Beyond the financials

Historical balance sheets tell buyers about a company's tangible assets, acquired intangibles and debts. But some liabilities may not appear on the financial statements. Examples of unrecorded liabilities include:

- Pending lawsuits and regulatory audits,
- Warranty and insurance claims,
- Uncollectible accounts receivable, and
- Underfunded pensions.

Hidden liabilities can be a major issue in stock sales. Unlike asset sales, in which the buyer cherry-picks assets and liabilities to acquire, stock sales transfer all the outstanding shares of stock to the buyer, and the business continues to operate uninterrupted. From a legal perspective, that means the buyer may be vulnerable to future lawsuits, such as employee discrimination or intellectual property claims that relate to conditions that existed before the deal closed.

Some issues, like broken equipment or obsolete inventory, can be unearthed only with a physical observation, so it's important for buyers to tour the company's facilities with any outside experts that are hired to help conduct due diligence.

Buyers also need to be skeptical of representations the seller makes to seal a deal. Misrepresentations that are found after closing can lead to expensive legal battles. An earnout provision or escrow account can be used to reduce the buyer's risk that the deal won't pan out as the seller claimed it would.

Hire a business valuation expert

Mistakes can be costly in M&A. Many private business owners are inexperienced when it comes to these complex deals. So, it usually pays in the long run to hire an outside business valuation expert to help evaluate the deal.

Do you have a
Question?
or want to speak to

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