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VacationSpot.com & Rent-A-Holiday: Negotiating a Trans-Atlantic Merger of Start-Ups in the New Economy

"I can't believe you asked us to come all the way to Seattle for this," exclaimed Karim Dhanani, one of the investors in Rent-A-Holiday. "This is not worth our time!!!" With that, the Rent-A-Holiday negotiating team stormed out of the VacationSpot.com offices bringing an abrupt end to the one-day merger negotiations. It was April 23, 1999.

Rent-A-Holiday (RAH) and VacationSpot.com (VS) were both on-line travel companies that focused on the independent leisure lodging segment of the travel market (i.e. villas and bed & breakfasts (B&Bs)) (see **Exhibit 1** for a description of the market). Both companies not only focused on the same space, but had started at around the same time (RAH in January 1997, VS in September 1997)—just in locations half-way around the world from each other: VS was a Seattle, Washington based company and RAH was a Brussels, Belgium-based company. The two companies had known of each other's existence for about one year before the two sides entered into formal merger negotiations in April 1999. As he stared at the door that had just closed behind Dhanani, Greg Slyngstad, co-founder and COO of VS, looked at Steve Murch, co-founder and CEO of VS.

> Steve, what in the world just happened? Did I see that right? The negotiations have been going really well; I mean this has been a *real* love-fest. We have just spent a couple of days discussing each company's vision and strategy and basically spent the time getting to know each other. Everything was going so smoothly up until the point we broached the subject of valuation. Both of us have recently completed a round of financing and all I did was say that we should use that as a basis for valuation: a 9:1 ratio based on a $27 million valuation for us and a $2 to $3 million valuation for them. It seems very logical but these guys just exploded. Do you think we have reached a point of no return?

At the same time Laurent Coppieters, co-founder and co-CEO of RAH looked at Dhanani as they were walking back to their hotel in downtown Seattle and said:

> Karim, these guys are proposing a valuation of our company that is completely unfair. Rent-a-Holiday is worth more than that. I don't know where these guys learned to value companies. It's a pity, though; these two days of face-to-face meetings went well. After we spent all that time looking for fit, I think we really

Dean's Fellow William J. Coughlin (MBA '99) prepared this case under the supervision of Professor Walter Kuemmerle as the basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation.

seemed to see a lot of advantages in a merger. I just can't believe this is falling apart.
I guess we will be back in Brussels sooner than planned.

As dusk approached on this rainy day in Seattle, both companies were left trying to figure out what had just happened and what each should do next. Both sides were basically in the same quandary. Was this the end of the negotiations or was this a temporary set back? Was this just a cultural misunderstanding or was this a fundamental problem? Was there any common ground possible on the valuation front and how could the negotiations be restarted? There was a plane for Brussels leaving Seattle at noon the next day. "Should we take that plane?" Coppieters wondered. "Or should we give it one more day?"

Independent Leisure Lodging: A Fragmented Segment of a Large Market

By 1999, leisure travel was a very large market with an estimated worldwide size of over $3 trillion.[1] The market comprised anything from air travel and car rentals to hotel reservations and package vacations. Moreover, the market was expected to offer tremendous growth opportunities for internet-based companies (See **Exhibit 1**). Forrester Research estimated that more than 8 million trips were booked online in 1998 generating over $3.1 billion in revenues. By 2003, Forrester estimated that consumers would book 65.5 million leisure trips online, generating $29.5 billion in revenues.[2]

Part of that larger market was the independent leisure travel lodging market. This broad market segment included condominiums, homes, ski cabins, chalets, villas, and timeshare property units and was estimated to have generated over $126 billion in revenues in 1998, but was quite fragmented and not well served by the existing reservation networks. The "traditional" channels—such as travel agents and tour planners—poorly covered these types of properties. Information was hard to find primarily because travel agents did not list the properties in any kind of computerized reservation system (CRS). CRS's, such as Sabre and Worldspan, were built primarily with large travel suppliers (airlines and chain hotels) in mind. Due to the ease of electronic reservation via CRS, consumers and travel agents chose to focus on selling lodging from the larger, less fragmented hotel chains and spent the rest of their time selling airline tickets and car rentals.

In addition, the independent leisure lodging segment was poorly marketed. There was no good source for print items on these properties (like brochures) and the owner, property manager, or rental agent was often unsophisticated. Marketing generally consisted of putting an advertisement in the local newspaper in the hopes that customers would see it. This lack of marketing sophistication was often due to the principal motives of the owner: Many independent leisure properties were purchased not as investments but for other reasons, such as weekend get-away destinations for the owners. This led to inconsistent pricing and massive under-utilization of the assets: estimates on average yearly vacancy rates were around 80% for these types of properties.

Yet there was considerable consumer appeal for this segment, particularly for the vast baby boomer leisure travel segment. Vacation rentals such as villas and ski condos came with more room, more amenities, and lower cost than any other lodging segment. Americans took 33 million ski trips each year, with over half of the overnight stays using condos or cabins instead of hotels. And business travelers used to the standard fare at chain hotels increasingly found unique getaways such as inns and B&B's far more enjoyable for their vacation.

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1 VacationSpot.com estimate.

2 Source: Forrester Research, *Online Leisure Travel Report*, September 1998.

At the beginning of 1999, there were several companies looking to take advantage of this situation by offering online services for this segment. Steve Murch (HBS '91), co-founder and CEO of VacationSpot.com, commented on the nature of the online independent leisure lodging market.

> There were several sites that addressed the segment, but most of the web sites were similar to online classified advertisements, offering a few lines of text and perhaps a picture. Moreover, most of these sites had relatively unsophisticated search functions and very little marketing support. For example, nearly all the sites allowed you to browse via a simple hierarchy but none let you search by amenities, price, availability, or style. Even fewer web sites offered real-time online reservation capabilities and those that did, like WorldRes, really did not focus on the villa, condo, and B&B segment; they targeted the hotel chains, just like the online travel agents like Travelocity and Expedia did.

Given the fragmented and unsophisticated nature of the industry, the founders of both VS and RAH felt that this was a tremendous opportunity for their respective companies. By April 1999 no other player was as far along in their development as VS and RAH.

VacationSpot.com History: Growing from Seattle

The Genesis of VacationSpot.com: A Honeymoon

After graduating from Carnegie Mellon University with a degree in Computer Science, Murch spent three years at Bell Communications Research (Bellcore) working with the large Baby Bells on ISDN research. (See **Exhibit 15** for the biographies of VS founders). Bellcore sent Murch to Stanford University for a Masters in Computer Science in 1987. In 1989, Murch left Bellcore and went to HBS, where he spent his summer working at the consulting firm Booz, Allen & Hamilton. After graduating as a Baker Scholar in 1991, while seeing most of his section choose consulting or investment banking jobs, Murch decided to join Microsoft, which was just beginning to ship Windows 3.0. Murch described his decision:

> While at HBS, I really wanted to start a company. I had worked on a business plan during my second year and had even received funding for it. But in the final lecture of his class, one of the professors gave a lecture that changed my thinking. He suggested that the best thing to do would be to pick an industry you are interested in and work for a moderately sized, rapidly growing company. From there you learn the ropes of your industry and eventually move on. The industry in which I was interested was this new phenomenon called interactive software and services. In fact, it was not a real industry yet, but I knew from my work at Bellcore that it could be huge. I chose to join Microsoft because at the time, it *was* a moderately sized rapidly growing company that focused at least somewhat on my industry.

Murch joined Microsoft and worked in several positions, including product manager for relational database products such as Microsoft Access and FoxPro, and later, he started the Internet Gaming Zone area within Microsoft. By 1999 this had become the largest games site on the Internet with over 10 million members. Murch had the VacationSpot idea when he was planning his honeymoon with his fiancé to the Tuscany region of Italy in 1996. Murch originally wanted to get a small villa for the trip but was unable to find one available, so he booked a hotel instead. When he arrived in Tuscany, he was shocked to see the vacancy rates of villas there, so he decided to do some investigating and found the segment to be a great opportunity. During his stint in the Consumer

Division at Microsoft, Murch met Slyngstad, who was then head of Expedia (an online travel service that Slyngstad changed from a CD-ROM product into an Internet site) and was formerly Group Program Manager of the Word group. After Murch had written a draft business plan, he turned to the retired Slyngstad for advice on the idea. Murch described his activities:

> The motivation of me joining Microsoft was to work with a small team of creative people who was trying to change the world. But over time the percentage of my time spent on doing that stuff decreased dramatically and I began to feel I was working at a *really* large company. Microsoft is the greatest 30,000+-person company anyone could work for, but it is still a 30,000+-person company. I wanted to start a company and a family but ideally a company first and a family later. That is why I jumped at the VacationSpot opportunity when I discovered it. It seemed like a perfect fit with the Internet: it was large enough to build a nice business but not so large as to attract immediate interest from established firms. Also, a reservation is a perfect virtual product to deliver. After working at Microsoft, I knew that Expedia and online offerings like it did not have enough time or resources to focus on the segment. They had to cater to the airlines and car rental companies and had barely enough time to seek out hotel chains to round out their product offering; there was no time for B&Bs. Yet it was still a $100 billion segment of a $3 trillion market where the average transaction size of $1,500-plus was high enough to make it worth our while.
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> So I wrote a pretty bad business plan at Microsoft at nights and weekends, and I sought out Greg, who was the guy who had sold Bill Gates on online travel while he was general manager of Expedia. When I asked Greg for his comments he said that he had two. His first comment was that he thought it was a great opportunity, but it would be perfect if I got an online, real time reservation system in place. His second comment was more of a question: Was I looking for a partner?

The Early Years at VacationSpot.com: Acquiring Technology and Property Inventory

Murch and Slyngstad started VacationSpot.com in September 1997 with a three pronged strategy. They wanted to have a comprehensive property offering, a superior reservation technology, and a strong distribution system. After using angel financing and their own money to get things started, they approached Microsoft in April 1998 for their first deal, but it wasn't for money. "We knew that asking Microsoft for cash would be a lengthy process," recalled Murch, "so we entered into a long term distribution deal. This gave us a premier position on Expedia in the accommodations segment for two years and lots of banner advertising for a modest amount [20%] of equity that valued us at $3 million post money." The company did raise money from investors with a first round private placement in July 1998 (see **Exhibit 2** for VacationSpot.com's financing history).

VacationSpot.com focused on executing its strategy through an aggressive acquisition program and through the execution of several distribution agreements (see **Exhibit 3** for a VacationSpot.com timeline of events). VS made a total of three acquisitions over a period of six months in an attempt to address weaknesses its strategy (see **Exhibit 4** for a description of its acquisitions). One of the acquisitions was of a company that developed a Windows-based reservation software product for inns and B&Bs. VacationSpot eventually developed this software into a reservation database management product called Avail that served both the company and customer's database needs, connecting into the VacationSpot.com site via the Internet to process reservations. "While we started out with paid listings while building out our supply, we are now in a position to effectively take a commission on all transactions," explained Slyngstad. "Eventually we will get a full commission [8% of sales] on reservations made through our site and a lower commission [4%] on reservations made off our site as a royalty for use of the database management program."

The other two acquisitions helped the company build its property offerings. "Starting out we felt that it was a cheaper way of acquiring properties," explained Murch. "we figured that it would cost us around $300 to acquire a supplier on our own and that the company acquisitions we made to get property listings would be cheaper.[3]" In total, these acquisitions allowed the company to make progress on fulfilling all three elements of its strategy. Slyngstad explained the dynamics of the strategy:

> Although the initial distribution agreement with Microsoft hurt us with respect to entering into other distribution agreements, all that changed when we got some scale with the acquisitions, especially the first acquisition which was one of the leading vacation rental sites at the time. People like Travelocity simply could not ignore us any longer. Additionally, our acquisitions improved our position with both our "suppliers" [property owners or managers] and potential distribution partners by strengthening all three areas of our strategy.[4] Once the technology issue was addressed, we started a virtuous circle where the more properties we signed-up, the more attractive a distribution partner we became and vice versa.

VacationSpot.com in April 1999

By April 1999, the company had completed a second round of financing, raising $7 million at a pre-money valuation of $20 million. Murch recalled the company's strategy.

> In our Series B round, we received term sheets from many investors but chose Technology Crossover Ventures [www.tcv.com] and the Madrona Group [www.madronagroup.com] over everyone else. We not only chose them because of their success with companies like CNET, Evite, Ariba, MyPoints [TCV], Amazon.com, and HomeGrocer [Madrona], but because their business approaches complemented our strategy. For example, we received a term sheet from Kleiner Perkins, but turned them down. KP is awesome at branding and PR but our ideas on building our business were different from theirs. At the time, Kleiner wanted to spend big money on building a brand fast; that works well when you have a well-established distribution channel and fulfillment nailed. In our space, we needed to *build* the distribution network, and *build* the reservation platform; it didn't exist when we started. It has taken us until now [April 1999] to feel like we have the network in place to be willing to drive branding full-stream. By April 1999, we had a strong group of investors that we worked well with, and very proactive support from them.

The company was still growing its listings and had recently changed its revenue model. In order to slow the burn rate, VS had started operations by charging a flat listing fee but switched to a commission-based system after the Avail 5.0 program was launched in March 1999 and was beginning to migrate its customers to this new model. (See **Exhibits 5 and 6** for an overview of the Avail 5.0 system and the VacationSpot.com site.) Under this new revenue system, VacationSpot.com effectively cut out the existing travel agents, charging a fee of around 8% compared to the average travel agent fee of around 10% (see **Exhibit 7** for an overview of the traditional vacation property value chain). The company was continuing to add listings and was getting more and more booking inquiries every day (see **Exhibit 8** for booking inquiries and property listings over time). While things were going well, the company was becoming somewhat concerned about the quality of the listings and the comprehensiveness of the offering. Murch explained:

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[3] At the outset, the RAH team estimated the cost of acquiring each property would be $500.

[4] Property owners, agents and the like will be referred to as suppliers throughout this case.

> We really feel that our strategy is falling into place. We feel that our distribution agreements and our proprietary software, and our upcoming Web-based reservation platform provide us with an edge over the competition and a way to scale our revenues rapidly with the number of consumers using our network. Although 95% of our transactions are still email request based, we are beginning to automate the process. Moreover, we believe that our property offerings give us more listings than any other site. The only real area of our strategy that we still need to address is in the comprehensiveness of our listings. We have recently conducted a review of our customer request profile and we have found that we are relatively weak in our European offerings. We could address this by focusing our business development efforts on Europe but this really doesn't satisfy our needs fast enough. The relationships and an understanding of the customer in the market are key. As a result, we feel that an acquisition would suit us better than a green field effort: it is an easy way to get scale and expertise at the same time.

With that in mind, Murch and Slyngstad decided it was time to contact Rent-A-Holiday about a possible merger.

Rent-A-Holiday: Growing From Brussels

The Genesis of Rent-A-Holiday: Another Honeymoon

Peter Ingelbrecht graduated from the University of Gent in Belgium with a degree in economics. (See **Exhibit 15** for the biographies of RAH founders). He first worked at Procter & Gamble as a Product Manager for brands such as Always, Ariel, and Punica. After eight years at P&G, Ingelbrecht enrolled at Stanford Business School from which he graduated in 1995. Although he initially wanted to do a start-up he decided against the idea and returned to Europe to work for The Boston Consulting Group in Brussels, Belgium. Ingelbrecht explained his choice.

> I really wanted to start my own company but the debts accumulated from Stanford made that impossible. So I decided to head back to Europe to work for BCG. I felt that I needed to be in Europe because I felt that I had an edge there and that I did not have one in the United States. I liked BCG because it was strong in consumer products and marketing, areas of interest and strength for me. Moreover I liked the short, three to four month cases and the strategic nature of the business. I felt that this would give me a good base of knowledge and flexibility for the future.

On his first case, Ingelbrecht worked with Laurent Coppieters, a three-year BCG consultant who had graduated from the Free University of Brussels (ULB) with a commercial engineering degree. They shared their ideas about long term career goals and found they had a mutual interest to start their own company. The two kept in touch over the next couple of years. Ingelbrecht then came up with the idea for RAH after having an experience similar to Murch while on his honeymoon in Spain in 1996. He had originally wanted to book a small villa and after spending a tremendous amount of time searching through the typical sources like agencies and newspapers, he found nothing was free so he booked a hotel instead. When he got to Spain, he was surprised to find there was plenty availability. Ingelbrecht explained what he found:

> Once I was there I saw *at least* 20% vacancy right off the bat and determined that this market must not be very efficient. So I went to some of the property managers to find out more about their business . . . and to find new lodging! . . . and found that marketing in the segment was very unprofessional, at least in Spain. They

> only advertised locally and had absolutely no clue about cross-border marketing. At the same time, property owners and tour operators granted substantial commissions to these people. So I knew there was an opportunity.

With this new knowledge, Ingelbrecht went to his colleague Coppieters and the two decided in January 1997, to quit their job at BCG and began Rent-A-Holiday. Coppieters explained the move:

> We did not have any funding at the time but we knew we had a good idea and we knew it needed our complete attention. So we quit BCG to create a rental company focused on Europe. We wrote a business plan and started in April 1997, with our own funds. The first capital round followed in June 1997.

The Early Years at Rent-a-Holiday: Building Property Inventory and Raising Capital

Rent-A-Holiday's strategy was to become a worldwide player by focusing first on Europe. According to the company's estimates, 90% of vacation rentals in Europe were to other European citizens. Moreover, RAH estimated that about 17% of all overnight stays in Europe were in B&Bs and another 17% were in vacation rentals; the corresponding figures were around 4% for both segments in the United States. By focusing on a "Fortress Europe" strategy, RAH felt that they could build up a solid business while protecting themselves from the threat of competition outside of Europe. The strategy was to be executed both through proprietary inventory development and through acquisitions, similar to VacationSpot.com. However, the RAH business was slightly different from VacationSpot.com in that not only did the entrepreneurs have to convince the suppliers to use their service but they had to educate them about the Internet as well. Since only 5%-10% of the potential suppliers used the Internet, the company had to rely on more traditional means of communication, like fax machines, telephones, and direct country visits.[5]

As a result the acquisition of suppliers turned out to be more costly than planned. While RAH had originally budgeted 3 man-years to acquire a certain number of suppliers and listings it eventually took 10 man-years to achieve the target. On the positive side RAH benefited from the fact that many Belgian's spoke several languages and that there was a considerable multilingual foreign population in Brussels, which was also the location of many administrative offices of the European Union. In comparison to the United States it was fairly easy to hire a workforce with outstanding language skills at a low cost. This multi-lingual and multicultural workforce could effectively build inventory via phone calls or local visits. The added complexity of having an end-user and a supplier that often times spoke different languages also complicated development of the website. As a result of this, RAH focused their technology development efforts on creating a user interface that could switch between seven major European languages[6] and help the supplier and the end-user communicate with each other. The founders believed that the development of this translation engine provided RAH with a distinct edge over their competition.

Because of the low Internet penetration among suppliers, RAH was unable to offer an interactive reservation engine to web-visitors. Instead, the company relied on a listing-fee-based revenue model. If a supplier wanted to list a home she would be charged a fixed annual listing fee on a sliding scale: BFr 3000 (~$75) (In1999, it went to BFr5000.) per year, if she wanted to list one home, BFr 25000 (~$600) if she wanted to list 25 homes.[7] Once a customer had identified a property he liked, he would submit an inquiry via the RAH web page. This inquiry would be automatically translated

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[5] The Internet penetration amongst suppliers in the US was around 50% according to VS estimates.

[6] English, Spanish, German, Italian, Swedish, Dutch, and Portuegese.

[7] During the start-up phase, RAH offered a certain number of suppliers free listings in order to create an inventory of properties.

into the supplier's language. The supplier would then get back to the traveler, by email, fax or telephone, to confirm availability and ask for payment. Dates of availability for each site could be updated by the supplier via the web.

One major difficulty the RAH founders did have throughout the course of building the business was in obtaining financing (see **Exhibit 9** for Rent-A-Holiday's financing history). Ingelbrecht explained:

> Although we had a similar vision and business model as VacationSpot.com, we had not been able to raise as much money. The venture capital community in Europe, and in Belgium in particular was not as developed as the VC market in the US. As a result, we had to spend a lot more time on capital raising than VS did, but got less money. Our first round of financing (completed in June 1997) took four, hard months to complete. We were finding ourselves spending the larger share of our time on such subjects as trying to convince investors that the Internet wasn't just for geeks![8]

Also, as a small company in Europe, the RAH founders discovered it was tough to attract talent, both in terms of number and quality. Moreover, Belgian tax law made it difficult to use options as an incentive for potential employees as the employee would be taxed immediately upon the grant of the option, unlike in the United States where the employee would be taxed upon selling the security the option had been converted into.

Rent-A-Holiday in April 1999

While financing and hiring issues probably slowed the growth of RAH, by April 1999 the company was the largest European player in the market and they had roughly the same number of property listings as VacationSpot.com. (See **Exhibits 10-14** for booking inquiries and property listings over time, comparative statistics, company financials, and comparable company valuations). RAH's founders felt that they were making good progress in terms of generating traffic and getting property listings. Also, the translation engine and user interface were unmatched by competitors. Financing had taken its time, however, and the founders were just getting started on the design of a European acquisition program to further increase their listings.

Up until the March 1999, RAH had followed a "Fortress Europe" strategy by building the best company in the space in Europe and by attracting as many European properties as possible. The question was whether and how a potential merger with a US company would change that strategy.

Merger Discussions between RAH and VS

The Courtship Begins...And Ends?

The first contact between the two companies had actually occurred one year before, in March 1998, when Coppieters e-mailed Murch. Murch recalled this first contact:

> Laurent actually contacted us in 1998 to discuss the possibility of link exchanges, and potentially a joint venture between our two companies. The proposal

[8] Vacationspot had spent about 80% of their time on acquiring and generating property listings according to the VS founders.

> was to share our property listings and to somehow share the revenues. They were actually a little bigger than we were at that time—about 4,000 listings to our 3,000—but we really didn't want to do a JV. Microsoft always preached the perils of joint ventures; it is extremely tough to align incentives in them. The history of JVs in high technology is littered with failures. So we decided to pass on the opportunity and we kind of lost sight of each other. Then when we completed the survey of our site and discovered that we were weak in Europe, I decided to give them a call.

Coppieters remembered that conversation:

> At the end of March, Steve called me out of the blue one day and asked me if we wanted to merge with them. That was really a crazy call! It took me completely by surprise. But we started talking, found that they were serious and decided it would be worth a trip out to Seattle. So I hopped on a plane to Seattle along with Karim, one of the investors.

From the initial telephone discussions through the first few hours of the face-to-face meetings in April, the two sides never discussed valuation. They spent their time instead trying to understand each company's business model and vision and simply trying to see if there was a "fit." "It almost seemed as if we were all avoiding the valuation issue in order not to lose sight of the fundamental issues," recalled Coppieters, "It seems both sides share the same long term vision and strategy." As both sides became comfortable with the direction the combined entity would follow, Slyngstad decided to begin the discussion about valuation. Slyngstad said that since both companies had recently closed a round of financing, that the valuation from the round would be the best place to start. So he made an initial offer where VacationSpot.com would merge with Rent-A-Holiday at a 9-to-1 ratio, subject to Ingelbrecht and Coppieters signing a long-term employment contract. Upon hearing the offer, Dhanani exploded and the RAH team walked out.

VacationSpot.com Reaction: Picking Up the Pieces

Sitting in their offices after the meeting, Murch and Slyngstad looked at each other again. They believed that their offer was more of a starting point for negotiations and that since both companies had recently completed a round of financing, their approach was rather reasonable. Slyngstad turned to Murch and said:

> Since we both had just raised money, I thought that the prior rounds were a good starting point for the negotiations. We started with a zero premium and were preparing to move on from there. But I don't understand what just happened and I am not sure how to interpret it. Was this a cultural misunderstanding and they really feel we low-balled them? Or was this just a negotiating tactic to get us to increase our offer? What's really strange is that we do not know if the talks are over or they are only suspended. I am leaning towards this being a negotiating tactic, but regardless, this is quite strange.

Murch was just as surprised as Slyngstad. However, Murch thought that there may have been a fundamental misunderstanding between the two parties and was somewhat more concerned than his partner about the status of their merger discussions with RAH. Murch responded to Slyngstad:

> We definitely want to resolve this misunderstanding with RAH. As a company, we need to get a stronger presence in Europe and although there are other companies out there, we like the fact they have a leadership position and we believe that their translation engine provides real value. What's more important is that we really liked Laurent and Peter. I think they are the *real* value in the business and that

> is why I want to get them into a long-term employment contract; we need to make sure the proper incentives are in place for them. The question is what kind of incentives do we need to offer them. We could also "conquer" Europe through a green field approach but this is the last thing we really want to do. There have been a number of U.S. companies that have gone to Europe, tried to use the same brand and tactics and have failed miserably. I think that proper business and cultural expertise is the most critical element of a foreign venture and I think that it is really difficult to develop internally. As a result, I really want to make an acquisition and I feel that these are the best guys out there.

Rent-A-Holiday Reaction: Take the Next Plane?

Back at the Sheraton Hotel, the Rent-A-Holiday team was trying to regroup. The low valuation offer was disappointing and RAH was just as unsure as to the direction of the negotiations. Coppieters had prepared for the negotiations by putting together a list of items that he thought could serve as a matrix for the valuation (see **Exhibit 11**). Since the VC market in the United States was so different from the VC market in Europe, they felt that these items rather than last-round valuations gave a much better indication of relative value than the prior rounds of financing. Coppieters outlined the RAH position:

> I put together a matrix that compared our companies according to several different operating and other statistics. In addition to this matrix, though, there are other considerations. For instance, the VS team is somewhat more advanced on the technological front. Although we realize that our translation engine provides a lot of value, their property management tool (Avail) is probably better than anything else out there and that holds a significant amount of value. In addition, they have much better financing sources than we do which would help us in several ways. For instance, it eliminates a lot of uncertainty potential European employees have regarding joining a small company like ours. Nevertheless, we do not *have* to continue with the negotiations. We could continue with our Fortress Europe strategy and compete against them effectively if they enter the European market without us. We have identified a couple of acquisition targets that would solidify our position in Europe and we could just as easily go that route if the deal is not fair. Also, the VC market in Europe is improving and we might be "overrun" by potential investors soon.

Another reaction of Coppieters was a result of the visit to Seattle rather than of the failed negotiation an hour before. Somehow the trip and the two-day search for fit made the entrepreneur realize that if a merger took place, the new home base of the firm would most likely be Seattle. This made sense: Seattle had better access to important inputs (such as capital and qualified employees) for the combined entity than Brussels. The merged company would keep offices in Brussels to develop the European market, but for how long and to what extent would Brussels become a subsidiary focused on strategy execution? And if Ingelbrecht and Coppieters wanted to co-lead would they need to move to Seattle? Despite their struggles in starting RAH Coppieters and Ingelbrecht really liked *their* company. Maybe it was better to continue alone.

Dhanani had some additional concerns. He not only felt that the offer for RAH was too low but felt that it was even more unfavorable to the investor group than it was to Ingelbrecht and Coppieters. He believed that the options that would be part of the potential employment contracts for Ingelbrecht and Coppieters were really a transfer of value from the investor group to the founders. Accordingly, he believed that the equity involved in the employment contracts was really part of the total consideration for the company and that the investors should get their pro rata share of these options.

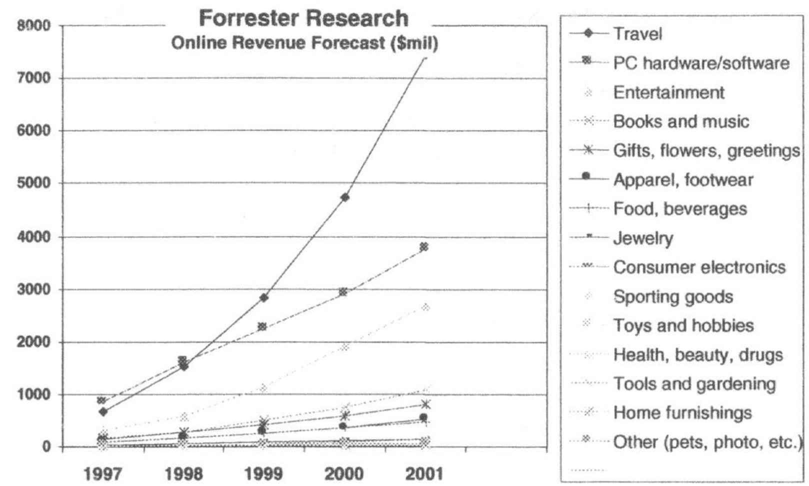
What's Next?

As they reflected upon what happened, both sides were not sure what the next move should be. Should they be the ones to reinitiate contact or should they wait for the other party to make the first move? As they sat in the hotel lobby Coppieters looked at the phone and said, "I think this is worth another try, but we are not going to make the first move. They owe us." At the same time Murch looked at Slyngstad: "I really don't know whether this is a fundamental problem or just a cultural thing or smart tactics on their behalf. What do you think, Greg?"

Exhibit 1 Overview of the Travel market and Independent Leisure Lodging Segment

Online Travel Market

Largest, fastest-growing e-commerce segment



Source: Forrester Research, VacationSpot.com

Independent Leisure Lodging Segment

A $126B segment... fragmented and under-served by existing solutions

Properties (est.)		$ Reservations/YR
250,000 properties	Chain Hotels	$600B
	Small Hotels and Resorts	$400B
	Independent Inns	**$100B**
100,000 properties	B&B's	**$14B**
2,000,000 units	Vacation Rentals	**$12B**
4,000,000 owners	Vacation Ownership (Timeshares)	$12B

Sources: Smith Travel Research, Lodging Research Network, VacationSpot.com

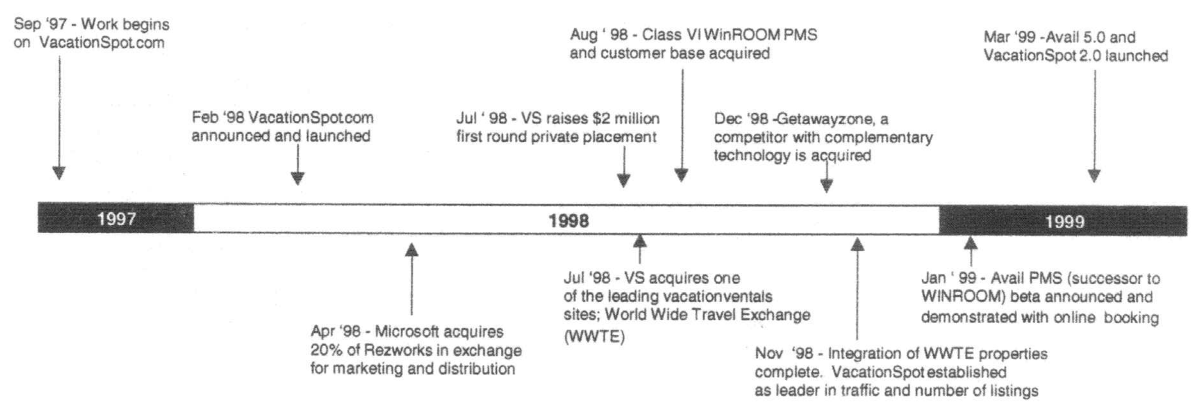
Exhibit 2 VacationSpot.com Financing History

Round	Inventor	Amount Raised	Premoney Valuation
Seed (August 1997)	Steve Murch, Greg Slyngstad	$200,000	$200,000
Distribution agreement (April 1998)	Microsoft	$ 0[a]	$3 million
First round—Series A (July 1998)	Various Seattle and Bay-area technology executives	$ 2 million	$6.1 million
Second round—Series B (March 1999)	Technology Crossover Ventures, Madrona Group, first round investors	$ 7 million	$20 million

Approx. Ownership Structure as of 4/99	
TCV	21%
Management	47%
Microsoft	12%
Madrona	2%
Others	18%
	100%

Source: VacationSpot.com
[a]No money was raised but Microsoft received 20% of the equity in exchange for a long-term distribution agreement

Exhibit 3 VacationSpot.com Timeline



Source: VacationSpot.com

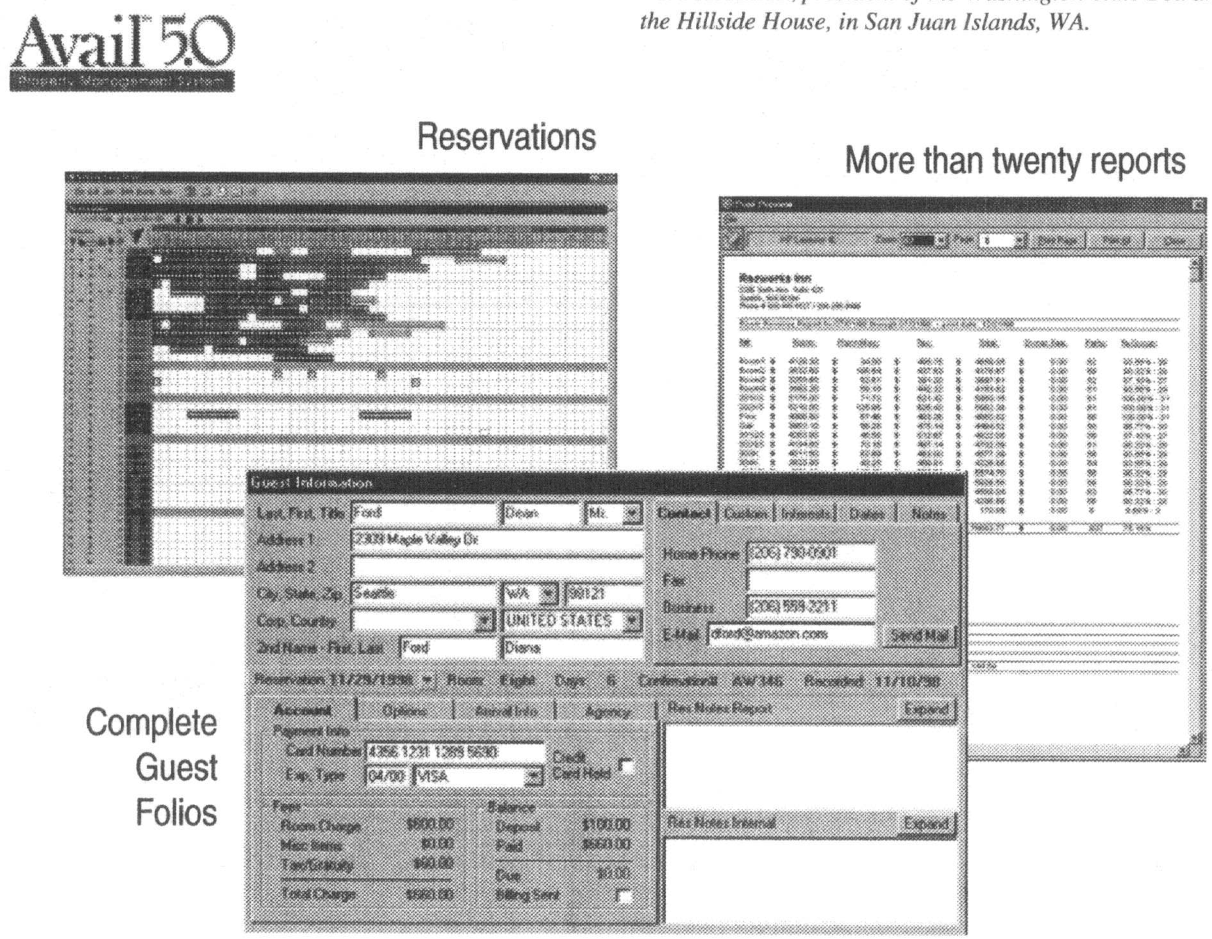
Exhibit 4 VacationSpot.com Acquisition History

Company	Date	Description	Cost
World Wide Travel Exchange (www.wwte.com)	Apr-98	Leading vacation rental site 2,800 Properties	$700,000 (mostly cash; 0.5% equity)
Class VI WinROOM Property Management Software	Aug-98	Leading reservation software company 1,000 Customers	$70,000 (or 0.5% equity)
Getawayzone.com	Dec-98	Leading competitor in ski market with complementary technology and management team 1,400 Properties	$500,000 (plus options for six employees)

Source: VacationSpot.com

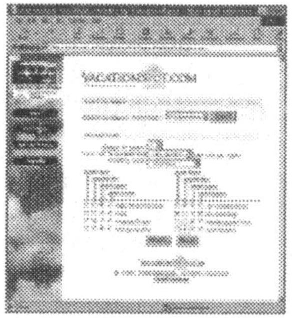
Exhibit 5 Avail 5.0 System Overview

'I've looked at most of the alternative reservation management solutions and this is not only easy-to-use, but it solidly addresses the needs of specialized properties like inns and bed and breakfasts."
Dick Robinson, *president of the Washington State Bed and Breakfast Guild and owner of the Hillside House, in San Juan Islands, WA.*

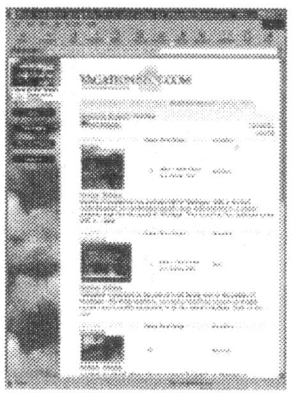


Source: VacationSpot.com

Exhibit 6 VacationSpot.com Site Overview

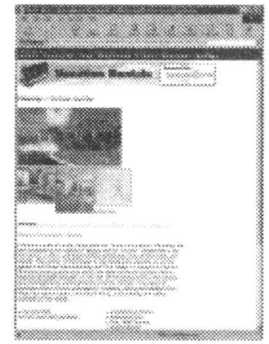


Easy Searching

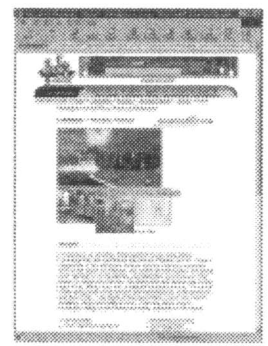


...Results

"The slickest site yet for vacation rentals" -- *Online Traveler, Nov. '98*



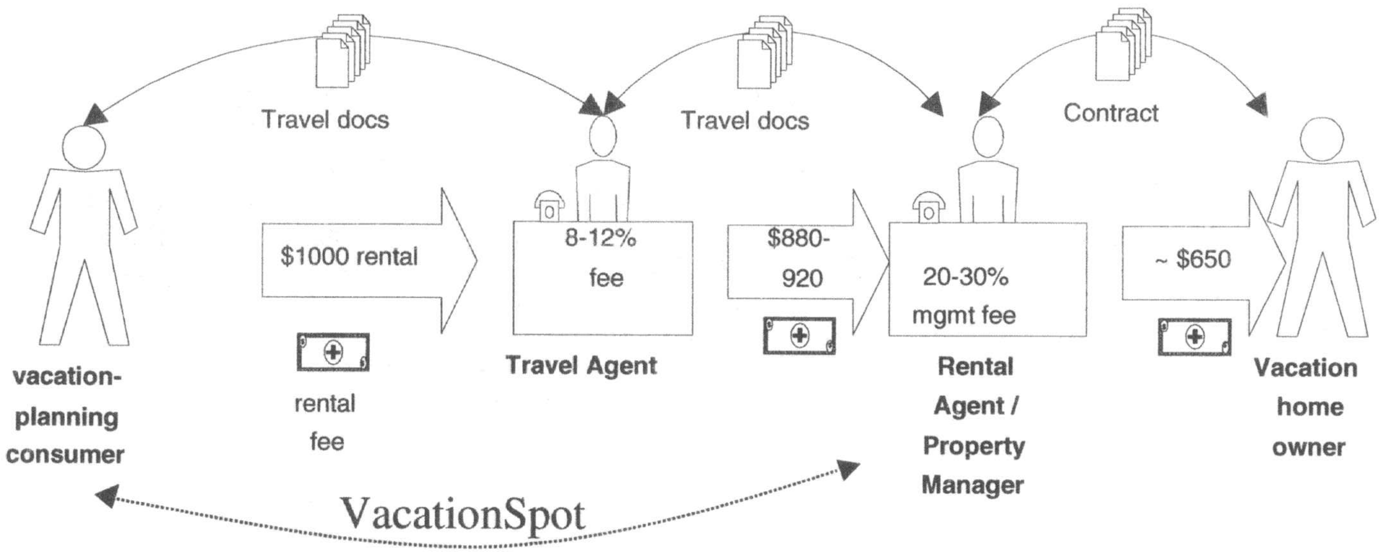
...on Rent.Net



...on InfoSpace

Source: VacationSpot.com

Exhibit 7 Vacation Property Value Chain

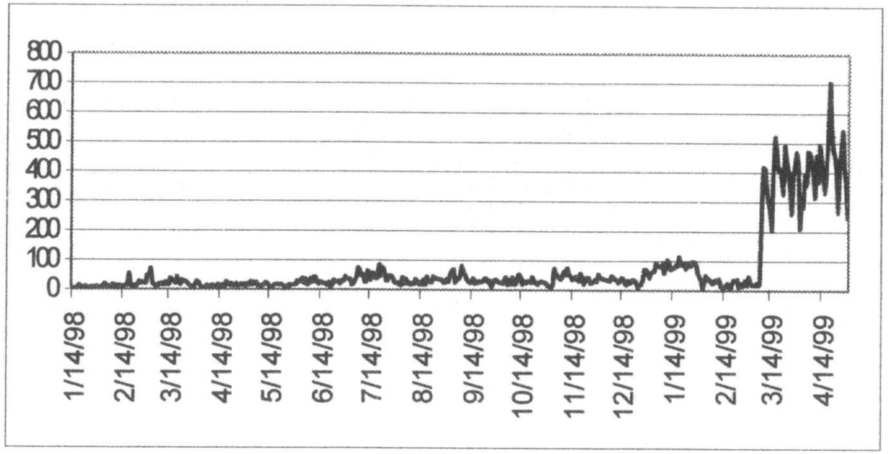


- Consumers want large selection, instant availability, market-efficient pricing, specials, reviews & more.
- Suppliers want improved distribution, more cost-effective marketing, easy-to-maintain electronic presence, yield management & more.
- No electronic reservation network yet exists for the vast majority of vacation property

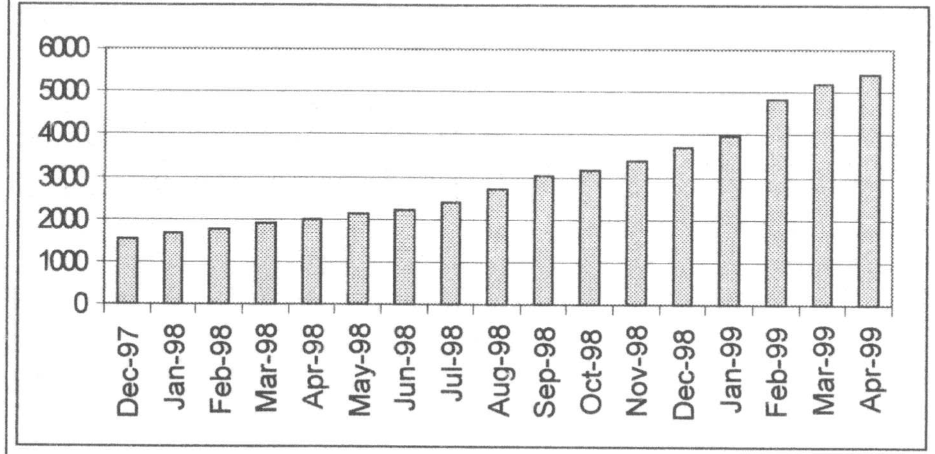
Source: VacationSpot.com

Exhibit 8 VacationSpot.com Booking Inquiries and Property Listings

Bookings Inquiries per Day



Property Listings



Source: VacationSpot.com

Exhibit 9 Rent-A-Holiday Financing History

Round	Inventor	Amount Raised	Premoney Valuation
Seed (April 1997)	Founders	$100,000	$ 0
First round (June 1997)	Investors	$700,000	$ 600,000
Second round (July 1889	Investors	$500,000	$1,800,000
Third Round	Investors	$400,000	$1,800,000

Ownership Structure as of 4/99	
Investors	73%
Founders	27%

Source: Rent-A-Holiday