

FOR EXECUTIVES SEEKING TO BUY, SELL, OR RECAPITALIZE BUSINESSES

## **Can You Afford To Employ A Dual Agent In A Business Sale?**

The pitfalls of hiring a dual agent in a business sale transaction

Most people have heard of dual agency in the context of a real estate transaction and have some awareness of the issues surrounding dual agency. In spite of the inherent conflict of interest, many people do not mind transacting residential or commercial property using a dual agent. The reason is pretty straight forward – while there is risk of not getting good representation, the downside is typically small. Property values are driven by comps and cap rates and in most cases, the amount of money left on the table is a small percent of the transaction value. The commodity nature and relative liquidity of real estate also helps make buyers and sellers comfortable with the risk level.

But does this logic apply to business sale transactions? Businesses, compared to real estate, are illiquid and the valuations and the ultimate closing prices vary dramatically from business to business. The deal amount can also change dramatically through the duration of a deal. In Business sale transactions, not having a fiduciary agent working for you can cost you plenty.

Let us start with an explanation of “fiduciary duty”. An agent used to represent a buyer or seller in a business transaction has a fiduciary duty. A fiduciary duty is the highest standard of care imposed at either equity or law. A fiduciary is expected to be extremely loyal to the principal. Among other responsibilities, a fiduciary must not put their personal interests before the duty and a fiduciary must not profit from the fiduciary position without express knowledge and consent of the principal. A fiduciary also has a duty to be in a situation where there is no personal conflict of interest and where there is no conflict of interest with another fiduciary duty.

In light of large sums of money at stake in a business transaction and these fiduciary responsibilities, let’s look at the three key issues faced by a dual agent in a business sale.

### **1. Conflict of Interest**

This is by far the most obvious and most damning part of being on both sides of a business sale transaction. A business intermediary is obligated to serve the best interests of his or her principal. Buyers and sellers by definition have conflicting interests. Who should the intermediary be loyal to? Is the agent looking after your best interests? Some agencies will tell customers that they will assign separate individuals to the buying side and selling side and create a Chinese wall.

*In practice, the wall between the two sides in the same company, even in a large company with processes to cover this type of conflict of interest, let alone a typical small to mid market intermediary, is more akin to a sieve than Chinese wall. An agency in this situation is in violation of the standards of being a fiduciary.*

## **2. Advocacy**

Any competent agent will tell you that, when two principles' interests are in direct conflict, the agent cannot advise, advocate, or give allegiance to either party if such counsel gives one party an advantage over the other. Not remaining neutral or showing favoritism would be illegal and can make the agent liable to potential damages. A careful dual agent would shun the risk of advocacy and will tell you that they will be extremely careful to represent both parties equally and fairly. In other words, both parties lose "advocacy" for their best interests! Is this what you pay your agent for? Wouldn't you rather pay an agent that advocates *your* interests?

*In practice, providing equal service to two parties is difficult and, even if the agent is highly ethical, agent's biases and self interests may tip the scales in difficult situations.*

## **3. Sensitive Information**

A business sale can take an extended amount of time and the seller or buyer may experience one or more personal events which, while not affecting the performance of the business being transacted, may have substantial impact on the negotiations. The agent may become aware of this sensitive information which, if disclosed to the other party, could harm one party and benefit the other. If the agent has one principal, clearly the agent will develop a strategy to minimize the impact to the principal. How does a dual agent handle this type of information about a client? Would you trust your sensitive information with a dual agent?

*In practice, the agent ends up playing favorites or in a worst case scenario, one or both of the parties' interests are sacrificed in the interest of "getting the deal done".*

**Summary:** Business sellers and buyers need to carefully pick their agent in a business sale transaction. Providing equal service to both clients is practically impossible in most deals. In the best case scenario, neither the seller nor the buyer is getting an advocate. In the worst case scenario, one or both of the parties are being sacrificed. For this reason some states do not permit dual agency. Much can be lost by employing agents who put themselves in the position of being dual agents and thus not living up to the fiduciary standards.

*For most business owners, a business sale is a once in a lifetime event with significant impact on how well the family's nest egg is feathered. With so much at stake, can you afford to employ a dual agent?*

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