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Deal Killers and How You Can Head Them Off

Due diligence may be the most feared aspect of the merger and acquisition (M&A) process for business owners, and their concern is valid. The results of the due diligence assessment can make or break a transaction.

During the due diligence process, the prospective buyer's representatives (typically third-party accounting, environmental, insurance, etc., firms) gather financial, operational, legal, and other data about the business to analyze and verify the accuracy of the information provided and uncover any hidden risks prior to finalizing the transaction.
Without proper preparation before you go to market, due diligence may uncover issues that jeopardize the transaction. The good news is that many issues are preventable with effective planning and transparency.

What Can Make a Deal Go Sideways?

M&A deals collapse for a variety of reasons. Here are the most common, impactful deal killers:

Financial and Accounting Issues

- Financial irregularities and accounting mistakes: Inconsistent, inaccurate, or incomplete financial statements, unexplained debt, undisclosed liabilities, and cash flow problems are major red flags that can derail a deal.

- Financial slowdowns and quality of earnings (QoE) issues: If a company's financial performance declines during the deal process or due diligence reveals lower-than-expected EBITDA or profitability, a potential buyer may walk away or attempt to write down the deal, lowering their offer or the quality of terms.

- Gap in perceived value: Discrepancies between what the seller expects to receive and what the buyer is willing to pay can lead to deal failure, particularly if the company's financials don't support the seller's valuation.

Legal and Compliance Risks

- Potential or unresolved legal issues: Potential or ongoing lawsuits, regulatory investigations, or compliance failures can scare off buyers or significantly reduce deal value.

- Intellectual property ownership issues: Failure to clearly prove ownership of intellectual property can be a deal breaker, especially in the technology and creative industries.

Process and Integration Challenges

- Poorly managed due diligence process: Inadequate or overly complicated due diligence processes can overlook or incorrectly identify risks as well as frustrate both parties, leading to deal collapse.

- Integration issues and cultural misalignment: Poorly planned or executed integrations, or significant cultural clashes between the organizations, can lead to operational disruptions,

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loss of valuable talent, and deal failure.

- Overvaluation and lack of strategy: Overestimating synergies or benefits, or entering into a deal without a clear strategic rationale, often results in failure to deliver expected value.

Communication and Seller Behavior

- **Poor communication and lack of transparency:** Inadequately disclosed issues or unexpected issues discovered during due diligence can undermine trust and kill a deal.
- **Seller distraction or neglect:** If the seller becomes too focused on the deal and neglects day-to-day operations, business performance can suffer, weakening the seller's position and potentially killing the deal.
- **Seller backs out:** Emotional stress, internal disagreements, or second thoughts can lead sellers to withdraw from the transaction.

External and Market Factors

- **Financing issues:** The buyer's inability to secure financing due to higher interest rates, lender reluctance, or industry downturns can prevent deals from closing.
- **Economic or regulatory changes:** Shifts in the economy, industry, or regulatory environment can affect deal viability.
- **Time delays:** Prolonged deal timelines increase the risk of negative events occurring during the M&A process (for example, losing a key client, experiencing a cyberattack, or sustaining profitability changes), which can quickly derail the transaction.

Set Yourself Up for a Successful Outcome

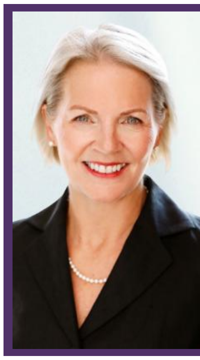
Don't be alarmed by these potential deal killers. As the business owner, you can take definitive actions to prepare your business, ensure a smooth M&A process, and achieve a successful transaction:

- Start planning well in advance of going to market with your business.
- Engage in the exit planning process early to help you prepare your business and guide you through the M&A process.

One way to avoid Deal Killers is to explore incorporating a comprehensive **Master Exit Planning®** process that will addresse all of the risks that can derail your deal. The DAK Group, through our partnership with Legacy Partners offers this comprehensive service to business owners. During both a quantitative and qualitative analyses of your business, we look for red flags that can potentially kill a deal. Identifying issues well in advance of going to market enables us to help you correct the problems and make enhancements that increase the value of your business, improving the chances that your transaction will cross the finish line smoothly.

So, alleviate your fear of the due diligence process: Plan ahead and address issues early to enhance your business, minimize unexpected issues, and instill buyer confidence. Doing the work upfront will result in a higher price and more favorable terms for you, and a smooth, mutually beneficial transaction for you and your buyer.

What's not to like about that?



About
Chris Vanderzyden
Chris Vanderzyden leads the Legacy Partners Worldwide Division of The DAK Group. She is a trusted advisor to clients and peers, an industry trailblazer in exit planning, and a mentor and leader to a team of top financial and M&A professionals. She can be reached at cvanderzyden@legacypartnersllp.com