

## **Acquiring the Acquisition Mindset**

*How to Prepare for an Exit daily*

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What is the acquisition mindset?

It is a mindset that says, “Whether or not I ever sell my company I will run it as if it is going to be acquired tomorrow.” The acquisition mindset enforces a discipline, structure, and rigor in your company that ensures you are running a professional organization that minimizes structural risk, maximizes work satisfaction, and ensures the highest levels of income today and wealth tomorrow (if you do sell). The acquisition mindset is a tool that helps you in all areas of your company whether you are running a lifestyle company, a venture backed company, a high growth company, or running a company on the side while you perform another day job.

### **Running the Company**

Incorporate very thoughtfully. Spend a lot of time thinking through partnership agreements.

Think through estate and tax planning issues right at company formation. Who owns the stock? Where does it reside? What will be the tax implications if you sold the company the next day? Should your kids own some of it now before it has any value so you avoid any estate taxes?

Create goals and metrics and strive to meet them. Analyze why you did or didn’t meet the goals, refine, repeat.

Build a management team. A strong one. Could the business run a week, a month, a quarter without you?

Equity in your company is valuable. Treat it that way. Have really important and good reasons to give away equity to partners and structure it as a future incentive rather than a grant.

Be professional. Have a professional image, maintain an organization chart, be disciplined, be prone to candid conversations (the more difficult the topic the quicker you should have a candid conversation about it). A “fun” culture and “discipline” are not mutually exclusive.

### **Record Keeping**

Maintain solid financial records including getting reviewed financials once you get to \$1MM in revenue and audited financials once you get to \$5MM in revenue. Understand why you may or may not be using GAAP accounting. Use the accounting that maximizes after tax income but understand why you are using it and how it reconciles to GAAP.

Maintain solid legal records including articles of incorporation, regulatory and other business licenses, board meeting minutes (yes, these add a huge amount of value by increasing trust and demonstrating professionalism to a potential acquirer), risk and liability records (environmental, various employment policies, insurance, etc.).

Invest appropriately in your IT and accounting systems. Investing appropriately means your systems are ready for the next 12-18 months of your growth.

### Advisors

The single most important relationship you want is with your bank. Constantly be communicating to your banker. Always have a line of credit that is 25% - 50% larger than what you need for the current year. This relationship should be on the same level as the one with your largest client.

Develop a solid professional network of attorneys around you including tax and estate planning attorneys when you incorporate; review these every \$3MM in revenue. If you don't feel comfortable calling your attorney at the first sign of legal trouble you don't have the right relationship with them.

Always have an experienced accountant working with you from the very start. Consider hiring a controller at \$2MM in revenue, a CFO at \$10MM in revenue, a General Counsel at \$15MM in revenue.

Develop a relationship with a M&A Advisor around \$3MM in revenue; they can apprise you of industry trends, valuations, exit preparation, and handle incoming offers for you.

Don't have an irrational fear of financial firms (VCs, PEs, bankers). Too many people give too much equity away to friends and too little to financials firms that can help them.

### Maximizing Value

Maximizing value is based on (1) understanding what buyers want, and (2) becoming an educated seller.

#### Understanding What Buyers Want

How do you know when to sell?

"I cant sell now. Last year was a down year and I want to show growth before I sell."

"I cant sell now. I'm growing 40% a year. I want to make the company much bigger before I sell"

"I cant sell now. I'm just about to get a very large contract and I'll sell after I get it."

"I cant sell now. The actual value of my product is SO MUCH higher than my financials show."

"I cant sell now. Because of the recession I'm sure buyers are not paying a lot."

All of the above reasons show a lack of understanding of the M&A process and why some companies get sold for so much more than other companies. Full and highest prices are paid by strategic buyers, which means your company, management team, product, fulfill a strategic need of the buyer and lead them to believe that there are synergies between the two companies that go beyond financial performance.

Being on the front end of a consolidation wave is essential to getting multiple offers which is what generates the best price and terms. Once a buyer buys a company to meet a certain need they will not replace that company by buying another one in the future no matter how much better the newer one is. And while you are growing at 40% a year, buyers with money are spending it on other companies which means that right at the time your growth slows down, there is a potential for fewer or poorer buyers thus driving down value even more. And buyers perceive a step down from 40% to 30% as a stumble not a sign of a maturing business and they tend to be wary of it.

Sell when you are growing to maximize cash at close value. But also because you will have the best opportunity to have a great relationship after the close and to maximize your earnout.

### Becoming an Educated Seller

Understand that highest growth rates and higher revenue don't necessarily lead to highest exit valuations. Having an exit mindset and running the company that way from day one will give you a much better chance of being a strategic acquisition target.

Educate yourself on the strategic outcomes that are possible for your company; organic and inorganic (acquisitions) growth methods, recapitalizations, full or partial sale of the company, ESOPs, IPOs.

Avoid the following mistakes:

- Overinvesting in one off offers for your company. The surest way to maximize value is by running a process and having multiple offers.
- Using the wrong advisors, or no advisor at all. The correct advisors can add 10% - 100+% to the value of the deal by bringing in additional buyers, minimizing due diligence mistakes, and being a strong advocate on your behalf.
- Marketing your company multiple times.
- Not thinking about your employees and management team during the exit process.
- Sloppy due diligence practices
- Legal risks and liabilities (pay your taxes and vendors, keep a harassment free workplace, and deliver what you promise to your clients)