# Chapter 1

# The Building Blocks of Mergers and Acquisitions

### *In This Chapter*

- Becoming familiar with the main vocabulary of mergers and acquisitions
- Understanding the rules of the road
- Opening your eyes to potential costs
- Figuring out where your company fits

Mergers and acquisitions is a complicated field, so this chapter provides a basic overview: an introduction to the basic terms and phrases, a discussion of decorum and the basic M&A process, a look at the players and the category of deals, and my handy-dandy guide to helping business owners determine what kind of businesses they have.

## Defining Mergers and Acquisitions

*Mergers and acquisitions* (or *M&A* for short — the M&A world is rife with acronyms and initialisms) is a bit of a catchall phrase. For all intents and purposes, M&A simply means the buying and selling of companies. When you think about it, mergers and acquisitions aren't different; they're simply variations on the same theme.

In the strictest sense, a *merger* is a combination of two or more entities where each merging entity has an equal stake in the new enterprise and each merging entity has a very clearly defined role in the new entity. This ideal is the vaunted *merger of equals.* Daimler's 1998 combination with Chrysler was a merger of equals. In a more practical sense, so-called mergers of equals are rare; one side usually ends up controlling the enterprise. For example, the years following the Daimler-Chrysler merger showed that Daimler executives planned all along to control the combined entity.

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Although actual mergers do occur, most of the activity in the M&A world centers on one company buying another company, or the acquisitions category. I like to think using the word *merger* keeps the uninitiated on their toes; plus, talking about combining two companies as equal partners rather than about committing a hostile takeover sounds much more egalitarian.

Mergers are far less common than acquisitions. An *acquisition* is when one company buys another company, a division of another company, or a product line or certain assets from another company. Actually, an acquisition is when any kind of business purchases another part (or all) of another business. Although some companies grow *organically* (from within by creating and selling products or services), an acquisition allows a company to bypass the growth stage by simply buying existing sales and profits. Starting up a new product line may be less expensive than buying an existing one, but the market may take a while to adapt to the new product, if it does at all. For this reason, buying other companies rather than relying on organic growth may make sense for a particular company.

The fact that one can transfer a company's ownership through a sale often comes as a bit of surprise to many people (including many business owners, believe it or not). Business owners, especially owners of middle market and lower middle market companies (with revenues between $250 million and $1 billion [middle market] and between $20 million and $250 million [lower middle market]), have spent their careers building a company, so the process of selling a business is often something new and foreign to them.

In addition to being an activity, M&A is an industry. As this book illustrates, the steps to doing a deal, the names of documents and processes, the conventions, and the sundry tips and insights I provide are all based on de facto industry standards that have developed over time, and my humble hope is that this book helps introduce you to those standards and conventions.

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# Introducing Important Terms and Phrases

Like any topic, M&A has a language that you have to get a handle on to understand the field. Although I introduce many more terms and phrases throughout the book, the following words are part of the basic building blocks of M&A.

The *lingua franca* of M&A is an amalgam of accounting and banking terms sprinkled with initialisms, acronyms, and words and phrases adjusted and twisted to suit certain needs at certain times. Pay close attention to the terms I define throughout the book. Although some are tricky, I use them all for a reason.

## Buyer

You can't sell something unless you have a buyer for it. Although Buyers (both potential and actual) are typically companies or entities, I often refer to them as individuals for clarity.

In documents and contracts and agreements, you usually see *Buyer* as a defined term, which means it's capitalized. When you read those documents, *Buyer* looks like the name of a person. In fact, to make it seem really formal, M&A professionals often drop the word *the* from *Buyer.*

"Buyer" isn't a one-size-fits-all category. A Buyer may acquire all or part of a company, the stock of the company, or certain or all assets and even assume some of the liabilities. Despite this wide variety of possibilities, Buyers typically fall into four broad types:

- **Strategic Buyers:** These Buyers are other companies planning to combine operations of the two companies to some extent (as opposed to buying strictly for financial reasons). For example, when Oracle buys a company, Oracle is considered a strategic Buyer because it buys companies that have some sort of synergy to its business.
- **Financial Buyers:** *Financial Buyers* are funds of money that buy companies. Financial Buyers of middle market and lower middle market companies are typically private equity (PE) funds, which are essentially large pools of money (see Chapter 4 for more).
- **Other companies backed by PE funds:** The company will be the new owner of the acquired company, but another entity (the fund) is providing the dough to do the deal.
- **Individuals:** Although it happens, an individual buying a middle market or lower middle market company is rare. When individuals buy companies, those companies tend to be small retail shops, consulting firms, or construction companies. Typically, these companies have revenues of less than $1 million.

As a Seller, know that who's on the other side of the negotiating table may change the way your M&A process works. Are the Buyers experienced deal people, or are they new to the process? For example, if your Buyer is a PE firm, rest assured that the people you're negotiating with know exactly what they're doing.

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## Seller

You can't buy something unless you have a Seller. Like Buyers, Sellers usually aren't individuals, though I often refer to them in the singular here for clarification purposes. *Seller* is a defined term, meaning it's capitalized for the purposes of documents and contracts.

Here's a quick look at the types of Sellers you may find in the world of M&A:

- **The spinoff:** A company may be divesting a division, a product line, or certain assets.
- **The change of control:** This company is selling enough of itself (more than 50 percent) to result in a change of control. In these cases, the owner or owners most likely receive the money. Colloquially, this approach is called *taking some chips off the table.*
- **The recap:** Sometimes an owner wants to take some chips off the table without giving up control of the company. This situation is called a *recapitalization,* or *recap* for short.
- **The growth capital:** A Seller may issue more stock for the purposes of raising capital to invest in the business. In this case, the owner isn't actually selling the company but rather selling more stakes in the company. The money from the sale doesn't flow to the owner; instead, the company retains the money to fund growth.

Remembering why the Seller is selling the company, how much of the company he or she is selling, and where the money goes is key. Follow the money.

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## Transaction (also known as the deal)

The *transaction* is when Buyer sells a company to Seller. It's an abstract concept, as in, "We're working on a transaction that will sell ABC to XYZ." It can also refer to the finished sale: "We completed the transaction yesterday." (Don't confuse the transaction with the *purchase agreement,* a contract that memorializes the transaction. See Chapter 15 for more on this document.)

*Transaction* is a more formal version of *deal;* most documents, agreements, and contracts use the word *transaction* (often capitalized as a defined term), but conversations and e-mails may use *deal* and *transaction* interchangeably. Think of *deal* as *transaction's* popular cousin from the wrong side of the tracks.

## M&A personality types

Regardless of whether you're buying or selling, one helpful trick for getting deals done is to assess the personality of your negotiating counterpart. Based on my experience, you're liable to run across the following types of people:

- **The highly motivated:** This person has to get a deal done or he's doomed. He's so desperate to do a deal that he may — strike that, *will* — leave dollars on the table.
- **The ruler-of-the-universe business magnate:** He's from Experienced, Wily, and Cagey, Ltd.; he's made countless deals and knows exactly what he's doing. If you find yourself matched against this person, look out. The worst thing you can do is to turn into the highly motivated (see the preceding bullet); you'll get your clock cleaned.
- **The know-it-all who's never sold a company:** This person is one of the potential problem children of the M&A world. Quite often, he's an expert in one field and thus thinks he's an expert in everything. The best way to counteract this type of person is by asking questions, reasoning, and getting him to explain his point of view. Avoid simply saying "no" if you don't like his proposal. Challenge him. Your only hope of changing this person's mind is getting him to change it himself.
- **Mr. Irrational:** Mr. Irrational is the insane twin of the know-it-all, except without the strong logic skills. As a result, employing logic and reason doesn't work. An irrational person is difficult to work with, so your ability to get a deal done is limited. Give it your best shot and then walk away when the proceedings begin to get petty and frustrating. Interestingly enough, these irrational people often come to their senses after the heat of the battle fades. Don't fuel their irrationality with endless negotiating and discussions.
- **The earnest first-timer:** The country cousin of the know-it-all and Mr. Irrational, this person is so intent on doing everything letter-perfectly that he misses the proverbial forest for the trees. Work to get this person to do as you want, or he'll end up irritating you to no end.
- **The professional:** Typically, this type is the best person to work with. He's a deal pro who's been around the block many times, leaves emotion out of the negotiation, and works to close a deal on mutually beneficial terms.
- **The chronic negotiator:** This exhausting individual negotiates and fights for excruciatingly minor details over and over again. Although attention to detail is important and worth the hassle, endlessly negotiating those details eventually evokes the law of diminishing returns — you put in more time for smaller and smaller advancements. At some point the nit-picky details aren't worth the hassle. This person blasts through that point.
- **The renegotiator:** Don't confuse this person with the chronic negotiator (though the same person can be both). This guy's MO is to wait until the deal is seemingly done before asking (or demanding) that you change the terms. Don't give in; changing the deal at the last minute comes back to haunt you because you may be needlessly agreeing to concessions. Don't let the rush of closing a deal cloud your decision-making.

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## Consideration

*Consideration* is what Seller receives from Buyer as a result of selling the business. In its most obvious form, the consideration is cash, but cash is not the only way to pay for a business. Buyer may issue stock to Seller in exchange for the business. Seller may accept a note from Buyer (Buyer promises to pay later). Or perhaps the price of the business is contingent, and Buyer pays Seller an *earn-out* based on the performance of the business after the transaction's completion.

Consideration is not an either-or situation. In other words, the consideration may consist of some cash at closing, stock in the acquiring company, and an earn-out. Or perhaps the consideration is a note plus an earn-out. No single right or wrong way to structure a deal exists. Structuring a deal by using various forms of consideration is similar to twisting the knobs on a stereo: To get it just right, you may have to increase the bass and turn down the treble. Chapter 4 provides a much deeper dive into the ways Buyers can finance deals.

Consideration is usually a defined term and therefore capitalized in documents and so forth.

## EBITDA

EBITDA (earnings before interest, tax, depreciation, and amortization) is one of those horrible business jargon terms, but it's unavoidable in M&A. EBITDA (and its variations) forms the basis for most deals.

*EBITDA* is the cash flow of a company without accounting for interest payments or interest income, tax bills, and certain noncash expenses (depreciation and amortization). In other words, EBITDA measures the cash generated from doing what the company is supposed to do: sell its goods or services.

Why is this number so gosh-darn important? EBITDA is often (but not always) the basis a company uses to determine its valuation (see Chapter 12) and is often a defined term in the agreements and contracts. Banks quite often include EBITDA as one of the covenants for making a loan.

EBITDA is commonly pronounced *ee*-bah-dah. And in case you're wondering, EBITDA is not a generally accepted accounting principles (GAAP) term. (Neither is adjusted EBITDA, which I cover in the following section.) However, both EBITDA and adjusted EBITDA are perfectly acceptable terms for the purposes of M&A activities.

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## Adjusted EBITDA

*Adjusted EBITDA,* which is EBITDA's wild and crazy cousin, is simply EBITDA with adjustments! For example, a business owner often takes a salary larger than industry standards, so a Buyer may want to add back part of that salary to arrive at a more reasonable level of earnings. Say the owner of a company with $20 million in revenue receives total compensation of $500,000 when the industry standard for the president of a like-sized company is $250,000. In this case, adding $250,000 (plus the pro-rated amount of income tax) back to the EBITDA figure makes sense.

Other adjustments to EBITDA may include add backs for other owner-related expenses (cars, gas, cellphone, country club, health club, and so on). If certain employees won't be part of the business after the deal is complete, adding back their salaries (and corresponding payroll tax and benefits expenses) is appropriate.

No set standard exists for adjusted EBITDA; adjusted EBITDA is whatever Buyer and Seller agree it is.

Although running certain personal expenses through a business may be common, the practice may run afoul of the IRS. Consult with your tax advisor for the proper treatment of personal expenses.

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## Closing

*Closing* is what Buyer and Seller dream of! It's why we M&A folks do what we do. In fact, it's so important that I devote an entire chapter (Chapter 16) to closing. In a nutshell, closing is the day when Buyer hands over the consideration to Seller and Seller hands over the company to Buyer.

# Adhering to Basic M&A Rules and Decorum

Knowing the M&A language is important (see the earlier section "Introducing Important Terms and Phrases"), but understanding the rules of the M&A game and the decorum for its participants is equally important. Much like a poker game, the actions, the inactions, the movements, the gestures — in other words, the "tells" — are hugely important in the world of buying and selling companies.

If you're going to get into the M&A business, you have to know what to do and what to expect. Those caught off guard are those who won't be successful. Simple as that. Inadvertently (and incorrectly) broadcasting yourself as an M&A amateur can be hazardous to the health of your deal.

## Follow the steps to getting a deal done

Remember that the M&A process is a serial process — transactions follow a step-by-step process. The following list gives you an overview of that process; I strongly encourage you to check out Chapter 3, where I discuss the steps in more detail.

Even though M&A follows a step-by-step process, the process often isn't linear. It goes through unforeseen twists and turns, so you have to be able to adjust.

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1. **Compile a target list.**

   For Sellers, this means creating a list of potential Buyers, and for Buyers, this means a list of business owners who may be potential Sellers.

2. **Make contact with the targets.**

   Reach out to an executive or owner of a company on your list from Step 1. I prefer to make phone calls when contacting Buyers and Sellers.

3. **Send a "blind teaser" if you're selling or ask for an executive summary if you're buying.**

   If both sides (Buyer and Seller) have some level of interest in exploring a deal after the initial contact, Seller provides Buyer with a little bit of info in the form of an anonymous *teaser.* That way, Buyer isn't inundated with too much info, and Seller maintains confidentiality and anonymity.

4. **Sign a confidentiality agreement.**

   In this legal document, Buyer promises not to disclose Seller's private information or even the fact that conversations about a potential transaction are ongoing.

5. **Send an offering document if you're selling, or review the offering document if you're buying.**

   The *offering document* is the deal book, the document that contains the information about the company for sale. A well-written offering document should contain enough information for Buyer to make an offer.

6. **Ask for an indication of interest if you're selling or submit one if you're buying.**

   Buyer submits a simple letter expressing his interest in doing a deal. If the indication meets Seller's approval, she invites Buyer to a meeting.

7. **Conduct management meetings.**

   Management meetings give Buyer and Seller an opportunity to meet face to face. Seller provides Buyer with updated figures from when the offering document was written, and based on this update, Buyer may or may not submit a formal offer.

8. **Ask for a letter of intent (LOI) if you're selling or submit one if you're buying.**

   The *LOI* is the formal offer. However, it's still nonbinding, so each party can still walk away from the deal at this stage.

9. **Participate in due diligence.**

   *Due diligence* occurs after Buyer and Seller come to terms. During this step, Buyer reviews, examines, and inspects Seller's books, records, contracts, and more to verify that all the Seller's claims are accurate.

10. **Craft a purchase agreement.**

    During due diligence, Buyer and Seller write a purchase agreement to finalize the deal both sides negotiated. This document is final and legally binding.

11. **Attend closing.**

    After due diligence is complete and the purchase agreement is drafted, Buyer and Seller close the deal. Seller turns over the keys of the business to Buyer; Buyer forks over money to Seller.

12. **Deal with post-closing adjustments and integration.**

    A deal is not done the day it closes! In most cases, Buyer and Seller have some post-closing adjustments to navigate, and Buyer has the task of integrating the two companies.

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## Understand M&A etiquette

If you aren't careful, you can easily give off the wrong signal inadvertently during your M&A proceedings. Failure to follow up quickly, return calls, and give complete answers is an easy way to turn off the other side and kill a deal. Show interest in doing a deal. If you're not interested in pursuing a deal, communicate that to the other side. Here are a few more quick pointers to help you make the best impression:

- **Respond to a direct question with a direct answer.** Sellers most often break this rule. Instead of addressing a basic question like "What were revenues last year?" with a simple answer, Seller decides to dive into a 15-minute monologue about something that sounds impressive. In this case, Seller doesn't impress Buyer; Buyer merely gets bored and may even wonder what Seller is hiding.

- **Don't put on airs.** Sometimes one side is so intent on impressing the other side that it instead looks foolish, childish, and amateurish. The best course of action? Just be yourself. Don't think you need to go out of your way to impress someone. Trying to impress someone rarely works and often backfires.
- **If you don't know something, just say you don't know it.** You're not going to impress the other side by talking about things you don't know. If you're not sure, simply say, "I need to check into that and get back to you."
- **When you say you're going to do something, follow through and do it!** No explanation needed.

## Know what to tell employees — and when

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Ambiguity is no one's friend. The disclosure to the outside world that a company is for sale can be a devastating bit of news. Competitors may pounce and try to steal customers by implying that the sale may impact product quality or through some other scare tactic. For this and many other reasons, news of a potential business sale should be a very closely guarded secret known to only a select few until the time is right to make the announcement.

Likewise, revealing a sale or impending sale to employees is a delicate, critical matter. The timing of such an internal announcement often depends on your situation and whether you're doing the buying or the selling. The following sections give you some insight into this important topic.

### When you're selling your company

If employees find out that their employer is for sale, they may get twitchy and nervous. The news that a company is for sale can cause key people to begin looking for work elsewhere. For this reason, Sellers should tell employees about a potential sale on a strictly need-to-know basis.

Staggering the release of the business sale news is acceptable. Not everyone needs to learn the news at the same time.

For example, key executives and managers need to know before lower-level employees. Exactly who that is depends on the specifics of each company. Generally, the CFO needs to know, and depending on the size of the firm, she may need to let certain key employees in on the secret. Financial disclosure is very important, and people in the accounting department can usually figure out when something is going on — they're suddenly inundated with very unusual and exacting requests for financial data!

If an employee asks you about a rumor that the company is for sale, neither confirm nor deny the rumor, but never lie. If you tell the employee that the company is not for sale and then the company makes a sale announcement two months later, that employee will feel betrayed and her trust will be broken. Instead, tell her that the owners are exploring some options, including bringing in investors to help take the company to the next level.

### When you're buying companies

For Buyers, letting employees know that the company is seeking acquisitions has little downside. Think about it: How much harm can come from your competitors finding out that your company is so successful that you're exploring making acquisitions?

Treat the confidentiality clause in the confidentiality agreement very seriously. Loose lips sink ships. A sure way to scuttle a potential deal is for Buyer to talk about it with people who aren't part of the process. See Chapter 7 for more details about confidentiality.

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# Considering the Costs Associated with M&A

Although the main cost in any M&A transaction is most likely the cost to acquire the company (or assets), both Buyers and Sellers incur other costs. These costs range from the retinue of advisors needed to close deals, paying off debt, adjustments made after the close, and, regrettably, taxes.

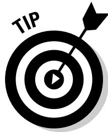
## Tallying advisors' fees and other costs

As I explain in Chapter 5, M&A deal-makers can't do the job alone. Any Buyer or Seller should retain a capital M&A advisor (investment banker), a lawyer, and an accountant. These people don't work for free, so their charges are part of the expenses of doing a deal. Of course, advisor fees vary based on the deal and how much work the advisor does, but here are some very general guidelines:

- A lawyer may charge anywhere from $25,000 to more than $100,000.
- An accounting firm may charge anywhere from $25,000 to $75,000.
- Investment banking fees vary, but in a very general sense, you should expect to pay roughly 3 percent to 10 percent of the transaction value.

Some deals involve other costs as well, including a real estate appraisal, an environmental testing, a database and IT examination, and a marketing analysis. Fees vary, of course, but all these functions likely cost anywhere from $10,000 to more than $100,000 apiece.

This section may seem a bit wide open, but nailing down the costs without knowing the deal is impossible. The best way to get a concrete estimate of a particular deal's fees is to speak with advisors and ask them to ballpark their expenses.




If you're worried about fees spiraling out of control, negotiate a flat fee, or a capped fee, from your advisors if possible. Not all will be willing to do this arrangement. If you get pushback, you can always agree that if the advisor does the work for a flat fee now, you'll give him the ongoing legal or accounting work post-transaction.

## Paying off debt

One of the areas that Sellers often overlook is the debt of the business. Unless stipulated, a Buyer doesn't assume the debt. If a company has $5 million in long-term debt and the company is being sold for $20 million, the Seller needs to repay that debt, thus reducing the proceeds to $15 million.

## Post-closing adjustments

Another area that Sellers often don't think about is the adjustments made to the deal after closing. Most often this is in the form of a *working capital adjustment,* which occurs when the *working capital* (receivables and inventory minus payables) on the estimated balance sheet Seller provides at closing doesn't match up with the actual balance sheet as of closing that the Buyer prepares at a later, agreed-upon date (usually 30 to 60 days after closing). Buyer and Seller do a working capital adjustment to *true up* (reconcile) their accounts; this adjustment is typically (though not always) minor. If the actual working capital comes in lower than the estimate, Seller refunds a bit to Buyer (often by knocking some money off the purchase price). If the figure comes in higher than the estimate, Buyer cuts Seller a check.

Say Buyer agrees to pay $10 million for a business and that Buyer and Seller agree that working capital has averaged $2 million. If Seller's estimated balance sheet shows working capital to be $1.5 million, Seller has to provide Buyer with $500,000. With a working capital adjustment, Buyer just pays Seller $9.5 million rather than $10 million.

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Why take working capital adjustments? Simply put, working capital is an asset, and if less of that asset is delivered at closing, Buyer is due a discount from the agreed-upon purchase price (and vice versa). Without a working capital adjustment, Seller would have every incentive to collect all the receivables (even if done at deep discounts), sell off all the inventory, and stop paying bills, thus inflating payables. Buyer would take possession of a business that has been severely hampered by the previous owner. Buyer then has to spend money to rebuild inventory and pay off the old bills and doesn't have the benefit of receivables.

### Sigh . . . talking taxes

Sellers often forget that they likely face capital gains tax on the business sale. That's one reason Sellers generally prefer stock deals; a stock deal likely has a lower amount of tax. For many (but not all) Sellers, an asset deal exposes them to double taxation: The proceeds are taxed at the time of the sale at the company level, and then the owner pays again when the company transmits the proceeds to her. (Chapter 15 gives you the lowdown on stock and asset deals.)

Speak to your financial advisor about your specific tax situation.

## Determining What Kind of Company You Have

As I state throughout the book, *Mergers & Acquisitions For Dummies* is primarily for Sellers or Buyers of middle market and lower middle market companies. But what exactly constitutes those types of companies, and how do you define other company types? The distinction has to do with size, most often revenues and profits.

Then you have the issue of critical mass. *Critical mass* is a subjective term, and it simply means size: Does the company have enough employees, revenues, management depth, clients, and so on to survive a downturn? Smaller businesses most often do not have enough critical mass to be of interest to acquirers. Capital providers who may be able to help finance acquisitions will have little or no interest, too. Although critical mass differs for different companies, in a general sense a company with $30 million in revenue and $3 million in profits has a better chance of surviving a $1 million reduction in profits than a smaller firm with only $500,000 in profits.

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If you're thinking about chasing acquisitions or selling your business, understanding where your business fits is important. Who may be interested in acquiring it?

Definitions vary, but for the purposes of this book, I've divided the market into sole proprietorship, small business, lower middle market company, middle market company, and large company (and beyond). Table 1-1 defines these companies at a glance; the following sections delve into more detail.

**Table 1-1 M&A Company Types**

| *Company Type* | *Annual Revenue* | *M&A Advisor* | *Number of US Companies* |
|---|---|---|---|
| Sole proprietorship | Less than $1 million | Business broker | 6 million |
| Small business | $1 to $10 million | Business broker | 1 million |
| Lower middle market company | $10 to $250 million | Investment banker | 150,000 |
| Middle market company | $250 to $500 million | Investment banker | 3,000 |
| Large company (and beyond) | $500 million+ | Bulge bracket investment banker | 3,000 |

*Source:* www.census.gov/epcd/www/smallbus.html

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## Sole proprietorship

*Sole proprietorships* are companies with revenues of less than $1 million. They're your neighborhood pizza joints, corner bars, clothing boutiques, or small legal or accounting practices.

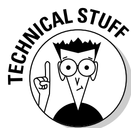
Although these businesses are viable *going concerns* (aren't facing liquidation in the near future) and often trade hands, they're too small to be of interest to PE firms and strategic Buyers, as well as corresponding service providers who assist in M&A work. (Flip to the earlier section "Buyers" for more on these kinds of Buyers.)

Why are sole proprietorships of little or no interest to an acquirer? Simply put, buying a $1 million business and a $100 million business requires about the same amount of time and the same steps and expenses, so if you're going

to go through the trouble of buying a company, you may as well get your money's worth and buy a larger concern. Making dozens of tiny acquisitions is just not worth the time or expense.

## Small business

*Small businesses* usually have annual revenues of $1 million to $10 million. These businesses are larger consulting practices, multiunit independent retail companies, construction firms, and so on. Unless the company is incredibly profitable (profits north of $1 million, preferably $2 million or $3 million), small businesses are too small to be of interest to most strategic acquirers and PE funds.




Although PE funds and strategic acquirers are usually not interested in smaller companies, they occasionally make exceptions if a company has a unique technology or process. In these cases, the acquirer can take that technology or process and deploy it across a much larger enterprise, thus rapidly creating value.

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## Middle market and lower middle market company

*Lower middle market companies* are companies with $10 million to $250 million in annual revenue; *middle market companies* have revenues of $250 million to $500 million. These companies typically have enough critical mass to be of interest to both strategic acquirers and PE funds. Also, because these deals are larger than small business and sole proprietorship deals, M&A transaction fees are large enough to justify the involvement of an investment banking firm.

## Large company (and beyond)

Companies with revenues north of $500 million are considered large, huge, gigantic, and, if revenues are well into the billions, Fortune 500. Although transactions are typically very large, the fact is very few companies are large. The middle and lower middle markets are far larger.

Firms in this category typically use *bulge bracket* investment banks. These entities are the largest of most sophisticated of investment banks. They also charge enormous fees.

The term *bulge bracket* originates from the placement of a firm's name on a public offering statement. Public offerings of securities typically involve multiple firms, and the largest firms, or managers of the offering, want their names to the left, away from the names of the smaller firms. The placement of the names looks as if they were bulging, hence the moniker.

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