



MidMarketCapital, Inc.

Business Sellers – Don't Allow the Process to Derail the Deal

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Most business owners sell only one business in their lifetime. It is complex, emotional and pressure packed. Given this backdrop, the odds of a great outcome are, well, not that great.

As Merger and Acquisition advisors, one of our most important functions is to prepare our client for the bumpy road ahead. The worst outcome is to go through the exhaustive process of marketing the business, corporate visits, and due diligence, only to have the deal crater in month eight because of some ruffled feathers or perceived bad faith dealings.

First we try to make the seller understand that as the process unfolds and as the buyer tries to memorialize the parties' understanding in documents, new elements are added. For example, taking a discussion between buyer and seller on value may be followed with a "non-binding" letter of intent where for the first time, the structure is described. The seller may react very negatively if he was thinking of a \$7 million wire transfer at closing and the written document combines \$4 million cash at close with a \$1 million seller note and an earn out that caps out at \$2 million. If we had not earlier forced the issue or warned our seller that this was a possibility, then maybe we deserved to have an unhappy client. Our goal is to turn this from a "he changed the transaction" deal breaker to a couple of deal points that we negotiate.

Another sticky point if the seller is not prepared is the concept of the net working capital adjustment. This is a customary deal approach from experienced buyers that is fair. Trying to explain it to the seller for the first time during the heat of battle can be problematic. In advance we tell our seller that the buyer is going to want a measuring point based on the latest financials he receives in order to make his offer. If, at that point, the current assets are \$350 K and the current liabilities are \$300 K then the company has net working capital of \$50 K. If that level changes then at the post closing true-up, an adjustment will be made to account for the change.

If a seller is not prepared for the pages of reps and warranties that are a standard part of most Definitive Purchase Agreements, the initial reaction is often, "no way." It is, however, a deal breaker for buyers, especially if they are public companies. With the new corporate governance scrutiny, these companies are very meticulous about protecting themselves.

The next potential stumbling block is when the buyer's corporate attorney gets involved to make sure that the mother ship is protected. It happened at the 11th hour and the way it was handled by the buyer almost blew up the deal. We had settled on the terms and conditions of the transaction and had worked out a 12-month consulting contract with the founder of the selling company. The senior management of the buyer detailed the duties and responsibilities in a "consulting agreement." When their corporate attorney received this document, he said that it is not a consulting agreement, but an employment agreement. Our client did not want to go from being a CEO to now being a VP. It was a drop in prestige for her and did not fit the image she had created for herself post acquisition. We had to talk her off the ledge and had to convince her that this should not be a deal breaker. We had to remind her that this buyer was the best fit for her company and she had the best opportunity of maximizing her earn out portion of the transaction with this buyer.

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We convinced her to sleep on it. We also enlisted the support of her CFO, husband and dear friend (all the same person). We were able to enlist his calm logical thought process and convince his wife that this was a relatively small impact, all things considered. She agreed.

Wait, you thought this was settled. Not so fast. Enter the Business Development/ Merger and Acquisition person from the buyer (BD). He attempts to push the deal through without adding employee benefits to the employment agreement because those benefits were not figured into his original financial analysis. He got very protective of his turf and made this counter proposal without consulting his President and EVP. Our client went ballistic. We literally had to walk her out of the conference room and cancelled the closing meeting until the next day.

We had already done two end runs around BD and we were worried that if we did a third we may cause doubt about the post acquisition behavior of our client in the eyes of the buyer president, or worse, cause BD to blow the deal up because we bruised his ego.

Well, we got lucky. The next day, before our meeting was due to begin, we ran into an individual doing a walk through at our client's offices. We introduced ourselves and asked her who she was. She replied that she was the head of HR for the buying company. We asked her if they typically had two classes of employees, one with benefits and one without. She looked at us incredulously and asked us what we were talking about. We explained and she said she would have it cleared up by the end of the day. She also gave our client her card and scheduled a call with her so she could implement the full package of employee benefits. Fast forward – BD has been moved out of the M&A position.

We had spent a tremendous amount of our client's time, the buying executives' time and our time and everyone involved knew that this was a good and fair transaction. With all of the pressure, emotion, and egos involved, sometimes even good deals do not get completed. You need experienced advisors that operates in the role of "shepherd of the deal" to guide the transaction through closing.

Dave Kauppi is a Merger and Acquisition Advisor with Mid Market Capital, Inc. MMC is a private investment banking and business broker firm specializing in providing corporate finance and business intermediary services to entrepreneurs and middle market corporate clients in a variety of industries. The firm counsels clients in the areas of M&A and divestiture, family business succession planning, valuations, minority interest shareholder sales, business sales and business acquisition. Dave is a Certified Business Intermediary (CBI), a licensed business broker, and a member of IBBA (International Business Brokers Association) and the MBBI (Midwest Business Brokers and Intermediaries). Contact Dave Kauppi at (630) 325-0123, email davekauppi@midmarkcap.com or visit our Web page <http://www.midmarkcap.com>

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