
CORDIS INSTITUTE

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The Preparation Gap in Early 2026

Post-LOI Adjustment Patterns in
Lower-Middle-Market Transactions

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NAMED FINDING

“73% of lower-middle-market transactions include at least one post-LOI price adjustment, averaging 18% of enterprise value. Primary driver: information asymmetry, not market conditions.”

This finding is the foundation of the Preparation Gap framework developed in this working paper.

AT A GLANCE

01

QoE Restatements

Appear in 45% of transactions. Average impact: 8–12% of enterprise value. These are not errors. They are the buyer's underwriting model applying a different lens to the same financials.

02

Customer Concentration

Above 40% triggers a mechanical 0.8x–1.2x EBITDA discount in PE underwriting models before the first meeting. Structural, not negotiable.

03

The Upstream Window

12 to 24 months before banker engagement is the only period in which preparation materially changes outcomes. Once the process begins, the buyer's model is already running.

1. Introduction

Across forty-seven closed transactions in the lower-middle-market over the past three years, we have observed a pattern so consistent that it no longer surprises us. A founder enters the LOI phase confident in their enterprise value, having built a profitable business over fifteen or twenty years, and emerges sixty to ninety days later staring at a materially different number. The business did not change. The market did not shift. What happened was underwriting.

The lower-middle-market sits in a peculiar position entering the second quarter of 2026. Private equity firms hold over one trillion dollars in uninvested capital (PitchBook 2026). EBITDA multiples have stabilized near cyclical norms. Lenders, while cautious, have resumed financing acquisitions in the two-to-fifteen-million-dollar EBITDA band. By every conventional measure, sellers should be transacting at favorable terms. They are not. Transaction volume in 2025 fell 23% year-over-year (Axial 2025), and the deals that did close carried post-LOI adjustments at rates that would alarm any rational seller who understood them in advance.

The paradox demands explanation. Record capital seeking deployment. Stabilizing pricing. A generational cohort of founders approaching retirement. Yet fewer transactions close, and those that do frequently close at prices below the signed LOI. The variable that reconciles these facts is not macroeconomic. Rates matter, regulation matters, but neither accounts for the specific pattern we observe in post-LOI repricing. The missing variable is preparation quality, and its absence produces a measurable, structural cost.

We call this cost the Preparation Gap: the value delta attributable to information asymmetry between buyer underwriting models and founder transaction preparation. The gap is not new. What has changed is the sophistication of buyer-side diligence. Private equity firms operating in the lower-middle-market have adopted institutional underwriting practices that, five years ago, were reserved for upper-middle-market transactions. Quality of earnings analyses are now standard below ten million dollars of EBITDA. Customer concentration modeling has become mechanical. Revenue quality frameworks distinguish between recurring, repeating, and non-recurring revenue with actuarial precision. Founders preparing for exit without understanding these frameworks are walking into a negotiation where the other side holds instruments they cannot see.

This paper presents evidence that the Preparation Gap is structurally predictable, measurable, and addressable in the upstream window before a transaction formally begins. We draw on GF Data transaction benchmarks, PwC exit survey findings, SRS Acquiom deal terms data, and Cordis Institute practitioner analysis to demonstrate both the scope of the problem and the specific mechanisms through which value transfers from seller to buyer during post-LOI diligence.

2. Market Context: The LMM Transaction Environment in 2025

2.1 Volume and Velocity

Lower-middle-market transaction volume declined 23% in 2025 relative to 2024, marking the second consecutive year of contraction in the segment (Axial 2025). The decline was not uniform. Transactions involving businesses with EBITDA below three million dollars fell at roughly twice the rate of those between five and fifteen million, suggesting that buyer selectivity, not capital scarcity, drove the contraction. The IBBA Market Pulse survey for Q4 2025 confirmed this interpretation: broker respondents reported stable buyer inquiry volume alongside declining conversion from indication of interest to signed LOI (IBBA 2025).

Deal velocity slowed in parallel. Average time from LOI execution to close extended to 97 days in 2025, up from 81 days in 2023 (SRS Acquiom 2024). Extended timelines correlate with expanded diligence scope. Buyers are not taking longer because they are uncertain about market conditions. They are taking longer because they are examining more deeply, and what they find during that examination changes the economics.

2.2 The EBITDA Multiple Environment

GF Data reported an average completed-transaction multiple of 7.2x EBITDA for the lower-middle-market in Q4 2025 (GF Data 2025). The headline obscures significant dispersion. Strategic acquirers paid a median of 8.1x for businesses with demonstrable synergy potential. Private equity platform acquisitions clustered around 6.8x to 7.5x depending on sector and growth profile. Add-on acquisitions, which comprised approximately 72% of PE deal volume in 2025 (PitchBook 2026), transacted at 5.5x to 6.5x, reflecting both the smaller scale of targets and the mechanical leverage of the buy-and-build thesis.

Family offices represent a growing but often misunderstood buyer segment. Their multiples are difficult to benchmark because family offices are under no obligation to report transaction terms. Anecdotal evidence from practitioner networks suggests a range of 5.0x to 7.0x, with significant variance based on the family office's existing portfolio, operational capability, and return expectations. A family office making its first acquisition behaves differently from one executing its eighth.

The critical observation for sellers is that "market multiple" is not a single number. A founder whose advisor quotes 7.2x as the expected outcome has received a statistical average that may bear little resemblance to the offers their specific business will attract. Buyer type, deal structure, and diligence findings each shift the realized multiple, and the Preparation Gap amplifies all three sources of variance.

2.3 Deployment Pressure and Its Limits

The trillion-dollar overhang of uncommitted PE capital creates real but frequently overstated leverage for sellers (PitchBook 2026). Dry powder creates urgency at the fund level, where deployment timelines and management fees on committed capital generate pressure to transact. That urgency does not, however, override deal-level underwriting discipline. A PE firm under deployment pressure will look at more deals and move faster to LOI. It will not relax its diligence standards or accept unresolved risk at close. The wealth transfer of an estimated ten trillion dollars across founder-led businesses this decade (SBA 2024) ensures that no buyer needs to compromise on any single transaction. Supply, in aggregate, exceeds demand for prepared, well-positioned businesses, but the total supply of businesses at market includes a substantial share that are not prepared.

3. The Preparation Gap: Definition and Mechanism

3.1 Formal Definition

The Preparation Gap is the difference between the enterprise value a founder expects based on headline market multiples and the value a buyer's underwriting model produces after adjusting for identified risk factors. The gap is not a negotiating tactic. Buyers do not create it strategically, though they benefit from it structurally. The gap exists because sellers and buyers optimize for different variables, prepare on different timelines, and reference different frameworks.

Akerlof's foundational work on information asymmetry in markets (Akerlof 1970) established that quality uncertainty depresses transaction prices and volumes in predictable ways. The lower-middle-market exhibits a specific variant of this dynamic. Unlike Akerlof's used car market, the quality of a lower-middle-market business is not fixed. Preparation can materially alter the information set available to buyers, reducing uncertainty and narrowing the gap. The tragedy is temporal: most preparation occurs after the point at which it can influence outcomes.

3.2 Driver One: Divergent Optimization Targets

Founders optimize for enterprise value. They think in terms of revenue growth, margin expansion, and the headline multiple that the market will assign. Buyers optimize for risk-adjusted return. A private equity firm underwriting an acquisition models downside scenarios, customer attrition rates, key-person dependency, and capital expenditure requirements that the seller has deferred. These are not opposing interests in the zero-sum sense. They are fundamentally different analytical frameworks applied to the same asset.

The divergence becomes visible in Quality of Earnings (QoE) analysis. A founder presents adjusted EBITDA reflecting what they believe the business earns on a normalized basis. The buyer's QoE provider, working from the same financial data, produces a different number. The difference is not error. It reflects different assumptions about addback legitimacy, revenue sustainability, and expense normalization

(Gompers, Kaplan, and Mukharlyamov 2016). When these two numbers diverge by fifteen or twenty percent, the post-LOI adjustment follows mechanically.

3.3 Driver Two: Temporal Misalignment

Preparation follows a sequence. Financial statement cleanup, customer diversification, management team development, systems documentation, and legal housekeeping each require time measured in quarters, not weeks. The effective window for this work is twelve to twenty-four months before engaging a transaction advisor. We call this the upstream window.

The observed pattern is inverted. Most founders begin substantive preparation after engaging an investment banker or M&A; advisor, which typically occurs six to twelve months before a hoped-for close. At that point, the advisor's incentive is to bring the business to market quickly, not to delay for preparation that should have occurred earlier. The founder discovers diligence vulnerabilities during buyer examination, when the cost of those vulnerabilities is measured in direct price concessions rather than in the relatively modest cost of upstream remediation (Lajoux and Elson 2022).

3.4 Driver Three: Absence of a Buyer-Readiness Framework

No standardized assessment exists for determining whether a business is prepared for buyer-level scrutiny before it enters a transaction process. Founders rely on their CPA, their attorney, or their own judgment. Each of these sources has limitations. The CPA knows the tax returns but may not understand how a PE buyer will recast the financials. The attorney has handled the corporate governance but may not anticipate representations and warranties insurance requirements. The founder has built the business but has never sold one.

The absence of a common framework produces inconsistent preparation. Some founders arrive at market having addressed every likely diligence finding. Others arrive with material gaps they do not recognize as gaps. The buyer's diligence process functions as the de facto readiness assessment, and it occurs at the worst possible moment: after an LOI has set expectations, when every finding translates directly into a price or structure concession (Hansen 2020).

4. Post-LOI Adjustment Patterns

4.1 Prevalence and Magnitude

GF Data's 2025 analysis of completed lower-middle-market transactions reports that 73% experienced a material price adjustment between signed LOI and close (GF Data 2025). The average adjustment was 18% of the original stated enterprise value. Adjustments skewed negative, with seller-favorable adjustments occurring in fewer than 8% of cases and typically involving minor working capital true-ups

rather than substantive repricing.

PwC's exit survey data reinforces the picture from the seller's perspective: 76% of founders who completed a transaction in 2024-2025 reported dissatisfaction with the final outcome relative to initial expectations (PwC 2025). Dissatisfaction correlated most strongly not with the absolute price but with the delta between the LOI price and the closing price. Founders can absorb a lower-than-hoped offer. What they struggle to accept is watching the agreed price erode during diligence.

4.2 Adjustment Categories

Six categories account for the substantial majority of post-LOI adjustments. Each operates through a distinct mechanism, and each has a different degree of addressability in the upstream window.

Working Capital Disputes. These appear in approximately 60% of adjusted transactions. The mechanism is definitional: buyers and sellers disagree on what constitutes "normal" working capital at close. The average dispute magnitude is 3-5% of enterprise value. Working capital targets set in the LOI using trailing averages frequently diverge from the normalized figure the buyer's accountants calculate during diligence. Prevention requires establishing a defensible working capital analysis before the LOI is negotiated, not after.

Quality of Earnings Restatements. QoE adjustments appear in roughly 45% of transactions and carry an average impact of 8-12% of enterprise value. Restatements typically involve reclassification of owner addbacks, identification of non-recurring revenue, and normalization of related-party transactions. A founder who has operated with aggressive but defensible addbacks for tax purposes discovers that a buyer's QoE provider applies a materially more conservative standard.

Customer Concentration Discounts. When a single customer exceeds 40% of revenue, a mechanical discount appears in buyer models. We address this in detail in Section 5. Frequency: approximately 25% of LMM transactions. Magnitude: 0.8x to 1.2x EBITDA.

Management Dependency Discounts. Buyers identify key-person risk when the founder or a single executive controls critical customer relationships, operational knowledge, or technical capability. This appears in roughly 35% of transactions with a typical impact of 0.5x to 1.0x EBITDA, often expressed through earnout structures rather than direct price reduction. The SRS Acquiom 2024 study found that earnout usage increased to 64% of PE-backed LMM transactions, up from 47% in 2020, and management dependency was the most frequently cited reason (SRS Acquiom 2024).

Deferred Maintenance and Capital Expenditure. Buyers capitalize what sellers have expensed. Equipment approaching end-of-life, deferred facility maintenance, and technology debt appear as required near-term capital expenditures in buyer models, reducing the effective purchase price by the estimated remediation cost. Frequency: approximately 20% of transactions. Typical impact: 2-6% of enterprise

value.

Earnout Substitution. When a buyer cannot justify the LOI price based on current performance, the structure shifts. A portion of the purchase price moves from cash at close to an earnout tied to future performance metrics. The LOI headline number may remain unchanged, but the risk-adjusted present value of the consideration declines materially. Pepperdine's 2025 data shows that earnout components averaged 22% of total stated consideration in LMM PE transactions, up from 14% in 2021 (Pepperdine 2025).

4.3 Compounding Effects

These adjustments do not operate in isolation. A business with a QoE restatement and customer concentration frequently experiences a compounding effect where the reduced EBITDA figure is then multiplied by a reduced multiple. A 10% QoE haircut applied to a business simultaneously receiving a 1.0x multiple reduction for concentration produces an effective price reduction far exceeding either adjustment alone.

5. The Customer Concentration Case

The 40% threshold deserves standalone treatment because it demonstrates how buyer underwriting creates mechanical, binary pricing effects that founders rarely anticipate.

Private equity underwriting models typically flag customer concentration when a single customer accounts for more than 25% of revenue and apply systematic discounts above 40%. The threshold is not arbitrary. Lenders who finance acquisitions use concentration as a credit metric, and senior debt availability contracts sharply when a single customer exceeds 40% of revenue. Because PE buyers rely on leverage to generate returns, reduced debt availability directly reduces what they can pay (Humphery-Jenner 2012).

The discount operates as a multiple reduction of 0.8x to 1.2x EBITDA. Consider a worked example.

Business A generates \$3 million of adjusted EBITDA with its largest customer representing 45% of revenue. At a baseline multiple of 7.0x, the pre-adjustment enterprise value is \$21 million. A 1.0x concentration discount reduces the effective multiple to 6.0x, producing a revised value of \$18 million. The concentration costs the founder \$3 million.

Business B is identical in every respect except that its largest customer represents 35% of revenue. No mechanical discount applies. The business transacts at 7.0x, or \$21 million.

The difference between 45% and 35% concentration on a single customer is \$3 million in enterprise value. That gap dwarfs the cost of virtually any customer diversification effort the founder could have undertaken

in the upstream window. A two-year effort to develop three new customers generating \$450,000 in combined annual revenue would shift the ratio below the threshold and preserve the full multiple.

What makes this pattern frustrating for practitioners who advise founders is its visibility. Concentration is not hidden. Every founder knows who their largest customer is. The disconnect is that founders frame concentration as a business risk they have managed successfully for years, while buyers frame it as a structural vulnerability they must price. Both perspectives contain truth. Only one determines the transaction economics.

Founders also underestimate the secondary effects of concentration. A buyer who identifies a 45% concentration will demand expanded representations and warranties related to that customer, larger indemnity holdbacks, and potentially a customer-specific earnout. The direct multiple discount is the visible cost. The structural concessions are the hidden cost, and they compound.

6. The Upstream Window

6.1 Defining the Window

The upstream window is the twelve-to-twenty-four-month period before a founder engages a transaction advisor. During this window, the founder retains full operational control, faces no transaction timeline pressure, and can make changes that will be reflected in the financial statements buyers will examine. After an advisor is engaged, the calculus shifts. The advisor has a financial interest in bringing the business to market within a reasonable timeframe, and the founder has psychologically committed to a transaction. Changes made after engagement are either invisible to buyers because they do not appear in historical financials, or suspicious because they appear to have been made specifically to dress up the business for sale.

6.2 What the Window Can Address

Customer diversification moves slowly. Reducing a 45% concentration to 35% requires either growing non-concentrated revenue or developing new customer relationships, both of which take twelve to eighteen months to produce financials that a buyer will credit. But it works. A buyer reviewing three years of financial statements will see the trend and underwrite it.

Management team development can change the key-person risk profile within twelve months. Promoting a second-in-command, delegating customer relationships, and documenting operational processes each reduce the dependency discount. The founder who arrives at market with a functional management team that has operated independently for twelve months presents a fundamentally different risk profile than the founder who promises a transition plan.

Quality of earnings preparation, done proactively with a firm experienced in transaction-side QoE analysis, identifies the adjustments a buyer's accountants will make. The founder then has twelve to twenty-four months to either change the underlying practices or build a defensible narrative around each addback. A proactive QoE costs \$30,000 to \$75,000, a fraction of the value it protects.

Financial statement quality, systems documentation, legal entity cleanup, and environmental or regulatory compliance can all be addressed in the upstream window. Each requires time. None requires extraordinary expense relative to the transaction values at stake.

6.3 What the Window Cannot Address

Some characteristics resist remediation. Industry cyclicality cannot be diversified away in two years. Geographic concentration in a declining market will not reverse. A business model dependent on a single proprietary technology with no patent protection presents a risk that preparation can document but not eliminate.

The honest assessment of the upstream window is that it addresses roughly 60-70% of the value at risk in typical post-LOI adjustments. Working capital normalization, QoE alignment, customer diversification, and management development collectively account for the majority of the 18% average adjustment. The remaining adjustments, those driven by structural business characteristics rather than preparation deficiencies, require different strategies: buyer selection, deal structure, or in some cases, a candid conversation about whether the current moment is the right time to transact.

6.4 The Sequencing Problem

Most founders begin preparation after engaging a banker. The banker, operating under a standard engagement of six to twelve months with a success fee, is incentivized to move quickly to market. Preparation that should precede the engagement instead runs concurrent with marketing, creating conflicts (Bruner 2004). The banker wants to distribute the CIM next month. The founder's CPA has just begun cleaning up three years of financial statements. The attorney has identified a lease assignment that requires landlord consent. The management team has not been told a transaction is underway.

This sequencing failure is the single most common pattern we observe in transactions that experience significant post-LOI adjustment. The preparation was not absent. It was late. By the time the issues surface in buyer diligence, the only remedies available are price concessions and structural accommodations. The upstream window has closed, and no amount of negotiation skill can reopen it.

7. Implications for Practitioners

If you advise business owners, whether as their CPA, attorney, wealth advisor, or peer group chair, the Preparation Gap reframes the conversation you should be having today.

7.1 For CPAs and Financial Advisors

Your client's tax-optimized financial statements are a diligence liability. Every aggressive addback, every related-party transaction structured for tax efficiency, every expense run through the business that a buyer's QoE provider will strip out creates a gap between the EBITDA your client believes they have and the EBITDA a buyer will underwrite. You have the relationship and the credibility to initiate a proactive QoE conversation twelve to eighteen months before your client calls a banker. That conversation may be the highest-value advisory engagement you provide to that client, ever, relative to the fee involved. A \$50,000 proactive QoE that identifies \$2 million in at-risk enterprise value represents a return your client will not find in any other professional service.

7.2 For Exit and M&A; Attorneys

Your engagement typically begins when the LOI arrives for review. By then, the Preparation Gap has already determined the range of likely outcomes. Consider offering a pre-transaction readiness assessment as a standalone engagement, twelve months or more before a deal is contemplated. Review the corporate structure, the cap table, the intellectual property chain of title, the real estate arrangements, the employment agreements. Every issue you identify early is an issue that will not surface during buyer diligence as a price reduction justification. Your clients are accustomed to paying you for defensive work. Frame this as defense of enterprise value.

7.3 For M&A; Advisors and Investment Bankers

You already know that prepared businesses close faster, at higher multiples, with fewer retrades. The challenge is structural: your engagement model starts when the founder decides to sell, which is typically twelve to eighteen months too late for preparation to take full effect. Consider whether a preparation-phase advisory offering, priced differently from your transaction engagement, serves your pipeline. A founder you help prepare for two years before engagement is a founder whose deal will close on terms that reflect well on your tombstone and your track record.

7.4 For Peer Group Chairs and CEO Advisors

Your members trust you with conversations their professional advisors never hear. You know which of your members are thinking about an exit in the next three to five years. You also know that most of them believe preparation means "get my financials in order and call a banker." The Preparation Gap framework gives you a structured way to challenge that assumption. Ask the question directly: if a buyer examined your top-five customer concentration, your management depth chart, and your last three years of

financials under QoE standards, what would they find? The members who cannot answer that question confidently are the ones who need this conversation most, and they need it now, not when they are ready to sign a banker engagement letter.

8. Conclusion

The Preparation Gap, the value delta attributable to information asymmetry between buyer underwriting models and founder transaction preparation, is structurally predictable, measurable, and addressable in the upstream window. The 73% post-LOI adjustment rate is not a market inevitability. It is the aggregate consequence of thousands of individual founders entering the most consequential financial event of their careers without understanding the analytical framework the other side of the table will apply.

The data presented here should concern any practitioner who advises founder-led businesses approaching transition. An 18% average post-LOI adjustment, applied to a \$20 million enterprise value transaction, represents \$3.6 million. That figure is not theoretical. It is the measured central tendency across hundreds of completed transactions.

Subsequent papers in this series will examine related structural patterns. WP-002 addresses the False Summit pattern: the tendency for founders to interpret early buyer interest as validation of their asking price, leading to premature process launches that collapse during diligence. WP-003 will map buyer lane distribution, analyzing how different buyer types underwrite the same business and why seller preparation must account for buyer-type variance.

One fact persists across every data set we have examined: the founders who close at or above their LOI price are not luckier, better negotiators, or running superior businesses. They are better prepared. Preparation is the only variable in this equation that the founder fully controls.

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