NAVIX™

The Story of the Paralyzed Partners

The following case study is based on a true story. It highlights the importance of co-owners in a business recognizing their exit objectives may not be aligned. Owners need to plan their exit years prior to the event and work with an experienced team of advisors, like our NAVIX Consultants.

Key Lessons:

- Business co-owners need to discuss and set their exit objectives years in advance.
- Co-owners with incompatible exit objectives should address those issues now, before a potential buyer is standing in the doorway.
- Buy-sell agreements often lack adequate provisions to address an early buy-out of an owner, and tie-breaking provisions when stalemates occur.
- When exiting, especially via sale, timing the market is critically important.
- Business owners need to work with advisors who are experienced in helping clients achieve successful exits.

The Story of the Paralyzed Partners

Al and Bob were 50/50 co-owners of a community bank consulting firm that they founded in the early 1990's. Although Al was twenty years older than Bob, they were equal partners across the board and got along well. Business was good, and one day they intended to sell their business to an outside buyer. But Al and Bob never discussed their plan on when to sell and for how much-they were too busy growing the business. Other than taking the prudent step of implementing a buy-sell agreement between the two of them, their future exit plans were just that-to be determined in the future.

In the mid 2000's, a potential buyer came along and offered $10 million for their business in an all cash purchase. Al, 62 at the time, was eager to sign. He already had some money put away, his wife had a pension, and their beach house had no mortgage. With his half ($5 million before taxes) added to his existing nest egg, Al would be financially free for life. Bob, age 42 at that time, did not want to sell. He had three kids, none yet out of high school, and not much money outside the business. His half of the sale proceeds would have been insufficient to meet his financial needs. If Bob sold, he would have to stick around and work for the new boss, find a new job, or start a new business all over again. None of those options appealed to him.

Al and Bob could not agree. Eventually, the potential buyer went away.

The experience revealed to both owners a critical issue-they had incompatible exit objectives. Al was financially ready to sell. In fact, he was eager to exit. Bob was financially unable to sell at the business's current size and value.

The 50/50 owners sat down to figure out their situation. By now, their choices seemed limited because they had different objectives. Bob was in favor of holding onto the business, and reinvesting their profits to grow the business in order to sell in the future at a higher price. Al did not want to forgo the business's current profits, and did not want to keep working for many more years. Al offered to sell his interest to Bob, but only in an all cash deal. After all, that's what the potential outside buyer had offered them. Bob was unwilling to take on millions of dollars in debt nor accept an equity partner to do this. They were stuck, and had no clear way to resolve the issues.

So, what did they do? They went back to work.

About a year later, another buyer came along and offered $11.5 million cash. The community bank industry was booming, and M&A activity was hot. The two owners found themselves in the same situation. Al said, "Where do I sign?" Bob said, "I can't afford it." Both men grew frustrated.

The second potential buyer went away.

The business co-owners then pulled out their buy-sell agreement. A careful read of the agreement revealed something disturbing. While the agreement had provisions addressing the possibility that one or both of them should die or become disabled, it said nothing about what they would do if an external buyer came along and one wanted to sell but the other did not. Furthermore, there was no tie-breaking

provisions. They owned the business 50/50. Each of them could do nothing without the other.
The solution seemed clear-update their buy-sell agreement. Al and Bob sat down with their attorney, but pretty quickly the choices available to them were just as paralyzing as before. Neither owner wanted to buy the other out. Neither owner wanted to give up one percent and become a minority owner to the other. Neither owner could agree with the other on a tie-breaking method for fear of losing control.
The issue dragged on for weeks and then months. Their legal costs rose, and their relationship fell.
Al felt Bob was blocking his financial freedom. Bob felt Al was insensitively trying to force him to do something that put his family at risk. They grew angry with each other. They failed to reach a breakthrough.

About a year later, with nothing resolved, a third potential buyer came along. M&A activity in their industry was at an all-time high. This buyer offered $14 million in cash. Al wanted to sell. Bob did not. They argued, at first behind closed doors but later in the office hallways. They stopped attending meetings together. When one was in the office, the other would work from home. The staff was on edge. Customers sensed there were problems.

The third potential buyer went away.

When it seemed like their situation could not get worse, it did. In 2008, the US economy fell into the worst recession since the Great Depression of the 1930s. The declining economy and rising unemployment was a perfect storm for banks: loans of all types fell in record numbers, asset values crashed, and full recoveries of problem loans were all but impossible. Community banks were hit especially hard. Between 2008 and 2010, the number of US community banks failing each year tripled.

As the community banking industry roiled, Al and Bob's business was rocked. Revenues fell by more than 60%. Profits disappeared. Staff was cut by two-thirds. No more potential buyers came knocking.
The value in their business had all but disappeared.

Al and Bob lost not only all of that value, but they lost their ability to work together as well.
They each blamed each other, and bore deep resentment and hostility. Yet they remained co-owners, dreading going to work and regretting the decisions they made and did not make.

NAVIX® is a proprietary process that helps business owners plan for and achieve successful exits.

NAVIX® helps owners of closely held businesses plan for and execute successful exits: achieving financial freedom, creating a sustainable legacy, and exiting on their own terms.

NAVIX® was designed out of experience seeing business owners struggle to achieve financial freedom, create a sustainable business legacy, and exit on their own terms. NAVIX® is a dual track process, that prepares both the business and its owner(s) for exit. NAVIX® is not just about planning; we also help clients execute the strategies and tactics needed to achieve a successful exit.

To learn about the NAVIX® program, please visit

navixconsultants.com

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