

There Are Options Other Than Selling Your Company... Management Buyouts

A Management Buyout ("MBO") is a type of transaction whereby the management team of a company buys the company from the owners. "Management" may be one or more of the company's existing managers. This can be a solution for an owner who wants to reward past loyalty, wants to see the company continue into the future largely unchanged, or who may have made some level of commitment to key managers that the business could someday be theirs.

Employees, even top level managers, don't typically have the cash an owner wants at closing. The Transition Companies *M&A Process* identifies a private equity group ("PEG") as the financing partner and structures a transaction with non-owner managers to buy the business and pay for it at closing much the same way a third party would. Partnering the same type of financing source with non-exiting family members may also be a solution when family members want to buy out other family members, or when owners want to pass the business to the next generation.

The sources of the funds for the MBO are money managed by the PEG and generally some amount of debt capital from a bank or other lending institution; management may also be allowed, asked, or required to invest money in the transaction. Members of the management team own a portion of the company and the PEG financing partner owns some as well. The amount each group owns at the completion of the transaction is generally a function of how important each is to the transaction and subsequent operation and success of the Company. The amount of money invested is usually the primary factor, but it is not the only factor.

The management team and the source of the financing rely on one another to complete the transaction, and to mutually benefit from the future performance of what will become their company. Each brings something different to the alliance. Management must be capable, experienced, actively involved in the inner workings of the business and completely committed to the transaction and successful future performance of the company if they are going to attract a financial partner to the transaction. The PEG financial partner expects that any transition from the owners to the management team will be brief and smooth, and that the management team will stay throughout the financial partner's involvement. Owners, who have played a key role in critical aspects of the business, for example product or service development, customer relations, production or service implementation, etc., will be leaving. Their roles have to be filled by the management team, or replacement talent will have to be hired.

The MBO begins no differently than any other type of M&A transaction and the objectives are the same: to provide the owners and managers with the greatest number of financing options to choose from to maximize the deal structure for the owners and management team while permitting them to choose the most beneficial financing partner.