Transition Time

Five ways to improve your startup exit strategy.

BY MATT MEDLIN

STARTUP ENTREPRENEURS are right to focus their time and energy on creating the great products and services that will build a company to its best exit point, whether it's an initial public offering (IPO) or a strategic acquisition. However, they should also understand how operational matters can affect a company's attractiveness to buyers, public or private.

By the time an exit is on the horizon, buyers, banks or investors will all ask you serious questions about how you manage risk, predict your finances and maintain compliance. You want to have convincing — and accurate — answers ready. Here are five ways you can help keep an exit on your terms as much as possible.

1. UPLEVEL YOUR CONTROLS. Is your company spending tracked and audited? Is your revenue recognition policy up to snuff? These types of controls are critical to maintaining a clean set of books. Uncertainty about financials is the last thing buyers want.

2. HUNT DOWN LIABILITIES. Buyers love to find unseen liabilities because it gives them negotiating leverage. One example we often see is uncollected sales tax. Early-stage companies often ignore their tax collection obligations in other states because the firms are small or because they misunderstand the rules. Once revenue starts rolling in, that bill can add up, and it can easily attract attention from your buyer's accountants or state tax authorities. At the very least, you should be tracking this issue so you know the level of risk.

3. GET YOUR SYSTEM RIGHT. Small-business accounting programs are great for emerging businesses. But they're a long way from the Fortune 500 accounting systems. Luckily, you can evolve into a system that's right for your company. Will you need foreign currency translations? A system that supports multiple lines of business or multiple simultaneous users? At minimum, review what you're using and see if this is the right time to upgrade.

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4. POLISH YOUR CRYSTAL BALL. OK, so you can't see the future, but you will be expected to demonstrate and defend your revenue and earnings projections. At some point, you'll have to look beyond short-term cash flow. If you have good data about where revenue will come from and where expenses will go, buyers will have more confidence.

5. AUGMENT YOUR ADVISER GROUP FOR AN IPO. If you are headed toward an IPO, you'll need specialists. The law firm you're using today might not handle IPOs. A similar situation prevails in accounting. According to Audit Analytics, the Big Four accounting firms (Deloitte, EY, KPMG and PwC) audit 99 percent of Washington public company revenue.* If you are close to an IPO, connecting with one of these firms is essential. Your existing CPA firm can be instrumental in guiding the IPO transition and assembling the array of documents and analyses that need to be created.

The takeaway is that you should augment your adviser team a year or so before an IPO to make sure you have the right resources in place.

Plan your exit.

There's no need to panic. If you're just starting a company, you shouldn't overinvest in controls, and flexibility can be a competitive advantage. Most exits become clear within a year or two of actually happening, so you have some time to get your ducks in a row. With focus, when you're getting close to an exit, your company will be ready to step up to the next level.

**For the most recent fiscal year reported as of July 31, 2015*

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