The way out

Selling can be a distressed company's best option

Financially distressed companies whose condition has deteriorated to the point where they can no longer keep up with current bills have few survival options. If there's any chance of getting an injection of short-term liquidity, such as cash from a private equity firm or new minority investor, a troubled company should seriously consider it.

More often, however, distressed companies that don't liquidate try to sell. But selling a distressed company is a delicate operation. Sellers must protect owners' and shareholders' interests while remaining flexible enough to attract a buyer.

Framing the sale

Before entering the M&A marketplace, distressed sellers need to obtain an accurate, current assessment of their companies' condition from an outside financial expert. Not only does this assessment help you understand your options and adjust your expectations to the facts, but an assessment can help you develop a "narrative" for your sale.

For example, your company might be burdened with obligations such as maturing loans you can't repay, but, at the same time, you're still generating revenues in an industry with considerable growth potential. When reaching out to potential buyers, acknowledge the debt, but highlight and accentuate your consistent or growing revenue stream.

Preparing for scrutiny

Before you start looking for buyers, you need to prepare your company for scrutiny. If at all possible, try to clean up your balance sheet. This includes getting current on accounts payable and receivable, and then tallying the remaining debt.

Whatever you do, don't use stalling tactics such as ignoring vendor invoices. Bad-faith practices will harm not only your reputation, but also your odds of finding a good buyer.

Next, draft a proposal for prospective buyers. In addition to listing assets and advantages, your proposal must be candid about current conditions; any negatives will come out during the due diligence phase. Plus, when you're open about the company's weaknesses, a prospective buyer will likely be more willing to believe that you've accurately stated your strengths.

Controlling the process

With distressed companies, a speedy and efficient sale is critical. That said, you want to avoid being overrun with "tire kickers" — prospective buyers who are mainly looking for a fire-sale price and will make lowball offers they hope you're desperate enough to take.

So while a "cattle call" offering is likely to draw the largest pool of potential buyers, a significant portion of that pool is likely to be unappealing. And by opening bids to all buyers, you could waste countless hours allowing them to examine your books and ask questions. The better option is to limit offers to a short list of buyers who agree to an abbreviated due diligence period.

In exchange, you can offer them concessions, such as agreement clauses that allow them to terminate the deal if certain financial conditions aren't met.

Making your list

What types of prospective buyers should you add to your short list? It depends on several factors, including:

- The financial condition of your company,
- How quickly you need to sell,
- Business-related goals, such as enabling longtime employees to keep their jobs, and
- Personal goals, such as realizing a sale price that will provide you with adequate retirement income.

For example, if you need to sell quickly, but not immediately, and one of your priorities is to sell your company to a buyer that will respect its culture, you might look at similar-size companies that produce related goods and want to expand their product offering.

Also, it's important to target buyers that have made an acquisition part of their long-term strategic plan and aren't simply jumping at an opportunity for which they haven't prepared. Such mergers are rarely successful. Finally, ensure prospective sellers have the cash or financing to make a deal. Credit is still hard for most companies to come by — particularly for risky acquisitions.

Managing under fire

Although many companies are in the same leaky financial boat, each distressed business must address a unique set of challenges. Good advice from an experienced M&A professional is essential if you want to find a buyer willing to help you make the best of a bad situation.

Don't neglect full disclosure

When it comes to selling a company, the devil's in the details — particularly when it comes to financially troubled businesses. Distressed companies are more likely to harbor financial and legal surprises — and their buyers are more likely to be wary of incomplete records or evasive answers.

To ensure you're telling prospective buyers everything they need to know to make an offer, provide them with information regarding:

- Outstanding debt obligations, listing all upcoming bond or loan maturities.
- Historical financial performance, particularly if it provides a contrast to your company's current financials.
- Key tangible and intangible assets, with estimates of their liquidation values.
- Major customers and important client relationships, emphasizing those that may represent cost savings if their contracts were renegotiated.
- Analyses of all outstanding litigation claims or regulatory violations.