Western Mass Venture Forum NEWS

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November 27 -

MANAGING CHAOS & BIOMETRICS2000

The November 27 session of the Western Massachusetts Venture Forum features a presentation by Bill Hanley, President & Owner of Millitech, LLC in Northampton on MANAGING CHAOS, CHANGE & UNCERTAINTY. Using his experience, he will focus on the fact that pain is inevitable in business but suffering is optional. Developing skill-based organizations that master business fundamentals, position themselves to cope with uncertainty and manage through chaos eliminates that suffering. Bill will use real life examples to punctuate how to do this in the real world.

The business plan - seeking $2M - will be presented by BIOMETRICS2000, a Springfield company which has developed a unique technology to turn fingerprints into data. This technology is used as the basis for its CheckME and AKcessKEY product lines used in physical access control applications. Each of the CheckME and AKcessKEY product lines is designed to attack a different segment of the physical access control market, which is $2.47 Billion a year. Because of the September 11 events, BIOMETRICS2000 believes that the biometrics enabled segment of the physical access control market, which was projected to grow by 50 million units a year before September 11, will grow at a faster rate.

Before buying Millitech, Hanley was with Galileo Corporation of Sturbridge where he rose from Vice President of Manufacturing to President and Chief Executive Officer. Bill developed the strategy and converted Galileo's business from 85% military to 95% commercial. He is a recognized leader in defense-to-commercial conversion and played a major role in state and federal government activities on this issue. He has appeared on CNN, Business Day, MacNeil/Lehrer and other national television and media programs.

Biometrics based reader techology has always held the greatest promise for becoming the next wave of physical access control technology. This is because it identifies the entrant positively without manual or video surveillance. The limiting factor has been cost and reliability. The BIOMETRICS2000 technology is a breakthrough in biometric technology because it deals with both issues.

Fingerprint based biometric technology has the most effective combination of characteristics to be the technology of choice. Although not as accurate as iris or retinal scanning, it is

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September 27 Forum Notes:

The Venture Forum's second-year began with GETTING THE MONEY, featuring a panel of three experienced money providers and the presentation of a business plan by CASTion corporation, a company looking to expand sales and marketing operations connected with its proprietary chemical separation equipment.

CASTion has had several rounds of angel and venture financing. Both EPA and DEP evaluated their technology and gave it awards. CASTion is now looking for a $2 million additional investment to establish branch office operations for sales and marketing. The plan was presented by John Gannon, President and CEO of CASTion corporation.

CASTion has found that its proprietary chemical separation technology can be used in industries beyond the metalworking trades where its original application was developed. The technology can create a zero discharge environment for end of process wastewater recovery.

The panel on GETTING THE MONEY consisted of Russ Howard from Berkshire Capital Investors; Richard Steele from Summer Street Investors and Richard Cranshaw from Capital Resources Fund.

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M & A Basics

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New products, technologies, competition and politics are constantly changing today's business world. Business owners are always looking to capitalize on these changes and enhance shareholder value. They can meet this challenge through substantial internal capital outlays and costly start-up phases.

Or they can consider the acquisition of a company that has already developed a business that meets their specific needs. Privately owned middle-market companies, such as family-owned businesses, can also benefit from this strategy. Let s review the basics of this popular yet often misunderstood process.

Ask the Tough Questions First

The prospective company (the target) is generally a company in your line of business that is either already operating in an area that your company plans to expand into or has a product that would complement your product line. Remember, cost effectiveness is key in any meger or acquisition.

As with any business plan, you need to give significant thought to any potential merger or acquisition. Ask yourself:

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Managing Chaos & Biometrics2000 - con't.

more acceptable in most applications and considerably cheaper than either. Fingerprint technology is convenient, familiar and intuitive; all advantages over iris or retinal scanning.

The Biometrics2000 management team is second to none in its history of bringing new products to market in the electronic security industry. Three principals founded the Company: Joseph Turek, Jr., President and CEO — Former president and founder of International Electronics Inc., a security products firm and currently the market leader in keypad technology. The company became publicly traded in 1983 and is NASDAQ listed. Joe is an electrical engineer and Vice Chairman of the Biometrics committee of the Security Industry Association. Frank Polidoro, Vice President - Former National Sales Manager for the Unican Electronics Division of Ilco Unican, a publicly traded, worldwide manufacturer of electronic access control equipment. Mike Iveson, Vice President - Served as president, VingCard Systems USA, a subsidiary of a Scandinavian company specializing in electronic locks.

September 27 Forum Notes - continued

Berkshire Capitol generally invests after an Angel investment has proven the technology and developed a prototype or proof of concept. They invest $500,000 to $750,000 themselves and provide access for larger dollars in later rounds. Because of the increased conservatism in the market, they find themselves teaming up with other investors and only investing where they are very confident that there is a clear plan with solid milestones.

Summer Street Capital is a Small Business Investment Company. They have a pool of $100 million to invest in later stage businesses. They look for companies with $5 million to $10 million in revenues. Summer Street Capital believes that many venture funds are functionally insolvent with portfolios which are underwater and not generating cash flow. The lesson for management is to go for less and get creative.

Capital Resources Fund is a privately owned company in the business of factoring accounts receivable. For a fee, they take your accounts receivable and turn it into cash within four to five days instead of 30 to 90 days. They look for a minimum of $100,000 of accounts receivable annually. They work in virtually any industry with verifiable receivables and are more interested in the financial condition of the customer than the company they are dealing with. Their principal concern is whether or not they believe they can collect the receivables. On average, they chage 3 percent per month which places the cost of factoring receivables somewhat above straight debt and somewhat below the cost of a discount program for early payment.

M & A Basics - continued

Aside from the product, will the target company's culture mix well with yours?

Is the target all it claims to be, or will you need to exert considerable energy to get it up to speed?

Should you buy the target with cash, notes, stock or a combination of these? Is a tax-free transaction viable?

Do you accept having the target's shareholders become shareholders of your company?

Do you need long-term contracts and noncompete agreements for the target's key employees and shareholders?

Consider Compatible Cultures

Cultural differences between companies matter greatly in mergers and acquisitions. For instance, your company might have an autocratic management style and the target might be managed more by committee.

Or your company may have an informal dress code and a flexible work schedule, but the target may require business attire and a rigid work week. Address these and similar issues beforehand. If the cultures are incompatible, melding of two companies into a profitable whole might be impossible.

Perform Financial Due Diligence

Financial statements are only as good as the numbers and management behind them. To determine a target's true picture, perform a due diligence review before the merger or acquisition is completed.

A due diligence review can vary somewhat depending on the business. But it generally evaluates the target's customers, products, plant and equipment, suppliers, accounts payable and receivable, and benefit plans, among other items.

Plan an Effective Purchase

How you'll pay for the target's assets is a significant issue in the negotiations. If the target is a corporation, you might have the option to acquire its stock in whole or buy some of its assets outright. Your decision might rest on your due diligence review. For example, the target may have an off-balance-sheet liability, perhaps an environmental problem. In this case, you may offer to buy only some target assets - rather than its stock - to avoid environmental liability.

But the target might demand cash, notes, stock or a combination. If cash is necessary to acquire the target or its assets, consider your company's liquidity or the collateral needed to raise the cash for the purchase. If you borrow cash, also consider its cost in terms of the interest rate charged as well as its impact on your future borrowing capacity.

An alternative to an outright cash purchase might be the issuance of notes. In consideration of notes, carrying charges must be weighed. If interest is too high, it could leave the acquisition nonviable. On the other hand, seller financing may be more liberal than bank financing in terms of the payment program and collateral.

If the taget's shareholders are interested only in your company's stock, consider offering them a second class of stock, possibly preferred stock or nonvoting common stock. A stock-for-stock transaction may open the door to a tax-free merger or acquisition between your company and the target. A tax-free transaction reduces the initial cost of acquiring a target corporation, a savings that applies to the target, the target's shareholders and you.

Beware of Management Issues

If the target or its shareholders are interested in your company's stock in lieu of some or all cash or notes, consider the fact that they will now be shareholders in your company. This could affect the management of your company, the succession of ownership and your estate plan. Of course, if the new shareholders own only a small portion, the day-to-day running of your company will probably not change.

In either case, pay careful attention to management changes. Some companies are viable only if some key shareholders and employees continue with the company. In that event, make every effort to keep key people through long-term contracts and compensation programs.

Size Doesn't Matter

Acquisitions and mergers can have a significant and positive impact on any size business and, at the same time, save money and start-up time. But, as always, exercise normal business caution. Please call us if you are considering a merger or acquisition. We're happy to help.

William Reichelt is a Partner at Themistos & Dane, P.C. He provides tax, accounting, financial planning and management services to firms throughout New England. He heads the firm's Tax Advisory Services department and works on litigation support and business valuation services for the firm.