

A hiker in a dark jacket and hat stands on a rocky mountain trail, holding a wooden stick. The background features a vast, hazy mountain range under a blue sky with light clouds. The foreground shows a path with stone steps and patches of snow on the mountain slopes.

The VC Guide to Mergers & Acquisitions

Exceptional founders.
Extraordinary journeys.

NOTION

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The Notion Capital View on M&A: An accelerated solution for an accelerated corporate world

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If executed correctly, acquisitions represent an efficient way of accelerating growth and significantly increasing company value. Whether you acquire for revenue, for product, to eliminate competition or simply to generate multiple arbitrage, the benefits of success mean that this strategy is always worth consideration.

A number of our portfolio companies have made acquisitions and in all cases they have had a positive impact on underlying performance. We think more high-growth startups should be thinking seriously about acquisitions as a business strategy. At the very least, it should become part of the entrepreneur's everyday role to evaluate the opportunities in the market and consciously decide not to make an acquisition, as opposed to inaction being the norm.

We broadly see three types of acquisitions:

- i. Product roadmap enhancements
- ii. Gaining market share
- iii. Distressed / opportunistic

All of these can add significant value to your company if pursued correctly.

They can also erode value if not.

For this guide, we have spoken to many companies that have performed acquisitions and captured their thoughts around the rationale, the process and the subsequent integration; which we think makes for fascinating reading.

Before getting into their stories, I wanted also to share my own view as to the elements that we, at Notion Capital, feel are important when considering whether or not to conduct an acquisition.

Appropriate Planning & Fit With Strategy

Examine your product roadmap and identify which gaps could be suitably plugged with an acquisition. You should evaluate the classic 'buy / build / partner' framework for each of your key areas and ensure that the financial analysis is rigorous and stands up to scrutiny.

You'll need to understand your market and all the players in it – from the bottom to the top. Create a persona based on the ideal characteristics of the sort of company that you want to buy and then evaluate possible targets rigorously against this specification.

If the deal is purely opportunistic, make sure you really test your assumptions as to why you are doing the deal. Challenge yourself to ensure that the deal will fit into your strategy, rather than being a distraction from the already stressful everyday experience of high-growth management.

Deal Structure

It is vital that you examine the deal through every possible lens until you are confident that you are not over-paying for an acquisition. Look at your growth and efficiency metrics and sense-check the proposed deal terms against them. You already have a benchmark of value in your existing business model, so: how much would it cost and how long would it take you to organically achieve the same amount of revenue if the acquisition were not to go ahead? Use discounting and other techniques to compare the acquisition cost with BAU.

If you are offering stock as part of the consideration, be sure to use proper valuations for your company, not a number simply tagged to your last round of funding. Stress test the modelling to ensure that you're better off issuing stock for the proposed acquisition as against raising a new round and following the organic route.

If you are making an acquisition in anticipation of a multiple arbitrage, (i.e. an increased valuation based on the acquisition of a company that is valued at a lower multiple of revenue), how and when will that value increase be realised? Are you purchasing a customer base and a certain revenue type to switch to your tech stack? Are you simply striking a good deal and therefore confident that your valuation will be higher upon ultimate exit?

If the deal is a distressed / opportunistic play, then don't be afraid to take a tough line on the consideration from the outset; as the company in question may not have many options. Consider moving value to the post-acquisition world in order to incentivise the management team to do the deal. Ultimately shareholders in distressed circumstances will take what they can get, so if you are able to shift value to the management team, then do so.

When it comes to the timeline by which a consideration is paid, I am not a big fan of earnout or other variable-consideration deals. I believe that there is always a danger that the addition of an earnout to a deal will be perceived as a lack of belief in the acquisition and/or a desire to try to drive down the ultimate price payable. I choose only to consider earnouts if there is a valuation gap that cannot be bridged - and even then it's a last resort.

Finally, it may be possible to structure the deal as an asset purchase (rather than an equity deal, whereby significantly less risk will transfer over to the buyer). It is not ideal from the seller's perspective so this may again be more relevant to distressed / opportunistic deals.

Team, Values & Culture

In most cases, particularly in acquisitions for roadmap acceleration, you will be placing a significant value on the team that you are acquiring. It is vital you ensure the acquired team are efficiently and comprehensively taken on the journey of migration into your organisation and properly incentivised within the new structure.

Learn who the key players are and the personal and professional levers which will motivate them. These may not just be cash or stock; recognition, validation and a raft of other softer points may need to be addressed in order to ensure retention and continued productivity. Speak to the C-Suite and ideally the next level of management in order to validate these motivators.

Just as important is to understand the values and culture of the target company - will it fit with yours? The fact that you have identified and validated the best company to acquire won't matter a jot if the culture is significantly different - the integration simply won't work.

Carve out time to spend with the key players and agree remuneration packages early to avoid doubt and unnecessary stress. Put cultural integration firmly on the agenda and agree the goals of the combined entity. A little time spent discussing these themes early in the process will go a long way.

“You will be placing a significant value on the team that you are acquiring. It is vital you ensure the acquired team are efficiently and comprehensively taken on the journey of migration into your organisation and properly incentivised within the new structure.”

Due Diligence

Be sure you have people on your team who are qualified to do this; as the skillsets required to build and grow a business are very different to those required to evaluate one. The main areas of concern will be technology, IP, tax, employees and customers.

If you feel that you need external support, don't be afraid to pay for it. There are plenty of capable advisory firms and smart experts to assist you in each of these specialist domains.

Run a thorough process across all of the above areas (and any others specialist to your sector or needs). Yes, there is warranty protection, but no-one wants to be claiming against these for a fundamental issue that could have been surfaced pre-deal. It won't buy back wasted time, effort or loss of focus.

Pay particular attention to customer contracts and ensure you understand the renewal profile. It is very common for churn to increase significantly post-acquisition, so do all the work you can to identify any risks. Speak to as many customers as possible to understand the target through the customer lens. Take back-channel references and get

a broad view on the state of customer satisfaction along with the issues which might change it (for better or worse).

Make sure that the financial model for the combined entity is robust; in particular that all anticipated synergies have been discussed with the relevant P&L owners on both sides of the deal and agreed. Where relevant, contractual terms must be examined and understood in depth; for example, it's no use planning rent synergies if there's no opt out. One of the most challenging areas to model is revenue synergies: it's very easy to overestimate these. Err on the side of caution and ensure that the acquisition still makes commercial sense on a very conservative basis - if you then still over-achieve, it will be even better!

Ensure that your lawyers have experience of corporate technology transactions and that they have suitable tax, employment and Intellectual Property specialists.

Integration

I've touched on team, culture and values as important pre-acquisition points to consider. It's just as important that you collaborate on developing the integration plan as soon as possible. There's no reason why, post-signing an LOI, you shouldn't pull together the teams and start to work on this.

There will, of course, be some areas which are more sensitive and can be addressed later in the process but you should aim to have the complete integration plan defined before the deal closes. Make sure that this correlates to the financial model!

A key component of the high growth toolkit.

At Notion, we are big fans of acquisitions, so long as they are appropriately thought through and sensibly structured. We believe that they can add tremendous value and can also de-risk execution against strategic goals for the acquiring party.

Yes, there are plenty of examples where acquisitions haven't worked, but there are also many more where they have. In the rest of this report, you will hear the M&A perspectives of some of the entrepreneurs in our own portfolio, alongside advice from experts in getting acquisitions profitably over the line. We hope you find their stories inspirational and that they help put the idea of acquisition where it belongs on your strategic agenda.



M&A Inbox: Keep an eye on the market. M&A Outbox: Master the art of integration

Ed Barrow

Vice President of Corporate Strategy at Optimizely

Ed was formerly the Founder and CEO of Idio, a Notion Capital portfolio company providing predictive content analytics and personalization for global marketing leaders including IBM, Salesforce, Intel, Fitch Ratings and S&P. Idio was acquired by Episerver (owned by Insight Partners), now known as Optimizely. Today, Ed serves as VP, Corporate Strategy for Optimizely, overseeing Corporate Development and Strategic Alliances.



Focus on market mapping

For many growth stage companies, M&A strategy is built on a product-first approach. A product rationale therefore drives the financial business case, in order to maintain a consistent market value proposition.

Companies should continuously assess a Build/Buy/Partner strategy across all product areas, looking at both known gaps and adjacent categories.

A Buy strategy becomes viable and preferable under a typical set of conditions:

- A need to accelerate your technology roadmap, based on a combination of factors, including: addressing a newly identified market opportunity, responding to the competitive environment, and/or demonstrably high cross-sell synergies;
- A lack of internal skills/experience to achieve this through Build (e.g. technical skills or market/product experience);
- When the market presents an opportunity for clear differentiation, usually indicated by less homogeneity within the wider technology ecosystem.

Ideally, an assessment of the companies which might fit the bill starts from the perspective of your own customer base: understanding the technologies they are using in conjunction with yours, and which are consistently driving most value in combination with your own. Customer advisory boards are great for this insight. In today's connected world where software products typically integrate with many others, establishing a technology partnership ecosystem (marketplace) can provide valuable insights into broader category adoption, and allow you to test the water on the potential for cross-sell.

Prioritising acquisition targets is a combination of:

Importance to customers:
how it is rated by its own customers and yours;

Competitor capability:
whether the business has a strong lead over the competition, or is vulnerable; and

Market opportunity:
the capacity for growth.

“Be under no illusion: closing the acquisition only gets you to the start line. Post-acquisition strategy and execution is everything.”

Within each category, it's important to keep options open by maintaining an active review of typically 5-10 key players who match some basic criteria of quality of solution (analysts, G2, are a great starting point) and acquirability (size, funding, growth rates etc).

Combine both inbound and outbound deal sourcing, through active relationships with sell-side investment banks, as well as through your own ecosystem, to build an 'always on' funnel of opportunities for review.

Individual assessment should be product-first with extensive pre-LOI Due Diligence on both product and financials to ensure that the target meets your criteria. Pre-LOI DD rather than post, is critical for three reasons:

- i. In order to gain real comfort and conviction around the target, their product, team and customer value proposition.

- ii. That effort in early-stage due diligence can have value even if a deal doesn't go ahead: some targets will become active M&A opportunities, but those that don't will often transition into partnership relationships.
- iii. Developing mutual satisfaction before moving to LOI - to ensure both sides are 100% onboard.

Some acquirers move very quickly to LOI, which can mean one or both sides undervalue the paper itself. More upfront effort renders the LOI a more serious and credible proposition.

Post-LOI DD is much more about validation and post-acquisition planning.

Structuring the deal

The decisions you will make on building deals are heavily dependent on your own financial structure and capacity, but they will invariably involve a combination of equity, cash and debt.

Debt can be very helpful, and there are plenty of Direct Lending/Private Credit options available, but this normally requires EBITDA-positive projections and a strong financial position from the acquirer to begin with.

For the purposes of equitable structure, there are three key dimensions:

- Equity, in order to maintain incentivisation for founders/key employees,
- Cash rollover (into equity), dependent on the target's capital structure,
- Cash-based retention packages, to help smooth the initial 18-month post-acquisition period; in combination with a longer-term options-based incentive.

Overall, this combination should be a meaningful portion of the overall return for the founders and key employees.

Solving the integration puzzle

M&A can be an exciting part of your overall business strategy. It can also have a dramatic impact on accelerating your commercial success. But be under no illusion: closing the acquisition only gets you to the start line. Post-acquisition strategy and execution is everything.

It is critical to start integration planning early, and not just for the 'day 1' announcements which will hit the tech press headlines, but the day 30/60/90 integrations which will be required to address everything from:

- Organisational design
- A communications plan (employee, customer, partner, analyst),
- Back-office systems (HR, Email, Finance, Procurement)
- Employee values alignment

... and plenty more besides.

Careful planning will be needed for any customer transitions (contacting them, ensuring short-term renewals) to ensure any change to their BAU doesn't derail the value of the business immediately post-deal. It's often the small things (like asking to change email systems or IT policies) that can completely undermine employee morale post-acquisition.

To keep things on an even keel, you will need strong, dedicated project management - established templates (and external support) for integration are available - as there are dozens of parallel work streams that will need a lot of cross-functional collaboration. Most employees have their 'day jobs' and will need to know clearly how to prioritise acquisition integration vs. BAU.

Process change is hard, and often has unexpected consequences and edge cases. Pushing fast can make this harder, so resist the natural desire to get 'post integration' done quickly.

There will inevitably be many aspects of the strategy going forward which will be undetermined at the point of acquisition, but that's no bad thing: you don't actually want to have everything figured out, otherwise many team members will feel left out of the decision making process. At the same time, everyone hates uncertainty - this is the key balancing act for leaders emerging into the post-acquisition landscape.

Key to resolving this challenge is having senior team members (particularly founders / your C-level team) completely aligned and able to fluently communicate the long-term, combined vision. Acquired employees will always have a healthy scepticism towards their new owners, so prior leaders/founders can play a huge role in smoothly steering them through the transition.

Openness, reasonableness and willingness: the heart of an M&A culture

Cisco Villalta

General Counsel and Head of Mews Ventures

Sacha Payette

M&A Manager at Mews Systems

Cisco Villalta serves as General Counsel and Head of Mews Ventures; Sacha Payette is M&A Senior Manager at Mews Systems. Mews Systems is the fast-growing global cloud platform for the hospitality industry, Mews Ventures is the M&A corporate investment arm for the Company that will target acquisitions, investments and partnerships in the hospitality tech sector.



Acquisitions are not to be taken lightly as the failure rate in M&A is high. More small companies than ever are conducting M&A, which is a new and exciting approach but fraught with risk.

Acquiring and integrating a business is a disruptive process - disproportionately so for small companies. The failure rate in M&A is high, and many smaller businesses won't survive one bad acquisition.

Therefore, the acquisition must be compelling, with demonstrable benefit. There are two kinds of acquisition for Mews:

- i. An opportunity to accelerate our go-to-market (GTM): buying a customer base to accelerate our growth and convert customers to Mews
- ii. Product acquisition: a complementary product which allows you to further your objective of creating something truly differentiated.

In the case of a GTM acquisition, our key concern is the customer base and whether it is a good fit to convert those customers to Mews. We ask: "if we buy this customer base, are there enough similarities in their use of a Property Management System that we can confidently migrate

them to Mews?" If there are too many gaps or differences when compared with the Mews product, we are unlikely to progress the acquisition.

For product acquisitions, we are not looking to just add yet another product to sell. In an early-stage business like ours, the acquisition should represent the opportunity to create new incremental value through integration with Mews; bringing something unique that the market doesn't have today and so creating a powerful market differentiation.

And there are some very good reasons to buy product:

- It's almost always going to make sense to buy (provided the economics work) because, especially in small organisations, your R&D team will inevitably be at full stretch with the typical development roadmap and support effort of delivering your own product.
- A build/partner strategy can be defined largely on the economics alone, but there's always further benefit in an acquisition: brand equity, time to market or revenue uplift, for example.

On a "build or buy" product continuum, if a company wants to move fast, we can almost always justify that it's better to buy, so long as we are buying something that's creating a market differentiation.

If that has whetted your appetite, it's time to refine your acquisition strategy. You will need to put in the hard yards to map out and understand all potential targets in the markets you're going after.

Once you understand the pool of targets, then you can narrow down the target list based on some pre-agreed factors, for example:

- Some will just not be the "right fit".
- Size will certainly be a factor. We're at a stage in our own growth where only acquisitions of a certain size are going to make sense.
- Location may be an important issue.

“If a company wants to move fast, we can almost always justify that it’s better to buy, so long as are we buying something that’s creating a market differentiation.”

There will be more; refine your list accordingly on some basic criteria that work for you.

But even with a partially reduced list, you should knock on as many doors as possible; because there are plenty of criteria of a potential target that you can’t fully appreciate until you actually speak to the owners. A good example is the team: are they willing, able and ready to work as part of a combined company?

So map out the market in as detailed a fashion as possible; and then simply tick non-runners and poor fits off the list.

Getting value from a changing Due Diligence environment

Historically, Mews was pretty light on pre-LOI Due Diligence. We would have a basic discussion, exchange a little information and then send an LOI. The bulk of DD followed on later.

But we have found that the LOI has, without any real justification, become a marker of progress towards a deal. It’s a dangerous perception. Once an LOI has been issued, it is easy for both sides to become dramatically more emotionally invested in the deal, and it similarly becomes harder to pull the plug.

Putting more effort into DD before the LOI is valuable, because you can be much more critical on both sides as to whether you want to move forward. Front-loading your DD is a good way to stay rational and objective for as long as possible.

Post-LOI, the key DD themes are in product and technology. For example, on one of our current acquisitions, we’re running a source code scan on the target, in order to see all the third party components embedded in the target’s code. This is a key risk area. Along with the run-of-the-mill corporate DD (such as change of control issues), we will cover a broad range of topics across all functional areas:

- Customer: contracts, degree of commitment, direction of travel, opportunities for upsell etc.
- Financial: business performance and metrics, revenue performance and signals
- Security and privacy: as you can imagine, when you’re thinking of acquiring a cloud product, you could find yourself acquiring huge liabilities here!
- Employees: tenure, skillsets and ongoing availability of skills, engagement

We would say that 75% of the request list stays as-is for each deal, particularly for targets which are broadly similar. In our previous three acquisitions of property management systems, we just tweaked our existing list.

Asset vs. equity

Mews is open to asset deals as well as equity deals. Typically, asset deals emerge when a much larger company chooses to divest itself of an asset that they no longer want to support or sell.

And from our perspective, we might choose to buy an asset either because the company selling it is simply too big for us to acquire outright, or it may have other assets (or skeletons in the closet) which we don't want to bring over or inherit.

This can be problematic for the seller, because they will be burdened with double taxation (once when they sell the asset, again when they realize the proceeds from the entity). A stock purchase or merger is much more tax-efficient for the seller. Barring any problems uncovered in the DD process, the asset/equity distinction is almost neutral for us as the acquirer – which allows us to do whatever is right for our business strategy.

There are further considerations. For example, the early integration phase of an asset deal is really tricky. Everything has to happen on day one, whereas with a stock purchase deal, both sides can ease into their new relationship more slowly.

Whatever the shape of the transaction, when structuring the deal, we put in measures that ensure both parties' definition of success are aligned. For example we might implement an earn-out based on certain metrics or deliverables. We have done this with our first and third deals, and it has worked really well in motivating key leaders post-acquisition.

“Once an LOI has been issued, it is easy for both sides to become dramatically more emotionally invested in the deal, and it similarly becomes harder to pull the plug.”

Build expertise in-house with a culture of “reasonableness”

There is plenty of support, advice and checklists you can tap into throughout the M&A process. There is no shortage of attorneys, deal experts, consultants and advisers.

However, while they will give you an important view on the target, their outside perspective is, by definition, less useful for looking at your own business. And an issue in finance or on the customer side post-acquisition will undoubtedly impact other parts of your business. From evaluation to integration, there are many steps and many opportunities to trip over.

Therefore, we feel that it’s crucial to have M&A expertise internally and to conduct due diligence internally and cross-functionally. From day one, at Mews, we have sought to bring people from our various teams onto deals and to create a culture that is heavy on DD. We want our functional leads and their teams to take ownership of the DD process and the subsequent integrations. It’s not just the M&A team asking them to “check a few things”: we put full functional ownership in place, with the M&A team orchestrating in the centre.

That culture doesn’t come naturally to a fast startup like Mews, as our people are already so busy! People are rightly focused on their own BAU. They want to grow the business, build products and support customers; so refocusing their priorities onto something new – when they already have a

huge degree of pride and ownership over their own domains – is a big ask. Our first deal was really tough, but we are in a much better place now.

Alongside openness and a willingness to take on new responsibilities and ideas, another ingredient of our M&A-friendly culture is reasonableness. Even those with an enthusiasm for the new are thinking about due diligence and “the way things are done” relative to Mews and our own experiences. But other companies do things in different ways. So we think it’s really important that alongside pride in what we do, curiosity and all the other motivators that push us forward at speed, we must temper that with a reasonableness which accepts that, “Hey, this is how they run their business.”

When we have both excitement for our own model and reasonableness towards the target, we can always be rational and realistic in thinking, “how will we make this work post close?” That’s why I think it’s really hard to find external advisors in the core areas like product and technology; success means finding the middle ground and making it work.

Cross-functional expertise is the ticket to post-acquisition success

Buying a business is the easy part. Integration is a team effort and, like everything, improves with experience.

Build a strong, small, internal M&A team and then identify champions across the business in product, tech, sales, finance and so forth. Getting them up to speed is hard, but over time they will become real experts.

An M&A transaction is probably the most cross-functional thing that a startup can do, so, for every deal, we identify the right people cross-functionally that we can rely on.

We start working on the high level integration plan as part of the DD workstreams, with the same people conducting the DD also owning the post-acquisition integration. This is critical. When a person knows that they will own the integration challenges, then they are incentivised to ask the right questions during DD to seek out the answers

which will form the integration plan. Where once upon a time, a functional lead might take some time out to run a DD checklist and then get back to the day job, now they think carefully about what their diligence findings mean with regard to integration, and directly use it to shape a 100-day post acquisition plan.

Thus, by the time we close a deal, the teams have their integration plans, own them and can present them clearly. Everyone understands the go forward plan at the point of close. If you try to get those plans together afterwards, it'll be chaos. You'll be caught in the cultural challenges of integration, miss considerations entirely and make mistakes. Integration is challenging, but it's a lot less challenging when the key strategic decisions have been made before any ink has dried.

Doing a deal can be easy! Delivering a great deal is much harder.

Jan van der Putten
Partner

Kevin McGovern
CEO

Wave Partners acts as an in-house corporate development & transactions (CD&T) team, adding value over the long term by developing a deep understanding of the business, providing impactful independent advice and then taking full ownership of M&A execution.



A great deal begins months before the first acquisition discussions, and ends well after closing.

We believe that an acquisition needs to be:

- Strategic in its (current) objectives,
- Methodical in its (near-term) deal execution, and
- Thoroughly Planned in its (longer term) integration. “SMP” is the art of a great deal!

Remember SMP: Strategic, Methodical, Planned.

Be brutal in continually reverting to the SMP method and don’t get “deal frenzy”, whereby the deal itself becomes the objective!

An Acquisition Strategy should always follow the Company Strategy. Never put the Acquisition Strategy first – that’s the tail wagging the dog! The clearer the Company Strategy, the better your ability to be precise about gaps that need to be filled, when and how.

In simple terms, gaps can be filled by:

- Building capability organically;
- Partnering with suppliers, consultants, competitors etc.;
- Buying a business (or part of one) – the Acquisition Strategy.

All of these approaches have their rightful place in Company Strategy. There is also a trade-off between them: speed, cost, influence as well as the risk, reward and effort involved in putting them in place are all factors to consider. Furthermore, these approaches are not mutually exclusive: it may be a valid strategy to partner first and then acquire (“try before you buy”). Alternatively part build, part buy; and many more permutations.

Generally an Acquisition Strategy makes sense when one or all of the following is true:

- The gap is a core part of your proposition and fundamental to your USP e.g. a key technology or essential offering to a hungry market;
- The sought capability significantly enhances your offering, opening up markets, access to budgets, and/or enhancing profitability;
- There is a strong people element, whereby the expertise you are acquiring can be deeply integrated into your own;
- Financial synergies are close to certain.

Opportunistic acquisitions do come along, but resist the temptation to jump on these just because they are available. Test your approach rigorously through the same lens of your strategic rationale.

There are other reasons to hold back on acquisitions.

Alignment is critical. An Acquisition Strategy does not make sense when the board and/or management team are not aligned on priorities and strategic options. For acquisitions to deliver on their promise takes much effort and a real commitment to making it work. If the roadmap to success is not universally shared in-house, it certainly won’t be shared by the target team through the complexity of an integration process.

It also never makes sense to acquire another business if there are fundamental flaws in your existing business. Two lame ducks never make an eagle!

“Personally connecting to as many potential targets as possible is time-consuming but time well spent.”

The chase is on: how to identify and classify targets

Firstly, it's important to understand that no one target is likely to meet your every objective.

Therefore, be clear on what your strategic gaps and corporate priorities are (see above), so that the objective of the acquisition is crystal clear.

Set your selection criteria accordingly, for example:

- Products
- Customer base type
- Geography
- Financial profile
- Management
- Reputation

... and rank each target accordingly in order to make objective decisions.

If you don't already have a strong list of targets gleaned from your daily operations, they can be sought through a combination of investor networks, customer insight, via desktop research (there are several freely available databases) or external buy-side advisors. Ensuring you are on the radar of relevant corporate finance houses is time-consuming but also time well spent, to ensure any companies for sale are surfaced to you.

We believe that personally connecting to as many potential targets as possible is also time-consuming but time well spent. You will quickly get a much better sense of who fits, both commercially and culturally, and who is genuinely willing to discuss an acquisition. Many potential targets will not be for sale on the face of it, but will be willing to consider a discussion if the deal logic and personal chemistry are right. Most sellers prefer to be sold to a buyer they trust; and investing the time to understand the seller's motivations can help fend off rivals.

It's important to have multiple options for acquisition, so you should continually revisit your priorities and retest your strategic rationale.

Whether to chase or let go most often depends on three factors:

- Does the target meet your selection criteria?
- Is the target available on acceptable terms; and most importantly
- Are the sellers motivated and aligned.

The answers to these questions may change over time, particularly as the names on your target list are refined.

Pre-LOI Due Diligence might feel like effort, but it's of incomparable value

We advise that acquirors undertake as much pre-LOI DD as possible, although sellers are often reluctant to share too much at this stage, until deal terms are understood. It is also key to understand the target's stakeholders (Shareholders, management team, founders, bank etc), decision makers and advisors so that everyone's motivations are clear; they are rarely the same for different stakeholders.

The DD at this stage should be a balance between the hard data (financial and non-financial KPIs, a deep dive on product and technology etc.) and the softer DD (e.g. the management team's aspirations, shareholders expectations).

Pre-investment DD must have:

- The facts: financials, KPIs, product, technology stack
- Alignment: management aspirations and shareholder expectations

Face-to-face meetings cannot be valued highly enough. Doing deals over Zoom is possible, but when the difficult conversations come up - and they always do - having a personal relationship is often the make or break factor.

The pre-LOI DD must be sufficient to build and confirm the business case hypothesis, in the context of the defined strategy. The deeper this upfront effort can be, the faster and more efficient the execution.

There are further benefits, too:

- Having a clear understanding of the target allows for a detailed LOI with substantially all the terms laid out. This helps to avoid any fundamental renegotiation which erodes trust and reduces the chances of a successful completion.
- A good understanding of the target pre-LOI also helps in guiding the post-LOI work, focusing confirmatory DD and legal work on the crucial areas of opportunity and risk.

Don't hesitate to get expert advice - it will pay for itself in multiples. The help you need is dependent on the skills you already have in-house, your capacity and knowledge of the market. Wave Partners should, of course, be your first phone call!

To be most valuable, external advisors must be given as specific guidance as possible on where they should focus their attention. They don't know your business, or the target's, as well as you; so don't assume they will direct their focus appropriately without your instruction. Time invested upfront in being clear on your areas of concern will make a dramatic difference in the quality and efficiency of their output.

Structuring win-win deals

Every deal is unique; and there are a number of levers that can be used to ensure that a deal works for all stakeholders and is aligned to the strategy.

A creative deal maker will use structuring to bridge gaps that may exist between the parties.

Example variables include:

- Cash and/or stock. Upfront, alongside/or deferred/earn-out;
- Different prices for different (classes of) shares;
- Staged purchases;
- Vendor loan notes; and
- Management incentives post deal.

In our experience, the simpler the structuring the better especially for smaller transactions, once complete you want to move on with delivering the plan, not be focussed for months on the structure.

Financing is dependent on the structure as discussed above. If cash is needed, you have several options, including equity, debt, venture debt, vendor loan notes.

The Integration Leader: A “People Person” Planning for Post-acquisition Prosperity

We are passionate about Planning!

Many acquisitions fail because of a lack of a properly-planned onboarding and integration process. In such cases, following a flurry of initial activity and excitement in which the buyer’s team is all over the acquisition and the seller’s team is excited by the prospect of something new and transformative, the momentum dies down into business as usual and, over time, the target enters, “the valley of despair.”

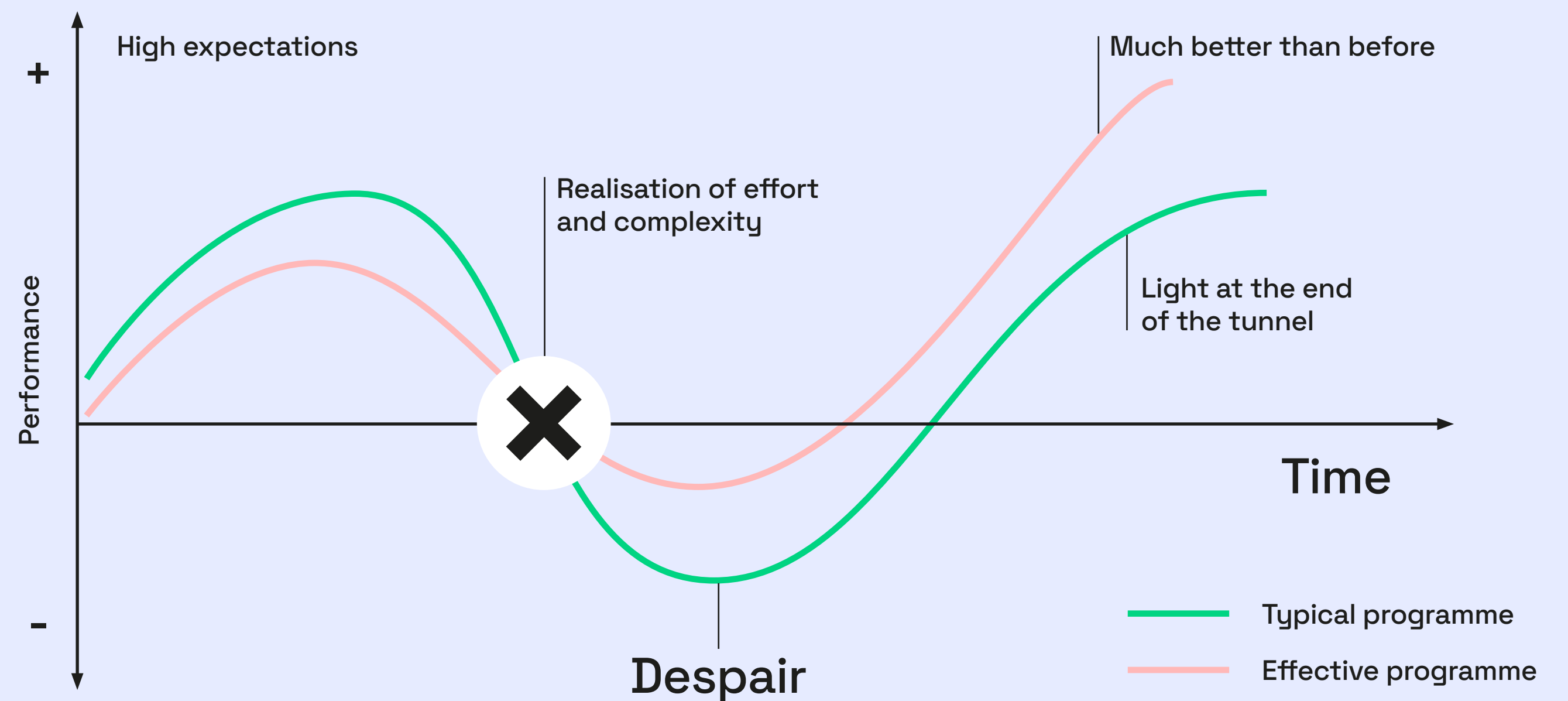
The post-acquisition valley of despair is destructive:

- The best talent leaves
- Customers churn
- The business flatlines and synergies are not realised

Avoiding the valley of despair is much harder than most founders realise. It demands an integration leader, someone comfortable operating in informal power structures, who is part process manager, part conductor of an orchestra and part psychologist. They must be a “people person”, always mindful of the challenges (and opportunities) of cultural integration.

The integration leader lives by one rule: communicate, communicate, communicate!

The classic change curve



Schneider’s Classic Change Curve

Integration preparations start during the DD process: this is a key lesson from every successful (and failed) acquisition.

An integration leader must be appointed as part of the DD team; their job is to prepare the integration plan. This plan is discussed as part of the acquisition deliberations and approved by the board pre-closing.

Post-closing, the target company is made fully part of the integration team and its objectives.

Do not underestimate how time-consuming the end-to-end process will be for the Management teams of both buyer and seller; and the effort required to ensure alignment between internal and external stakeholders. Many balls are dropped through incorrect assumptions that go unchecked! Question, validate and realign constantly – it's the only way to ensure that two juggernauts with significant momentum of their own will end up pulling in the same direction.

Be Strategic, Methodical and Planned, “SMP,” and you will deliver a great deal!



From Full Disclosure to Full Potential: Key considerations when making an acquisition

Melissa Di Donato
CEO of SUSE

Melissa Di Donato is one of Notion Capital's Executives in Residence and CEO of SUSE, a global leader in enterprise-grade open source solutions. SUSE services in Enterprise Linux, Kubernetes and Edge solutions are relied upon by more than 60% of the Fortune 500 to power their mission-critical workloads. Melissa also serves as an Independent non-executive Director at JP Morgan.

Determining whether an acquisition strategy makes sense fundamentally comes down to two factors:

- i. Do you have the means to acquire (not just access to finance and/or cash, but integration capabilities, etc.)?
- ii. Does the acquisition benefit you: is it more efficient than growing on your own?

In terms of assessing that benefit, an acquisition makes most sense when it is aligned with strategic goals, for example:

- i. Filling in existing product gaps, where building organically may present a risk or take too long
- ii. Increasing top-line revenue
- iii. Expanding the company product portfolio to provide customers with more value or to follow market trends and meet customer expectations
- iv. Elevating the profile of the company (market and/or investor perception, demonstrating growth which matches the trend in the sector, etc.).

It's then time to identify targets. What is usually a long list of potential candidates is first whittled down to a short list by the ability to acquire and alignment with the sorts of goals listed above. Typically, there will be a "right" size of business in the market which suits your strategic needs.

Once you have this short list, it makes sense to meet with all candidates who make the cut. The goal is not only to learn about the targets, but also to understand the market factors impacting them. Ideally, these initial meetings will allow you to narrow down your search to around two prime candidates worthy of further investigation through additional meetings and pre-LOI Due Diligence in order to determine which target is best, based on their tech, financials, etc.

“Typically, there will be a ‘right’ size of business in the market which suits your strategic needs.”

The Due Diligence trade-off: time and money for insight

Every acquirer wants the maximum insight from the Due Diligence process, for minimum effort and expense. It's a gamble to conduct a thorough analysis of a business early, only to find skeletons in the closet which preclude an acquisition; equally it would be a fool's errand not to find those skeletons and make a bad purchase.

I think the simplest way to differentiate pre- and post- DD is the level of specificity and depth with which you are able to interrogate data. Pre-DD will not involve a deep dive into specifics like legal contracts, which involve plenty of work - and therefore cost. There will be a raft of similarly complicated topics influencing the business; or bear traps to uncover, which can only be found by a full DD process, post-LOI.

However, you can interrogate the target's financial data in great detail upfront - this is especially important when buying a larger business. As well as the obvious insight into the financial health of the company, understanding the financial levers of the target will help you to model the shape of the combined business in order to test your thesis around achieving the expected benefits. It will also inform your negotiations on the structure of the deal. The most prominent structures for SUSE are cash, equity, and debt; we use a combination of all three depending on the circumstances.

Do get help!

“We place a premium on our people. In growth companies, the people in the target organisation are incredibly important.”

Acquisitions mean a lot of detailed work which can burden internal teams. We heavily leverage advisors of all sorts (banks, consultants – in our case BCG, etc.) to help support our internal teams as well as provide insights important to confirming the business case. We will bring in specialists in finance, technology, legal and HR to deep dive on important matters where our business doesn't have the bandwidth to conduct DD or other work around the acquisition outside the normal course of business. Advisors can also play a critical role in validating the fundamentals of the business case (both the target's business and the combined operation) and the thesis for acquisition, based on their current knowledge and any ongoing market changes (size, shape, direction, competitors etc.).

There is much that can go wrong, from DD through to the final negotiations; so remember: the deal is not done until the merger agreement is signed.

Post acquisition integration: achieving full potential

At SUSE, we have an Integration Management Office (IMO). This team is brought in early in the Due Diligence process to track the thesis and the Full Potential Plan (FPP) with responsibility for working with the various teams to ensure the FPP is realized. This is critical to ensuring not only that the goals are tracked but also that the myriad aspects of people, systems, etc. are adequately assessed in order to make the combination successful.

In our case here at SUSE, it's also worth mentioning that we place a premium on our people. In growth companies where the focus is to build and rapidly grow the business, the people in the target organisation are incredibly important. There must be a strong focus on understanding the people, the culture, and how the integration process can be a positive experience in order to drive the ideal commercial outcome.



“API on Steroids”: A new integration-first model makes acquisitions more attractive

Derek O'Carroll
CEO, Brightpearl

Since taking the helm as CEO of Brightpearl, Derek O'Carroll has led the retail operations platform from stagnant growth to more than \$30 million in revenue, nearly 3,000 customers worldwide, and managing more than \$5 billion in orders. Shortlisted for CEO of the Year at the Business Leader Awards in 2021, the father-of-two is now recognized globally as a retail expert.

Brightpearl, now part of the Sage Group, is the future proof retail operating system (ROS), built to help modern merchants grow.

An all-embracing retail, e-commerce and logistics product, the business covers end-to-end operations, with a particular focus on automation, order management, data/insights and growth. It now also features an app store of integrations for high-footfall e-commerce engines like Amazon, Magento and Shopify. In September 2021, Brightpearl completed the acquisition of Paris, France-based Inventory Planner, giving Brightpearl merchants the tools to accurately predict demand.

A clear and proven rationale for acquisition.

The rationale for Brightpearl's purchase of Inventory Planner was to give us a complementary product which would allow us to increase our share of wallet while we focused on our underlying platform and infrastructure.

We looked at several options and identified demand forecasting as a critical challenge for retailers seeking to optimise their businesses. We realised it was a high-value application that would derive new value from our data and

give us the space we wanted for infrastructure work. It therefore became a key focus for our target search.

We are fortunate that Brightpearl has a large customer base and an open API. We started working through the list of partners using our open API and ran reports to identify the most active applications. We were pleasantly surprised by just how many companies had integrated to Brightpearl and were using our data to deliver value to our customers.

That insight and the breadth of partners on offer meant we could go fishing with some confidence and with an increasingly firm specification in mind. We looked for companies that were:

- i. Profitable, not dilutive;
- ii. With a low cost of acquisition;
- iii. Who offered self-service onboarding and support;
- iv. With a reasonably comprehensible, scalable and modern technology core; and
- v. Whose customers were also representative of our ideal customer profile (ICP).

Several companies became apparent, but Inventory Planner best met our criteria. They ticked all the boxes: they had a large customer base - of whom quite a few also used Brightpearl. Most importantly, their customers loved them.

“We were pleasantly surprised by just how many companies had integrated to Brightpearl and were using our data to deliver value to our customers.”

“We are fortunate that Brightpearl has a large customer base and an open API. We started working through the list of partners using our open API and ran reports to identify the most active applications.”

Proof through partnership

We opened our relationship by white labelling Inventory Planner as an OEM partnership two years prior to the acquisition. In my experience, partnering with a complementary technology company is a great way to start a relationship that might result in an acquisition.

Inside the Brightpearl ecosystem we renamed the product Demand Planner, launched it to the market and pushed hard for 14 months to prove the demand within our customer base. We soon realised that we could sell the product for an increasingly high price and that our sales teams loved it, successfully attaching Demand Planner to 80% of their new sales. After this visible success, we approached our board and presented the rationale for the acquisition.

At the point of acquisition, Demand Planner was proven with our customers and was accretive in many ways - increasing our win rate on new deals, increasing overall revenues and increasing customer satisfaction. At the same time, it had a much larger total customer base, with the majority of their customers in our ICP and to whom we could therefore sell the core Brightpearl platform.

At the time of the OEM agreement, Inventory Planner was a small and highly technical team of 7. The business had achieved \$2.7m ARR, growing at 60%pa, but was facing a serious point of inflection: they did not have the resources and strategic bandwidth in-house to manage a period of substantial growth. At Brightpearl, conversely, we had shown our ability to grow the business. We had also recently raised \$30m, so we were well placed for an acquisition that would add so much proven value.

Shaping the deal

One of my biggest realizations has been that smaller companies can be hard to buy. Our DD was rightly detailed, but as the larger party, the greater burden of hiring lawyers, bankers and other advisors fell on us. We did spend money to get the DD right from every angle, securing experts in technical, tax and finance DD:

- NCC for security
- Tech DNA for technology DD
- Dornando for French tax (Inventory Planner is based in France).
- KPMG for US tax

The offer resolved at a cash offer; plus an amount tied to tech remediation and a small escrow for liabilities.

A Letter of Intent was submitted in April 2021 and signed in May with an agreement to sell. The deal closed on August 31st 2021. The partnership process, which proved the model, took plenty of time; but I wouldn't do it any other way: we had to move slowly at first in order to ultimately move fast. At the point the deal closed, Inventory Planner's ARR was already at \$4.1m, well up from when we first engaged with them.

Platform management instead of full integration

Brightpearl is a core platform, in effect an underlying operating system for retailers. We offer an open API and have many complementary applications that integrate seamlessly with our service.

Our intention is therefore to treat Inventory Planner as an independent, best-of-breed application which plugs directly into Brightpearl. This offers the added benefit of allowing Inventory Planner to continue to innovate and to acquire new customers beyond Brightpearl's reach.

We have installed an experienced COO to support the Inventory Planner team through the technology transformations mandated in the DD process, and we will then put our focus on price optimization and then brand. We have also put in place generous retention payments for key employees, provided they stay for 12 and 24 months.

Our thesis is that we are entering an era of "APIs on steroids", whereby customers want a core application platform inside which they can curate the experience and the technology

for themselves. We want to be that platform for the retail world, integrating effectively with other products - some ours and some from other manufacturers - to optimise the retailer experience and maximise value.

Inventory Planner are rightly proud of what they have achieved; and they serve many of our customers; equally they serve many who are our competitors' customers! We have therefore given them a clear assurance that they can operate ethical walls. Those customers want choice and best-of-breed; but over time I am sure many will see the value of switching to Brightpearl in any case.

We want to keep acquisitions 'outside' the platform, but export a minimal set of most important best practices around data, privacy, security etc. from Brightpearl into the acquisition. So we will run Inventory Planner independently, but install great people alongside them to help them scale, while they operate day-to-day in a parallel lane. We will continue to identify the barriers to growth, get buy-in from the team, and then help them to execute.

Platforms, Partners and Patrons: In today's ecosystem you probably already know your target

Christian Lohmann

Dixa

Dixa's COO Christian Lohmann has a solid track record in the world of investment banking, with a background in finance and business administration from universities in both Denmark and the US.

Christian joined Dixa in February 2021 to lead the company's Series C funding round, notably led by General Atlantic, boost the company's ambitious go-to-market strategy, with a focus on strategic acquisitions, and accelerate global expansion.

With Dixa's acquisition of the Australian knowledge base, Elevio, Christian has played a seminal role in implementing the platform as part of Dixa's overall value proposition.



When it comes to the acquisitions that we seek out, there are two types each with a different M&A profile and objective, these are technology and revenue arbitrage. For a technology acquisition we're looking to buy technology.

We're talking about the code, engineers and product managers. We also only look for minimal revenue because then we won't also be buying the overhead of a go-to-market and customer support team. When it comes to these kinds of acquisitions, I'm all about paying less and getting cleaner assets.

Revenue arbitrage, meanwhile, is a cheaper way of funding customer acquisition than traditional sales and marketing. Here, the ideal profile is a comparable company, but with a legacy product and around 20% of Dixa's ARR (Annual Recurring Revenue). A side consideration is that these companies should ideally be cash-positive.

So whilst an acquisition is the result, the strategies demand opposite target profiles:

- For tech acquisitions, we look for a lot of technology and minimal revenue.
- For a customer base, we look for a lot of revenue, but minimal or legacy tech.

Acquisitions in a platform world

Strategically, there are three fundamental requirements to delivering on our promise to help our clients deliver world-class customer engagement and experiences that turns customer service into value:

- i. The core platform: The core Dixa platform manages and routes all customer data and conversations; it is the system of record;
- ii. Knowledge: In order to deliver outstanding service to customers, Dixa users need quick and simple access to knowledge related to the topics with which customers need support; and
- iii. Automation: Customer service specialists need to be able to automate interactions in order to deliver the level of service customers expect. The Dixa platform therefore needs to route conversations intelligently, with machines doing as much of the work as possible.

We could build all three of those elements, but it makes sense to us to focus on the core platform and then selectively build, partner, or buy for the other two components; which is the approach we have undertaken.

Furthermore, as a platform, the more partners we have, the more value we can offer our clients and the stickier our product. Partnering is a crucial part of our business strategy and also a great precursor to acquisition.

Our core platform uses open APIs and has been built to be open to the world from the outset. This means we've always been able to onboard and manage partners in both the knowledge and automation disciplines which help our end users work smarter.

This open platform approach means:

- i. Plugging gaps - Broadly, our acquisition strategy is to seek businesses which might plug gaps in our knowledge and automation domains. For example complementary API-led third-party applications that create competitive differentiation and, ideally, also bring incremental revenue.
- ii. Leveraging our customers - We are able to leverage our own customers' research and experiences when we decide to consider an acquisition to increase our competitive advantage in the knowledge space. We are quickly able to identify the best targets, in essence the ones our clients use and love the most. In the example of Elevio, we were already partners with Elevio before we acquired their business. We had shared customers and we knew their product inside out.

“Partnering is a crucial part of our business strategy and also a great precursor to acquisition.”

Looking for the “Wow Effect.”

When it came to Elevio, we had a specific rationale for the acquisition:

- Product differentiation which equaled increased value to customers;
- Great tech to leverage into our business;
- Potential for significant future growth across our platform customers

We had a clear picture of the sort of business we wanted to buy from the start, which enabled us to be super-focused on the businesses that we looked at. But what did that mean in reality?

- i. We look for acquisitions that are relatively small in revenue but profitable, so that they are additive in terms of tech, revenue, and cash.
- ii. We look for businesses that we know and have already worked with. A minimal go-to-market team and revenue to pay for doesn't just cut cost and complexity. It also means the financial and customer due diligence is relatively light, and when the target is already a partner (as was the case with Elevio), the remaining tech and product due diligence are also quite straightforward and can be performed by the functional teams. With Elevio, we knew each other's tech stack and we knew that it was working for some of our largest clients, so it was stress-tested and proven.

- iii. We want great founders; people who are highly entrepreneurial and who want to join us on the high growth journey.
- iv. And finally we want an M&A target that has a competitive edge on the tech side; that brings something new to our product. Internally, we call it the “wow-effect”: if we buy something, it needs to “wow” our customers and our employees.

“For tech acquisitions, we look for a lot of technology and minimal revenue.”

As part of the Elevio acquisition, we also inherited 500 customers, some of whom were already using our product. That was not the rationale for the investment, but it has undoubtedly been a benefit. The transition of those customers to Dixa has not necessarily been completely straightforward and will perhaps be more work than we originally envisioned, but the acquisition has been very successful overall. The technology is great and the Elevio team has been a very positive addition to our business.

Due diligence: Downscaled and delegated

Our partner-first approach means we have been able to minimise the due diligence process. Financial due diligence is a very limited exercise, as we actively seek out companies without any financials.

Instead, the assessment hinges on more of a commercial scan of the horizon, which comes down to asking how many customers and how much of the ARR we feel we can retain. We want to know if we can grow, or at least maintain, the target's revenue and decide whether we're going to continue to operate the business as a standalone brand.

We also look for one fundamental criterion: in order for the business case to make sense, it must be possible to integrate the target business – to have a fully up and running product - within three months. If that can be promised, we consider due diligence to be done.

We will figure out the resource requirement to achieve that between both management teams, and of course it takes effort to find out how much work is involved. But at the outset, we look for commitment to the process to ensure that a market-ready product will be available in a clear timeframe so that sales can start clocking up.

That commitment comes from the whole team, because they will be crucial in delivering an integrated product on a tight schedule. We delegate due diligence responsibility and decision-making to the teams - finance, legal, tech, etc. - and they all have to say yes. If they don't all like the deal and the integration process, it doesn't go ahead. I run M&A deals quite transparently and have found that the team at Dixa are keen to be involved. Many have never been in M&A situations, so this is a great opportunity to get involved and learn new skills. I've found that it's fairly easy to motivate teams to get involved and go the extra mile to assess a deal in depth.

We also simplify our due diligence with our deal structure. At the opening of dialogue, we insist that financial investors will be paid out 100%. All VC funds and non-active angel investors will be entirely paid out in cash. We believe that most will prefer this to becoming new Dixa shareholders, but more importantly, if investors and VCs are asked to roll over to Dixa, it will inevitably start a complex due diligence process.

Under the Dixa M&A regime,

- Only founders and colleagues get Dixa shares
- They will be paid half in cash and half in Dixa shares, vesting over four years.

In terms of financing, this has so far been off balance sheet but, going forward, we will almost certainly finance through debt, which is increasingly available in these situations.

Keeping due diligence minimal, we also try to do as much as possible internally, apart from some specific legal activities. Elevio is a good example. The company is based in Australia, so during this acquisition we retained a lawyer to advise on legal due diligence, employer law, IP, tax etc. under Australian law. It's not something we knew about, and on that basis getting external advice made good commercial sense.

Use the decision window just before the deal closes to make really fast progress post acquisition

On one hand, an M&A puts you in something of an inevitable knowledge vacuum, there is uncertainty everywhere.

On the other, it is my belief that there is a moment, just before the acquisition, when participants are incredibly open-minded to big decisions, because they just want to get the deal done.

With that in mind, perhaps the best piece of advice I can offer is that you can make a slew of decisions upfront. You won't be much more knowledgeable six months down the road, as many issues - should we keep the brand, fully integrate the tech, etc. - will still be guesswork. Everyone will have an opinion, and you should be open-minded enough to listen to all parties and change your mind when necessary, but at a time of dramatic changes in both businesses, making some upfront decisions will help you maintain a cadence which can only serve you well.

Hold some hard lines on any acquisition

For me, I was firm on just a few key points with Elevio:

- i. We must integrate within three months
- ii. We must not lose more than 5% of the acquired target's existing customers
- iii. Upsell to at least 20% of their customers

I didn't know at the time whether or not these numbers made perfect sense, but they gave us clarity, direction and firm foundations for the effort required in integration. Adjustments to strategy inevitably have to be made post-acquisition, but it's better to commit to some key decisions and maintain pace than hope for insight that will never materialise.

More than a number: the factors in a successful M&A deal and how to make them work

Ross Davies

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Ross Davies is Of Counsel in the London office of Wilson Sonsini Goodrich & Rosati, where he has a wide-ranging corporate and mergers and acquisitions practice. Over the past decade, Ross has guided clients on structuring, negotiating, and executing high-profile and complex mergers and acquisitions, including in the technology, private equity, alternative investment, and venture capital sector. He has also advised UK-listed clients on bespoke public and private M&A activity, joint ventures, fundraisings, stock exchange matters, and equity capital markets work.

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There are many reasons to pursue an M&A strategy, but three stand out for us:

- Growth: A non-organic route to customer acquisition
- Innovation: Many larger companies become worse at innovation over time because they become entrenched. Early stage companies can also find innovation tough, because of a lack of resources. So it can make great sense to find businesses with good technology but poor commercialisation, in order to gain their IP, their knowledge and their customers.
- Talent: An acquisition is often a competency grab, especially in today's overheated engineering talent market. We are increasingly seeing acqui-hires, in which a business is gutted of its talent rather than a full M&A transaction, but the acquisition route is still very much a path to skilled teams, especially if there are other aligned benefits to be gained.

Advisors should be engaged early. Typically, a relatively sophisticated company will engage us at around the LOI stage. But even that can feel rather late, because by that stage the process can be somewhat frenetic. We would prefer to engage with the company 6-12 months prior to an acquisition. If we arrive when Heads of Terms have largely been negotiated, it limits our ability to add value.

Of course, the main reason for not involving advisors is cost. Many business owners think that a small deal should be simple and therefore cheap, but the opposite is invariably the case: small deals are often more complex, they can include different classes of stock as consideration, deferred consideration and earn-out structures - there's a law school exam's worth of potential issues involved!

“We like to say that we give business owners the scaffolding on which to assemble the right information to support an efficient and smooth deal.”

Creating certainty in a deal full of variables

Our role as advisors is to establish clarity and certainty (both on the buyer and the seller sides) in order to knock out as many major challenges as possible.

We like to say that we give business owners the scaffolding on which to assemble the right information to support an efficient and smooth deal. Engaging and communicating with your advisors is a good opportunity to revisit the key facts and levers of the deal. If you can't explain the value of the deal to your advisors, you can't expect them to act effectively on your behalf:

- Value: As a lawyer, I often have to push for a simple answer to the obvious question: why are we doing this deal? Is it the talent, the IP, the customers? How does the target's business tie to yours? And how you are going to integrate it; because integration is tough and not guaranteed: studies on M&A value consistently show results to be mixed. In LOI language, you are conducting "confirmatory diligence"; confirming that you have assessed the sources of value in the target business. You can't know everything in pre-LOI DD, but you can make some key assumptions and stress test them:
 - What is the source of value?
 - How certain are you that you will achieve it?
 - Is anything going to change between signing and closing, or indeed after closing, which could impair value realisation?
 - Will key employees leave? Will customers terminate their contracts?
- Alignment: Does everyone agree on the value discussed above? We particularly see a variance in larger companies where the corporate development team and the business team disagree over whether to do a deal or not. That lack of internal engagement should raise concerns. We want to see everybody equally excited about the deal.
- Price: On the sell-side, the key focus is price. We concern ourselves particularly with how certain factors might change that price, including:
 - Adjustments for e.g. working capital, debt and cash
 - Post-closing remedies structure e.g. cash in escrow or cash payments simply being deferred for a certain period
- Financing: incredibly, we often get into LOI discussions and find that the proposed buy-side financing isn't clear. The acquiror knows that they want to issue shares and that the numbers add up. But the management team hasn't communicated fully with key stakeholders to confirm that the deal is on value terms which they will support. Is any dilutive impact acceptable, for example? Acquisition teams don't necessarily know what consents and approvals are needed. It's crucial to get stakeholders aligned early.

“In the UK and Europe, the price of doing a deal means something different to the US: selling shareholders are much more risk averse in terms of the warranties, indemnities and other protections that they are willing to provide”

- Conditionality: What certainty of execution do we have? A simultaneous signing and closing minimizes risk; but these are increasingly rare.
 - Are there any major regulatory approvals or implications which might raise a red flag or have an impact on timing?
 - Are there non-standard closing conditions attached to the deal which raise the risk of the transaction going off the rails (customer consents, engineering fixes, guarantees of employee commitments etc.)? The buyer may request a number of these commitments, and they will all add to a seller’s nerves!
- Permissible deal structures in the jurisdiction in which you are operating. In the UK, for example, a US-style merger is not really an option (as the equivalent infrastructure does not exist in the UK) – only a share or asset purchase will, generally speaking, be on the table. In continental Europe, of course, every country has its own legislation and processes.
- Tax is a huge driver too. For example, asset purchases are not uncommon in the US. However, in the UK most sellers will run away screaming, because they feel the tax implications will be so much worse than via a share purchase.
- Conditionalities and risk: Your deal may need to be structured to account for possible risks and/or material changes if there is a gap between signing and closing to account for regulatory conditions or other consents which might delay the transaction (or hold the deal back completely).
- Drag rights: As a buyer, getting to 100% of the target’s shares is very important. The structure of the transaction must ensure that you achieve this, and if DD suggests that the threshold for triggering the drag is particularly onerous (75% is generally standard), then it is important to consider other mechanisms to ensure that the buyer can obtain 100% control of the company.
- Contractual protections: This is often the source of most contention, because market practice varies hugely from jurisdiction to jurisdiction. In the UK and Europe, the price of doing a deal means something different to the US: selling shareholders are much more risk averse in terms of the warranties, indemnities and other protections that they are willing to provide (especially compared to what would be expected in the US). And expectations in this regard are not always set at the LOI stage - you’d be surprised how often we get a long way down the road before reaching loggerheads where there is no agreement between the parties on the allocation of risk.

Structuring a great deal

When thinking about structuring deals, your decision will be influenced by many factors:

A Side note on asset purchases:

This isn't absolutely always the case, but in most jurisdictions and for most deals, the tax outcome for the target will usually be worse on an asset deal than a share deal; because the company selling you the assets will be taxed, and then the distribution of the proceeds to your owners will be taxed.

The tax rate on either of these components may be higher, too. Things are a little less black-and-white in the US, so US buyers shouldn't be surprised to get a visceral reaction against asset deals in the UK!

Many businesses conducting fairly straightforward deals seek a simultaneous signing and completion. However, many owners are not willing to speak to all shareholders (particularly where the company has a large shareholder base) prior to signing the deal, because they worry about the risk of leaks.

That means it's almost impossible to guarantee 100% buy-in on a simple sign / close basis. Even if it's only a week of frenetic shareholder management, most deals will need a small window to get minority shareholders signed up or to invoke any relevant drag mechanisms.

In terms of financing the deal, cash on hand is, of course, always easiest. Stock is fairly simple too, because other than the approvals, it's something you can do without too much third-party involvement. If you don't have cash to hand, consider the value of deferred consideration, which is becoming increasingly prevalent:

- Earn-outs – a performance-based future price adjustment which reduces your immediate need for cash
- Rollovers – a requirement for the seller to commit a proportion of their consideration to the equity in the post-M&A entity, again therefore reducing the buyer's immediate requirement to pay cash upfront.

If you do have to raise money to fund the deal, be prepared for a bumpier ride and to put significant effort into internal PR. Financing invariably lags behind the M&A deal, which can in turn make the deal drag and lead to a deterioration in the relationship between the parties.

The key lessons

Clearly, M&A is not to be taken lightly. It's a complex, unsettling and stressful experience on both sides. Putting effort into some key considerations at an early stage will reduce your risk of failing to do a deal, and even more importantly, drive continued success into the integration phase.

- Unpack your own expectations and make sure you understand the other side's expectations too. Making assumptions and failing to see other people's position is the main reason for deals to go sideways. Particularly in cross-border M&A, you're working in what is guaranteed to be a different corporate landscape and deal culture. You don't have to solve everything immediately but everyone should put their cards on the table so you recognise the key points of difference early.

- Price is only part of the story. On the sell side, founders invariably think that a good deal means a number. But that's only one lens through which to look. This is their baby – they created the company! So a good outcome includes thinking about how long they are happy to commit to the buyer, and in what capacity. Do they even want to do this? How do they feel about how today's employees are taken care of? The broad concept of "what does a good deal look like?" is really important.
- Manage your key stakeholders throughout the process. It requires constant communication on "the three c's": consideration, certainty and contractual protections; all of which will look different depending upon the jurisdictions you are working with.



Make the big decisions pre-deal for a smoother life later..

Justin Fitzpatrick
COO, FullCircI

Justin is the Co-founder and COO of FullCircI (formerly Artesian:DueDil), a Customer Lifecycle Intelligence platform that helps financial services providers do better business faster. FullCircI provides more than 600 leading UK banks, insurers and FinTechs with tools to engage the right business customers, onboard them faster and keep them for life, driving down the cost to acquire and serve. Prior to FullCircI, Justin was most recently Co-founder CEO of DueDil, a Know Your Business (KYB) provider to UK financial services organizations. Outside of DueDil he was Co-founder and Non-Executive Director of Innovate Finance, a membership organization that serves as the voice of global FinTech. Justin has more than 15 years' experience scaling high growth enterprise SaaS and data businesses in the US, APAC and Europe. He's an avid outdoor enthusiast, traveler (COVID-permitting) and foreign policy geek.

The Artesian

DueDil merger thesis is simple: we have complementary products targeted at the same customers; and yet with 600 combined customers, at the point of acquisition we only had 8 that overlapped.

We recognised that by creating an enhanced proposition based on the strengths of our two respective companies, we would have plenty of opportunity to upsell and cross-sell existing customers, as well as attract new ones.

Before a deal is done, both sides should assess each other's businesses from many angles. We spent considerable time with the founders of Artesian running through our values and products. We needed to be confident that there was clear enough overlap to create a working set of shared values and a strategy that would mean the sum was greater than the parts.

We shared a presentation and accompanying paper with both boards. These outlined the rationale for the deal in varying degrees of detail. We followed this written communication with discussions with many different stakeholders to stress-test the deal rationale and generate buy in.

Importantly, we identified all the potential leadership conflicts and questions; and resolved most (but not all) of them well ahead of the transaction.

Strategy and leadership decisions are only the start. Just as importantly, we knew that our teams would have plenty of questions. We spent time anticipating these questions and agreed consistent messages on the key themes. This included speaking with key talent; talking them through the plan and ensuring they were aligned. We set expectations that coming together was the start of something new; and reinforced this message via a series of All Hands meetings with both companies held right before the deal completed. It made for a clear internal rationale which would help guide the teams through the transition.

In addition, we were deliberate about creating opportunities for individuals in our respective teams to get to know each other and build their working relationships as early as possible. Following a review of all talent to make sure we had the right people in the right seats we started matching people up to work on challenges related to the integration of the two companies.

We also agreed upfront to a rebrand of the combined business, although the process of implementing that rebrand started post-merger and is ongoing.

“We set expectations that coming together was the start of something new; and reinforced this message via a series of All Hands meetings with both companies held right before the deal completed.”

Unlock the latent goodwill in your people, unlock new value fast

Partly because of our focus on the people aspects of the process and partly because of the natural fit of our businesses, there's been much goodwill on both sides. We've capitalised on this to bring the teams together and accelerate our ability to integrate.

Overall, our people have got along well and embraced the idea of working together as one new team. Our customers and the broader ecosystem have also been supportive. A positive response from one group reassures others. In terms of the main lessons from the experience so far, I'd highlight the following:

- i. We've been very organized and moved rapidly to realize the projected synergies;

- ii. We all adopted the EOS framework for running the business, which has been a good guide as we merge the company;
- iii. We brought the story to our customers early and often in order to encourage their buy in - and most have;
- iv. We profiled the entire leadership team and key leaders the next level down for intrinsic drivers and values -- this has helped us understand how to communicate more effectively and work better as a team; it's also flagged where we might have an issue we need to address
- v. We've been disciplined about spending time together working on business issues but also on how we work together, although it would have been better if more of this could have been in person; and
- vi. We were proactive about identifying journalists to tell the story to, and we gave them insight into the rationale as to why the merger is an exciting combination.

“Us and them”: from the team to the press, it's tough to stamp out

All of that said, the “us-and-them”-speak always dies hard. I think it's inevitable that people are tribal - it's a function of the loyalty that founders nurture and use in every high-growth business. And those old ways of thinking can take a while to die.

Part of the rationale for the rebrand has been to bring our unified business a single, new identity. Sometimes it's difficult to avoid distinguishing between the two sides, and occasionally it's become apparent in an unconstructive way. It's very hard to root out and just takes time.

“ We profiled the entire leadership team and key leaders the next level down for intrinsic drivers and values – this has helped us understand how to communicate more effectively and work better as a team.”

“People are tribal - it’s a function of the loyalty that founders nurture and use in every high growth business.”

We were also afraid of spooking talent in a hot job market, and in some cases I feel that we tolerated the wrong people in the wrong seats for too long. It hasn’t been a major challenge, but on reflection we should have moved quicker to press the people in question as to whether they were truly onboard with the shared project or not. They left the company in any case, so some sort of voluntary redundancy package probably would have done the job.

I feel we were slower than we should have been in addressing known differences in levels of compensation. This naturally has an effect on employee engagement and motivation; and that’s an unnecessary brake on the momentum and excitement of integration.

Also, remember that bad news always travels faster than good. We suffered a negative press article about the deal that was picked up by one or two sources, but I’m not sure there’s much we could have done ahead of time. Sometimes journalists take information out of context and think there’s a story there where there isn’t. When it happened we followed up with a few friendly journalists and gave them more context, which went some way in helping turn a negative into a positive.

There are a number of things I think we did well, but there are definitely things I would do differently:

- i. Complete the leadership profiling exercise before the deal completes.
- ii. Be brutal about putting the right people in the right seats fast; offer voluntary redundancy to clear out those who aren’t bought in.
- iii. Address disparities in pay upfront and more systematically rather than on a case-by-case basis.
- iv. Engage more face-to-face and in person across the teams (this was difficult for obvious reasons)
- v. Finally, start the rebrand exercise as early as possible.

Our journey to value is well under way

We're some way off from an exit event that will ultimately realize the value we are creating, but the steps to get there are progressing in line with our plan: growing revenues, increasing customer satisfaction, creating a combined product proposition and mobilizing the team.

We're on track, if not slightly ahead on realizing our expected synergies. As expected, there's been some collateral damage along the way, but we've managed to keep most people in the boat and the metrics prove that we are making good progress as one team. The original thesis for bringing the two businesses together has held; and we're doing what we said we'd do.

It's a well-known fact that most M&A fail. Although there have been bumps in the road and there will undoubtedly be more, the rationale for the deal and the motivation of people from both sides to make it a success is paying dividends. Most importantly, the combination creates an exciting new entrant in a market with huge opportunity. The deal has proven the right move for our combined company and shareholders.

Thank you for reading
our 'VC Guide to Mergers
& Acquisitions'

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