

## M&amp;A; EXECUTION PROGRAM

PART 02 OF 12 · PART 1: DEAL FOUNDATIONS &amp; STRATEGY

# PART 2

## THE LETTER OF INTENT & VALUATION

*How to structure an LOI that protects your position without killing the deal — and how to anchor valuation using EBITDA multiples, DCF, precedent transactions, and the holdback trap.*

## IN THIS PART

- Binding vs. non-binding LOI clauses
- Exclusivity and no-shop provisions
- EBITDA multiple vs. DCF valuation frameworks
- Working capital peg in the LOI stage
- Holdbacks, escrows, and earnout bridges
- The CFO's LOI negotiation checklist

## THREE CASE STUDIES

*Each session includes one fully worked case study with detailed calculations, negotiating dynamics, and CFO-level decision frameworks.*

### ■ ■ SESSION 2: THE LETTER OF INTENT

## The LOI: A Non-Binding Agreement You Cannot Afford to Get Wrong

The Letter of Intent (LOI) — sometimes called a Term Sheet or Memorandum of Understanding — is paradoxically the most important document in the entire M&A; process, despite being largely non-binding. It establishes the commercial framework: the purchase price, the structure, the exclusivity period, the key conditions, and the fundamental economics of the deal. Once signed, the LOI creates powerful psychological anchoring effects that make it extremely difficult to renegotiate terms discovered during due diligence.

The CFO's role in LOI negotiation is to ensure that every number in the document is defensible, every definition is precise, and every clause that is binding is intended to be binding. Ambiguity in an LOI is always resolved against the party that drafted it — or more often, resolved in favor of the party with better lawyers.

### Binding vs. Non-Binding Provisions

Provision	Binding?	Why It Matters
Purchase Price / Valuation Range	Non-binding	Subject to diligence adjustments; anchor for negotiation
Deal Structure (Stock/Asset)	Non-binding	Can evolve; but changing structure mid-deal is costly
Exclusivity / No-Shop Clause	BINDING	Prevents seller from shopping the deal during diligence period; protects buyer's investment in DD
Confidentiality / NDA	BINDING	Governs use of disclosed information; survives LOI termination
Break-Up / Reverse Break-Up Fee	BINDING	Compensates aggrieved party if deal fails; creates commitment
Governing Law / Dispute Resolution	BINDING	Determines jurisdiction for LOI disputes
Target Closing Date	Non-binding	Indicative timeline; rarely binding; triggers go-shop periods
Working Capital Definition	Non-binding (important)	Sets framework; precise definition negotiated in SPA
Material Adverse Change Definition	Non-binding (critical)	Defines what kills the deal; negotiate carefully in LOI

## Valuation Frameworks: The Four Methods Every CFO Must Master

M&A; valuation is not a single number — it is a range derived from multiple methodologies, each of which tells a different part of the story. The CFO's job is to build a valuation bridge that synthesizes all four approaches and presents a defensible range to the board.

### Method 1: EBITDA Multiple (Market Approach)

The most common valuation shorthand in private company M&A.; The enterprise value is calculated as a multiple of EBITDA (Earnings Before Interest, Taxes, Depreciation, and Amortization). The multiple is derived from comparable transactions in the same sector, from public company trading multiples (discounted for illiquidity), and from the specific attributes of the target.

## ◆ EBITDA MULTIPLE METHOD

## EBITDA MULTIPLE VALUATION

Target EBITDA (LTM, as-reported): \$8,200,000

Adjustments (see Session 4):

+ Owner compensation above market: \$420,000

+ One-time legal settlement: \$350,000

+ Non-recurring facility relocation: \$180,000

**Adjusted / Normalized EBITDA: \$9,150,000**

Comparable transaction multiples (sector): 8.0x - 11.5x

Selected multiple for this business: 9.5x

(justification: 18% YoY growth, 92% retention,  
but 35% customer concentration risk – mid-range)

**Indicated Enterprise Value: \$9.15M × 9.5x = \$86,925,000**

Less: Net Debt: (\$3,200,000)

**Indicated Equity Value: \$83,725,000**

## Method 2: Discounted Cash Flow (Intrinsic Approach)

The DCF values the business based on the present value of projected free cash flows plus a terminal value. It is theoretically the most rigorous method but is highly sensitive to growth rate and discount rate assumptions. Small changes in the terminal growth rate can move the value by 20-30%. The CFO must be prepared to defend every assumption.

## ◆ DCF VALUATION

## DCF VALUATION — SIMPLIFIED 5-YEAR MODEL

WACC (discount rate): 12.0%

Terminal Growth Rate: 3.5%

Year FCF Projection PV Factor PV of FCF

1 \$6,800,000 0.8929 \$6,071,429

2 \$7,616,000 0.7972 \$6,071,429

3 \$8,529,920 0.7118 \$6,071,500

4 \$9,553,510 0.6355 \$6,070,756

5 \$10,699,931 0.5674 \$6,071,231

**Sum of PV (Years 1-5): \$30,356,345**

Terminal Value:  $FCF_5 \times (1+g) / (WACC - g)$

$\$10.7M \times 1.035 / (0.12 - 0.035) = \$130,190,953$

PV of Terminal Value ( $\div 1.12^5$ ): \$73,899,000

**Enterprise Value (DCF): \$30.4M + \$73.9M = \$104,255,345**

**NOTE: TV = 71% of total value — model is TV-driven**

**Sensitivity: +/-1% on WACC changes EV by ~\$18M**

## The Valuation Bridge: Reconciling the Methods

A robust valuation presentation to the board shows all methods in a football field chart and explains why the negotiated price sits where it does within the range.

Method	Low	High	Midpoint	Weight
EBITDA Multiple (8.0x-11.5x)	\$73.2M	\$105.2M	\$89.2M	35%
DCF (Base Case)	\$88.0M	\$122.0M	\$105.0M	35%
Precedent Transactions	\$79.0M	\$98.0M	\$88.5M	20%
LBO Floor (PE Buyer)	\$71.0M	\$83.0M	\$77.0M	10%
<b>Blended Weighted Value</b>	<b>\$80.1M</b>	<b>\$107.7M</b>	<b>\$93.9M</b>	<b>100%</b>

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## CASE STUDY 1

## Pinnacle SaaS Group

*LOI Negotiation — High Multiple vs. IP Warranty Holdback***Background**

**Buyer:** EnterpriseStack Corp., a strategic acquirer. **Seller:** Pinnacle SaaS Group, \$14.8M ARR, 115% NRR, \$4.2M adjusted EBITDA. Key intellectual property: a proprietary natural language processing engine that powers the product. The seller's founder wants 13x EBITDA (\$54.6M). The buyer's LOI comes in at 11x EBITDA (\$46.2M) — plus a \$6M escrow holdback for 24 months contingent on IP warranty representations.

## ◆ PINNACLE LOI BRIDGE

## PINNACLE — LOI ECONOMICS: BUYER vs. SELLER POSITIONS

Seller's Ask:  $13 \times \$4.2\text{M EBITDA} = \$54,600,000$

Buyer's LOI:  $11 \times \$4.2\text{M EBITDA} = \$46,200,000$

Gap at LOI: **\$8,400,000**

## BUYER'S HOLDBACK TERMS IN LOI:

Total escrow: **\$6,000,000**

Duration: **24 months**

Release condition: **No IP ownership claims from prior employers of the engineering team**

Risk priced by buyer: **prior-employer IP dispute**

## SELLER'S COUNTER-ANALYSIS:

PV of \$6M held 24 months @ seller's 12% hurdle rate:

$\$6\text{M} / 1.12^{24} = \$4,783,163$

'Real' price to seller (net of holdback PV loss): **\$41,416,837**

Effective multiple to seller: **9.86x**

## NEGOTIATED RESOLUTION:

Price increased to **11.75x (\$49.35M)**

Holdback reduced to **\$3.5M / 18 months**

IP reps limited to **'knowledge of the Company'**  
(vs. absolute warranty — lower risk for seller)

Effective price net of holdback PV: **\$47,661,000**

Effective multiple achieved: **11.35x**

### ■ THE HOLDBACK PV LESSON

Sellers must always calculate the present value of any holdback, escrow, or deferred consideration. A 24-month holdback is not free money waiting to arrive — it costs the seller the time value of capital. At a 12% hurdle rate, \$6M held for 24 months is worth only \$4.78M today. The CFO must translate deferred consideration to present value before accepting any LOI.

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## CASE STUDY 2

### Canyon Road Distribution

*Exclusivity Trap — How a 60-Day No-Shop Almost Killed the Deal*

## Background

Canyon Road Distribution signed an LOI with Primary Acquirer Inc. at \$38M enterprise value with a 60-day exclusivity period. During due diligence, Primary Acquirer discovered a customer concentration issue (one client = 42% of revenue). They used this to re-trade the price to \$32M in week 7. The seller, locked in by exclusivity, could not explore the competing \$40M offer that had materialized from a strategic buyer.

#### ◆ EXCLUSIVITY TRAP ANALYSIS

##### CANYON ROAD — EXCLUSIVITY COST ANALYSIS

LOI signed price: \$38,000,000

Re-traded price (week 7): \$32,000,000

Price reduction demanded: \$6,000,000

Competing strategic offer (emerged week 5): \$40,000,000

Could not be explored — exclusivity in effect

Opportunity cost of exclusivity: \$8,000,000

(\$40M strategic - \$32M re-traded)

OUTCOME: Seller walked from Primary Acquirer at day 62

(exclusivity expired; no break-up fee in LOI)

Re-engaged strategic buyer; closed at \$39.5M

Lost 9 weeks and \$120,000 in due diligence costs

But avoided the \$8M value destruction of re-trade

LESSON: Exclusivity should be 30-45 days maximum

Break-up fee protects seller against re-trading

Material price reduction = breach of good faith

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## CASE STUDY 3

**BrightPath Education LLC***Earnout Bridge — Closing the Valuation Gap in an Uncertain Business***Background**

BrightPath Education provides corporate training services with lumpy revenue recognition. The seller projects \$12M revenue in the forward year (Year 2); the buyer only credits \$9M (based on signed contracts). The gap of \$3M × a 7× revenue multiple = \$21M in enterprise value disagreement. The bridge: a structured earnout tied to revenue milestones.

## ◆ BRIGHTPATH EARNOUT MECHANICS

## BRIGHTPATH — EARNOUT STRUCTURE

Base price (on \$9M 'certain' revenue × 7×): \$63,000,000

Earnout pool maximum: \$21,000,000

Tier 1: Revenue \$9.5M-\$10.5M → Pays \$7M earnout

Tier 2: Revenue \$10.5M-\$11.5M → Pays \$14M earnout

Tier 3: Revenue \$11.5M+ → Pays full \$21M earnout

Measurement period: 18 months post-close

Payment: 12 months after measurement period end

(total cash timing: up to 30 months post-close)

## SELLER PV ANALYSIS (10% discount rate):

Full \$21M in 30 months:  $PV = \$21M / 1.10^{2.5} = \$16,925,000$

Effective value of earnout to seller: \$16.9M max

Total effective consideration: \$63M + \$16.9M = \$79.9M

Effective revenue multiple: ~8.4× (acceptable)

## ■ SESSION 2 KEY TAKEAWAYS

## 01

**The LOI Is the Commercial Deal**

Every number in the LOI must be built from first principles. Do not accept a buyer's proposed LOI without running your own full valuation.

## 02

**Always PV the Holdback**

Any deferred consideration must be discounted to present value. A 24-month holdback at 12% costs the seller 19 cents on the dollar.

### 03 **Limit Exclusivity to 30-45 Days**

60+ day exclusivity gives buyers a re-trading option. Structure exclusivity with a break-up fee and a rolling extension option.

### 04 **Earnouts Are Not Free Money**

Earnouts are contingent, time-delayed, and administratively complex. Model the probability-weighted PV before accepting them as real consideration.

### 05 **Valuation Is a Range, Not a Number**

Present the board with a football field showing all four methods. The negotiated price should be defensible within the range.