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