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## Competitive Advantages For Family Offices In **Direct** Acquisitions of Private Companies

An alternative to investing in private equity

**In a competition** to acquire private middle market companies, private equity (PE) funds can seem like an insurmountable opponent, with near-unlimited resources and an engine of investment bankers, lawyers and diligence teams driving the deal forward. However, family offices can triumph over PE far more often than one might expect, and their unique qualities may give them a competitive advantage that's attractive to sellers. Let's explore ways family offices can outperform in the race for private company acquisitions.

### Historical Context

As advisors to both family offices and middle market companies seeking to be acquired, we've seen a significant increase over the past handful of years in the frequency with which family offices are seeking to make direct investments in private companies as opposed to doing it indirectly through investing in PE and venture capital (VC) funds.<sup>1</sup> Families are taking more risks than with a pooled vehicle, in exchange for more control, the hope of better returns and lower fees.<sup>2</sup> Before that period, investment bankers and other mergers and acquisitions (M&A) professionals would typically exclude family offices from the pool of parties to whom they would shop their clients seeking to be sold. Family offices weren't viewed as serious or experienced buyers and didn't have enough capital to pay an appropriate valuation or were otherwise unlikely to be competitive in an auction-type environment against PE and VC funds.

For sellers and M&A community professionals, the certainty of closing is at a premium, and acquisition by a family office seemed risky.

To combat this, family offices banded together (both informally and formally) to share the limited opportunities they were presented with and pool resources to pay a compelling price.<sup>3</sup> While more successful than going at it alone, this approach didn't result in many victories for the family offices.

Family offices didn't give up. Instead, they changed strategy. Many added infrastructure to their offices and further professionalized the business of managing the family's wealth and deploying the family's capital by bringing in former investment bankers and PE professionals to lead these efforts.<sup>4</sup> These individuals were already well networked in M&A organizations and among potential referral sources. As a result, family offices started being shown more potential deals. This allowed them to be more selective in the companies they sought to acquire and, for this small group of targets, to take advantage of their strengths to be selected as the buyer. The future is likely to be even better than the past for family offices, especially for those able to understand and communicate which strengths best resonate with sellers.

### M&A Process

In a typical M&A process, an investment banker or trusted advisor (such as an attorney, accountant or financial advisor) compiles a list of parties they think might be interested in buying a target company. After an informal outreach and sharing some high level financial data, a pool of active participants in the process is created. Participants are encouraged to submit an indication of interest that sets forth a range of valuation and certain assumptions to justify such price. From that group, a handful will be



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invited to the second stage of the process, in which additional due diligence is performed, meetings with sellers are held and formal letters of intent are submitted. In the last step of the process, the letters of intent are evaluated relative to several criteria, most of which are negotiated before the eventual buyer is selected.

Examples of such criteria include:

- Structure for transaction and related impact on taxation, regulatory approvals and third-party consents.
- Valuation, type(s) of consideration (for example, cash, stock or promissory note), timing of payment (that is, at closing or subsequent) and conditions to receipt of such payment (for example, earned based on financial results or operating metrics).
- Indemnity-related items such as how long a period representations and warranties survive, the type and amount of indemnity “basket,” the size of the indemnity “cap” and whether representation or warranty insurance is being obtained to provide some or all of the resources to provide such indemnity (as opposed to holding monies back or placing a portion of the purchase price into an escrow account).
- Terms of employment agreements and non-compete covenants.
- Conditions for closing, the most significant of which is whether obtaining financing is included.
- Cultural fit for the organization.
- Strategic opportunity in the larger industry landscape.
- General “likability.”

Each seller weighs these and other criteria differently. Some want the highest valuation. Others care more about how long they must sit on the sidelines under their non-compete covenant. In our experience, most sellers view those items and the risk/indemnity criteria as being the highest priorities. Many, though, view the cultural fit, strategic opportunity and likability as the second most important tier of criteria. In our experience, as long as the purchase price is within the range of the top couple of offers, family offices hold a significant competitive advantage in this second tier.

## Competitive Advantages

If a seller is being paid in equity or retaining a portion of the company after the closing, they’re usually motivated by how much money they can make down the road when that equity subsequently gets sold. As such, they’re trying to assess which buyer has the best chance to grow the company’s profitability and fetch the highest price when they resell the company one day. The “second bite at the apple” is influenced by the expertise of the interim caretaker and the length of time available to implement their strategy.

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Founders and senior members of a family office often have unique industry knowledge and connections to draw on that can quickly improve a target company’s performance. This is especially the case when they have expertise in a certain sector and research or analytical capabilities.<sup>5</sup> Vendors, suppliers, distributors and customers of the target company may already know their reputation and values. Some even have a history of growing and selling companies in this industry, and a strategy used successfully in the past may be viewed as likely to work in the future. PE funds may own companies in the same industry as the target company, but most don’t have their own operational expertise. As a result, family offices tend to be viewed as being well-skilled in identifying and executing strategic opportunities in the larger industry landscape.

Family offices typically have no restrictions on how long they can own a target company before reselling it. Whereas a PE or VC fund has a limited period contractually to liquidate their investment in a private company, and an even shorter amount of time if they hope to be successful in raising their next fund, a family office can take a longer, strategic view.<sup>6</sup> Additionally, because they have no



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contractually mandated period in which they need to liquidate the investment, family offices don't need to obtain contractual rights to force the founder/seller to repurchase their equity or to sell the whole company after a couple of years. This further aligns interests between the parties and reduces the chances of needing to sell at an inopportune time. A founder may be more confident in a positive outcome if there's more time to achieve it.

Equally important, a seller will want to understand how the proceeds of an eventual resale will be distributed. Family offices have far greater flexibility in structuring deals than PE and VC funds. Because they don't have limited partners, they don't need to generate any amount of return on investment. As a result, they can hold common equity instead of preferred. Being on equal footing is highly attractive to the seller because it increases the percentage of sale proceeds received. For instance, most preferred equity accrues a preferred return each year (for example, 8% of the capital committed or a payment-in-kind). On an exit, all the PE fund's capital, plus unpaid preferred return, is paid before any of the common equity holders see any money. If they take preferred equity, family offices have the flexibility to accept a lower than market rate preferred return (for example, less than 8%) and rarely use a payment-in-kind strategy. If they get common equity, then there would be no preferred return, and the founder gets paid pro rata contemporaneously with the family office getting paid. Finally, family offices rarely charge the company an oversight or management fee to fund their operations (as PE funds typically do). This eliminates a drain on cash flow and increases the company's profitability for everyone's benefit. All these aspects result in significantly more money for the seller than they otherwise would receive.

Family offices are often not as reliant on debt as funds are but can use it as a resource when desirable. Thus, they may have a higher certainty of closing. PE funds typically use a significant amount of debt to finance a purchase because interest rates are often less than the return they promised their limited partners. Family offices don't have third-party limited partners primarily focused on performance; they have family members with varying needs and

goals. While certainly investment performance is important, other factors such as cash flow, long-term strategy, family governance, tax planning and succession provide more flexibility to consider the "value" of a potential acquisition. Family offices can enjoy strategic growth with consistent base hits instead of needing to swing for the fences, which provides them with a significantly larger pool of potential investment or purchase opportunities. This flexibility offers sellers and companies seeking strategic investment and partnership a new group of suitors in which to find a match.

General "likability" and cultural fit are two areas where family offices shine the brightest. This is because they have similar backgrounds and experiences. They often know many of the same people, have attended the same trade shows and worked with the same suppliers/vendors. This provides credibility and familiarity and fosters commonality of the working environment. At times, there can be a preference for doing business with someone from "Main Street" instead of "Wall Street." Family offices tend to be more familiar with and sensitive to a seller's estate-planning efforts and goals as well as non-financial concerns, such as their reputation in the industry and legacy. Stakeholders and principals of the family office intimately understand the entanglement of private wealth and the business and personal needs so that they can offer a seller a more unique perspective than a PE fund or its investment banker. In this sense, family offices have a clear advantage in being able to hone in on key concerns because they've been in the seller's shoes.

### Succession Planning

Sophisticated, professional family offices are using their unique characteristics to attract potential targets and referral sources and enjoying success with increased profitability of the target company or the appreciation in value obtained over a longer hold period. It's also getting them better results beyond the balance sheet and significantly benefits the family itself.

Advisors pay a great deal of attention to advising family offices and other closely held business investors in what's often referred to as "pre-liquidity

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transaction planning,” though advisors will differ in opinion about how “pre-liquidity” transaction the planning needs to have occurred. The structures used often involve a variety of different irrevocable trusts and charitable vehicles designed to meet at least some of the *selling* party’s goals for tax-efficient wealth transfer and income tax structuring, but similar principles apply to pre-acquisition transaction planning for the acquiring family office investor(s) in anticipation of future growth and/or eventual sale of the target investment.

The most successful of these structures are implemented long before the courting of the company begins, and the decisions to engage in succession planning have been made at a time unconnected to the potential liquidity planning. Commonly, planners will focus on the need to have separation from a liquidity event because of valuation positions being asserted in the wealth transfer structure. The hope is to transfer the interest at a lower value (whether as a whole and/or considering valuation adjustments due to lack of control and/or lack of marketability, for example). The closer to a liquidity event, when the market has arguably set the fair market value between a willing buyer and a willing seller, the more difficult it is to sustain in an appraisal report an alternate position on the value of the interest transferred within the family.

Aside from this valuation issue, there are more practical potential roadblocks to navigate in wealth transfer planning in parallel with a potential liquidity event. First, the seller may feel pulled in multiple directions. The goal becomes a deal closing, and structures that slow down the process or complicate the picture may not be the strategic goal of all advisors collaborating with the seller. Second, the seller has *a lot* to think about, and expecting them to simultaneously think about what can be viewed as an entirely separate complex transaction within the family can prove too much, given the pace of a deal. For tax and non-tax reasons, many of the most successful and elegant wealth transfer solutions have been put into place long ago, and the exit is the culmination of that foundational planning, no different than the sale of the company itself being the culmination of the

foundation and development of the business into a successful desirable target for acquisition.

Family offices and private company sellers have a common ground they might not always realize: They can understand the desire for strategic succession planning in the value from a liquidity event, the growth potential of the acquisition and broader succession opportunities presented by the transaction. This commonality presents opportunities both for the seller, who may have more flexibility for implementing pre- and post-liquidity planning, and for the family office to acquire strategically in line with their family’s overall governance and succession goals.

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Common estate-planning principles apply in the family office’s acquisition of the private company, transferring assets to a younger generation while at a low(er) value or acquiring new ventures as a co-invest or entirely at the level of the younger generation in a manner that the wealth grows outside of the senior generation’s estate. For example, when forming the entity used to acquire the investment or portfolio company, family members (or trusts or other vehicles for their benefit) can be brought in as participants from the outset. This can be accomplished through capital already seeded into existing irrevocable trust structures or through new entities and trusts established for this purpose, but families should consider the other capital responsibilities the acquiring entity will have and whether the trusts and/or family entities will have appropriate sources of capital or access to financing, if necessary. The family office can thoughtfully consider how to




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address the management and control of the new family investment. Non-voting equity can be used, as can a manager-managed limited liability company to maintain management with the family office founder or another appropriate family member or committee. In essence, the family develops its own tailored approach, rather than being limited to an LP interest in a PE fund's structure.

### Looking Ahead

PE and VC funds continue to thrive and position themselves as market leaders. In 2024, they rebounded in dealmaking after two years of decline, with a notable increase in the value and number of large PE deals. In terms of value, exit activity started to whirl again as well, especially fund-to-fund exits. Significant amounts of “dry powder” (the amount of capital committed but not yet deployed) remain. On top of that, fundraising for future deals continues to be strong. However, deals in excess of \$500 million in the technology and health care industries are largely behind these numbers.<sup>7</sup> That leaves open a lot of opportunity for family offices, particularly in the middle market (which many define as deals below \$250 million).

Meanwhile, the recent growth of family offices has been staggering. According to the Deloitte Family Office Insights, there were an estimated 8,030 single family offices worldwide in 2024, up from 6,130 in 2019.<sup>8</sup> This number is projected to grow to more than 10,720 by 2030, a remarkable 75% increase.<sup>9</sup> In 2024, approximately 3,180 of the family offices were in North America. The North America region is expected to undergo the greatest growth, with its number of family offices expected to nearly double from 2,210 in 2019 to 4,190 in 2030—a 90% increase.<sup>10</sup>

Looking forward, it appears that in the middle market company deal space, family offices will have greater and greater opportunities. If they continue to professionalize and call on their unique strengths, we believe they'll become the successful bidder for an even greater percentage of the available deals. When interests are aligned in a meaningful way, it benefits both the family members behind the family offices and the stakeholders of the target companies. That's a competitive advantage for everyone.<sup>11</sup> 

### Endnotes

1. Family office investment in private equity and venture capital funds continues to be a sizable portion of their portfolio. Pursuant to the 2024 “PWC Global Family Office Deals Study” (PWC Study), since 2014, family offices have shifted their investment focus away from real estate and funds and towards direct investments (that is, start-ups and mergers and acquisitions). See [www.pwc.com/gx/en/services/family-business/family-office/family-office-deals-study.html](http://www.pwc.com/gx/en/services/family-business/family-office/family-office-deals-study.html).
2. Canadian Family Offices (May 8, 2025), [https://canadianfamilyoffices.com/special-reports/pooling-money-helps-families-past-multi-million-minimums-for-high-quality-alts/?utm\\_source=linkedin&utm\\_medium=social](https://canadianfamilyoffices.com/special-reports/pooling-money-helps-families-past-multi-million-minimums-for-high-quality-alts/?utm_source=linkedin&utm_medium=social).
3. Pursuant to the PWC Study, *supra* note 1, “club deals” have recently accounted for 60% of family office investments by volume. The study also identified some interesting trends for the second and third generations from the family founder. They tend to like to invest together with others, possibly with contacts from their university days, which helps explain the increase in club deals. This generation also sees itself as committed to a sustainable future, which helps to explain the rising interest in impact investing.
4. Deloitte Private's 2024 Family Office Insights Series—Global Edition, [www.deloitte.com/global/en/about/press-room/global-edition-explores-the-rapid-expansion-family-offices-and-ffers-vision-of-the-future-landscape.html](http://www.deloitte.com/global/en/about/press-room/global-edition-explores-the-rapid-expansion-family-offices-and-ffers-vision-of-the-future-landscape.html).
5. See *supra* note 2.
6. Per the PWC Study, *supra* note 1, “there's also an interesting contrast with private equity firms, whose balance of investments and exits is significantly higher than for family offices—reflecting the fact that family offices are under less pressure to reinvest the proceeds from exits and are able to take more time in assessing future investment opportunities.”
7. McKinsey & Company, “Global Private Markets Report 2025: Braced for shifting weather,” [www.mckinsey.com/industries/private-capital/our-insights/global-private-markets-report](http://www.mckinsey.com/industries/private-capital/our-insights/global-private-markets-report).
8. See *supra* note 4.
9. *Ibid.*
10. *Ibid.*
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