

Maintaining Order In The Acquisition Process: Deal Killers and How to Avoid Them

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“Deals Die 1000 Deaths; Good M&A Advisors Learn How to Bring Them Back to Life Quickly and Cost-Effectively.”

–Unknown

“How and why do deals die? Sometimes they linger, sometimes they fizzle and sometimes they explode. But often the problem can be laid at the feet of the professional advisors, who take it upon themselves to kill good deals.”

– William May

Maintaining Order in the M&A Process: Keep Deals on Track

- Putting a master strategic plan in place (with realistic financial and post-closing synergy expectations)
- Building the right team
- Communication and teamwork
- Orchestration and leadership
- Momentum and timetable accord
- Avoid emotion/don't call my baby ugly syndrome (sellers) and buyers must avoid falling in love with a given transaction
- Early start on governmental and third party appeals
- Creative problem solving
- Cooperation and support from financing sources
- Agreement on the key value drivers of the seller's business/intellectual capital issues

Bottom Line: Coordinate / Communicate / Anticipate = No Surprises

The Source of the Problem Will Dictate the Solution

Seller	<u>Stakeholders</u> <ul style="list-style-type: none"> <input type="checkbox"/> Minority shareholders <input type="checkbox"/> Key employees <input type="checkbox"/> VC investors <input type="checkbox"/> Family members 	<u>Third Party Approaches</u> <ul style="list-style-type: none"> <input type="checkbox"/> Regulatory <input type="checkbox"/> Lenders <input type="checkbox"/> Lessors <input type="checkbox"/> Unions 	A L L P A R T I E S
Buyer	<u>Sources of Capital</u> <ul style="list-style-type: none"> <input type="checkbox"/> Debt <input type="checkbox"/> Equity <input type="checkbox"/> Mezzanine 	<u>Professional Advisors</u> <ul style="list-style-type: none"> <input type="checkbox"/> Lawyers <input type="checkbox"/> CPA's <input type="checkbox"/> Investment Bankers <input type="checkbox"/> Consultants 	

Notes:

- A deal killer for one side is not necessarily a deal killer for the other side
- To solve the problem, first diagnose the cause
- Alignment of the needs of all parties is critical

Murphy's Law: What Causes Deals to Get Off Track?

- Egos clash
- Misalignment of objectives
- Inexperienced players
- Internal and external politics (board-level, executives, venture investors, etc.)
- Due diligence red flags/surprises
- Pricing and structural challenges (price vs. terms)
- Valuation problems (tax/source of financing/in general)
- Third party approval delays
- Seller's/buyer's/source of capital remorse
- Employee and customer issues
- Overdependence on the founder/key employee/key customer or relationship

Murphy's Law: What Causes Deals to Get Off Track? *(cont'd)*

- Loss of trust/integrity during the transactional process
- Nepotism
- Failure to develop a mutually-agreeable post-closing integration plan
- Shareholder approvals
- Accounting/financial statement irregularities (post-Worldcom)
- Sarbanes-Oxley post-closing concerns
- Breakdowns in leadership and coordination/too little or too many points of communication
- Too little or too much “principal to principal” communications
- Crowded Auctions
- Impatience to get to closing vs. loss of momentum (flow and timing issues)

Murphy's Law: What Causes Deals to Get Off Track? *(cont'd)*

- ❑ Incompatibility of culture and/or business systems (e.g. IT Infrastructure, costs and budgeting policies, compensation and reward programs, accounting policies, etc.)
- ❑ Force-feeding deals that don't meet M&A objectives (square peg/round hole) (Bad deal avoidance/good deal capture — systems and filters)
- ❑ Who's driving the bus in this deal? (M vs. A)
- ❑ Changes in seller performance during the transactional process (upside surprises vs. unexpected downside surprises)
- ❑ Loss of a key customer or strategic relationship during the transactional process
- ❑ Failure to agree on post-closing obligations, roles and responsibilities
- ❑ Environmental problems (buyers less willing to rely on indemnification and insurance protections)
- ❑ Unexpected changes in the buyer's strategy or operations during the transactional process (including a change in management or strategic direction)

Kissing a Lot of Frogs (and learning along the way)

“The more you look, the more you find.

The more you find, the more you learn.

The more you learn, the better the chances of getting the right deal done right.”

– Dr. Mark Sirower
Author, *The Synergy Trap*

Problems Dictate Solutions

Most “deal killers” can be put into one of the following major categories:

- Price and Valuation
- Terms and Conditions
- Allocation of Risk
- Third Party Challenges

Solutions: Tools to Fix a Broken Deal

(assuming it can and should be fixed)

- Earn-out's/deferred and contingent post-closing consideration
- Representations, warranties and indemnities (tools to adjust allocation and assumption of risk) (weighting of priorities issues)
- Adjusting the post-closing survival period of R&W's
- Holdbacks and security interests
- Closing date audits
- Third party performance guaranties/performance bonds/escrows
- M&A insurance policies
- Restrictions on sale by seller of buyer's securities issued as part of the overall consideration
- Recasting of financial projections and retooling post-closing business plans

And the Ultimate Solution...

- “...don’t be afraid to...**walk away.**”
- Bad deals deserve to die a peaceful death.
- Not all deals are meant to be done:
 - ❑ At this time
 - ❑ At this valuation
 - ❑ Under these terms and conditions
 - ❑ Between these parties

About the Moderator/Presenter

Andrew J. Sherman, Esq. is an internationally-recognized authority on the legal and strategic aspects of business growth. A summary of his accomplishments include:

- ❑ Mr. Sherman is a senior partner with **McDermott, Will & Emery (MWE)**, an international law firm with nearly 1,000 lawyers worldwide, where he manages a significant corporate and transactional practice representing Fortune 500 corporations as well as technology-driven, and rapidly growing businesses and government contractors in the areas of mergers and acquisitions, capital formation and growth strategies, business and strategic planning and the leveraging of intellectual capital. He is the co-developer and practice leader for the MWE **Intellectual Property Protection and Leveraging Analysis (IPPLA)** special practice and has written and lectured extensively on intellectual property protection and leveraging.
- ❑ He is the author of twelve (12) books on business growth, capital formation and the leveraging of intellectual property, including the best-selling and critically-acclaimed **Raising Capital** (Kiplingers, 2000), **Mergers and Acquisitions from A to Z** (AMACOM Books, 1998), **The Complete Guide to Running and Growing Your Business**, (Random House, 1997) and **Franchising and Licensing: Two Ways to Build Your Business**, (2nd edition) (AMACOM Books, 1999), and the third edition was published in Dec. 2003, and **Fast Track Growth Strategies** (Kiplinger) which was released in January of 2002.

- ❑ He has appeared as a guest and a commentator on all of the major television networks as well as **CNBC's** "Power Lunch," **CNN's** "Day Watch," **CNNfn's** "For Entrepreneurs Only," USA Network's "First Business," and **Bloomberg's** "Small Business Weekly" and various other regional and local television broadcasts as well as national and local radio interviews for **National Public Radio** (NPR), Business News Network (BNN), Bloomberg Radio, **AP Radio** Network, Voice of America, Talk America Radio Network and the USA Radio Network, as a resource on merger and acquisitions, capital formation, entrepreneurship and technology development.
- ❑ He has served as a top-rated Adjunct Professor in the Masters of Business Administration (MBA) programs at the **University of Maryland** for twelve (12) years and at **Georgetown University** for six (6) years where he teaches courses on Entrepreneurship and Business Planning, Growth Strategies and New Venture Financing, and has won various teaching awards including the Krowe Award for Teaching Excellence in 2000.
- ❑ He serves as **General Counsel** to several of the nation and region's leading entrepreneurship and business growth organizations, including the **Young Entrepreneurs Organization (YEO)**, the **Collegiate Entrepreneurs Organization (CEO)**, the National Foundation for Teaching Entrepreneurship (NFTE), the Let's Talk Business Network (LTBN) and the Morino Institute's Netpreneur program, since the inception of these organizations. He was one of the co-founders of the Washington, D.C. regional chapter of the Association for Corporate Growth and serves on the Inner Circle and as a key advisor to the Dingman Center for Entrepreneurship at the University of Maryland. He is the co-founder and **Chairman of the Board** of the newly-formed **Small and Emerging Contractors Advisory Forum (SECAF)**, an education and networking resource headquartered in Washington, D.C. to support small and mid-sized government and defense contractors.

- ❑ Mr. Sherman is a frequent author, serves as a resource and has been quoted for articles in a wide variety of the nation's leading magazines, newspapers and websites including the Wall Street Journal, the New York Times, Fortune, Investor's Business Daily, USA Today, Inc., Nation's Business, Success, the Washington Post, Forbes, My Business, U.S. News and World Report, Business Week, Money, Legal Times, Washington Business Journal, Crain's, Entrepreneur, Reuters News Service, AP News Wire, CNNfn.com, Inc.com, Fortune.com, Office.com, MSNBC.com, and the Kauffman Center for Entrepreneurial Leadership's EntreWorld.org websites. In the December/January 2002 issue of Fortune Small Business, he was recognized as one of the nation's top ten (10) gurus and thought leaders on entrepreneurship and the legal and strategic issues facing small and growing companies.
- ❑ Mr. Sherman is the Chairman of the Professional Advisory Board of the National Commission on Entrepreneurship (NCE), the Chairman of the Technology and Innovation Committee for the Washington Board of Trade's Potomac Conference, serves on the Board of Directors of Youth Services America, the Editorial Advisory Board of Inc. Magazine's latest publication, International Franchising, to be launched in January of 2002), the Board of Advisors to the Collegiate Entrepreneurs Organization (CEO), the Research Institute for Small and Emerging Businesses (RISE Business), NFTE (Former Chairman 1993-1995), YEO, the Washington Business Journal's Editorial Advisory Board, Inc. Magazine's Business Consulting Services Advisory Board, the Opportunity International Board of Governors, the Gazelles/Masters of Business Dynamics Advisory Board and serves on the advisory boards of several business incubators and early-stage and rapidly-growing technology companies.
- ❑ Mr. Sherman serves as an on-line columnist for two of the internet's leading sites for small and emerging growth companies. He writes the "Can This Business Be Saved?" column for FortuneSmallBusiness.com as well as the "View from The Trenches" column for AOL's Netbusiness.com and serves as a key member of the AOL Small and Emerging Business Champions Team. He is also a frequent contributor to the "Leading Advisors" section of the Kaufman Center for Entrepreneurial Leadership's website, EntreWorld.org.

- ❑ He is a frequent national and international lecturer at business conferences where he has delivered speeches and lead seminars on entrepreneurship, capital formation, mergers and acquisitions, the protection and leveraging of intellectual property and business planning for organizations such as **Inc. Magazine** (Growing Your Company, Capital Formation, ThINC.Out Loud and CEO Symposium Conferences), the **MIT/Inc./YEO** "Birthing of Giants" programs, the **Association of Financial Professionals**, the **Young Entrepreneurs Organization** (international meetings and local chapter presentations), the **National Restaurant Association**, **iBreakfast.com**, the **U.S. Chamber of Commerce**, the **New York Venture Group**, the **Dingman Center for Entrepreneurship**, **Netpreneur.org**, the **Baltimore-Washington Venture Group**, the **National Association of Credit Managers**, **PC Expo**, the **International Franchise Association**, **Microsoft's** Small Business Crossing Seminar Series, the **Regional Investment Bankers Association**, the **Collegiate Entrepreneurs Organization**, the **Association for Corporate Growth**, the **American Management Association**, the **Council for Growing Companies**, and various other international and regional business organizations.

- ❑ He is the developer and lecturer for several different business growth courses and seminar series, including serving as the author of two workbooks and videos for Kiplinger's, entitled **Growing Your Business** and **Corporate Transition Management and Exit Strategies**, as well as a four-part cyber-conference and workbook on **Mergers and Acquisitions** for the Association of Financial Professionals, a seminar series on **Strategies for Protecting Your Intellectual Property** for Padgett-Thompson, a series of conferences on **Growth-Oriented Distribution Strategies** for the American Management Association and a series of conferences on **Strategies for Doing Business Abroad** for the International Franchise Association.