FOUNDER MYTHS & CHALLENGES — 3 OF 4

Acresis is a company of Founders, for Founders. We have earned our way through many important life and work lessons, truths that stand out as "things I wish I had known before I started." Below are some of the most important Founder myths and challenges that we have had to work through in our own businesses and in partnership with over 100 of our Founder clients. Many may seem obvious, but we also know that when everyone is in the trenches, even when you are leading the charge, it is easy to lose sight of what can really make a difference in the success or failure of your business.

"Is now the time to take chips off the table?":

If your business is operating with 'A' grade performance metrics, you can still sell and exit successfully even if markets are flat or down.

If you are a pure SAAS company, you can still sell typically at a 4x to 8x revenue multiple, if your business is:

- Growing at > 40% CAGR,
- Delivers > 80% gross margins
- Has >$5M ARR in TTM and
- Exceeds the 'Rule of 40' test
- Is no worse than break even and ideally cash generative

If you are a Consulting and Services company, you can still sell at a 6x to 10x EBITDA multiple, if your business is:

- Growing at > 20% CAGR,
- Has gross margins > 50%
- Has Ebitda > 15%
- Has >20% recurring revenue
- and is cash generative

If however, your business is still developing with significant improvements required ahead of you, then we recommend deferring a transaction. What is universally true on both sides of the Atlantic, is that strategic buyers and investors are subjecting potential transactions to far great scrutiny and transactions are only completing where buyers and investors have deep conviction for both the market and the deal in question. Conclusion.... launch a proactive, persistent campaign to develop relationships with strategic buyers, alliance partners and investors who may be interested in a transaction with you in the future.

"Why Should I Sell?":

Acresis is often asked by Founders, why should I sell? Over the years, Acresis has gathered a number of reasons that can instigate an Exit process:

- The equity value that a founder holds in their company represents a significant proportion of that founder's wealth and net worth. In some cases, their company represents > 90% of their entire net worth. Some founders can live with this real risk over multiple decades, but most founders reach the point where de-risking and 'taking chips off the table' becomes a key next step.
- Exposure to persistent, long term risks gets old: tough economic conditions, the dot.com crash, the Great Recession post Lehman's collapse, high inflation, war, global pandemic, regulation, compliance, Brexit, impact of GenAI etc etc. Indeed . . . . what's next!?!?
- Tough credit/debt conditions, DSOs lengthening, and fast growing companies that sadly consume greater working capital, all result in the founder often being the day to day lender supporting their business coupled with tougher Personal Guarantees required by lenders. Again, over time, these stresses get very tiresome and can dull the entrepreneurial spirt.

If a Founder wants to step back from day to day leadership of the company, treating their equity as a 'long term hold' and acting more as a Shareholding Board member, then the Founder needs to attract, develop and retain very strong management team leadership for the company. This can be even more challenging than launching the company in the first place, for example:

- Retaining existing talent can be challenging, especially great talent in hot sectors
- Upgrading new, more professional talent, vs. "loyal amateurs"

Over time, relationships and ambitions between Co-founders can diverge and the safest route forward may be to Exit. Reasons for a Co-Founder leaving the business:

- a Founder's ambition outside the current business can drive timing on exit:
- Ensuring and realising 'first generation' wealth
- Ensuring and realising 'second generation' wealth, ie wealth transfer to the next generation
- Having capacity and time to prioritize dealing with a health or medical issue
- Spousal divorce
- Moving on to founding 'venture #2'
- Moving on to a philanthropic and purpose-led career stage

"How should I think about Proceeds from the Exit?"

The good news is, there are many different deal constructs open to founders, from a 'one and done' model right the way through to multiple drinks from the liquidity well over a 5-10-15 year duration. If you plan properly well in advance of the Exit, with the help of experts such as Acresis, bankers, wealth management, legal, tax . . . 'forms of consideration' can include:

- Cash upfront – Day 1
- Earn-outs: time-based and/or performance-based payments which can be in the form of cash or equity
- Interest bearing Loan Notes, which settle either on a fixed timeline or on the next liquidity event
- Roll-forward equity into a PE backed 'NewCo' – this can range from 20% to 60% with the goal being that roll forward equity cashed out in the future will be at a much higher valuation and absolute value than the portion on Day 1 with NewCo.
- Sweet Equity or Option Grants
- Salary plus variable cash compensation.
- Potential participation in a "Management Incentive Plan (MIP)" – equity equivalent, usually not taxable until there is a future liquidity event.
- It is worth remembering that buyers will require Escrows of approximately 10% of Enterprise Value, to cover potential liabilities such as unpaid employers' tax, sales tax, legal, regulatory, client litigation et al, which be released post the deal close (usually 1-2 years). Well run companies should not be fearful of these escrows. In some circumstances it may be possible and economic for sellers to purchase Representations & Warranties Insurance (RWI) to materially reduce the amount of cash held back in Escrows. For example, with RWI you can often garner 95% of the Cash Consideration upfront on Day 1, versus only 70% to 90%.

Acresis can safely say that over the past few years, transaction structures are placing a markedly greater proportion of consideration subject to performance of the business post acquisition . . . aka performance-based 'earnouts'.

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