

DysFUNCTION: Finding humor amid chaos



By Harvey Nachman

Turnaround managers have been described as a blend of the good Lord and the infamous suicide doctor, Jack Kavorkian. “We try to save the companies with which we work, or else we try to bury them with dignity.”

Even in cases in which the vision and accompanying strategies can be identified for a successful turnaround, daily tension is the rule and not the exception. When attempting to implement a revised company business plan, resistance and denial by existing management can often lead to very interesting situations.

The passionate pursuit of most turnaround professionals is finding ways to convince smart but recalcitrant CEOs, COOs or founders to change how “their” businesses operate, after having functioned their way for so many years. Too often, the difficulty is convincing these seasoned executives that the turnaround professional best understands how to handle the recovery process that involves lenders, creditors, lawyers and/or unions within a troubled environment. Convincing management that the professional can accomplish the tasks required to achieve the plan objectives, without the emotional baggage normally associated with management or the distrust often harbored by the lenders, is the challenge.

How, then, does one find fun in dysfunction? One simple example recently occurred. A corporate senior officer extended his hand in greeting and offered his business card. It clearly stated “John Smith,

President.” Shortly after that encounter, a second executive entered the conference room and offered a similar business card, which read, “Jim Smith, President.” It did not take a rocket scientist to realize that this firm was in trouble, even if senior management did not recognize the level of difficulty.

Numerous financial early warning signs can predict with a reasonable degree of accuracy whether a firm can continue to be profitable or is quickly approaching disaster. Among these are tests for accounts payable beyond 60-day term, accounts receivable aging and slow inventory turns. Often to get beyond the numbers, we check out the executive parking lot and apply the “TMM” test. If there are “too many Mercedes” automobiles (or Porsche, Lexis or BMW vehicles as well), this firm is probably abusing its sales, general and administration (SG&A) figures.

Dysfunctional management comes in many shapes, sizes and officer levels in the corporate world. It may be seen at the sales management level, when results do not meet forecasts and the excuses offered include the blame game (“it’s someone else’s fault”), the weather or events surrounding 9/11. Honesty and logic disappear, and rationalization overtakes good corporate behavior.

Of course, in many instances the chief financial officer (CFO) is no shrinking violet in this process either. By creating or re-creating graphs, lineal function lines and modified forecasts to show that his or her plan made sense and that others did not perform, the CFO can create tension along the other line officers by not proactively and continuously updating the cash and profitability reports.

In a recent engagement, a client company had purchased its largest competitor three years earlier and had increased its debt exposure by many millions of dollars. In an effort to protect the company should interest rates rise substantially, the CFO purchased an interest “collar.” Three years later, the company experienced a substantial downturn in business and offered many of the excuses mentioned earlier for failing to incorporate the acquisition properly into its organization and culture.

Upon learning of various covenant defaults and that the lender increased the basic interest charge from LIBOR-based to prime-plus, including default rates, the

CEO had a knee-jerk reaction. Aware that interest rates had fallen by 4.5 basis points and not willing to admit to his lack of success in the integration process, he alleged that the CFO not only allowed the lender to raise interest rates to the default level, but also did not do enough to protect the company. He rationalized that initially protecting the company against a rise in interest rates was not considered a prudent decision when faced with the current reality of declining rates.

As in professional sports, owners do not get fired—only managers. The dysfunctional relationship between CFO and chairman became intense, and the CFO was dismissed, even though his efforts were directed at protecting the company from disaster. It has been said that many turnaround professionals know how to restore profitability and management harmony to a troubled business. The challenge in achieving a successful engagement is to make the solutions acceptable to the management team and palatable to the lender or equity sponsor groups that are worried about their capital or debt. While this effort may be Herculean at times, maintaining a sense of calm and realizing that there can be fun in the obvious dysfunction makes it all worthwhile.

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NachmanHaysBrownstein, Inc. (NHB) is

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