Understanding Management's Leverage in a Divestiture Process

The scenario is played out time and time again. Management works diligently over many years to build the value of a business. Just when all is going well, the business owner decides it is time to sell and liquefy the value created in the investment.

Having received only paychecks over the years, and believing they have no control over their futures, management teams often feel betrayed. Managers often believe the rewards of ownership are just an out-of-reach dream since they have little equity or discretionary funds to purchase the very business they were so instrumental in creating.

Why is it that in a majority of cases, when an owner decides to sell a company, management is not actively involved in the divestiture process? The answer appears to lie in the faulty assumptions that managers do not have the wherewithal or the knowledge to affect the transaction. Management clearly does not realize that it has the ability to maximize its future ownership and control. ***The reality is that key managers have sign ficant leverage because they were an integral part of the value creation and will likely be key contributors in the future success of the business.*** By obtaining control of the divestiture process, management can chart its own future course by establishing the terms of entry into ownership. Key benefits, among other things, may include an equity promote, favorable employment contracts and the potential for board control.

As a part of gaining control of the sale process, management needs to identify and prioritize owner objectives. Does the owner wish to maximize value? Does the owner want the business to survive and run autonomously? Management must obtain answers to these and many other questions before approaching owners with a plan to purchase the business. Furthermore, because of its familiarity with the business, management has significant advantages in the purchase agreement negotiations over a third-party buyer and these advantages would be viewed favorably by the seller.

In most cases, managers are surprised that the seller is more than willing to sell the company to key managers if those managers can meet owners' goals as well as prove that they have the wherewithal to accomplish the transaction. In fact, owners may go out of their way to reward management for ajob well done. It is often more rewarding to owners to see value accrue to trusted managers instead of to a third-party buyer.

Finally, managers are often pleasantly surprised by the amount of private funds available to accomplish management buyouts. They are further pleased to learn that there are solid merger and acquisition advisors available to assist them step by step through their quest for ownership.