TECHNOLOGY ACQUISITION UPDATE

18 Reasons the CEO Should Not Sell the Company

CEOs and founders can sell their own companies—unquestionably. They do it all the time. However, can they do it effectively? Can they run the company and at the same time devote the significant time that sell a company requires? Will they reach out to a wide range of buyers and generate competitive offers? Will they get the best price for the shareholders?

At first glance, it is tempting for a CEO to try to sell his or her own company. After all, he or she knows the company and the market very well. A CEO's mindset can often be characterized as: (a) I know the industry; (b) I know how to negotiate; (c) I'm a smart guy… I can sell the company. In addition, we will save a fee.

Over the years I have observed many CEOs attempting to sell their own companies. Most CEOs do not engage in a transaction process that leads to an optimal deal structure. Selling a company at the best price and terms to the best buyer with minimal problems is a difficult endeavor. CEOs often make rookie mistakes and these blunders can cost the shareholders real money.

What follows are 18 common mistakes that founders and CEOs often make when trying to sell the company themselves.

1. This will be Easy

Many CEOs think selling a company is easy and the process straightforward. Selling a company appears to be an interesting challenge as well.

What they fail to realize is the tremendous amount of time and effort required to do the job right. Without experience in M&A, they miss the subtleties that can lead to a the best price, better terms and a smoother process. Even if a CEO has previous M&A experience, he or she can't be objective; plus, he still must run the company—a full-time job in itself.

2. Too Narrow a Search

CEOs tend to pick the low hanging fruit, thus their search process is rarely extensive. CEOs typically do a limited search, typically contacting about six buyers. They think they know the market and which companies would be good or poor buyers. Some are convinced that one particular buyer will pay the highest price. CEOs rarely seek buyers in tangential and fringe markets.

Once a CEO begins discussions, he stops looking for additional buyers. He is content to engage one or two potential buyers. Deals can fall apart; however, and it is smart to get multiple offers and generate competitive bidding.

Reaching out to additional buyers simply creates more work for the CEO. Many CEOs tacitly assume that the incremental price will not be worth the incremental effort. This is not the case.

3. No Full-Time Commitment

Identifying and contacting candidates is a full time task that takes several months. This process can be very tedious—something that an executive level person may not want to undertake. A CEO who is running a business cannot possibly give full attention to a comprehensive search process.

4. Ignoring Opportunity Cost

Where can the CEO add the most value? Trying to sell it or continuing to build the company? More value is created when the CEO continues to build the company—increase revenues, serve customers, and develop new products. The value of these activities will eclipse the value of any fee saved.

5. Selling the Future

Most CEOs are accustomed to raising capital and they see selling the company as similar to raising capital. When trying to sell the business, they paint the same picture. They sell their vision—large markets, rapidly growing revenues and substantial profits. They focus on where they are going, not where they are. In other words, they are selling the future.

A business plan is forward looking. It is about growth. A selling memorandum is different. It is a snapshot of the current situation. There is a big difference between selling the future and selling the company as it exists today.

6. Presenting the Wrong Information

CEOs don't take the time to develop the proper documentation to promote the sale. Most fail to draft a selling memorandum or even a short summary of the acquisition opportunity. Most CEOs just send out the business plan.

Since they are not M&A experts, CEOs are not aware of what information should be communicated at different stages of the M&A process. They will often give the wrong depth of detail—too much information too soon or too little information too late.

7. Poor Positioning

CEOs generally are not skilled at positioning the company to potential buyers. How should the company be presented? What technology or assets should be emphasized?

Value must be viewed from an external perspective, not from management's internal perspective. Since value is extrinsic, buyers will view value differently. This may be very different than how the CEO views value.

8. Glossing over the Negatives

CEOs portray their company in a good light. “Everything is going great. We have great marketing, great technology, and great people.” It is difficult for them to view the transaction from the buyers’ eyes. Glossing over the negatives is a red flag for most buyers.

CEOs rarely admit that they have done a poor job in marketing or sales. However, a company with excellent technology that has not had the capital to undertake a serious marketing effort can be positioned as an opportunity for the buyer.

9. Representation without Representation

If a buyer receives an inquiry from an investment banker, it signals that the company is serious about selling. Buyers don't want to waste time with a company that is not serious about selling.

10. Unable to Ramrod the Transaction

The CEO cannot push the transaction without appearing desperate. He cannot call the buyer every other day. An intermediary can ramrod the transaction, calling the buyer four times a week to keep the deal moving. This is the advantage of being a third party; he is just doing his job. Buyers expect him to be persistent. A persistent CEO, on the other hand, is perceived as a desperate seller.

11. Setting the Wrong Price

A CEO's own prejudices can cloud the value issue. Unrealistic value expectations can be deadly. What the market is willing to pay may be very different from what the CEO thinks his company is worth or ought to be worth.

CEOs may want to sell only if the price is greater than a certain threshold (where his stock options are in the money). This may misprice the deal and it may not be in the best interests of other shareholders.

12. The Fallacy of a Narrow Value Range

This is a subtle mistake, but a common one. CEOs assume that value falls within a narrow range and that an interested buyer will pay them what their company is worth. This presupposes, of course, that they know what their company is worth.

A technology company can vary widely in value. The same company could be worth $3 million, $6 million, or $9 million depending on the strategic fit with the buyer. The high price is three times the low price—a huge range of value! Don't assume that buyers will pay similar prices.

13. Failure to Manage the Process

The sale of a company involves a multitude of detailed activities. The process must be effectively managed. One doesn’t just make some calls and have a few meetings. A professional intermediary can, coordinate the activities, overcome the inevitable obstacles, and move the transaction along in a timely manner.

14. Not Listening

Buyers will tell a third party things they would never tell the CEO directly. This enables the third party to pick up clues along the way about how strategic the technology is to the buyer and how the buyer perceives value.

A CEO usually focuses on the points *he* wants to make and what *he* wants to say. One must listen with big ears. What is the buyer saying between the lines? What are they really after? A good negotiator is a keen listener.

The negotiator's job is to figure out the other side's issues and motivations. A danger is not being aware of a problem before it becomes full blown. You can't head off a problem if you are not aware of it.

15. Uncreative Structuring

There are many ways to structure a deal; it is not simply stock or cash. CEOs are generally not very imaginative in coming up with creative structuring ideas in which both parties might be better off. The key to good structuring is to understand the objectives of each party and have an open, creative mind set.

16. Adversarial Beginnings

Friction can develop between the buyer and seller. To avoid an adversarial relationship, it is a good idea to have an intermediary handle the negotiations. An experienced third party will be more adept at dealing with troublesome issues.

A case in point is negotiating the president's salary and option package. Who can best negotiate these items—the CEO himself or a third party? Let the third party be the bad guy.

17. Incorrectly Valuing the Buyer's Stock

If the seller receives stock from the buyer, what is the accurate value of that stock? The public company's stock price may not represent its true value. Most investment bankers have significant experience determining value.

18. The Fallacy of Saving a Fee

Everyone loves to save a fee. Is trying to save a fee really worth it? Is the amount of the fee saved greater than the incremental value that the CEO could add by focusing on building the business?

A CEO creates the most value by running the company effectively. He or she provides leadership, keeps things running smoothly, solves problems and keeps the team pulling in the same direction.

Rarely is the amount of fee saved greater than the opportunity cost of the president's time. Plus any fee saved is negligible in the overall context of the deal.

Summary

Most CEOs underestimate the time and effort required to do an effective job of selling a company. There are many moving parts in the sale of a company. The best thing for the shareholders is to have a professional intermediary sell the company, not the CEO.

Seattle, Washington
206-779-7707
www.tvmetz.com