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### **Spring Cleaning For Businesses**

This isn't about going through your files or cleaning out the office. This process is a bit more important than that and could even be titled "*Customers we should fire!*".

One of the things all businesses SHOULD do, and most don't do often enough, is to evaluate all customers. Evaluate how? Is the work done for each customer profitable? Revenue is obvious. Cost data is required, and if you don't have it, you need it. It's not just needed for this exercise, but always. Evaluating all direct costs is essential when determining if price increases or decreases are warranted?

After gathering data, compare / rate customer profitability. Which customers contribute more, and why, and can profitability be improved for all customers, not just those contributing less. Take a look at how the customer pays as that's also an important factor.

The G&A factor. That's short for Grief & Aggravation! What do we do about each difficult customer? Which customers are a pleasure to deal with? Which customers should we ask to go elsewhere? That's never an easy decision and rarely if ever made soon enough. It takes analysis and knowing that it's necessary to take a thorough review of all aspects of each customer.

Here are a few examples that are known to the authors that reinforce the above:

A metal plating & anodizing business owner called his banker and said that six months ago they contacted their largest customer about a price increase. The customer demanded

### **LACK OF NEGOTIATION FLEXIBILITY**

Negotiations in the sale of a business are never easy. You need to be prepared for an emotional roller coaster ride. In small business sales, in most instances, negotiations are between a first-time buyer and a first-time seller. The negotiations typically involve the biggest and most important transaction of both parties' careers. And both parties are usually Type A personalities, further complicating the ability to reach an agreement.

#### **Type A personalities**

Here's how Wikipedia describes Type A personalities: "The theory describes a Type A individual as ambitious, aggressive, business-like, controlling, highly competitive, impatient, preoccupied with his or her status, time-conscious, and tightly-wound. People with Type A personalities are often high-achieving "workaholics" who multi-task, push themselves with deadlines, and hate both delays and ambivalence." Does that describe you pretty well? That same description will also likely apply to the buyer of your business. Both parties are used to "having it their way." In light of that, it is not surprising that business sale negotiations are so difficult to conclude successfully.

#### **Preparation - The key to successful negotiations**

As emphasized in other issues of this newsletter series, preparation is the key. Hopefully, the first two paragraphs of this newsletter help you understand the need to be flexible. Imagine trying to negotiate with yourself! Thorough preparation before selling your business can help minimize the likelihood of contentious negotiations. Especially by pricing the business reasonably and disclosing known negative issues up front, you can eliminate the source of major problems. Overpriced businesses and known but undisclosed "skeletons in the closet" are major hurdles that usually result in failed negotiations. The good news is that those issues are within the seller's control and can be addressed early on in the process.

#### **Typical areas of unresolved issues that require negotiations**

Assuming you've done so, there will still be numerous areas of unresolved conflicting interests that will require negotiations. In addition to price, following are examples of other unresolved issues open to negotiation: undesirable due diligence requests (asking to speak with employees or customers), the structure of the sale (asset sale vs. stock sale), non-compete agreement terms, consulting/training agreement terms, purchase price allocations, seller financing requests from the buyer, terms of seller financing and security, accounting measurement issues (such as work-in-process or inventory), earn-out terms (contingent

lower prices and ultimately left for another manufacturer. The banker asked how the business was doing since losing their largest customer. The owner replied, "Now we're making money"! When asked "why", the reply was that the customer that left produced virtually no Gross Profit, and with them gone, they were able to provide better service to other customers and as a result, earned more business with better margins.

Another manufacturer produced mostly low-volume parts that were labor-intensive. They secured a new, large-volume parts order that required automation. They quickly invested in an automated, high-volume production line to accommodate this order. Since the new production line took up a large percentage of floor space, the company decided to notify some smaller customers that they could no longer easily complete their orders. Some of these customers left and others accepted price increases that in some cases were over 50%. The price increase more than compensated for the increase in manufacturing time and effort. The frustration part is that prices likely could and should have been raised prior to this point.

Reviewing your customers should be a continuous endeavor, but unfortunately rarely is. Making tough decisions about customers almost always improves business performance. No matter what your business goals are, perhaps to sell at some point in the future or just to be stronger, "Spring Cleaning" is needed.

If you would like to know the value of your business and get some ideas of its strengths or weaknesses, or if you might consider selling or buying another business, feel free to get in touch to discuss your options. And as always, with no obligation!

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portion of a purchase price); language of representations and warranties made by the seller in the definitive documents, etc.

### **Resolving Issues**

The key to successful negotiations is to maintain flexibility. Recognize your Type A personality and subdue your urges. Be patient, do not be overly aggressive or controlling and most importantly - listen. Try to determine why particular aspects of the terms being negotiated are important to the buyer. Ask him to explain his reasoning. Listen.

Then create a list of unresolved issues and determine which of the items remaining to be resolved are most important to you. Explain to the buyer why certain terms are so critical for you. Determine which of his important issues you can compromise on, subject to his willingness to compromise on your important issues. Let the buyer know you are interested in a win-win situation where both parties feel good about the negotiated settlement. It may take several rounds of open communication to resolve all issues, so maintain your patience.

Depending on the nature of issues and where you are in the sale process, your intermediary can handle most of the communications in negotiations. In most instances, it's better to present solutions in writing - through formal offers and counteroffers. At times, you might consider face-to-face negotiations, but always include the broker as a buffer in case things get explosive. If you can't work things out face to face, a good intermediary might still succeed in helping the parties to find mutually acceptable terms.

### **Use your attorney as an advisor, not a negotiator**

Although you've probably involved your attorney prior to the writing of the definitive documents, it is imperative to control your attorney at the final stage. Use your attorney as an advisor, not a negotiator. Many attorneys tend to try to dominate in negotiations, and when negotiations occur between the lawyers for the buyer and seller, both cannot dictate the terms. As in the negotiations between buyers and sellers, solutions need to be "win-win".

Every business sale transaction has risks on both sides. Tell your attorney up front that you want to understand the risks, but you also want to make a deal. Let him know you intend to be the decision-maker on any contentious issues. As opposed to communicating directly with the buyer's attorney, ask your lawyer to communicate through your intermediary.

### **Concluding thoughts regarding negotiations**

A few concluding thoughts: Often your first offer is your best offer. Take the time to give that first offer serious consideration and counter the offer with terms acceptable to you. And finally, almost every deal will seem hopeless several times during negotiations regarding the offer, due diligence and the definitive documents. Don't give up. With patience and a good intermediary, most issues can be resolved to reach a successful sale.

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**NEXT ISSUE**  
Controlling Emotions

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