

DAY 7

THREE POPULAR DEAL STRUCTURES



Deal structures

A deal structure is how you put together the payment for the business; it ideally allows you to use none of your own money, or to use very little of it.

The earn-out strategy

This is flexible deferred consideration. The payment made changes depending on the performance of the business. It's a great way for buyers to protect themselves.

Three key advantages of an earn-out:

 You never overpay 1	 The seller can achieve more so your deal looks better 2	 You share the risk with the seller 3
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» Three-year forecast

Ask the seller for a three-year forecast showing how they believe the business is going to perform; that will be used to establish the earn-out structure.

An alternative but similar structure:

- » Pay a percentage of the turnover or profit of the business for a period of time.
- » It's a no-risk way of paying for the business: if turnover or profit go down, you pay less.
- » It's easier to use turnover than profit.
- » The percentage paid might diminish over time.

The earn-out strategy allows you to de-risk the acquisition so you get the business without overpaying.

The property strategy

Used when the owner also has a property to sell. Common in location-specific businesses, e.g. veterinary practices. With these, if you relocate, the business might fail.

If you only want to buy the business, find a property investor.

Both transactions – the sale of the property and the sale of the business – occur on the same day. The money for the property goes to the seller on completion day; you put money down.

You buy the business on 100% deferred consideration; you pay for business out of the profits of the business.



Demerger

If both property and business are owned by the same company, you must do a demerger. In the UK you need HMRC approval.

You create:



A new holding company



A new subsidiary of the holding company

Then:



The property moves through the holding company into the subsidiary



The property investor buys the subsidiary



You buy the original company



The holding company is closed down

In the UK, use JLA Accountants in Barnet.

Using the target company's cash

- » The target company is the business you are buying.
- » Use this method when you buy the company, not when you buy the assets.
- » Small business owners think the cash at bank is theirs. They are wrong; it belongs to the company.
- » They can take it as a dividend, or as income via the PAYE system. The reason they haven't taken it out is the tax that will be due.
- » In the UK, you can help them achieve a very low rate of tax – 10% on the first £1 million and 20% thereafter.
- » By including the cash at bank in the sale and purchase agreement you can use it as the initial consideration and the seller can pay 10% tax rather than (potentially) 40% tax.
- » Ask the seller early on: 'How much cash is in the bank?'
- » If there's a substantial sum, you can effectively buy the business with that cash.