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Sell-Side Due Diligence: Maximizing Value in the Sale Process

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The divestment of a business to a strategic or private equity acquirer, either in its entirety or through a “carve-out” of existing assets, is a common path for business owners looking to transition ownership.

The sale process, however, can be complicated and tedious for a seller and its employees. Maximizing value from the sale while also enduring minimal operational disruption can be challenging.

For a smooth and successful sale process, sellers should consider partnering with a qualified third-party due diligence provider. The transaction experience and expertise provided by such professionals can better prepare sellers navigating the complexities of the sale process.

What is sell-side due diligence?

The goal of any seller is to successfully close a transaction at the highest valuation possible while ensuring a quick sale process with minimal business interruption. In today's increasingly competitive merger and acquisition market, this requires significant preparation and investment on behalf of a seller. A seller that takes the time to perform sell-side due diligence – a full assessment of its own business – in anticipation of a sale is much more likely to achieve its goals.

Engaging a third-party due diligence provider to perform sell-side due diligence allows for an objective view of the seller's business and financial performance through the lens of a buyer, well in advance of a buyer's due diligence. Throughout the sell-side due diligence process, the due diligence provider performs procedures similar to those of potential acquirers. This trial run prepares the seller for what to expect during the buyer's due diligence process and gives the seller an opportunity to address shortcomings and potential business risks that might affect negotiations with a buyer prior to the sale. A seller that has a complete understanding of the financial, operational, and strategic aspects of its own business will more likely experience a successful transaction.

The focus of sell-side due diligence includes a quality-of-earnings analysis of the seller's historical earnings, which allows for adjustment and validation of the recurring earnings required for valuation. In addition, sell-side due diligence includes analysis of the seller's assets and liabilities, working capital trends, the seller's customers, the seller's products and services, and other key performance metrics. This process helps sellers identify any potential issues a buyer might encounter, including financial or accounting irregularities, financial reporting concerns, and any industry-specific impacts to the business's financial results.

The sell-side due diligence findings typically are summarized in a report that might be provided to prospective buyers on behalf of the seller. This report provides information and analysis similar to what is sought by potential acquirers and is intended to mitigate the additional work buyers will require. It also serves to identify key transaction considerations and risk areas for the buyer, to expedite the due diligence process.

In addition to preparing a third-party report, a sell-side due diligence provider also might provide other services throughout the sale process, as required by the seller. These services can include preparing data-room documents, directly responding to buyer requests and inquiries, coordinating with other advisers of the seller, and providing insights related to the sale and purchase agreement between buyer and seller.

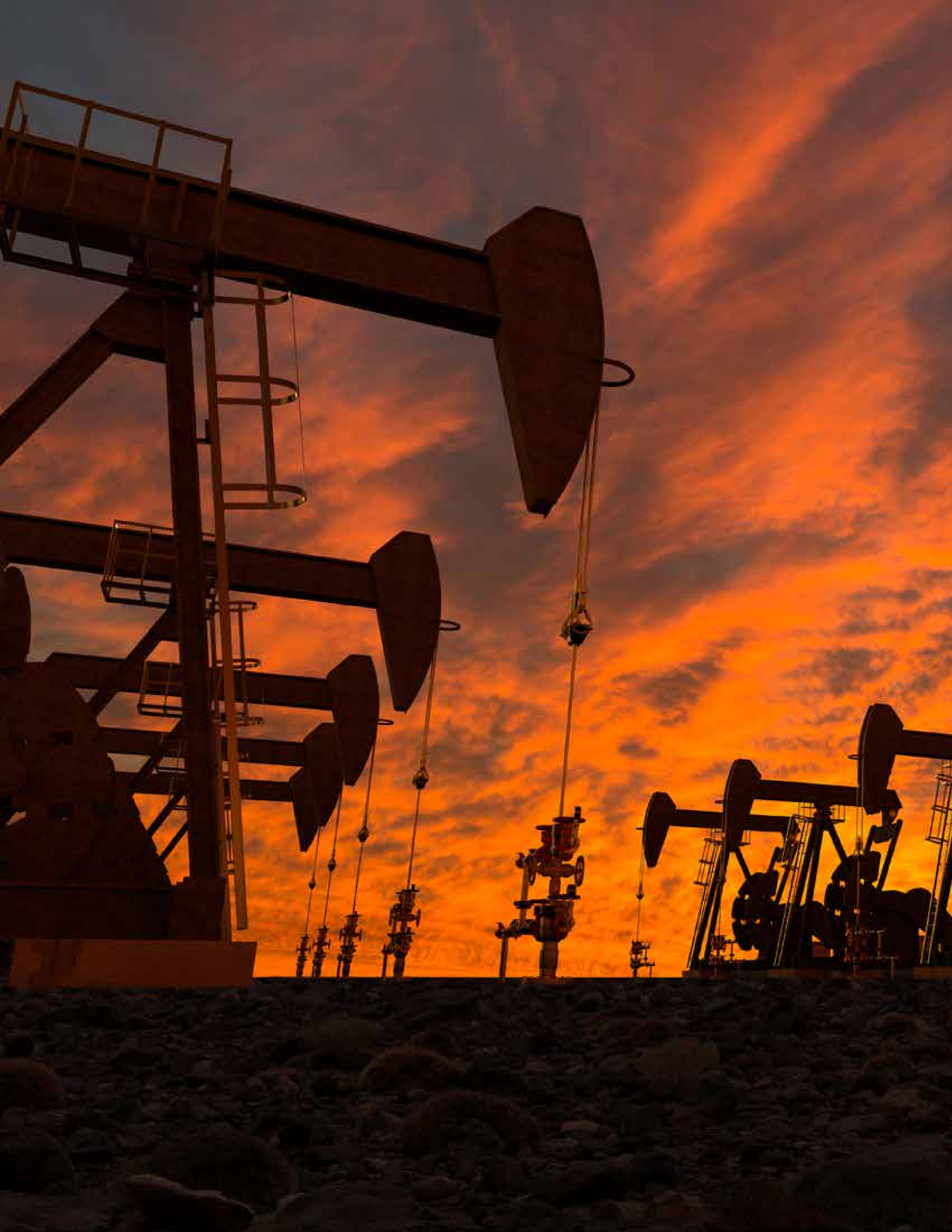
Benefits of sell-side due diligence

The sell-side due diligence process can provide benefits to both the seller and prospective buyers, resulting in an expedited sales process and successful transaction closing.

Sellers benefit because the financial and operational results provided to buyers already have been vetted and analyzed by the third-party sell-side due diligence provider. Sellers will have more confidence in the data and responses they might provide to buyers because objective third-party professionals already have performed similar work. Essentially, third-party sell-side due diligence does a large part of the work for the seller, and that is why it is so valuable to today's businesses, which often are operating with limited resources and might have neither the time nor the staff to adequately prepare for a sale process. The sell-side due diligence provider might assist the seller with:

- Specific accounting and financial reporting topics
  - Identifying, understanding, and vetting potential earnings before interest, taxes, depreciation, and amortization (EBITDA) adjustments that affect the seller's quality of earnings
  - Establishing a normalized level of working capital required to operate the business
  - Understanding the transaction implications of complex accounting topics
  - Assessing net debt and debt-like items subject to negotiation
  - Providing strategic advice in the presentation of historical financial results and the drivers of change in these results
- Specific operational areas
  - Understanding the performance of international operations, complex organizational structures, and differences between business units
  - Understanding the pro forma impact of facility, employee, or other structural changes that might have occurred in the business
  - Understanding the trends in revenue and profitability of products, customers, or locations using advanced data analytics

Numerous benefits exist for the buyer, too. As the seller is better prepared and able to quickly respond to a buyer's questions and requested information, the buyer might experience fewer inefficiencies and negative surprises during its due diligence. This will allow for an expedited sales process, with minimal deadlines missed. Additionally, it will enable the buyer to focus its efforts on the operations of the seller's business, which will help facilitate a successful transition period post-closing.



The sell-side due diligence process

The sell-side due diligence process includes three main phases:

1. **Preparatory phase.** During the preparatory phase, the third-party due diligence provider follows a due diligence process similar to the one a buyer would be expected to follow during its due diligence, including providing data requests to the seller, due diligence procedures and supporting analysis, and interviews with the seller's management team. The due diligence provider also typically prepares the formal due diligence report at this point in the process.
2. **Go-to-market phase.** In the go-to-market phase, the due diligence team might provide strategic advice to the seller and its financial advisers. This often includes input into the financial results presented within the seller's offering memorandum prepared by the seller's financial advisers. The due diligence report created during the preparatory phase also might be provided and discussed with potential acquirers. Additionally, the due diligence provider can assist with preparing various data-room documents to be provided to buyers.
3. **Acquirer assistance phase.** When buyers begin to express interest in acquiring the business – either prior to or after an executed letter of intent – the third-party due diligence provider can help the seller respond to buyer questions and requests for data or provide strategic advice. In addition, the due diligence provider can assist with review of the sales and purchase agreement prior to the transaction close.

Consider a third-party due diligence provider

Sale of a business can be a lucrative transition strategy for business owners. Preparing for a sales process, however, can be complicated and time-consuming for sellers. To maximize value from the sale while increasing the certainty of closing, sellers should consider the services of a third-party due diligence provider that can assist throughout the sale process.

Learn more

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