A CUBE CAPITAL PUBLICATION

Founder Thesis

ISSUE 13

Technology M&A

Arc Two: The Other Side of the Table

The Deal That Falls Over on the Seller's Side

Thesis: Most deals that collapse after terms are agreed do not fail because the buyer changed its mind about the business. They fail because the seller entered exclusivity carrying structural conditions she did not know she had. The buyer wanted the company. It did not want to inherit unresolved title, consent, employment, IP and warranty risk. Once those problems surfaced, the seller no longer had a market. She had a condition.

01 One Question

The term sheet had been signed on a Friday.

She had run a competitive process. Four buyers had received the information memorandum. Three submitted indications of interest. Two came to management presentations. One emerged as the clear preferred party. Terms were negotiated over three weeks. Exclusivity was executed. Her adviser told her the hard part was behind them.

Three weeks later, the question arrived from the buyer's counsel.

It was not about revenue quality. Not customer concentration, margin, roadmap, or churn.

It was about whether she could actually sell what she had agreed to sell.

A former co-founder who had left the business four years earlier still held a seven percent interest. There was no shareholders agreement. No drag-along provision. No written record of what, if anything, had been agreed when the relationship ended.

The buyer's counsel asked how the seller proposed to obtain his consent.

She did not have an answer. The co-founder was no longer in contact. The separation had not been clean. Her lawyer confirmed that without his consent, or a court order, the transaction could not proceed on the terms agreed.

The deal did not collapse that morning. But it did not close on the timeline either party had planned. The delay cost her the preferred buyer. By the time the structural problem was resolved, exclusivity had lapsed, the buyer had deployed capital elsewhere, and the process restarted from a smaller field.

The problem had existed for four years. It had never been examined. It was invisible in the business, in the financials, and in the information memorandum. It became visible only when the transaction required proof.

02 Where Deals Die

Commercial failures in M&A are usually visible early in a process. A buyer who loses confidence in the market, the growth trajectory, or the customer quality shows it in the offer. The multiple is conservative. The structure is cautious. The process moves slowly.

Structural failures are different. They do not arrive in the offer. They arrive after the offer has been accepted.

The buyer wanted the business. That question was settled. Exclusivity was signed. The seller had removed the competing parties, committed to a single counterparty, and entered the most consequential phase of the transaction with the least leverage she would ever have in it.

Then diligence found something.

Not a commercial finding. A structural one. Something in the cap table, the contract suite, the employment records, or the IP chain that the seller could not resolve cleanly, could not resolve quickly, or could not resolve without creating a new disclosure that introduced a further condition.

Before exclusivity, the seller holds structural leverage. Other parties are in the process. The buyer is competing. Problems that surface early can be managed in the offer structure, priced into the consideration, or remediated before close with both parties motivated to move.

After exclusivity, the seller has eliminated that leverage voluntarily. Every condition the buyer's counsel identifies is now a problem only the seller can resolve. The buyer does not need to manufacture pressure.

The seller's own process has already removed the alternative.

The structural problem does not need to kill the transaction to do damage. It only needs to produce a condition the seller cannot meet on time. A lower price. An escrow the seller had not modelled. A timeline that breaks the deal commercially while the parties remain formally engaged.

What the founder needed, before she entered that process, was not a better information memorandum. She needed a condition inventory: a prior assessment of every shareholder, customer contract, licence, employment arrangement, contractor relationship, and corporate record that could become a closing condition once a buyer's counsel began work. Most of them were knowable. None of them had been looked at.

03 Clean Title

The most common structural problem in Australian mid-market software transactions is not hidden in the financials. It is in the share register.

A founder who has built a business over eight to twelve years has usually issued equity in informal circumstances. A co-founder who departed without a properly documented exit. An early employee who received equity through a conversation rather than a formal deed. An investor or adviser granted an interest that was partially but not correctly documented at the time.

None of this creates operational problems. The business runs. The customers pay. The share register is a governance matter that sits quietly in a file no one has opened for years.

It becomes a live problem the moment a buyer's counsel is asked to confirm that the seller can deliver clean title to one hundred percent of the shares.

A drag-along right, properly drafted in a shareholders agreement, allows the majority to compel the minority to sell on the same terms. Without one, each minority holder has, in effect, a veto. A minority holder who is no longer in contact, who cannot be located, or who understands the leverage the moment a transaction is on the table, can stall the process or extract a price the seller had never modelled.

The fix, when relationships are functional, is not complicated. It requires a shareholders agreement with appropriate drag provisions, properly documented share transfers, and a clear record of how each equity interest was granted and what subsequently happened to it. Done with time available, this is a weeks-long legal task.

Done inside exclusivity, with parties who may no longer be cooperative, it can take months or become impossible.

The buyer does not experience this as a governance clean-up. It experiences it as title risk. And title risk is not negotiated the way valuation is. It is cleared, conditioned, deferred, or the buyer walks.

04 Change of Control

A buyer acquires the company's contracts as part of the business. What its legal team is confirming is whether those contracts survive the acquisition.

Change of control provisions appear in customer agreements, vendor arrangements, technology licences, and premises leases. They give the counterparty the right to consent to, or exit, the arrangement when ownership of the contracting party changes. In a software business, the most consequential concentration of these provisions is in the customer base.

A founder who has not reviewed her customer contracts for change of control obligations does not know, with confidence, whether her contracted revenue survives the transaction. The buyer's legal team will find out. If a material proportion of annual recurring revenue is subject to customer consent requirements, the buyer will

require those consents before close, or insert a condition that ties consideration to the proportion of revenue that has consented.

This is not merely a consent mechanics problem. It is a revenue certainty problem. A customer consent condition that cannot be resolved before completion creates a gap between the revenue the seller represented and the revenue the buyer will actually receive. That gap can become a de facto re-underwriting of ARR at the worst possible moment.

Issue 07 covered the commercial dimension: whether revenue will renew. The structural question here is different. It is whether the contracts that produce that revenue can be transferred at all. A founder who has resolved the commercial question but not examined the structural one has done half the work.

The founder who has reviewed her contracts, understood the consent obligations, and planned how material consents would be handled before a process begins is not creating problems. She is removing the conditions that allow a buyer to create them.

05 People Risk

Two categories of employment-related conditions surface consistently in legal diligence on Australian software companies.

The first is contractor classification. Software businesses commonly engage engineers and other technical contributors as contractors over extended periods. Extended arrangements that are continuous, exclusive, and integrated into the team can cross the line between independent contracting and employment. The risk is not only back-payment of entitlements. If a contributor who built material parts of the codebase was never subject to a properly executed IP assignment agreement, the chain of title to the software is defective. IP title uncertainty and employment liability arrive in diligence together.

The second is informal arrangements with key people. A business built over a decade accumulates verbal commitments: equity interests described in conversations but never documented, exit entitlements mentioned in emails that do not constitute enforceable agreements but create expectations the seller cannot dismiss and the buyer cannot price. A key engineer who was told he would receive "something at exit" has an undocumented claim that must be resolved before close. If it has not been agreed in advance, it becomes a condition inside the most pressured part of the timeline, financed by the seller and timed by the buyer.

People risk does not stay in the HR file. In a transaction, it becomes a consent, a release, a retention payment, a warranty disclosure, or a condition.

06 A Promise You Cannot Make

A transaction requires the seller to make, in formal legal documents, representations and warranties about a long list of things. Ownership of shares and assets. The completeness of disclosed contracts. The accuracy of financial statements. The absence of undisclosed obligations. The state of IP ownership. The standing of employment arrangements.

These are not administrative formalities. They are the seller's promise that what the buyer agreed to buy is what it will actually receive.

> ***A founder often does not discover that she cannot make a representation cleanly until she is asked to make it under legal obligation, inside an exclusivity period, with the competing buyers already gone.***

A founder who has run her business well, with the correct priorities of a working company, will often arrive at a sale process with corporate records that do not fully support the representations she is being asked to make. Board minutes never formalised. Share transfers not properly documented at the time. IP created by contributors whose assignment obligations were never captured in writing. Employment arrangements that evolved without paperwork.

None of this necessarily defeats the transaction. But it creates remediation work that must be completed under the timeline pressure of an active process. Work done under that pressure is more expensive, produces more

disclosures, and exposes further conditions. Every new issue identified during remediation is an additional warranty disclosure. Every disclosure is a point the buyer's counsel can use.

The seller who completes this work before a process begins is not eliminating the buyer's right to raise conditions. She is removing the conditions that are already there.

07 Before Exclusivity

Structural failure is the most preventable category of deal collapse. It requires no commercial breakthrough, no product investment, and no organisational change.

It requires a prior look.

The condition inventory is not a legal audit commissioned to produce a clean bill of health. It is an honest list of every element of the business that could become a closing condition once a buyer's counsel begins work: every shareholder and the documentation supporting their interest, every material customer contract and its transfer provisions, every technology licence, every contractor relationship and the IP assignment attached to it, every informal people arrangement that could create an undisclosed obligation.

Some items on that list will be minor. Some will require targeted attention. A small number will be genuinely time-sensitive, involving parties whose cooperation cannot be assumed and whose willingness to assist does not improve under transaction pressure.

A founder who commissions this work eighteen to twenty-four months before a process has time to resolve the difficult items with functional relationships, without a buyer in the room and without a closing timeline creating the pressure. A founder who discovers them inside exclusivity has already given up the thing that makes resolution possible: the option to walk away.

The logic of structural preparation is the same as technical debt preparation, and the same as the founder dependency problem. Known conditions can be solved, priced, or sequenced. Unknown conditions discovered after exclusivity become someone else's leverage.

Many transactions do not fall over because buyers find the unimaginable. They fall over because sellers arrive at exclusivity carrying conditions a methodical prior review could have found and the seller could have resolved with time.

The prepared business is not the one with no problems. It is the one whose problems are already known, sequenced, costed, and controlled before the buyer gets the chance to turn them into conditions.

The deal was ready.

The business was not.

NEXT ISSUE
Issue 14, ***The Prepared Business Premium,*** *closes Arc Two by asking what the full picture of exit preparation is worth: not as a philosophy, but as a price.*

Cube Capital advises founders and boards of Australian software and technology companies on exit preparation and cross-border M&A transactions. The firm works exclusively on the sell side, retained by founders who want an independent view of how buyers will price their business, where value may be lost, and what can be done before a transaction begins.

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