**Pg. 559** Lewicki (022006). Negotiation w/cases [6]                                                                                                                                      (VitalSource Bookshelf

**Case 1: Capital Mortgage Insurance Corporation**

Frank Randall hung up the telephone, leaned across his desk, and fixed a cold stare at Jim Dolan.

* OK, Jim. They’ve agreed to a meeting. We’ve got three days to resolve this thing. The question is, what approach should we take? How do we get them to accept our offer?

Randall, president of Capital Mortgage Insurance Corporation (CMI), had called Dolan, his senior vice president and treasurer, into his office to help him plan their strategy for completing the acquisition of Corporate Transfer Services (CTS). The two men had begun informal discussions with the principal stockholders of the small employee relocation services company some four months earlier. Now, in late May 1979, they were developing the terms of a formal purchase offer and plotting their strategy for the final negotiations.

The acquisition, if consummated, would be the first in CMI’s history. Furthermore, it represented a significant departure from the company’s present business. Randall and Dolan knew that the acquisition could have major implications, both for themselves and for the company they had revitalized over the past several years.

Jim Dolan ignored Frank Randall’s intense look and gazed out the eighth-floor window overlooking Philadelphia’s Independence Square.

* That’s not an easy question, Frank. We know they’re still looking for a lot more money than we’re thinking about. But beyond that, the four partners have their own differences, and we need to think through just what they’re expecting. So I guess we’d better talk this one through pretty carefully.

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**Company and Industry Background**

CMI was a wholly owned subsidiary of Northwest Equipment Corporation, a major freight transporter and lessor of railcars, commercial aircraft, and other industrial equipment. Northwest had acquired CMI in 1978, two years after CMI’s original parent company, an investment management corporation, had gone into Chapter 11 bankruptcy proceedings. CMI had been created to sell mortgage guaranty insurance policies to residential mortgage lenders throughout the United States. Mortgage insurance provides banks, savings and loans, mortgage bankers, and other mortgage lenders with protection against financial losses when homeowners default on their mortgage loans.

*Source:* Capital Mortgage Insurance Corporation (A), Harvard Business School Case 9-480-057. Copyright ©1980 by the President and Fellows of Harvard College.

This case was prepared by James P. Ware as a basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation. Reprinted by permission of the Harvard Business School. This case written in 1979. For a variety of reasons, it is not possible to update the financial information or the fact pattern in the case. We continue to use it in this book because of the teaching value of the case, in spite of its age.

Lending institutions normally protect their property loan investments by offering loans of only 70 percent to 80 percent of the appraised value of the property; the remaining 20 to 30 percent constitutes the homeowner’s down payment. However, mortgage loan insurance makes it possible for lenders to offer so-called high-ratio loans of up to 95 percent of a home’s appraised value. High-ratio loans are permitted only when the lender insures the loan; although the policy protects the lender, the premiums are paid by the borrower, as an addition to monthly principal and interest charges.

The principal attraction of mortgage insurance is that it makes purchasing a home possible for many more individuals. It is much easier to produce a 5 percent down payment than to save up the 20 to 30 percent traditionally required.

CMI had a mixed record of success within the private mortgage insurance industry. Frank Randall, the company’s first and only president, had gotten the organization off to an aggressive beginning, attaining a 14.8 percent market share by 1972. By 1979, however, that share had fallen to just over 10 percent even though revenues had grown from $18 million in 1972 to over $30 million in 1979. Randall attributed the loss of market share primarily to the difficulties created by the bankruptcy of CMI’s original parent. Thus he had been quite relieved when Northwest Equipment acquired CMI in January 1978. Northwest provided CMI with a level of management and financial support it had never before enjoyed. Furthermore, Northwest’s corporate management had made it clear to Frank Randall that he was expected to build CMI into a much larger, diversified financial services company.

Northwest’s growth expectations were highly consistent with Frank Randall’s own ambitions. The stability created by the acquisition, in combination with the increasing solidity of CMI’s reputation with mortgage lenders, made it possible for Randall to turn his attention more and more toward external acquisitions of his own. During 1978 Randall, with Jim Dolan’s help, had investigated several acquisition opportunities in related insurance industries, with the hope of broadening CMI’s financial base. After several unsuccessful investigations, the two men had come to believe that their knowledge and competence was focused less on insurance per se than it was on residential real estate and related financial transactions. These experiences had led to a recognition that, in Frank Randall’s words, “we are a residential real estate financial services company.”

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## The Residential Real Estate Industry

Frank Randall and Jim Dolan knew from personal experience that real estate brokers, who play an obvious and important role in property transactions, usually have close ties with local banks and savings and loans. When mortgage funds are plentiful, brokers often steer prospective home buyers to particular lending institutions. When funds are scarce, the lenders would then favor prospective borrowers referred by their favorite brokers. Randall believed that these informal relationships meant that realtors could have a significant impact on the mortgage loan decision and thus on a mortgage insurance decision as well.

For this reason, CMI had for many years directed a small portion of its marketing effort toward real estate brokers. CMI’s activities had consisted of offering educational programs for realtors, property developers, and potential home buyers. The company derived no direct revenues from these programs, but offered them in the interest of stimulating home sales and, more particularly, of informing both realtors and home buyers of how mortgage insurance makes it possible to purchase a home with a relatively low down payment.

Because he felt that real estate brokers could be powerful allies in encouraging lenders to use mortgage insurance, Randall had been tracking developments in the real estate industry for many years. Historically a highly fragmented collection of local, independent entrepreneurs, the industry in 1979 appeared to be on the verge of a major restructuring and consolidation. For the past several years many of the smaller brokers had been joining national franchise organizations in an effort to gain a brand image and to acquire improved management and sales skills.

More significantly, in 1979, several large national corporations were beginning to acquire prominent real estate agencies in major urban areas. The most aggressive of these appeared to be Merrill Lynch and Company, the well-known Wall Street securities trading firm. Merrill Lynch’s interest in real estate brokers stemmed from several sources; perhaps most important were the rapidly rising prices on property and homes. Realtors’ commissions averaged slightly over 6 percent of the sales price; *Fortune* magazine estimated that real estate brokers had been involved in home sales totaling approximately $190 billion in 1978, netting commissions in excess of $11 billion (in comparison, stockbrokers’ commissions on all securities transactions in 1978 were estimated at $3.7 billion).[1](http://digitalbookshelf.southuniversity.edu/books/0072973102/content/id/ch91en01) With property values growing 10 to 20 percent per year, commissions would only get larger; where 6 percent of a $30,000 home netted only $1,800, 6 percent of a $90,000 sale resulted in a commission well in excess of $5,000—for basically the same work.

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There were also clear signs that the volume of real estate transactions would continue to increase. Although voluntary intercity moves appeared to be declining slightly, corporate transfers of employees were still rising. One of Merrill Lynch’s earliest moves toward the real estate market had been to acquire an employee relocation company several years earlier. Working on a contract basis with corporate clients, Merrill Lynch Relocation Management (MLRM) collaborated with independent real estate brokers to arrange home sales and purchases for transferred employees. Like other relocation companies, MLRM would purchase the home at a fair market value and then handle all the legal and financial details of reselling the home on the open market. MLRM also provided relocation counseling and home search assistance for transferred employees; its income was derived primarily from service fees paid by corporate clients (and augmented somewhat by referral fees from real estate brokers, who paid MLRM a portion of the commissions they earned on home sales generated by the transferred employees).

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Later, in September 1978, Merrill Lynch had formally announced its intention to acquire at least 40 real estate brokerage firms within three to four years. Merrill Lynch’s interest in the industry stemmed not only from the profit opportunities it saw but also from a corporate desire to become a “financial services supermarket,” providing individual customers with a wide range of investment and brokerage services. In 1978 Merrill Lynch had acquired United First Mortgage Corporation (UFM), a mortgage banker. And in early 1979 Merrill Lynch was in the midst of acquiring AMIC Corporation, a small mortgage insurance company in direct competition with CMI. As *Fortune* reported,

* In combination, these diverse activities hold some striking possibilities. Merrill Lynch already packages and markets mortgages through its registered representatives. . . . If all goes according to plan, the company could later this year be vertically integrated in a unique way. Assuming the AMIC acquisition goes through, Merrill Lynch will be able to guarantee mortgages. It could then originate mortgages through its realty brokerages, process and service them through UFM, insure them with AMIC, package them as pass-through or unit trusts, and market them through its army of registered representatives.[2](http://digitalbookshelf.southuniversity.edu/books/0072973102/content/id/ch91en02)

It was this vision of an integrated financial services organization that also excited Frank Randall. As he and Jim Dolan reviewed their position in early 1979, they were confident that they were in a unique position to build CMI into a much bigger and more diversified company. The mortgage insurance business gave them a solid financial base, with regional offices throughout the country. Northwest Equipment stood ready to provide the capital they would need for significant growth. They already had relationships with important lending institutions across the United States, and their marketing efforts had given them a solid reputation with important real estate brokers as well.

Thus Randall, in particular, felt that at least he had most of the ingredients to begin building that diversified “residential real estate financial services company” he had been dreaming about for so long. Furthermore, Randall’s reading of the banking, thrift, and real estate industries suggested that the time was ripe. In his view, the uncertainties in the financial and housing industries created rich opportunities for taking aggressive action, and the vision of Merrill Lynch “bulling” its way into the business was scaring realtors just enough for CMI to present a comforting and familiar alternative.

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## The Metropolitan Realty Network

Frank Randall spent most of the fall of 1978 actively searching for acquisition opportunities. As part of his effort, he contacted David Osgood, who was the executive director of the Metropolitan Realty Network, a national association of independent real estate brokers. The association, commonly known as MetroNet, had been formed primarily as a communication vehicle so its members could refer home buyers moving from one city to another to a qualified broker in the new location.

Randall discovered that Osgood was somewhat concerned about MetroNet’s long-term health and viability. Though MetroNet included over 13,000 real estate agencies, it was losing some members to national franchise chains, and Osgood was feeling increasing pressures to strengthen the association by providing more services to member firms. Yet the entrepreneurial independence of MetroNet’s members made Osgood’s task particularly difficult. He had found it almost impossible to get them to agree on what they wanted him to do.

One service that the MetroNet brokers *were* agreed on developing was the employee relocation business. Corporate contracts to handle transferred employees were especially attractive to the brokers because the contracts virtually guaranteed repeat business in the local area, and they also led to intercity referrals that almost always resulted in a home sale.

MetroNet brokers were also resentful of how Merrill Lynch Relocation Management and other relocation services companies were getting a larger and larger share of “their” referral fees. Osgood told Randall that he had already set up a committee of MetroNet brokers to look into how the association could develop a corporate relocation and third-party equity capability of its own.[3](http://digitalbookshelf.southuniversity.edu/books/0072973102/content/id/ch91en03) Osgood mentioned that their only effort to date was an independent firm in Chicago named Corporate Transfer Services, Inc. (CTS), that had been started by Elliott Burr, a prominent Chicago broker and a MetroNet director. CTS had been formed with the intention of working with MetroNet brokers, but so far it had remained relatively small and had not met MetroNet’s expectations.

As Randall explained to Osgood what kinds of activities CMI engaged in to help lenders and increase the volume of home sales, Osgood suddenly exclaimed, “That’s exactly what *we’re* trying to do!” The two men ended their initial meeting convinced that some kind of working relationship between CMI and MetroNet could have major benefits for both organizations. Osgood invited Randall to attend the next meeting of MetroNet’s Third-Party Equity Committee, scheduled for March 1. “Let’s explore what we can do for each other,” said Osgood. “You’re on,” concluded Randall.

## The Third-Party Equity Business

Randall’s discussion with David Osgood had opened his eyes to the third-party equity business, and he and Jim Dolan spent most of their time in preparation for the March 1 committee meeting steeped in industry studies and pro forma income statements.

They quickly discovered that the employee relocation services industry was highly competitive, though its future looked bright. Corporate transfers of key employees appeared to be an ingrained practice that showed no signs of letting up in the foreseeable future. Merrill Lynch Relocation Management was one of the two largest firms in the industry; most of the prominent relocation companies were well-funded subsidiaries of large, well-known corporations. [Exhibit 1](http://digitalbookshelf.southuniversity.edu/books/0072973102/content/id/ch91fig01) contains Jim Dolan’s tabulation of the seven major relocation firms, along with his estimates of each company’s 1978 volume of home purchases.

Dolan also developed a pro forma income and expense statement for a hypothetical firm handling 2,000 home purchases annually (see [Exhibit 2](http://digitalbookshelf.southuniversity.edu/books/0072973102/content/id/ch91fig02)). His calculations showed a potential 13.1 percent return on equity (ROE). Dolan then discovered that some companies achieved a much higher ROE by using a home purchase trust, a legal arrangement that made it possible to obtain enough bank financing to leverage a company’s equity base by as much as 10 to 1.

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Randall and Dolan were increasingly certain that they wanted to get CMI into the employee relocation services business. They saw it as a natural tie-in with CMI’s mortgage insurance operations—one that could exploit the same set of relationships that CMI already had with banks, realtors, savings and loans, and other companies involved in the development, construction, sale, and financing of residential real estate. The two men felt that real estate brokers had a critically important role in the process. Brokers were not only involved in the actual property transactions, but in addition they almost always had local contacts with corporations that could lead to the signing of employee relocation contracts. Equally important, from Randall’s and Dolan’s perspective, was their belief that a close relationship between CMI and the MetroNet brokers would also lead to significant sales of CMI’s mortgage insurance policies.

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The March 1 meeting with MetroNet’s Third-Party Equity Committee turned into an exploration of how CMI and MetroNet might help each other by stimulating both home sales and high-ratio mortgage loans. After several hours of discussion, Frank Randall proposed specifically that CMI build an operating company to handle the corporate relocation business jointly with the MetroNet brokers. As a quid pro quo, Randall suggested that the brokers could market CMI mortgage insurance to both potential home buyers and lending institutions.

The committee’s response to this idea was initially skeptical. Finally, however, they agreed to consider a more formal proposal at a later date. MetroNet’s board of directors was scheduled to meet on April 10; the Third-Party Equity Committee could review the proposal on April 9 and, if they approved, present it to the full board on the 10th.

As the committee meeting broke up, Randall and Dolan began talking with Elliott Burr and Thomas Winder, two of the four owners of Corporate Transfer Services, Inc. (CTS). Though Burr had been the principal founder of CTS, his primary business was a large real estate brokerage firm in north suburban Chicago that he operated in partnership with William Lehman, who was also a CTS stockholder.

The four men sat back down at the meeting table, and Randall mentioned that his primary interest was to learn more about how an employee relocation business operated. Burr offered to send him copies of contracts with corporate clients, sample financial statements, and so on. At one point during their discussion Burr mentioned the possibility of an acquisition. Randall asked, somewhat rhetorically, “How do you put a value on a company like this?” Burr responded almost immediately, “Funny you should ask. We’ve talked to an attorney and have put together this proposal.” Burr reached into his briefcase and pulled out a two-page document. He then proceeded to describe a complex set of terms involving the sale of an 80 percent interest in CTS, subject to guarantees concerning capitalization, lines of credit, data processing support, future distribution of profits and dividends, and more.

Randall backed off immediately, explaining that he needed to learn more about the nature of the business before he would seriously consider an acquisition. As Jim Dolan later recalled,

* I think they were expecting an offer right then and there. But it was very hard to understand what they really wanted; it was nothing we could actually work from. Besides that, the numbers they were thinking about were ridiculously high—over $5 million. We put the letter away and told them we didn’t want to get specific until after the April 10 meeting. And that’s the way we left it.

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## Preparation for the April 10 Meeting

During the next six weeks Randall and Dolan continued their investigations of the employee relocation industry and studied CTS much more closely.

One of their major questions was how much additional mortgage insurance the MetroNet brokers might be able to generate. Frank Randall had CMI’s marketing staff conduct a telephone survey of about 25 key MetroNet brokers. The survey suggested that most brokers were aware of mortgage insurance, although few of them were actively pushing it. All of those questioned expressed an interest in using CMI’s marketing programs, and were eager to learn more about CMI insurance.

By early May a fairly clear picture of CTS was emerging. The company had been founded in 1975; it had barely achieved a break-even profit level. Annual home purchases and sales had reached a level of almost 500 properties, and CTS had worked with about 65 MetroNet brokers and 35 corporate clients. Tom Winder was the general manager; he supervised a staff of about 25 customer representatives and clerical support staff. Conversations with David Osgood and several MetroNet brokers who had worked with CTS suggested that the company had made promises to MetroNet about developing a nationwide, well-financed, fully competitive organization. To date, however, those promises were largely unfulfilled. Osgood believed that CTS’s shortage of equity and, therefore, borrowing capacity, had severely limited its growth potential.

Jim Dolan obtained a copy of CTS’s December 1978 balance sheet that, in his mind, confirmed Osgood’s feelings. The company had a net worth of only $420,000. Three of the four stockholders (Elliott Burr, William Lehman, and Michael Kupchak) had invested an additional $2 million in the company—$1.3 million in short-term notes and $700,000 in bank loans that they had personally guaranteed. While CTS owned homes valued at $13.4 million, it also had additional bank loans and assumed mortgages totaling $9.8 million. Furthermore, the company had a highly uncertain earnings stream; Frank Randall believed the current business could tail off to almost nothing within six months.

**EXHIBIT 3: CTS Balance Sheet**

During late March both Randall and Dolan had a number of telephone conversations with Burr and Winder. Their discussions were wide ranging and quite open; the CTS partners struck Randall as being unusually candid. They seemed more than willing to share everything they knew about the business and their own company. On one occasion, Burr asked how much of CTS Randall wanted to buy and how Randall would feel about the present owners retaining a minority interest. Burr’s question led Randall and Dolan to conclude that in fact they wanted full ownership. They planned to build up the company’s equity base considerably and wanted to gain all the benefits of a larger, more profitable operation for CMI.

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In early April, Randall developed the formal proposal that he intended to present to MetroNet’s board of directors. The proposal committed CMI to enter negotiations to acquire CTS and to use CTS as a base for building a third-party equity company with a capitalization sufficient to support an annual home purchase capability of at least 2,000 units. In return, the proposal asked MetroNet to begin a program of actively supporting the use of CMI’s insurance on high-ratio loans.

**EXHIBIT 4: Letter of Intent**

Randall and Dolan met again with the Third-Party Equity Committee in New York on April 9 to preview the CMI proposal. The committee reacted favorably, and the next day MetroNet’s board of directors unanimously accepted the proposal after discussing it for less than 15 minutes.

**Formal Negotiations with Corporate Transfer Services**

On the afternoon of April 10, following the MetroNet board meeting, Randall and Dolan met again with Elliott Burr and Tom Winder. Now that CMI was formally committed to acquisition negotiations, Burr and Winder were eager to get specific and talk numbers. However, Randall and Dolan remained very cautious. When Burr expressed an interest in discussing a price, Randall replied, “We don’t know what you’re worth. But we’ll entertain any reasonable argument you want to make for why we should pay more than your net worth.” The meeting ended with a general agreement to firm things up by April 25. Later, reflecting on this session, Jim Dolan commented,

* Our letter of agreement committed us to having an operating company by July 12, so the clock was running on us. However, we know that after the April 10 board meeting they would be hard pressed not to be bought, and besides they were obviously pretty eager. But at that point in time we had not even met the other two stockholders; we suspected the high numbers were coming from them.

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**Further Assessment of CTS**

Even though the April 10 meeting had ended with an agreement to move ahead by April 25, it quickly became evident that a complete assessment of CTS and preparation of a formal offer would take more than two weeks. Other operating responsibilities prevented both Randall and Dolan from devoting as much time as they had intended to the acquisition, and the analysis process itself required more time than they had expected.

During the first week of May, Jim Dolan made a “reconnaissance” trip to Chicago. His stated purpose was to examine CTS’s books and talk with the company’s local bankers. He also scrutinized the office facilities, met and talked with several office employees, observed Tom Winder interacting with customers and subordinates, and generally assessed the company’s operations. Dolan spent most of his time with Winder, but he also had an opportunity to have dinner with William Lehman, another of CTS’s stockholders. Dolan returned to Philadelphia with a generally favorable set of impressions about the company’s operations and a much more concrete understanding of its financial situation. He reported to Randall, “They’re running a responsible organization in a basically sensible manner.” At the same time, however, Dolan also reported that CTS was under increasing pressure from its bankers to improve its financial performance.

Dolan’s trip also provided him with a much richer understanding of the four men who owned CTS: Elliott Burr, William Lehman (Burr’s real estate partner), Michael Kupchak (a private investor), and Tom Winder. Of these four, only Winder was actively involved in the day-to-day management of the company, although Elliott Burr stayed in very close touch with Winder and was significantly more involved than either Lehman or Kupchak. From their meetings and telephone conversations, Randall and Dolan pieced together the following pictures of the four men:

* **•***Elliott Burr,* in his middle 50s, had been the driving force behind Corporate Transfer Services. He was a classic real estate salesman—a warm, straightforward, friendly man who enthusiastically believed in what he was doing. An eternal optimist, he had been an early advocate of MetroNet’s getting into the employee relocation business. Burr knew the relocation business extremely well; he personally called on many of the large Chicago corporations to sell CTS’s services.Burr appeared to be very well off financially. Burr and Lehman Real Estate was one of the largest realty firms on Chicago’s North Shore, and Burr was held in high regard by local bankers. One banker had told Dolan, “Burr’s word is his bond.”
* **•***William Lehman,* Burr’s real estate partner, was in his mid-60s. He appeared to be much more of a financial adviser and investor than an operating manager. Lehman personally owned the shopping center where Burr and Lehman Real Estate was located, as well as the office building where CTS was leasing space.Dolan characterized Lehman as an “elder statesman—a true gentleman.” Dolan recalled that when he had had dinner with Lehman during his visit to Chicago, Lehman had kept the conversation on a personal level, repeatedly expressing concern about Dolan’s plane reservations, hotel accommodations, and so on. He had hardly mentioned CTS during the entire dinner.
* **•***Michael Kupchak* was the third principal stockholder. Kupchak, about 50, had been a mortgage banker in Chicago for a number of years. Recently, however, he had left the bank to manage his own investments on a full-time basis.Dolan met Kupchak briefly during his Chicago visit, and characterized him as a “bulldog”—an aggressive, ambitious man much more interested in financial transactions than in the nature of the business. He had apparently thought Dolan was coming to Chicago to make a firm offer and had been irritated that one had not been forthcoming. Frank Randall had not yet met Kupchak face-to-face, although they had talked once by telephone.
* **•***Thomas Winder,* 44, had spent most of his career in real estate–related businesses. At one time he had worked for a construction company, and then he had joined the mortgage bank where Michael Kupchak worked.Kupchak had actually brought Winder into CTS as its general manager, and the three original partners had offered him 25 percent ownership in the company as part of his compensation package.Winder was not only CTS’s general manager, but its lead salesperson as well. He called on prospective corporate clients all over the country, and he worked closely with MetroNet. That activity primarily involved appearing at association-sponsored seminars to inform member brokers about CTS and its services.

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It was obvious to Jim Dolan that CTS had become an important source of real estate sales commissions for the Burr and Lehman partnership. Most of CTS’s clients were in the Chicago area, and a large portion of the real estate transactions generated by CTS were being handled by Burr and Lehman Real Estate.

Dolan also inferred that the three senior partners—Burr, Lehman, and Kupchak—were close friends socially as well as professionally. The men clearly respected each other and valued each other’s opinions. On one occasion Burr had told Dolan, “It’s because of Bill Lehman that I have what I have today. I can always trust his word.” Tom Winder was also woven into the relationship, but he was apparently not as closely involved as the other three. Randall and Dolan both sensed that Elliott Burr was the unofficial spokesman of the group. “I have the impression he can speak for all of them,” commented Dolan.

In late April, Randall obtained a copy of a consultant’s report on the employee relocation industry that had been commissioned by MetroNet’s Third-Party Equity Committee. The report estimated that there were more than 500,000 homeowner/employees transferred annually, generating over 1 million home purchases and sales. However, fewer than 55,000 of these transfers were currently being handled by relocation services companies. Dolan’s own analysis had projected a 10 to 15 percent annual growth rate in the use of relocation companies, leading to industry volume estimates of 60,000 in 1979, 67,000 in 1980, and 75,000 by 1981. The consultant’s report stressed that success in the relocation business depended on a company’s ability to provide services to its corporate clients at lower cost than the clients could do it themselves. In addition, profitability depended on a company’s ability to turn over its inventory of homes quickly and at reasonable prices. Dolan’s own financial projections showed a potential return on equity of over 30 percent by 1983, assuming only an 8 percent share of the market. And that return did not include any incremental profits resulting from new sales of CMI mortgage insurance policies generated by MetroNet brokers. Randall in particular was confident that the close ties between CMI and MetroNet would result in at least 5,000 new mortgage insurance policies annually—a volume that could add over $400,000 in after-tax profits to CMI’s basic business.

On May 10, Randall and Dolan attended a Northwest Equipment Corporation financial review meeting in Minneapolis. Prior to their trip west Randall had prepared a detailed analysis of the CTS acquisition and the employee relocation industry. The analysis, in the form of a proposal, served as documentation for a formal request to Northwest for a capital expenditure of $9 million. Randall had decided that he was willing to pay up to $600,000 more than the $420,000 book value of CTS’s net worth; the remaining $8 million would constitute the initial equity base required to build CTS into a viable company. The financial review meeting evolved into a lengthy critique of the acquisition proposal. Northwest’s corporate staff was initially quite skeptical of the financial projections, but Randall and Dolan argued that the risks were relatively low (the homes could always be sold) and the potential payoffs, both economic and strategic, were enormous. Finally, after an extended debate, the request was approved.

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**Formal Negotiations with CTS**

When Randall and Dolan returned from Minneapolis, they felt it was finally time to proceed in earnest with the acquisition negotiations. Randall sensed that at present CTS was limping along to no one’s satisfaction—including Elliott Burr’s. The company was sucking up much more of Burr’s time and energy than he wanted to give it, and its inability to fulfill MetroNet’s expectations was beginning to be an embarrassment for Burr personally.

In spite of these problems, Randall remained interested in completing the acquisition. Buying CTS would get CMI into the relocation business quickly, would provide them with immediate licensing and other legal documentation in 38 states, and would get them an experienced operations manager in Tom Winder. More important, Randall knew that Elliott Burr was an important and respected MetroNet broker, and buying CTS would provide an effective, influential entry into the MetroNet “old boy” network. Though he couldn’t put a number on the value of that network, Randall believed it was almost more important than the acquisition of CTS itself. Randall was convinced that the connection with the MetroNet brokers would enable him to run CTS at far lower cost than the established relocation companies, and he also expected to realize a significant increase in CMI’s mortgage insurance business.

**May 21, 1979**

Now, as Randall and Dolan sat in Randall’s office on May 21, they discussed the draft of a formal purchase offer that Dolan had prepared that morning.. The two men had decided to make an initial offer of $400,000 more than the $420,000 book value of CTS’s net worth, subject to a formal audit and adjustments depending on the final sales prices of all homes owned by CTS as of the formal purchase date. This opening bid was $200,000 below Randall’s ceiling price of $600,000 for the firm’s goodwill. The offer was for 100 percent of the ownership of the company. The $2 million in outstanding notes would pass through to the new company owned by Randall and Dolan. The offer also included a statement of intent to retain Tom Winder as CTS’s general manager and to move the company to CMI’s home office in Philadelphia.

As Randall and Dolan reviewed their plans, it was clear that they were more concerned about how to conduct the face-to-face negotiations than with the formal terms themselves. In the telephone call he had just completed, Randall had told Elliott Burr only that they wanted to meet the other stockholders and review their current thinking. At one point during the conversation Jim Dolan commented,

* I really wonder how they’ll react to this offer. We’ve been putting them off for so long now that I’m not sure how they feel about us anymore. And our offer is so much less than they’re looking for.

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Randall replied,

* I know that—but I have my ceiling. It seems to me the real question now is what kind of bargaining stance we should take, and how to carry it out. What do you think they are expecting?