

ACQUIRING ANOTHER COMPANY IS  
A SIGNIFICANT STEP TOWARD  
GROWTH. KEEP IN MIND—  
SUCCESSFUL ACQUISITIONS  
CALL FOR DILIGENT  
STRATEGY AND PLANNING.



## JUST ACQUIRE IT!

### A look at the acquisition process

#### By Kraig Kramers

Business success is about planning, leading, and managing *profitable growth*. The “growth” part involves developing and acquiring sales volume. This acquiring of sales is a daily duty, but you can also grow by acquiring other companies.

One of the most important lessons in the acquisition process is to communicate your goals clearly. If you want to acquire companies, you need to inform the world of your objective. Then you’ll have people *bringing you deals!*



#### SIX KEY STEPS IN THE ACQUISITION PROCESS

- 1. *Decide you want to do acquisitions.***  
You’ll get ready and be ready, making acquiring a lot easier!
- 2. *Find and evaluate candidates.***  
It’s tougher than it sounds. The finding is harder, the evaluating is easier. Yet thorough *due diligence* takes time and is the *most important thing* you can do.
- 3. *Obtain a letter of intent.***  
This is a non-binding agreement in

which you and the seller agree on price and general selling terms. This can be an emotional step because the seller isn’t always ready to sell.

#### **4. *Reach a definitive agreement.***

This can take from 60 days to many months—sometimes it never occurs. It involves a long document that specifies all the terms of the sale.

#### **5. *Close the deal.***

The more time between steps 4 and 5, the less likely the deal will get done and the more likely unhappiness and litigation. Ideally, close while signing the definitive document.

#### **6. *Make it work after the deal.***

This is the most important part of all! Involve all employees, work hard *not* to change what makes the business successful. The others you can change!

#### ACQUISITION CRITERIA

You should determine your acquisition criteria—so brokers know what to look for and you know what you’re after. When you buy a company, you want the “acquiree” to feel like they are joining a family, not being “acquired.” This is critical not only to key managers who stay on board after the merger, but essential in attaining a smooth cultural transition for the entire organization. Specific criteria for a target may include:

- Headquartered in the U.S.
- Annual revenues between \$25 and \$100 million
- Operating and management team which owns a significant part of the company
- Management team that is willing to stay
- Leader in its niche, segment, or industry
- Profitable performance record

You may also want to state things you *don't* want to acquire—such as turnarounds, start-ups, capital-intensive, or highly regulated companies. Whatever your criteria, it's a good idea to write them down and then use this for periodic mailings, emails, or faxes to brokers. It gives you an opportunity to stay in touch. People do business with people they like, and they'll like you because you communicate with them.

### Pre-Acquisition Checklist

- Get financial statements.
- Determine the asking price.
- Make the Owner/CEO comfortable with you.
- Prepare a tailored understanding of facts, tuned to this deal.
- Get the letter of intent signed.
- Establish a timetable for doing-in-depth due diligence.

### FINDING AND SCREENING CANDIDATES

First, you need to develop a list of desirable candidates. Look in the Yellow Pages under "Business Brokers" and "Investment Bankers." Join the Association for



Corporate Growth, an international organization that meets once a month to discuss acquisition issues. Talk to your CPA, attorney, and lender. They're always looking for deals for their clients. Once you get a list of sources, stay in touch with them.

Perhaps the most important question to ask is—Why are they selling the business? To make the evaluation easier, develop a candidate screening form with the following pieces of information:

- Business name and description in two lines
- Financials (including gross margin) for three years
- How the seller wants to get paid
- Fit with your acquisition criteria
- Asking Price and other terms

### PRICE VERSUS MORE IMPORTANT CONSIDERATIONS

Worry less about price and more about what you are actually buying and why. Do you plan to change the company or position it differently? If so, formulate your strategy before proceeding. Look at worst case scenarios. *Any price* is too much if it's the wrong business or your plan fails. Be rigorous in your due diligence and your review of current financial performance.



Pay less attention to past or future financial performance—the past is often not a good predictor of the future. What's the business doing *now*?

Let the seller focus on the price—you can reduce it by focusing on the terms! If you're buying assets and liabilities, make sure you understand each one in detail. Understand what representations and warranties will end up in the definitive agreement. Be very specific about offsets and indemnities.

As the acquisition price rises, so does the riskiness, irrespective of the nature of the business. As price, risk, and technology climb, the payment should shift from cash, to cash and notes, to notes, to paper, to an earnout plan. With an earnout, the seller doesn't get the full price if the business doesn't perform.

EBITDA which is annual operating income plus depreciation and amortization added back.

Simply average the three values you determined above and you'll be within plus or minus 10% of the value the business will actually sell for. For really high tech companies, true dot.com's, and companies without revenues or earnings, special valuation methods need to be used.

## POST-ACQUISITION

People are the biggest part of the deal—so make the sellers and their people feel comfortable. If sellers stay on board after the deal gets done, they are the ones who will ultimately make things happen. Take steps to acknowledge that the deal has been consummated—send out news releases, drink champagne, send wine to sellers' spouses at closing, take senior management on a golf outing—in short, celebrate! It's not often that you get the opportunity to make a fresh start.

Then, if it is going to be run as a separate company, jointly set guidelines and leave it alone. A business is like a banana—both bruise easily. Work with your management team to develop a sound written strategy and long-range plan. Reach agreement on goals and realistic timetables for achieving them. Provide adequate capital and give the authority and autonomy to succeed. Have a simple, timely reporting system. Reward successful achievement with lots of things, but mostly *recognition for results they produce!*

## ABOUT THE AUTHOR

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## VALUATION METHODS

Different industries use different valuation methods, based on economic factors. Nevertheless, 99 out of 100 privately-owned businesses can be accurately valued using a simple average of three values:

### 1. **Price/Earnings (P/E) Multiple.**

Determine a value using a multiplier of 10-18 times after-tax earnings after adjusting those earnings to reflect what the buyer would really see. Higher multiples reflect higher tech businesses, more consistent earnings, and lower debt to equity situations.

### 2. **Book Value Multiple.**

Get a second value using a 1.5-3 times stockholders equity, also known as net book value or net worth.

### 3. **EBITDA Multiple.**

Finally, determine your third data point by using a 3-6 times multiplier on