INSIGHTS FROM THE BDO TECHNOLOGY PRACTICE

WEBINAR RECAP

SUSTAINING VALUE: TOP M&A STRATEGIES FOR TECH COMPANIES

By Aftab Jamil, Rich Morris, Charles Irvin and Valentina Midura

Tech M&A activity—driven by strong capital markets and digital disruption—has been robust this year. Fierce competition coupled with soaring equity valuations and positive business sentiment have spurred many strategic acquisitions. Meanwhile, the pressure for businesses to digitally transform has led to sky-high valuations of cloud storage, cloud security, business intelligence, and data analytics companies, among others.

M&A is an important part of tech companies' corporate strategy. Nevertheless, navigating a complex transaction isn't easy. High growth companies often face unique challenges, including limited resources and/or a lack of in-depth tax and accounting knowledge. On top of that, myriad external risk factors—including market volatility, regulatory uncertainty, changes in trade policy, tax reform, rising interest rates, and more—further threaten to delay or end promising deals. To mitigate risk, organizations must carefully craft deal narratives and integration strategies that differentiate them from the crowd and enhance shareholder value.

We recently examined important M&A considerations for tech companies in our webinar, "**Sustaining Value: Top M&A Strategies for Tech Companies**."

Read more ▶

Here are our key takeaways.

GETTING READY: BUY & SELL-SIDE DUE DILIGENCE

Before finalizing a deal, buyers and sellers should have:

Business Strategy Alignment

- **A post-acquisition strategic plan:** Both parties must understand and agree on the post-closing expectations. Strategically, buyers should present their investment strategy to the seller, outlining how they plan to either absorb the target company or manage it on an autonomous basis. This allows the seller to evaluate the transaction structure and strategy, and the buyer a formal process to conduct thorough due diligence, including meetings with key shareholders, executive employees, and customers.
- **Clear expectations on reported metrics and KPIs:** One important question sellers should ask before closing a deal is, "What reporting requirements will there be post-closing?" Both parties must agree on their goals and metrics to prevent future misalignment in the reporting structure. If new measurements are created, it should be clear how they will help the buyer run the business. This is particularly important if there are earnouts contingent on future performance.
- **Agreement on governance:** Both parties must agree on the formal governance structure of the combined organization, with clear interactions and responsibilities outlined.
- **Awareness of important cultural values:** The failure to address culture during M&A deals can subtly impact both a buyer and seller's performance. For one, inattention to cultural values can lead to the stagnation or cancellation of a deal. Productivity and innovation can also decline if employees begin to question if the culture they "signed up for" will change. Eventually, these disruptions can erode value and profit margins.

Financial Due Diligence

- **An understanding of both parties' financial performance and profitability (current and historical):** Buyers should take a deep look at their target company's annual and quarterly financial statements to understand its financial performance and condition, including its profit margins. At the same time, buyers should assess whether their target's future projections are reasonable and manageable; determine what normalized working capital and investments will be needed to run the business; and how this and future earn-outs will be calculated.
- **Awareness of current and potential liabilities:** Buyers should examine their target's current and contingent liabilities, and note the condition of its assets, outstanding indebtedness, and any current filed or pending litigation or claims.
- **Deep knowledge of business operations:** PE firms and other buyers look closely at a target's operations to assess how they can improve the business. If key operational or performance details are missing, it will be much more difficult to properly evaluate its worth.
- **Clean books and records (following GAAP accounting policies):** Having clean books and records—including compliance with the new revenue recognition standard—is critical to a deal's success. A compliance mismatch—in which one party is compliant, while the other is not—can easily derail a deal. Sellers can also leave money on the table if they're not aware of how recent revenue recognition changes might affect their revenue streams. Commissioning a "quality of earnings" report from an independent third-party firm may be a good idea to ensure compliance.

Tax Strategy Planning

- **An overall tax planning strategy:** To improve functionality and mitigate compliance risks, both buyers and sellers must have a tax planning strategy in place before a transaction begins—and then revisit it when taking stock of the eventual combined entity.
- **Awareness of their total tax liability:** Buyers should review their target's current and historical global, federal, state, and local tax returns to see if there are any outstanding liabilities that need to be addressed or improvements to be made.
- **Awareness of critical tax reform changes:** Tax reform has introduced many changes that could impact buyers and sellers' tax strategies and the deal transaction.
- **Understanding of *South Dakota vs. Wayfair's* resulting tax implications:** Tech companies—especially e-commerce sellers and digital service providers—must not neglect the impact of the Supreme Court's *South Dakota vs. Wayfair* case ruling on their tax profile. Even before *Wayfair*, forgetting to factor in sales tax was often the biggest tax-related risk in a tech deal. Post-*Wayfair*, figuring out sales tax liability will be even more challenging.

Read more

SUSTAINING VALUE: POST-ACQUISITION CONSIDERATIONS

Preparing for a deal may be half the battle, but the other half is making it successful after it closes. Here are some best practices on how tech companies can sustain the value of a deal long-term:

- **Develop a comprehensive integration strategy framework—including one for each functional or business unit.** Integration must happen at both the organizational and functional level. Each business unit needs to understand its integration responsibilities and be equipped with the resources it needs to complete them successfully.
- **Align executive leadership and governance goals, processes, and responsibilities.** Companies should clearly define the governance responsibilities for specific decisions and tasks at the combined entity.
- **Develop a cultural integration strategy.** Companies must create a cultural integration strategy that aligns with the leaders' and employees' goals and expectations, as well as those of the overall business.
- **Ensure the integration of core business processes, IT systems, and practices.** A clearly delineated business-IT strategy is crucial to achieving a combined entity's business goals.
- **Plan for a seamless continuation of internal and external operations**. During a transaction, companies must maintain smooth internal and external operations to prevent customer churn.
- **Focus on retaining key talent.** Retaining key talent is a critical success factor, but many organizations struggle to do it successfully. Businesses should remain as transparent as possible during the deal lifecycle and cultivate excitement for the eventual combined entity.
- **Keep abreast of new and emerging risks:** Alongside the usual financial, tax, and legal due diligence, it's important to keep abreast of other risks, including corruption. Buyers should be aware of their target's previous transgressions and monitor high-risk business activities. It's recommended that buyers conduct a post-acquisition non-financial audit, if needed.
- **Communicate clearly to all stakeholders:** Companies should maintain clear communications to their stakeholders before, during, and after the transaction to keep customer and employee loyalty.
- **Involve external advisors early on.** This is especially important for smaller or mid-market companies that may not have all the resources or knowledge needed to navigate today's complex regulatory environment.

For more information, visit:

WEBINAR RECORDING

NEW STANDARD IMPLEMENTATION PAGE

REVENUE RECOGNITION CENTER

TAX REFORM HUB

SOUTH DAKOTA VS. WAYFAIR HUB

People who know Technology, know BDO.

CONTACT:

AFTAB JAMIL
Assurance Partner & Global Technology Practice Leader
408-352-1999 / ajamil@bdo.com

VALENTINA MIDURA
BDO Capital Advisors Senior Managing Director
617-422-7593 / vmidura@bdocap.com

RICH MORRIS
Transaction Advisory Services Partner
415-490-3197 / rmorris@bdo.com

CHARLES IRVIN
Transaction Advisory Services Managing Director
714-338-2555 / cirvin@bdo.com

BDO TECHNOLOGY PRACTICE
BDO works with a wide variety of technology clients, ranging from multinational Fortune 500 corporations to more entrepreneurial businesses, on myriad accounting, tax and other financial issues.

ABOUT BDO
BDO is the brand name for BDO USA, LLP, a U.S. professional services firm providing assurance, tax, and advisory services to a wide range of publicly traded and privately held companies. For more than 100 years, BDO has provided quality service through the active involvement of experienced and committed professionals. The firm serves clients through more than 60 offices and over 650 independent alliance firm locations nationwide. As an independent Member Firm of BDO International Limited, BDO serves multi-national clients through a global network of more than 73,800 people working out of 1,500 offices across 162 countries.

BDO USA, LLP, a Delaware limited liability partnership, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms. BDO is the brand name for the BDO network and for each of the BDO Member Firms. For more information please visit: www.bdo.com.