An Introduction to the Independent Sponsor Model
Presented by Opus Connect

Moderator:
Chris Sheeren, Huron Capital Partners

Panelists:
Christopher Freeburg, Skyline Global Partners
Grant Kornman, NCK Capital
Conor Mullett, Red Oak Growth Partners
Dan Negrea, MTN Capital Partners LLC

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Questions for the panel?

• Please submit your questions via “Q&A” to “All Panelists”
• Moderator will select questions as needed
• Designated time for Q&A at the end
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  – Founder of Genero Capital Partners

• **Chapters: LA, NY, San Francisco, Chicago, Orange County**  
  – Monthly seminars  
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  – Only accomplished senior executives, vetted by selection committee

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Facility Size (in millions)
• $1 - $20

Purpose
• Acquisitions
• Growth Capital
• Turnaround/restructuring

Business Segments
• Manufacturers
• Wholesalers
• Business services
• Retailers & e-commerce
• Specialty Finance

Financing Structures
• Accounts receivable – domestic & foreign
• Inventory revolvers
• Senior stretch
• Term loans – M&E

Client Benefits
• Speed & certainty of close
• Speak directly with decision makers (no BDO’s)
• Creative financial solutions
• Do not take upsides

About Accord
35 + years history
Publicly traded (TSX:ACD)
Strong balance sheet
Who Is Huron Capital?

- Based in Detroit since 1999, with a satellite office in Toronto
- Over $1.1 billion in capital raised across four funds
- Target industries: niche manufacturing, consumer, healthcare and business services
  - Revenues of up to $200 million
  - EBITDA of at least $5 million
- Majority investor, in companies based in the U.S. and Canada
- Have done four independent sponsor deals; looking to do one a year
- Operations oriented; our professionals have diverse backgrounds
Who Is Chris Sheeren?

- **Position:** Partner with Huron Capital. Joined in 2004. Portfolio responsibilities have included specialty chemicals, auto aftermarket, building products, lab testing, and others.

- **Experience:** Previously worked in turnaround consulting (interim CFO), public accounting, and sales. Registered CPA. Don’t hold that against him.

- **Education:**
  - B.A. from the University of Nebraska
  - M.B.A. from the University of Michigan

- **Family:** Four children (17, 15, 14, 11)

- **Interests:** College football, basketball, fantasy baseball, theater
MTN Introduction

- Founded 10 years ago
- Completed 14 deals, $500 million total purchase prices
- Ten professionals
- MTN Difference:
  - Strong emphasis on origination
  - Use of industry experts – critical role
- Repeat capital partners: Incline, Argosy, RFE and Angelo Gordon
Background

- **50+ years experience as both investors and operators**
  - 30+ years of combined direct investment experience in private equity, 9+ years directly investing together
  - Founding team member at Updata Partners that raised and invested over $450M in private equity capital over the past 12 years
  - 20+ years of successful operating and exit experience in senior executive roles (CEO/COO/Founder) in software and business services
  - Raise over $500M senior and subordinated debt financings in connection with private equity transactions

- **Previously General Partners at Updata Partners**
  - Sourced, sponsored or co-managed 15 portfolio company investments at Updata deploying $140mm in invested capital.
  - Jointly led the most successful realized investment at Updata (Jobs2Web)
  - Successfully raised 3 institutional private funds totaling over $450mm in LP commitments from blue chip investors including family offices, endowments, pension funds and fund of funds
Skyline Global Partners

- Boutique private equity sponsor firm in Chicago
- 3 Partners have over 40 years of private equity experience
- Focus on lower middle market
  - Buyouts, recapitalizations and growth equity
  - Invest $10 million to $100 million in equity
  - Revenue of $20 million to $100 million
  - EBITDA of $3 million to $15 million
- Industries in which we invest include:
  - Healthcare
  - Business Services
  - Manufacturing
  - Software
  - Consumer
  - Food
- Unique network of global strategic relationships
Portfolio Companies

- **Captek Softgel**
  - Contract manufacturer and distributor of specialty softgel nutraceuticals
  - Our investment provided liquidity for shareholders and growth capital for the business

- **iMDsoft**
  - Worldwide leader in high acuity clinical information systems for hospitals
  - Our investment provided liquidity for shareholders and growth capital for the business

- **DCRX Infusion**
  - Specialty infusion pharmacy for dialysis patients
  - Our investment provided liquidity for shareholders and growth capital for the business
About NCK Capital

- Family owned and operated.
- All of our current portfolio companies we founded and built.
- 15+ years of direct investing experience.
- 30+ years of C level experience.
- Focuses on acquiring and investing in lower, middle market companies with $2 million to $10 million of EBITDA.
- Geographic Focus: Southeast, Southwest, Midwest and Mountain regions. Strong focus on Texas.
- Core Industry Focus:
  - Restaurant/Hospitality
  - Alternative/Consumer Finance
  - Industrial Services
  - Business Services
- Based in Dallas, TX
What is an independent sponsor? Who are they, and where do they come from?

Dan Negrea
Managing Partner, MTN Capital LLC
Many private equity professionals, doing many quite different things, call themselves Independent Sponsors (“IS”).

It is a spectrum with lots of variations in between.

At one end of the spectrum is the ENTREPRENEUR IS.
- He thinks more like a small proprietor – very focused on a relatively small portfolio of smaller companies.

At the other end of the spectrum is the QUASI-PE IS.
- He thinks he is just like any other PE firm, it’s just that he finances his acquisitions on a deal-by-deal basis. He would like to have a larger portfolio of larger companies, like a funded PE firm.
Spectrum: The Entrepreneur
Spectrum: The Quasi-PE
# Spectrum - Summary

<table>
<thead>
<tr>
<th></th>
<th>Entrepreneur</th>
<th>Quasi-PE</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Size of the deal</strong></td>
<td>Mostly under $3 million EBITDA</td>
<td>Mostly over $5 million EBITDA</td>
</tr>
<tr>
<td><strong>Deal Monitoring</strong></td>
<td>Very active, often becomes CEO or Chairman of the Board</td>
<td>PE - style</td>
</tr>
<tr>
<td><strong>Capital Partner Involvement</strong></td>
<td>Limited – IS leads due diligence, monitoring and exit</td>
<td>CP is decision maker; IS is the junior partner</td>
</tr>
<tr>
<td><strong>Sources of Capital</strong></td>
<td>HNW individuals, Family offices, Personal capital <strong>Hedge Funds, Pension Funds, Insurance Companies</strong></td>
<td>PE Groups, Control Mezz Groups <strong>Hedge Funds, Pension Funds, Insurance Companies</strong></td>
</tr>
<tr>
<td><strong>Skin in the game</strong></td>
<td>Meaningful amount</td>
<td>Limited amount because CP is decision maker</td>
</tr>
<tr>
<td><strong>Eggs and baskets</strong></td>
<td>IS perspective: All eggs in one basket – watch basket</td>
<td>IS perspective: Not all eggs in one basket-investment portfolio</td>
</tr>
<tr>
<td>IS Roles in a Transaction: The Entrepreneur</td>
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<tr>
<td>---------------------------------------------</td>
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<tr>
<td><strong>Independent Sponsor</strong></td>
<td><strong>Capital Partner</strong></td>
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<tr>
<td><strong>Sourcing Deal</strong></td>
<td>Full responsibility</td>
<td>Not Involved</td>
</tr>
<tr>
<td><strong>Identify Industry Expert</strong></td>
<td>Full responsibility</td>
<td>Not Involved</td>
</tr>
<tr>
<td><strong>Initial Due Diligence Auction</strong></td>
<td>Full responsibility</td>
<td>Not Involved</td>
</tr>
<tr>
<td><strong>Initial Due Diligence Non-Auction</strong></td>
<td>Full responsibility</td>
<td>Not Involved</td>
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<tr>
<td><strong>IOI</strong></td>
<td>Full responsibility</td>
<td>Not Involved</td>
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<tr>
<td><strong>Management Meeting</strong></td>
<td>Full responsibility</td>
<td>Not Involved</td>
</tr>
<tr>
<td><strong>LOI</strong></td>
<td>Full Responsibility</td>
<td>CP Brought in after LOI</td>
</tr>
<tr>
<td><strong>Hire Professionals</strong></td>
<td>Main Responsibility</td>
<td>Some Responsibility</td>
</tr>
<tr>
<td><strong>Select Lenders</strong></td>
<td>Main Responsibility</td>
<td>Some Responsibility</td>
</tr>
<tr>
<td><strong>Final negotiations</strong></td>
<td>Main Responsibility</td>
<td>Some Responsibility</td>
</tr>
<tr>
<td><strong>Board Control</strong></td>
<td>Main Responsibility</td>
<td>Some Responsibility</td>
</tr>
<tr>
<td><strong>Management Interface Post-Acquisition</strong></td>
<td>Main Responsibility</td>
<td>Some Responsibility</td>
</tr>
<tr>
<td><strong>Sale Decision</strong></td>
<td>Joint Responsibility</td>
<td>Joint Responsibility</td>
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## IS Roles in a Transaction: The Quasi PE

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<th>Activity</th>
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<th>Capital Partner</th>
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<td>Not Involved</td>
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<tr>
<td><strong>IS PRESENTS DEAL TO CP</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management Meeting</td>
<td>Joint</td>
<td>Joint</td>
</tr>
<tr>
<td>LOI</td>
<td>Junior Partner</td>
<td>Decision Maker</td>
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<td>Hire Professionals</td>
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</tr>
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Predictions: Continued Growth of IS

• The Entrepreneurial IS - will always be there.
• The Quasi-PE IS will continue to grow because of powerful driving forces:
  • **Deals**: Tens of thousands of middle market companies. Hundreds for sales each year.
  • **Intermediaries**: We have a database with 5,000 names
  • **Professionals to be IS**: Senior investment bankers; former PE professionals and corporate executives
  • **Capital**: MTN has 1,000 names for lower end of middle market CPs.
Predictions: Increased Use of Industry Experts

- PE started by buying companies cheap and leveraging them.
- It evolved to improving operations with generalist executives.
- The next phase will be the use of specialized executives.
- Again, there are powerful driving forces at work:
  1. A plentiful supply of former senior executives. For ex., MTN stats: Over 5,000 executives in our data base.
  2. LinkedIn and other networking sites make it possible to see thousands of resumes.
  3. The recognition by CPs that it is valuable to have an industry expert validate the investment thesis, help with due diligence, and monitor the company as a member of the board.
Predictions: Consolidation among IS

- This is a scalable business. We will see the emergence of larger IS with many professionals.
- We have nine professionals at MTN and we continue to grow.
- Models are merchant banks like Allen & Co. (Future name for some IS?) or investment banks like Focus and Headwater.
- No major disadvantages in being larger and many advantages: brand name, access to data bases of executives and CPs.
- Someone joining a larger IS gives up a share of their economics on any particular deal but expects to (1) Do more deals and (2) Get better economics as part of a larger firm.
How does an independent sponsor deal work? How do they get compensated?

Conor Mullett
Managing Director, Red Oak Growth Partners
## Independent Sponsor: Value Proposition and Process

An independent sponsor must add value to the transaction process in order to justify its economics.

<table>
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<tr>
<th>Sourcing</th>
<th>Strategy</th>
<th>Closing</th>
<th>Management</th>
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</table>
| – Attractive entry price  
– Unique, proprietary deals | – Growth strategy development | – Detailed diligence and negotiation | – Chairman, Lead Director  
– Active and ongoing management → operations and M&A |

- Typically, the sponsor sources the transaction and can either negotiate and execute the LOI exclusively or involve a prospective financing source.
- The sponsor lays out a clear and executable growth strategy consisting of organic and inorganic initiatives, including actionable M&A targets.
- Detailed diligence is conducted by both the independent sponsor and prospective investor over the course of multiple management meetings.
- The sponsor and investor are active board participants going forward, though there are some passive investors who prefer limited involvement.
Independent Sponsor: Compensation Mechanics

- Though each deal is different, independent sponsors are typically compensated through a mix of origination fees, monitoring fees, and equity incentives.

<table>
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<tr>
<th>Origination Fees</th>
<th>Monitoring Fees</th>
<th>Equity Incentives</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Typically 1.0% to 2.0% of Enterprise Value</td>
<td>- Typically 2.5% to 5.0% of EBITDA</td>
<td>- Typically 10% to 20% of fully-diluted equity</td>
</tr>
</tbody>
</table>

- Origination and monitoring fees are often split with investment partners.

- Equity incentives can be subject to performance-based hurdles.

- Investment partners typically assume responsibility for “broken deal” expenses.
What are the advantages and disadvantages of the independent sponsor model?

Christopher Freeburg
Partner, Skyline Global Partners
Advantages of Independent Sponsor Model

- Independent Sponsor
  - Build firm from ground up
  - Flexibility
  - Speed
  - Significant LP/GP dry powder
  - Leverage equity partners’ resources and capabilities
  - Avoid having to raise and administer dedicated fund
  - Reasonable economics

- Capital Partner
  - Proprietary deal flow
  - Value added investor and partner
  - Expedited deal timing

- Intermediary & Service Provider
  - Potential buyer or client
  - Value added investor and partner
Disadvantages of Independent Sponsor Model

- **Independent Sponsor**
  - Selling the target company and their intermediary
  - Raising capital deal by deal
  - Subject to equity partners’ Investment Committee(s)
  - Rules of engagement
  - Governance
  - Expedited deal timing
  - Negotiated economics

- **Capital Partner**
  - Competition for deal flow
  - Rules of engagement
  - Governance
  - Expedited deal timing
  - Alignment of incentives
  - Economics sharing

- **Intermediary & Service Provider**
  - Unfunded vs. funded sponsor dynamics
  - Rules of engagement
How can an independent sponsor compete with a funded private equity group?

Grant Kornman
Managing Partner, NCK Capital
It’s Pretty Simple…Don’t Compete With Them?

1. Create proprietary deal flow - full auctions are tough
2. Build deep relationships with sellers/owners
3. Focus on industries that you know - don’t be a generalist
4. Partner with key industry executives that create value for target companies
5. Present yourself differently then funded private equity groups
Have Your Capital Figured Out Early

1. Develop deep relationships with core group of equity partners.
2. Be honest... trust is key.
3. Get your equity partner involved as soon as possible.
4. Clearly define roles and responsibilities so you do not confuse the sell side.

1. Don’t usurp the Independent Sponsor.
2. Educate your partner about your needs and process.
3. Support your partner so they can win the deal.
4. Be flexible.
Why should I work with an independent sponsor?
Q&A with the Panel

• Please submit your questions via “Q&A” to “All Panelists”
Thank you!

• You will receive:
  – Survey about today’s webinar
  – Contact information for our panel
  – Link to a recording of today’s webinar (on Monday March 3rd)

• Questions? Contact Nick Zobel (nick@opusconnect.com)
  – Potential members are invited to attend TWO Opus Connect chapter meetings free of charge.