TRANSACTION ACCOUNTING

What Your Books Need to Look Like Before an Acquisition

Whether you are selling your company, raising a growth round, or acquiring another business, the condition of your accounting records is one of the most controllable factors in how the transaction goes. Here is what sophisticated buyers and investors look for — and what creates deal risk.

The Standard Buyers Apply to Your Books

Most business owners spend years building a company worth acquiring and very little time preparing the financial records to survive the scrutiny that comes with it. Sophisticated buyers evaluate your books against a specific standard: would these financial statements hold up under audit? The elements of that evaluation are reliability, completeness, documentation, and consistency.

> *Every accounting issue a buyer finds in diligence becomes leverage. Every issue you find and remediate before going to market becomes preparation. The work is the same — the timing determines whether it helps or hurts you.*

The Six Areas That Most Often Create Deal Risk

1. Revenue that is difficult to reconcile

If a buyer cannot trace your revenue from the contract to the invoice to the cash receipt to the GL entry, they will assume the worst about what they cannot trace. Revenue reconciliation — a schedule that ties the contract backlog to recognized revenue, deferred revenue, and cash collected — is one of the first things a sophisticated buyer will build. If you build it first, you control the narrative.

2. Understated liabilities

Understated liabilities are the most common source of working capital adjustment disputes. The most frequently missed: accrued payroll and PTO, sales tax obligations in states where you have nexus but have not been filing, deferred revenue that was billed but not recognized, and warranty obligations that have not been estimated. A buyer's diligence team will reconstruct your accrued liabilities from your contracts, payroll records, and tax history.

3. Accounts receivable that will not collect

Buyers test AR aging in detail. Invoices over 90 days, credit memos issued after period end, and receivables from customers with known disputes will be scrutinized. If your allowance for doubtful accounts does not reflect the actual collection risk, the buyer will haircut the AR balance in their model — and in the purchase price.

4. Owner-dependent or unsustainable adjustments

Quality of earnings analysis will identify non-recurring revenue, owner compensation that is not at market, and expenses run through the business that will not continue. These are normal in a closely-held company. The risk is not having them — it is not being able to explain and document them before the buyer's accountants identify them as findings.

5. No audit or review history

If your financial statements have never been audited or reviewed by an independent CPA, buyers will apply a risk premium to every number. An audit or review performed before going to market is almost always worth more than it costs in terms of purchase price credibility.

6. Accounting complexity that has not been addressed

Leases not evaluated under ASC 842. Revenue streams not analyzed under ASC 606. Equity compensation not measured and expensed. Intercompany transactions not eliminated or documented. These are not unusual for a company that has been growing quickly with a lean finance team — but they create significant diligence findings when discovered.

How to Prepare: A Pre-Transaction Accounting Checklist

Step	What It Involves	Why It Matters in Diligence
Reconcile the balance sheet	Every balance sheet account reconciled to a supporting schedule with no unexplained items	Buyers test reconciliations. Unreconciled balances are either errors or fraud risk.
Document revenue recognition	ASC 606 policy memo, contract population listing, and deferred revenue tied to contracts	Revenue quality is the first question in every QoE. Have the answer ready before it is asked.
Assess your accrued liabilities	Rebuild the schedule from your contracts, payroll records, and tax history	Missing liabilities become purchase price adjustments. Finding them yourself gives you options.
Review your tax compliance	Sales tax nexus analysis, payroll tax filings, and income tax returns reviewed for completeness	Tax liabilities discovered in diligence are typically escrowed or deducted from proceeds.
Document accounting policies	Written policies for revenue recognition, expense capitalization, depreciation, and significant estimates	Undocumented policies create the perception of inconsistency.

Prepare normalized financials	Three years of income statements adjusted for owner compensation, non-recurring items, and non-business expenses	Buyers build this themselves — if you build it first, you control the starting point.

The Bottom Line

The condition of your accounting records is a transaction variable — as controllable as your lease terms or your customer concentration, and more controllable than your market conditions. Companies that invest in accounting preparation before a transaction close at higher prices, with fewer adjustments, and in less time.

Preparing for a transaction? Start with the books.

VAO CPA helps companies on both sides of a transaction — sellers preparing their financial records for diligence, and buyers evaluating what they are actually acquiring.

contact@vaocpa.com · (832) 542-6229 · vaocpa.com