Unfinished Business Transfers in the Finnish Small Businesses

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Objectives

Business transfers are becoming gradually more common among small businesses, largely due to aging of entrepreneurs. Existing business transfer research, however, tends to focus on mergers and acquisitions of publicly traded large firms. In our paper a business transfer is defined as a change of controlling ownership of any firm or business to another person or firm outside the family. Earlier research has presented evidence both on successes (for example Tall 2014, Varamäki, Heikkilä, Tall, Viljamaa, and Länsiluoto 2013; Teerikangas 2012; Seth, Song, and Pettit 2002; Aiello, and Watkins 2000) and failures (for example Baker, Butta, Saadi, and Zhu 2012; Chatterjee 2009; KPMG 2006; Langford, and Brown 2004; Dyer, Kale, and Singh 2004; Seth, Song, and Pettit 2002; Marks, and Mirvis 2001) of business transfers. Failure in a business transfer can mean either failure before or after the actual business transfer. In the first case the potential transfer does not take place despite negotiations. In the latter case the intended results are not achieved although the transfer is accomplished. Previous research has largely focused on how the integration succeeds, how the new owner is able to achieve his objectives, and how well the integrated firm performs under the new ownership (see for example Marks, and Mirvis 2011; Very, and Schweiger 2001). Business transfer negotiations that fail without achieving a transfer have received little attention among researchers.

In order to promote and support quantitative and qualitative success of business transfers, it is important to understand why some business transfers fail during the negotiation phase. Therefore, the purpose of this paper is to explore, from the buyers' and sellers' perspective, the reasons business transfers fail at the negotiation phase. The objectives are to analyze a)

the problems and key reasons for unfinished negotiations in small business transfers, b) learning from and satisfaction with the negotiation process and c) whether the previous experience in selling and acquiring a firm has any connection with the level of progress achieved in business transfer negotiations.

Literature Review

Challenges and success factors of business transfers can be divided in accordance with the process (Graebner, Eisenhardt, and Roundy 2010, 78-81; Very, and Schweiger 2001, 19). This paper focuses on pre business transfer phase and more precisely on business transfer negotiation phase. Negotiation phase starts with the first contact between potential seller and potential buyer and ends with the making of an actual agreement on the business transfer (Tall 2014, 156). Pre business transfer phase critical success factors include 1) choice and evaluation of the strategic partner among limited number of potential candidates and identification of potential business transfer advisors, 2) the right price, 3) overall strategy and accumulated experience on business transfers, 4) courtship (Gomes, Angwin, Weber, and Tarba 2013, 17; Very, and Schweiger 2001, 19). Establishing trust and confidence through 'courtship' can allow realistic action planning, effective communication and appropriate negotiation and bargaining styles (Gomes et al. 2013; Sebenius 2002; 1998). Lack of trust makes it difficult to evaluate target business resources, competences and the buyer´s intentions (Gomes et al. 2013, 21). For the buyer reliable information about the target business is essential (Very, and Schweiger 2001, 18). According to earlier research, successful buyers build an experienced deal team that gets involved in the business transfer (Rovit, Harding, and Lemire 2004, 20; see also Varamäki et al. 2013).

Methodology

The data was collected during the summer 2014 using an internet survey aimed at sellers and buyers who had experienced a failure in business transfer negotiations in Finland during the years 2011–2014. A total of 156 replies were received, 40 from buyers and 116 from sellers. The data was analyzed with SPSS using distributions, averages and T-tests.

Description of the Sample

The average size of the target firm, in both selling and acquiring, was from two to four employees and a turnover between 100 000 € and 499 000 €. This fits earlier results in Finland (Varamäki et al. 2013) suggesting that similarity in size between sellers and buyers is common. Most of the target firms were in the service sector (40 percent for selling, 35 percent for acquiring) and located in the same area as the buyer (over 50 percent). The level of previous experience, measured with a 1 to 5 Likert scale (1=no experience at all to 5= considerable experience) in acquiring a firm was 3.3 (buyers) and 2.1 (sellers), and in selling a firm 2.2 (buyers) and 2.4 (sellers), i.e. buyers had more experience in acquiring (p<.001) and sellers slightly more experience in selling.

Results

The negotiations lasted between one to six months on average, and progressed until middle phase or a bit further. The items on which the parties had agreed upon prior to ending the negotiations included the object of the transfer (87 percent), the role of the seller after the transfer (55 percent), timing of the transfer (39 percent), price (35 percent) and other terms of the business transfer (26 percent). Previous experience in selling a firm had a positive effect on the number of items the parties were able to agree upon (p=0,002). However, experience in acquiring didn’t have similar effect.

The failure of negotiations was generally the result of several problems rather than a single issue. From the buyer's perspective, the seller's high asking price was the main problem (average 4,0 on a scale of 1-5, 1= not a problem and 5=an extremely big problem) followed by valuation (mean 3,2) and funding (mean 2,7). Preparing the contract and learning about the target have no serious trouble. For sellers, the key problems were funding (mean 3,3), finding the buyer (mean 3,2), valuation (3,0) and buyer's too low a price offer (2,9). Funding was a major problem in retail trade (mean 3,8) and manufacturing (mean 3,7) but less so in the service sector (mean 2,9; p=.012). Valuation was a more of a challenge among micro firms than slightly larger firms (mean 2,9 for firms with 2-9 employees and 2,7 for firms with ten or more employees; p=.023). Of the buyers, 68 percent rate *the sellers' high asking price*, and 45 percent the *target not meeting their expectations* as the most or the second-most important reason for the failure to complete the deal. Of the sellers, however, 63 percent find that the most or the second-most important reason for failure is that *the buyer did not really want to buy* and 47 percent that *the buyer was unable to secure financing*. The differences between buyers' and sellers' perceptions are statistically very significant (p=.000).

Altogether 83 percent of the buyers but only 55 percent of the sellers would not do anything differently in the negotiations, were they to start over now (p=.003). Learning from transfer negotiations seems cumulative. The respondents with previous experience would more often do something differently than those for whom this was the first such process. Of those who would do something differently, both sellers and buyers would plan the process better and use more external expertise. Also, many of the sellers would adjust their asking price and try to move the process along faster. Ultimately, however, 39 percent of the buyers and 18 percent of the sellers were either satisfied or very satisfied with the fact that the negotiations failed and the transfer was unfinished.

Conclusions

The **main contribution** of the study is that it examines the reasons for failure of business transfer negotiations among small businesses. In unfinished business transfers the problems are more numerous and the gaps between the views of the two negotiating parties are wider than in successfully concluded business transfer negotiations. The results highlight the importance of unfinished small business transfers as an essential element of a dynamic business transfer market; a substantial share of the potential buyers and sellers are satisfied with the outcome even though the transfer did not occur.

The study also has a number of **managerial implications**. First, several factors usually contribute to the failure of business transfer negotiations. For the buyer, the negotiations are foremost a process of familiarizing oneself with the target business as the negotiations proceed. Second, high asking prices are a serious problem and unrealistic initial valuations can cause failure in early phases. Third, in many cases the unfinished business transfers remain unfinished because the target firms in question are no longer viable. Even aging entrepreneurs should continue to develop their business. Fourth, once negotiations begin, every effort should be made to move them along efficiently. Negotiations that stall should be cut off without undue delay. Fifth, the utilization of business transfer experts in the transfer negotiations is recommended.

A proposal for **further research** would be to follow-up on the unfinished business transfer processes, that is, to see how the buyers and sellers fare with their possible new negotiations. A longitudinal follow-up after 1–2 years could discover whether the targets examined here have later found buyers, and the buyers now unable to make a business transfer, targets to acquire.