INTRODUCTION: WHAT HAPPENS AT THE END?

If you treat an individual as he is, he will stay as he is,

but if you will treat him as if he were what he ought to be and could be,

then he will become what he ought to be and could be.

\- Goethe

Let's begin with an ending.

One April afternoon in 2010, at about 3:30, the Executive Vice President of Material Tech called all three hundred employees of the company to the cafeteria for a special announcement. At Material Tech, a high tech manufacturer of precision parts made from exotic alloys for the medical and energy industries, this was an unusual occurrence, so everybody hurried out of their offices, and left stations on the manufacturing plant floor, speculating about what was going on, seating themselves at the tables and on folding chairs. It was a cold room, gray linoleum floor, vending machines lined up along one wall, overcrowded with two shifts worth of people. The Executive VP stepped up on a chair, and asked in a higher-pitched voice than usual: "Can everyone hear me?" Then he delivered the news. Bob Borden, Material Tech's President and majority stockholder, had sold his stake in the firm to a private equity group well known for its investments in material sciences. At first, there was stunned silence. There had been no hint of this. No rumors. No water cooler chat. No online blogging speculation. Everybody was taken by surprise.

After the employees had gotten over the initial shock, the inevitable question popped into their minds. What does this mean ***to me****?* They pondered this as they listened to the Exec VP give more details of the transaction. It sounded as if it would be a good thing. Material Tech would continue to operate independently, largely as it had, although the Executive VP was becoming President and CEO while Borden assumed the post of non-executive Chairman. The plant would stay right where it was. There would be no lay-offs. There would be fresh capital to make some much-needed equipment purchases to help the company expand. People breathed a little easier.

Then…a jaw-dropper. Of the substantial enterprise value Borden personally realized in the capital gain, he had set aside $6 million of his personal proceeds to be distributed among the employees. On average, each one would receive about $20,000 in cash in their next paycheck as a partial acknowledgement of their role in making the company successful. Once again, there was silence. Then somebody began to clap. More people joined in. Chairs scraped back as a few jumped to their feet. Pretty soon everybody was standing and clapping. There were eyebrows raised, grins and tears of joy and gratitude, whistling, and cheering. The racket went on for a full three minutes.

But Bob Borden was not personally present in the cafeteria to witness the response to his generous action. Later, when I asked him why, he explained that he hadn't done it for the recognition or praise. Besides, he said, public outpourings of emotion always made him uncomfortable. Still, I could tell he was deeply moved. Thirty years earlier, he had started his working life as an hourly employee on Material Tech's manufacturing floor. He had worked his way up through the ranks. As he described it, almost all that was good in his life seemed to somehow have come from his relationship with the company—he had met even met his wife Jacki there for goodness sakes. There was no question that Borden had earned this wealth creation event, and he and Jacki were committed to recognizing the contribution of all the employees who had helped achieve Material Tech's success. Now he could move on to the next chapter of his life. He told me there were many new challenges he wanted to take on.

Bob Borden is the exception that proves the rule. He had a clear idea of what a positive outcome would look like, for him, his company, his family... in fact, for all the stakeholders. But most entrepreneur owner-managers (EOM's) do not have a picture of how they would like things to turn out. They don't begin with the desired end in mind. And frequently as they get closer to it, they're still uncertain what course to take.

Beginning this book with The End is more than a rhetorical tool—it reflects a deeply embedded idea in how I think and interact with our clients. As we work together, what is our desired destination? What is our intended outcome? Starting with the end lets us dream, consider different destinations, set goals, and plan how we might get there. Obviously, no one can predict with precision what will occur in the future; the future is not knowable. And as you'll see, there are aspects to the private capital markets we inhabit that are especially resistant to accurate prediction. The truth is that we as advisors, can envision what will actually happen at the closing table only a little better than you, the entrepreneur owner-manager, can. What we do know with absolute certainty is that a rich and robust conversation now about your personal life *after* the business transaction—in other words what we term the *simultaneity* of the personal transition and the professional transaction—is directly connected to achieving a successful outcome for the wealth creation transaction.

That means asking and answering questions about your evolving role in your business and how your personal identity is wrapped up in it. It means imagining what life will really be like on the first Monday after the closing. It means picturing the lives of your customers, vendors, and employees; of your partners and your family; of you and your spouse after the new owners are driving the car that you lovingly washed and waxed for so long. And it means learning about how you might manage the newly liquid wealth that will be created in a transaction someday. It means thinking about and exploring a new life purpose, or at the very least, a changed role in the enterprise. Will you imagine it?

Too personal? Too off topic? Hardly. This is personally challenging stuff, but so is building a legacy. I have seen again and again how professional transactions and personal transitions are tightly intertwined. Together they merge as a legacy, *your legacy*. In the pages ahead, I will guide you along the converging pathways of the professional and the personal. I hope to show you how the people I consider to be my best friends and greatest teachers—seasoned, successful owner-managers—are able to earn a fortune *and* simultaneously create a permanent positive legacy. I see this book not so much as a checklist about "how to" and more about the "why to."

If you are a seasoned, successful entrepreneur owner-manager ("owner-manager"), then acting on what you learn from reading this book will positively change your life. You will learn firsthand details about how other owner-managers like you built and captured a capital gain beyond their wildest expectations, and earned a positive legacy that brought them respect of their families and peers that will likely persist for generations. These chapters will share hard won insights to how they did it. They will give you direction, which you can then choose to employ (or not). While this book was written for owner-managers, the same goes for expert advisors to owner-managers; you live this every day with your clients.

Plenty of books have been written for would-be entrepreneurs. Some of them are "how-to" books: how to write a business plan, how to raise capital, how to buy a business, how to protect your invention, how to incorporate. If you are a budding entrepreneur or piloting an early-stage venture, we wish you much luck and good fortune. In this book, you will almost certainly encounter insights that are worth returning to as your journey unfolds, but it wasn't written for you. Nor is this book written for the academic community. To me, the idea of an academician instructing a group of would-be entrepreneurs on the theories of building and capturing enterprise value is rather like a group of novitiates in a monastery talking about sex.

The readers who will find immediate, even life-changing guidance here are seasoned, successful owner-managers—and their professional expert advisors helping them succeed and thrive as the entrepreneurial journey enters its most productive closing chapters. And by the way, when I use the term "owner-manager," I am referring to three related but distinct animals: CEO's with family stockholders, CEO-founders, or CEO's with institutional investors. I don't want to cause any misunderstanding that the term entrepreneur applies only to "start-ups" or early stage ventures.

I focus in these pages on stories of positive successes I have personally witnessed, on owner-managers who strive and ultimately flourish, who give life to our highest hopes, and make the world a better place. Success doesn't necessarily come quickly to them, but ultimately, with perseverance and patience, it does. How did the people who succeeded beyond their wildest dreams do it? Read on.

Most owner-managers are street-smart critical thinkers who value their liberty and independence and don't want a lot of help. Nor, candidly, do they need it. And nothing in this book is to suggest anything about the owner-managers' *operation* of their business or conduct of their personal lives. The genesis of this book is the pang of regret I feel after a wealth creation transaction when I hear an owner-manager say "If I'd only known *then* what I know *now*." My intention is to give you a glimpse of that care in advance—call it wisdom won out of scar tissue.

What a gift it is for those of us who are owner-managers in the Twenty Teens compared to the 1980s or even the 1990s. Technology has leveled the playing field between large and small firms, and the advantage enjoyed since the 1950s by large hierarchical bureaucratic organizations has diminished. But it is more important than ever to have a clear idea of your desired outcome, because the private transaction market (where we play and about which we will go into in detail in Part II) has become highly complex, with asymmetrical information and sophisticated investors who typically have much more experience in the market than owner-managers. In the 1980s, the standard transaction involved an owner-manager who had reached the end of his career and wanted to sell the business. The typical purchaser was a strategic investor, usually operating within the same industry, who would buy the entire company and assimilate its operations into its own. The owner-manager got a pay-out and made his exit. It wasn't until the end of the '80s that private equity groups (PEGs) were invented and came on the scene. They provided a new source of capital as well as a new style of investment. They were not interested in a 100 percent purchase of a company or in managing operations. They act more like a partner—a highly focused and motivated partner—than a traditional buyer.

The Merger & Acquisition (M & A) advisor role has changed, too. It used to be that you could choose to work with a smaller advisory firm which had the benefit of being local and, thanks to its size, might give you individualized attention. Or you could go with one of the large, legacy, logo Wall Street firms. They sold themselves on their expertise with bigger transactions, access to proprietary financial data, and dedicated research staffs.

I am not objective about all of this, as you can imagine, but it's clear to nearly everyone that the big M & A advisory firms have no inherent advantage any longer. Scrappy boutique M & A advisory firms have access to the same databases and get the same information on every company in the world at exactly the same time as the Wall Street firms do. What's more, the economy of scale that may once have been an advantage for the big firms is now, I believe, a diseconomy of scale. These firms are so big and bureaucratic they have no business advising private owner-managed companies that are a fraction of their size and are run by hands-on leaders with skin in the game, rather than corporate caretaker/employees. They simply do not understand or empathize with the challenges of owner-managed private enterprises, nor for the most part are they effective with them.

Not only do the investors and advisors look different today, the profile of the typical owner-manager has also changed and will continue to do so. They are planning and achieving their business transitions earlier in their lives. Some build more than one business and go through more than one wealth-creation event. They're living longer and have greater expectations for the years that used to be called retirement.

We're seeing a rapid gender shift in owner-managers. More and more women will be making legacy decisions for the companies they have created and built. Although most of the seasoned successful entrepreneur owner-managers I have met in my practice so far have been men, I am happy to say that my intuition, and some good data, tells me those days are over. A recent study by the Kauffmann Foundation[1] found that 30 percent of the owners of entrepreneurial firms are women, and reported that men and women see the challenges facing entrepreneurs the same way, that women have no more difficulty raising the financial resources necessary than men, and that women have always wanted to be part of an entrepreneurial culture. In fact, in the study, women were more likely than men to say that "working for someone else doesn't appeal to me." Add to the equation the growing education advantage that women have and it is clear to me that women will soon close the entrepreneurial "gap."

We are living and working in an era of great change and huge potential. Over the next two decades, we're going to see a monumental shift in ownership along with the largest transfer of

[1] (Kauffmann, 2010)

wealth in history. There is so much opportunity ahead that more buyers—and new types of buyers—are flooding onto the scene from all over the world, with vast amounts of capital to invest specifically in successful privately owned businesses.

In writing this book, I realize that our sample size—the number of companies my firm and I have worked directly with—is relatively small, and the work is necessarily qualitative; our knowledge can never be complete. So I have attempted to weave in insights from the most gifted and influential thought leaders who play at the intersection of entrepreneurship, psychology, finance, and probability theory, including Marty Seligman, Danny Kahneman, E.O. Wilson, David Brooks, Steve Jobs, Steven Rollnick, Nassim Taleb, Peter Drucker, Barry Schwartz , Michael Mauboussin, Clay Christensen, Atul Gawande, Dan Gilbert, Dan Pink, Richard Zeckhauser, Chris Peterson, and many others.

Still, although my sample size may be small, given the total number of transactions that have taken place in the past thirty years, I have met thousands of successful owner-managers and have had the opportunity to consult closely with hundreds of them. I have energetically pursued my career—actually I think of it as a calling—because I believe that the entrepreneur owner-manager of a private enterprise is one of the most important pro-economic, and pro-social forces on the planet. That is because we all share in the massive capital gains created through the recapitalization or sale of these companies. The liquidity they generate quite literally funds the entire philanthropic not for profit sector as well as investment in new enterprises. Think that is a bold claim? A quick glance at the names of the hundred largest private charitable foundations provides ample proof that it is true: Gates. Buffet. Ford. Getty. Johnson. Hewlett. Kellogg. Lilly. Packard. MacArthur.. Moore.. Every single one began as an entrepreneur owner-manager.

Those entrepreneurial fortunes—indeed, all sustainable wealth—is created in just one way: by the efforts of owner-managers captured in a capital gain. Entrepreneurial fortunes do not arise from the net profit of their enterprise being "saved up" and invested in a bank account or even in some other investment or business. Instead, fortunes are almost always created as a result of a capital gain, that is, the discounted value of the future stream of excess cash returns in your concentrated, risky, illiquid, private business. Realizing the fortune you have built in your company is not as simple as riding your industry and watching the business grow. It requires identifying the drivers of enterprise value in your industry and ferociously concentrating all your resources on them. The brilliance of entrepreneurial capitalism is that the system allows selfish goals at the individual level to be converted into highly positive and constructive results for the greater good of the community as a whole.

Why should all this matter to us? Well, according to government statistics, fully half of all businesses fail before their fifth year. I know from hard personal experience that when a company goes under, it generates negative energy: sorrow and woe, lost jobs, lost investment, demands for personal guarantees, scuffles with banks and investors, abandoned real estate, shattered dreams, broken hearts. Even when a business does go the distance, the reward may not be as great as it could be. Far too many private business owners don't focus on or don't know how to optimize the enterprise value of their businesses, nor do they understand how to capture it, even if they have created it. We need private enterprise to "secure the economy's future" and, I would add, we need private businesses to create as much wealth as they possibly can for all stakeholders.

That is why I wrote this book. As I've said, I can't count the number of times owner-managers have said to me, "Pete, if only I had known then, when I was running the company, what I know now, after I've sold it, I would have done so many things differently."

These owner-managers are some of the most positive, generous, caring, demanding, energy creating, challenging, and tirelessly persistent people in the world. They are my best friends. I like them as people, and I empathize with just how hard it is to go to work day after day with their capital at risk, managing through the people issues, technical issues, and regulatory issues to build an enterprise of hundreds of employees and tens of millions of enterprise value designed to last forever. I hope my empathy, appreciation, and affection are evident throughout these pages.

Why does the architecture of this book start with the end? This method creates a potential destination; it informs readers through real life narratives drawn from my thirty plus years of scar tissue of working with owner-managers and their expert advisors. It is supported by the practical applications of the leading edge of theoretical foundations from psychology and finance. Can a rigorous methodology be created and applied that prepares owner-managers to capture—both psychologically and financially—their hard earned wealth in a capital gain and create a positive legacy? Yes it can. Although such a methodology will not be found in the conventional corporate finance literature, I offer it in this book. It is based upon my years of helping our clients to identify and build on their corporate and individual strengths so they position their enterprises and themselves to achieve optimal organizational success and live their lives to the fullest.

A Brief Guide to the Book

In Chapter One, "The Unique Character of the Entrepreneur Owner-Manager," and Chapter Two, "Four Hats, One Head, Big Challenge," I examine the character, roles, and thinking styles of the entrepreneur owner-manager. It sounds theoretical, and there is a bit of theory involved, but it is mostly practical. I start the book this way because I have found that owner-managers — not having been exposed to character assessment tools — are not always aware of the fundamental nature of the entrepreneur and of the decision-making biases the entrepreneur is often are prone to. This understanding may not be of great importance while you are building a business, but it becomes critical when planning and executing a wealth-creation event and company transition. If you don't understand how your own approach and method of making decisions differ from those of your advisors and potential new majority owners, it's easy to make mistakes and operate under incorrect assumptions.

In Chapter Three, "Creating Enterprise Value," we get down to brass tacks, as I address the fundamental question: How do you assure the longevity of your enterprise beyond your personal ownership of it? In this chapter, I examine the practice of enterprise value building by considering the four questions that you will be asked — and must be able to positively answer — when the discussions with potential investors begin. Is your industry in or out of favor with institutional investors? Do you have a simple, clear, and coherent business plan? Does your superior financial performance validate your strategy? And, can we find the best-fit investor who has a compelling reason to invest now? This is the heart of the matter. Start here if you want.

In Chapter Four, "Seller Beware: The Private Transaction Market," I provide an overview of the private transaction market and the key players who you will interact with there: the strategic investors, private equity groups, and private equity platforms. It is very important to understand the market you are entering, because you will be dealing with high-powered, highly-professional, coldly-objective investors with loads of experience in company assessment and deal-making. You need to be armed with as much information and knowledge as you can take in before you begin to work with your advisor to identify a best-fit investor.

In Chapter Five, "Capturing Enterprise Value," I take you through the entire transaction, starting with what you need to do and know before you even start to talk with potential investors, how and why to engage your management team, what you're looking for an investor, and the stages of the transaction.

In Chapter Six, "Creating a Positive Legacy," I delve into a topic that is rarely discussed and almost completed ignored by entrepreneur owner-managers who are contemplating a company transition: what comes after the event takes place? We have observed that owner-managers are wildly underprepared for the next chapter of their lives and go through four predictable post-sale stages: realization, hibernation, experimentation, and reinvention. Although it's impossible to fully prepare yourself for what's to come, a better understanding of the issues can make the transition much easier and more fruitful for all involved.

In the concluding chapter, "The Beginning," I list six things you can do *right now* to start building the value of your enterprise and preparing for a company transition, and a bit of philosophy on what your efforts are so valuable and important — not just to you, but to all of those around you, and to our society as a whole.

As I stated in my Author's Note, stories I tell in this book are all true. There are no "composite" stories or made up tall tales to "make a point". All involve real people in real life situations, real companies, and real capital gain transactions, although the names and identifying details have been disguised to guard the privacy of my friends/clients.

A final word before you dive in. You are approaching the largest and most important challenge of your career. It's usually the largest single financial event in your life. Who you choose to become the next majority investor in your business will have a great deal of impact on your legacy and on the lives of all stakeholders. It's a decision you have never faced before and you may never have another chance to get it right. This is no time for teaching error. You want to successfully overcome the challenges you will encounter on this journey so you can be delivered to a positive and generative legacy…a place where you are rich and enriched…an ending made clear in the beginning.

There is no doubt that after reading and absorbing this book you will know more about building and capturing enterprise value, and creating positive legacy than 99.7% of all the people in the world. There's a stake in the ground for you. Let's get started.