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SPECIAL REPORT

# EIGHT WAYS TO BUY A BUSINESS

Jonathan Jay's DEALCLUB

# *Eight Ways to Buy a Business Without Using Your Own Cash*

THIS MONTH, you will learn:

- Eight methods of buying a business without using your own cash
- How to introduce the concept of not paying 100% on completion

We've got eight solid ways to buy a business without using your own cash. They are:

1. You buy the company for £1
2. The consideration for the business is 100% deferred
3. You pay only a percentage of the consideration on completion
4. You use the money in the business to fund the initial consideration
5. You use retained profits to fund the initial consideration
6. The property strategy
7. The earn-out
8. The director's loan strategy

Let’s take a closer look.

## 1. You buy the company for £1

In this situation you buy the assets and the liabilities of the company, typically for £1, because the liabilities are equal to or greater than the assets — the owner just wants to walk away.

This technically means that the company is insolvent and there are director responsibilities and legal responsibilities to be dealt with when a company is insolvent.

Buying a business in this way is not for the faint-hearted. This is not for the complete newbie who doesn't know anything about buying a business and you should never do this unless you know what the problem with the business is and, more importantly, how to fix it. However, if you have the solution and you have the confidence and the knowledge to do this, it can be a very fast way of acquiring what could be a very large company for nothing.

## 2. The consideration for the business is 100% deferred

With this, you defer the full payment for the business into the future so you don't pay anything for the business on completion. Well, technically you would have to pay something – although maybe just a pound – as that's a requirement of English contract law. So, say you are paying £500,000 for the business, you pay one pound now and defer £499,999 pounds into the future.

For this, you need a highly motivated seller. This is typically someone who hasn't been able to sell their business, they're at their wits' end, there is a deadline looming, they just want to get out and you're very much in the right place at the right time. The sum you agree to pay is paid over, for example, three years, with the first payment due after ninety days. Of course, all of these payments are going to come out of the profits of the business, they're not going to come out of your own pocket.

You have to hunt for these deals, they might not be commonplace but they are possible in the right, and also tight, circumstances.

## 3. You pay only a percentage of the consideration on completion

A percentage of the consideration is paid on completion and the balance is deferred. You can fund that initial consideration using either of two methods: asset finance or invoice discounting. Let me explain what they are.

**Asset finance** is where you place finance on a fixed asset. This is a tangible asset that the business owns and that releases money; I'll give you an example of that in a moment.

**Invoice discounting** is pretty similar, but we're getting finance on the outstanding business debtors. These are people who owe money to the company, they must be business customers, not consumers, and they're all operating within their agreed credit terms and you can get effectively an advance on that money owed. You might be able to release 70%, 75% even 80% of the value of those invoices.

We can use that asset finance or advance to fund the initial consideration, and then the balance, the deferred element, is paid from the profits of the business over time. A little note of caution: ensure that the deferred payments are no more than 50% of the profit of the business. Why? Because you want to leave yourself some headroom, in case of profit dips or so you can take some money out. So if the business makes £100,000 pounds profit a month, then your deferred payment should be no more than £50,000 pounds a month.

**Example: asset-based finance**
Equipment value: £500,000
Finance owed: £100,000
Equity: £400,000
Refinance: £400,000
Repay original finance: £100,000

Cash released: £300,000

In this example, the value of our equipment is £500,000, with £100,000 still owing on finance. That means there's equity of £400,000.

We can refinance at 80% loan to value, gaining £400,000. Out of that we repay the original finance owed of £100,000, meaning the cash released is £300,000.

There are three things that you can do with that cash that's been released: you can use some or all of it to pay the owner of the business, so there's your initial consideration; number two, you can use it as working capital to grow the business; and number three, you could pay yourself a deal fee.

Remember we talked about how to make money when you buy the business, not just when you operate and sell it? Well, this is your way to make money when you buy the business. Of course you've got to do this sensibly because the business now has to generate the profit to pay back this asset-based loan and that comes at a cost – there's going to be an interest rate applied. And you can't default because otherwise the assets are repossessed and you haven't got a business. The assets presumably produce whatever is the business sells so you've got to do these things sensibly. That's where having a good lawyer and a good accountant on your deal team really helps.

How much are you able to take out? I know of someone who refinanced the assets of a business that he bought and released capital of £7.2 million, out of which he paid himself a £7 million pound deal fee. I'm not a tax adviser so I'm not going to give you advice on the tax implications – this is where your tax adviser and your deal team come in.

If you can't repay the asset finance – well, you need to make sure that you can. um quite often uh these days maybe not so much a few years ago. these days personal guarantees are required as well so again you've got to take a view you've got to say well look is it worth it am I happy with a personal guarantee we'll talk more about pgs later but you've got to take a view on this, we're grown up business people here we need to be sensible about what we do you know is there a degree of risk well yeah but there's a degree of risk of getting up in the morning. it's about how how comfortable you are with these things and I think that the more deals you do, the more time you've been in business, the more you are quite prepared to take a degree of risk because you can always manage the downside you know what's the worst that can happen and you can always deal with what the worst is

## 4. You use the money in the business to fund the initial consideration

People often think whatever money is in the bank must belong to the seller, but it may well belong to the business. The money in the bank only belongs to the seller if it's profit in excess of working capital. If that's the case, they can take that money out prior to the sale of the business to you.

The working capital in the bank can fund the initial consideration. We do this a lot because nursery businesses get money from the local authority to pay in advance for the term about to start. The money for the new term starting January is sitting in the bank in December. It's for a service that hasn't yet been provided and that we're going to provide, so it doesn't belong to the seller, it belongs to the business. That money is transferred to us on completion because that's our money to look after the children next term. However, we can use part of that to fund the initial consideration.

If we do it will mean that cash flow will be tight at first, because we've used some of our working capital to pay for the business, but the way to balance that is to make some immediate cost savings. And here's a little tip: quite often those immediate cost savings happen automatically because the owner of the business is no longer involved. Some owners put a lot of personal stuff through the business, so as soon as that owner is gone all that personal expenditure is gone as well. That means your cost savings can be found immediately.

## 5. You use retained profits to fund the initial consideration

The seller may be sitting on a large balance of cash that they've left in the business because they don't like the idea of the high tax bill they're going to get when they take it out as income. It's a bad strategy – you shouldn't leave large balances in your business bank account. Now, that is their money, but we can also use that to fund the initial consideration. Let me explain.

Say there's £500,000 in the bank and we put in the sale and purchase agreement that we'll pay them the money that's in the bank as the initial consideration, it means they only get a 10% tax bill because they can use entrepreneurs' relief. So we can save them a lot of money.

Again, this is where you've got to know more about buying a business than they know about selling a business. When you understand this concept and explain it to them, they will realise that by doing it this way they are going to save themselves a fortune in tax, so effectively it's free money.

You need to keep an eye on the situation with regard to entrepreneurs relief, as it can be subject to change.

## 6. The property strategy

- If the seller owns a property and you don't want the property, then team up with a property investor.
- The property investor buys the property, providing the seller with the Initial Consideration.
- You buy the business on 100% Deferred Consideration.
- You may need to do a demerger of the property from the trading company which requires HMRC clearance and a specialist accountant.

This is a great strategy you can use when the seller of the business owns a property, typically the property that the business trades from, and you don't want it. You team up with a property investor and they buy the property, providing the seller with the initial consideration. Say the property investor buys the property for £500,000; they give that money to the seller, meaning they have their initial consideration and you effectively buy the business on 100% deferred consideration. You pay the balance over a period of time from the profits the business generates. It makes no difference to the seller where the money comes from; they've got their exit and the balance will be paid over time.

You may need to do a demerger of the property from the trading company, which can be a little tricky – not every accountant knows how to do this. However, it needs to be done properly as you need HMRC clearance. Once that's been dealt with you can effectively pull the property out of the trading company, which is what the property investor will want. You'll need good advice from your deal team on this strategy because there are always important details to warngle and every deal is slightly different.

## 7. The earn-out

This strategy is another favourite of mine because it links payments for the business with the future success of the business. This offers very good protection because it means that you are not going to overpay for the business. If the business does well then the seller is paid more, but the converse is also true; if the business takes a bit of a dip because there's something comes around that we're not expecting – like a pandemic, for example – then the seller is paid less. This is actually a really neat way of making sure that you don't overpay.

Every seller is going to tell you that the future is incredible; you might want to encourage them to create some forecasts of what they believe is going to happen over the next three years, and if you do I'll bet those forecasts will be very rosy. That allows you to say, 'Look, this business is going to do great. I've got a way of paying you that means if the business does what you say it's going to do over the next three years, we're going to pay you a lot more than what you originally were after.' That's the that's the carrot for the seller. You then say, 'If the business absolutely collapses the day after we buy it, neither of us gets anything, so we're kind of in this together.' But if they believe in their business, then what's the problem? And if the business doesn't perform as well, you pay less for it.

Typically we would do this over a three-year period. Some of my private clients are using this strategy to buy businesses on a percentage of revenue, these are businesses without any assets, typically service-based businesses, and they come to an agreement with the owner to pay maybe 20% of revenue in year one, 1%of revenue in year two, and 10% of revenue in year three, so the percentage amount diminishes over time. The reason they can do this on revenue is that they know exactly what the profit margins are in the business.

Why would you want to do it on revenue? Well, if you say it's a percentage of profit, the first thing that the solicitor for the seller is going to say is that profits can be manipulated – companies reduce their profits all the time to pay less tax. Why wouldn't they reduce their profits to pay the seller less money? It’s a very good point. So the fairest way of doing this is to pay a percentage of revenue. You can get a deal done really quickly like this because, especially if you're buying the assets, what due diligence are you really doing? You've got absolutely nothing to lose.

## 8. The director's loan strategy

The director's loan strategy is this: if the director has taken money out of the company as a director's loan, so they haven't paid any tax on it, they need to repay it on completion because it's not their money. Alternatively, they can either vote it as a dividend, if there's sufficient retained profits, or take it as PAYE, which means that 50% of it disappears in tax. People don't usually want to do that, or they can't do it because they've taken out more than they have in distributable profits, so they never can pay it back. That means that repayment forms part or all of the initial consideration.

Let me give you an example. Say the directors have taken half a million pounds out of the business and used it to buy a house. They don’t have the cash to pay it back and they can’t pay 40% tax to take it as PAYE. You are buying the business for one million.

You jump in with the problem-solver mentality we talked about earlier and say, ‘We'll help you out here. That director's loan is 50% of what we're paying for the business, so we'll show on paper that you've paid it back and then we've given to you as the initial consideration. That means that you can apply a 10% tax rate to it because that £500,00 that you bought your house with was, in fact, payment for shares and you can apply your tax relief to it.’ Again, you've got to take good advice on this. Some accountants might say you can't do that, but you absolutely can, it's all about how you position it. What you need is a deal team that says yes, you can do it, let's work out how we can make it work.

## Round up

Those are my eight ways to buy a business without using any of your own cash. However, if you do have some cash to put in that will open up the number of businesses you can buy. What I would strongly suggest is you don't put all of your money into one acquisition – do a combination of one of these strategies with maybe a little bit of your money in a way that will allow you to do a deal.

If you're not going to use any money at all you can't go out and buy just any business, you've got to choose your businesses carefully, and it may mean that you need to do a little bit more of that that deal origination, do more of that deal flow, because you've got to dig a little deeper to find these businesses. They do exist, though. I’ve bought ten businesses since lockdown and all of the deals have been done using a combination of these methods. We've also said no to loads, because I wanted ones I could buy with none of my own money, simply because the upside is so huge and it completely de-risks it from my perspective.

Buying a business using a system will be 10x faster than using trial and error – I think this is really important to remember. I see comments from people who say they've been doing a deal – or trying to, anyway – and they're really confused and overwhelmed, and it's because they don't have a process. It can take them months to get anywhere and life is too short to learn things by trial and error. I think you need to cut to the chase and say what's the process and then just implement it.

## Introducing the concept of not Paying 100% on Completion

You might be wondering how it is you get a seller who thinks they're going to walk away with all the money on completion, which most of them do, to accepting that isn't going to happen. It can be tricky, most of them have never sold a business before and so they don't know there are other ways of doing things.

It's your job to educate them as to why 'that's just not how deals are done'. Even private equity firms don't pay everything on day one, no one does, it just doesn't work like that.

I explain to people that if we were going to be paying all this money on day one we would have to go to a bank, and that's a really tough process. In that regard you are actually being helped right now by the environment that we're all currently in. It is a tough process and it's tougher now than it was even six months ago. I explain that if we have to go to a bank it might take six months to get a decision on a loan and even then the chances are fifty-fifty whether it's yes or no – and if it's no we're back where we started.

If they still insist they want all the money on day one, I say, 'Well, you know, money doesn't grow on trees.' I love using that phrase: money doesn't grow on trees. I repeat that to do that for them we'd have to go to the bank in six months' time we could be right back where we started and we need to move on with our lives. I often say that, as well, because sellers have that in their head: I just need to sell this business and move on with my life. I say what's in their head already. It's just simple psychology.

Then I say, 'Look, if you want to sell this business quickly then we need to be more imaginative.' I don't use the word 'creative' because 'creative accounting' has connotations attached. I say, 'We need to be more imaginative with what we're doing here, but I'm sure if we put our heads together we can come up with something.' Then I show the seller how they can get what they want, which is an exit from the business and some money, faster and easier if they agree to the structure that I'm proposing. That might mean using the money in the bank, using the director's loan, using the deferred consideration model and so forth. I rationalise it for them. However, there's usually some seller's anxiety around this method.

## Dealing with seller's anxiety

The fear is that they won't get paid. They're thinking, how do I know, Mr Buyer, that you will pay me that deferred consideration? How do I know you're going to pay me?

There is certainly a value here in the seller liking you and having a decent rapport with you and having already built up some trust with you, but the short answer is, 'That's what your solicitor's for!' Often, once they hear that, they accept it. In some cases they don't want to ask any more questions because they're going to show themselves up as being a bit naïve. I remind them there's going to be a big chunky contract, it's going to run to around a hundred pages – if it's a share purchase agreement it very likely will – so there's a contract that says we've got to pay you, if we don't you can sue us and I don't want you to do that. I also point out it would ruin my reputation if we didn't pay. Word would get around the sector, everyone knows everyone, it would ruin my reputation. and then I add, 'Well, it's guaranteed.'

Between those four comments – that's what your solicitor's for; it's a big chunky contract; it would ruin my reputation; it's guaranteed – you get what you want. You might want to say a little bit further down the path, that's what we do in all of our deals, every business that we own, that's how we've done it, because people feel a little safer when they know other people have done it before them.

The first thing their solicitor is going to say is they need to get a personal guarantee. That's pretty much their default setting, we could we could bring in ten solicitors and ask them the same question and they would automatically, without hearing the other people's answers, say we need a personal guarantee. We don't want to give a personal guarantee, so, how do we guarantee the deferred consideration? We use the special purpose vehicle (SPV) that's buying the business. (We'll talk about corporate structure in a moment.)

## How to guarantee the deferred consideration

The guarantee should come from the SPV that's buying the business, not from the holding company, and it should not be a cross guarantee from another business that you've got. Why? Because that gets you in hot water later. A clever solicitor will push for that but you need to push back, and your leverage is your relationship with the owner of the business.

Tell them their solicitor's being a little bit awkward, say, 'I thought we had an agreement, your solicitor is going to mess it up for us.' We want to develop just a little bit of a chink in the relationship between the seller and their solicitor, because if the seller blindly follows what their solicitor says then there are times you just can't get a deal done because the solicitor effectively talks the owner out of it. We want to keep the seller on our side.

Use the four phrases – that's what your solicitor's for; it's a big chunky contract; it would ruin my reputation; it's guaranteed – and you can also say, 'If you feel that we wouldn't pay you, don't do the deal, because I don't think you should be selling your business to someone that you feel about in that way,' and a motivated seller will probably never raise the question again.

You've planted the seed of an ultimatum – if you're going to push for this then you clearly are showing that there's no trust in us and we don't think we should buy a business from someone who doesn't trust us. It's not really a logical argument, but this is more emotional than logical.

## Personal guarantees

Let me just explain the nature of a personal guarantee. It means if there's a company default then the seller can come to you as an individual to get their money. If you say you're not going to pay, they can sue you personally. They will most probably be successful, and you're forced to pay up if you've got the cash or sell assets to raise it if you don't. The that everyone always gives is you're forced to sell your house. Now, that's like our absolute worst-case scenario and there's a lot leading up to that, it doesn't happen overnight.

When it comes to personal guarantees, you can add a clause to your heads of terms agreement to explain that the directors are not in a position to offer a personal guarantee. Then, when the solicitor says they need a personal guarantee, you say we've already agreed that we're not going to do that. Now, most of the heads of terms document isn't legally binding, so it doesn't really mean anything, but you both put your signature to a piece of paper and you play the card that the seller is going back on what was agreed.

You can also say that both directors, let's say there's you and someone else, would have to guarantee and one of you can't, which makes it not fair on the other one. It's either both or neither and one can't do it.

You might also want to explain that your assets are pledged elsewhere. For a personal guarantee to be effective there needs to be assets standing behind it. You might say, 'I bought a couple of businesses recently, as you know, and we have given personal guarantees and effectively our assets are therefore pledged to those other businesses. If I gave you a personal guarantee it wouldn't mean anything.' Now that's both true and not true. With personal guarantees there is no hierarchy like there is with a loan, for example, where you have a first charge, a second charge, a third charge and everyone knows the third charge probably won't get anything. Again, archaic system. There's also no official way of releasing a personal guarantee in the UK; an email saying you've paid the debt, we no longer are going to call on the personal guarantee is actually all you need to get. But if you explain that your assets are pledged elsewhere then you're being very upfront about it, you're showing that you're happy to give a personal guarantee but explain it would mean nothing, and therefore they want something that means nothing. Again, it's a bit of a false argument but again, this is an emotional negotiation. Also, it's a corporate purchase, it's not a personal one.

A favourite answer I use is, my lawyer won't let me. You can leave this issue to the very last moment so everyone's forgotten about it, you've conveniently ignored that paragraph in any emails that you've received, and then suddenly you're completing tomorrow, they say, ‘Oh my goodness, we need the personal guarantee,’ and you say, ‘My lawyer won't let me. If that's what you really want, we can't do the deal.’ They're so emotionally connected to ‘tomorrow's my day of freedom’ that they say let's just do it. Every seller gets to the point where they'll sign anything just to sell that business. I know, because I have myself. You just want to get it done and you start to you start to concede on points that you wouldn't have conceded on before.

Alternatively, you might just sign the personal guarantee. It depends how confident you are about the business, your attitude towards risk and whether you can handle it. I signed a personal guarantee on a lease recently and it was a tiny lease, it was £12,500 a year. I can handle that, that doesn't terrify me. Everyone has different sense of what's a big number and a small number, so it's always going to be down to the individual.

# Key points

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**You don't:**

- pay all the money on day one
- issue personal guarantees

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Buying a business in this way is not for the faint-hearted. This is not for the complete newbie who doesn't know anything about buying a business and you should never do this unless you know what the problem with the business is and, more importantly, how to fix it. However, if you have the solution and you have the confidence and the knowledge to do this, it can be a very fast way of acquiring what could be a very large company for nothing.

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If we do it will mean that cash flow will be tight at first, because we've used some of our working capital to pay for the business, but the way to balance that is to make some immediate cost savings. And here's a little tip: quite often those immediate cost savings happen automatically because the owner of the business is no longer involved. Some owners put a lot of personal stuff through the business, so as soon as that owner is gone all that personal expenditure is gone as well. That means your cost savings can be found immediately.

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The seller may be sitting on a large balance of cash that they've left in the business because they don't like the idea of the high tax bill they're going to get when they take it out as income. It's a bad strategy – you shouldn't leave large balances in your business bank account. Now, that is their money, but we can also use that to fund the initial consideration. Let me explain.

Say there's £500,000 in the bank and we put in the sale and purchase agreement that we'll pay them the money that's in the bank as the initial consideration, it means they only get a 10% tax bill because they can use entrepreneurs' relief. So we can save them a lot of money.

Again, this is where you've got to know more about buying a business than they know about selling a business. When you understand this concept and explain it to them, they will realise that by doing it this way they are going to save themselves a fortune in tax, so effectively it's free money.

You need to keep an eye on the situation with regard to entrepreneurs relief, as it can be subject to change.

## 6. The property strategy

• If the seller owns a property and you don't want the property, then team up with a property investor.
• The property investor buys the property, providing the seller with the Initial Consideration.
• You buy the business on 100% Deferred Consideration.
• You may need to do a demerger of the property from the trading company which requires HMRC clearance and a specialist accountant.

This is a great strategy you can use when the seller of the business owns a property, typically the property that the business trades from, and you don't want it. You team up with a property investor and they buy the property, providing the seller with the initial consideration. Say the property investor buys the property for £500,000; they give that money to the seller, meaning they have their initial consideration and you effectively buy the business on 100% deferred consideration. You pay the balance over a period of time from the profits the business generates. It makes no difference to the seller where the money comes from; they've got their exit and the balance will be paid over time.

You may need to do a demerger of the property from the trading company, which can be a little tricky – not every accountant knows how to do this. However, it needs to be done properly as you need HMRC clearance. Once that's been dealt with you can effectively pull the property out of the trading company, which is what the property investor will want. You'll need good advice from your deal team on this strategy because there are always important details to warngle and every deal is slightly different.

## 7. The earn-out

This strategy is another favourite of mine because it links payments for the business with the future success of the business. This offers very good protection because it means that you are not going to overpay for the business. If the business does well then the seller is paid more, but the converse is also true; if the business takes a bit of a dip because there's something comes around that we're not expecting – like a pandemic, for example – then the seller is paid less. This is actually a really neat way of making sure that you don't overpay.

Every seller is going to tell you that the future is incredible; you might want to encourage them to create some forecasts of what they believe is going to happen over the next three years, and if you do I'll bet those forecasts will be very rosy. That allows you to say, 'Look, this business is going to do great. I've got a way of paying you that means if the business does what you say it's going to do over the next three years, we're going to pay you a lot more than what you originally were after.' That's the that's the carrot for the seller. You then say, 'If the business absolutely collapses the day after we buy it, neither of us gets anything, so we're kind of in this together.' But if they believe in their business, then what's the problem? And if the business doesn't perform as well, you pay less for it.

Typically we would do this over a three-year period. Some of my private clients are using this strategy to buy businesses on a percentage of revenue, these are businesses without any assets, typically service-based businesses, and they come to an agreement with the owner to pay maybe 20% of revenue in year one, 1%of revenue in year two, and 10% of revenue in year three, so the percentage amount diminishes over time. The reason they can do this on revenue is that they know exactly what the profit margins are in the business.

Why would you want to do it on revenue? Well, if you say it's a percentage of profit, the first thing that the solicitor for the seller is going to say is that profits can be manipulated – companies reduce their profits all the time to pay less tax. Why wouldn't they reduce their profits to pay the seller less money? It’s a very good point. So the fairest way of doing this is to pay a percentage of revenue. You can get a deal done really quickly like this because, especially if you're buying the assets, what due diligence are you really doing? You've got absolutely nothing to lose.

## 8. The director's loan strategy

The director's loan strategy is this: if the director has taken money out of the company as a director's loan, so they haven't paid any tax on it, they need to repay it on completion because it's not their money. Alternatively, they can either vote it as a dividend, if there's sufficient retained profits, or take it as PAYE, which means that 50% of it disappears in tax. People don't usually want to do that, or they can't do it because they've taken out more than they have in distributable profits, so they never can pay it back. That means that repayment forms part or all of the initial consideration.

Let me give you an example. Say the directors have taken half a million pounds out of the business and used it to buy a house. They don’t have the cash to pay it back and they can’t pay 40% tax to take it as PAYE. You are buying the business for one million.

You jump in with the problem-solver mentality we talked about earlier and say, ‘We'll help you out here. That director's loan is 50% of what we're paying for the business, so we'll show on paper that you've paid it back and then we've given to you as the initial consideration. That means that you can apply a 10% tax rate to it because that £500,00 that you bought your house with was, in fact, payment for shares and you can apply your tax relief to it.’ Again, you've got to take good advice on this. Some accountants might say you can't do that, but you absolutely can, it's all about how you position it. What you need is a deal team that says yes, you can do it, let's work out how we can make it work.

## Round up

Those are my eight ways to buy a business without using any of your own cash. However, if you do have some cash to put in that will open up the number of businesses you can buy. What I would strongly suggest is you don't put all of your money into one acquisition – do a combination of one of these strategies with maybe a little bit of your money in a way that will allow you to do a deal.

If you're not going to use any money at all you can't go out and buy just any business, you've got to choose your businesses carefully, and it may mean that you need to do a little bit more of that that deal origination, do more of that deal flow, because you've got to dig a little deeper to find these businesses. They do exist, though. I’ve bought ten businesses since lockdown and all of the deals have been done using a combination of these methods. We've also said no to loads, because I wanted ones I could buy with none of my own money, simply because the upside is so huge and it completely de-risks it from my perspective.

Buying a business using a system will be 10x faster than using trial and error – I think this is really important to remember. I see comments from people who say they've been doing a deal – or trying to, anyway – and they're really confused and overwhelmed, and it's because they don't have a process. It can take them months to get anywhere and life is too short to learn things by trial and error. I think you need to cut to the chase and say what's the process and then just implement it.

## Introducing the concept of not Paying 100% on Completion

You might be wondering how it is you get a seller who thinks they're going to walk away with all the money on completion, which most of them do, to accepting that isn't going to happen. It can be tricky, most of them have never sold a business before and so they don't know there are other ways of doing things.

It's your job to educate them as to why 'that's just not how deals are done'. Even private equity firms don't pay everything on day one, no one does, it just doesn't work like that.

I explain to people that if we were going to be paying all this money on day one we would have to go to a bank, and that's a really tough process. In that regard you are actually being helped right now by the environment that we're all currently in. It is a tough process and it's tougher now than it was even six months ago. I explain that if we have to go to a bank it might take six months to get a decision on a loan and even then the chances are fifty-fifty whether it's yes or no – and if it's no we're back where we started.

If they still insist they want all the money on day one, I say, 'Well, you know, money doesn't grow on trees.' I love using that phrase: money doesn't grow on trees. I repeat that to do that for them we'd have to go to the bank in six months' time we could be right back where we started and we need to move on with our lives. I often say that, as well, because sellers have that in their head: I just need to sell this business and move on with my life. I say what's in their head already. It's just simple psychology.

Then I say, 'Look, if you want to sell this business quickly then we need to be more imaginative.' I don't use the word 'creative' because 'creative accounting' has connotations attached. I say, 'We need to be more imaginative with what we're doing here, but I'm sure if we put our heads together we can come up with something.' Then I show the seller how they can get what they want, which is an exit from the business and some money, faster and easier if they agree to the structure that I'm proposing. That might mean using the money in the bank, using the director's loan, using the deferred consideration model and so forth. I rationalise it for them. However, there's usually some seller's anxiety around this method.

## Dealing with seller's anxiety

The fear is that they won't get paid. They're thinking, how do I know, Mr Buyer, that you will pay me that deferred consideration? How do I know you're going to pay me?

There is certainly a value here in the seller liking you and having a decent rapport with you and having already built up some trust with you, but the short answer is, 'That's what your solicitor's for!' Often, once they hear that, they accept it. In some cases they don't want to ask any more questions because they're going to show themselves up as being a bit naïve. I remind them there's going to be a big chunky contract, it's going to run to around a hundred pages – if it's a share purchase agreement it very likely will – so there's a contract that says we've got to pay you, if we don't you can sue us and I don't want you to do that. I also point out it would ruin my reputation if we didn't pay. Word would get around the sector, everyone knows everyone, it would ruin my reputation. and then I add, 'Well, it's guaranteed.'

Between those four comments – that's what your solicitor's for; it's a big chunky contract; it would ruin my reputation; it's guaranteed – you get what you want. You might want to say a little bit further down the path, that's what we do in all of our deals, every business that we own, that's how we've done it, because people feel a little safer when they know other people have done it before them.

The first thing their solicitor is going to say is they need to get a personal guarantee. That's pretty much their default setting, we could we could bring in ten solicitors and ask them the same question and they would automatically, without hearing the other people's answers, say we need a personal guarantee. We don't want to give a personal guarantee, so, how do we guarantee the deferred consideration? We use the special purpose vehicle (SPV) that's buying the business. (We'll talk about corporate structure in a moment.)

## How to guarantee the deferred consideration

The guarantee should come from the SPV that's buying the business, not from the holding company, and it should not be a cross guarantee from another business that you've got. Why? Because that gets you in hot water later. A clever solicitor will push for that but you need to push back, and your leverage is your relationship with the owner of the business.

Tell them their solicitor's being a little bit awkward, say, 'I thought we had an agreement, your solicitor is going to mess it up for us.' We want to develop just a little bit of a chink in the relationship between the seller and their solicitor, because if the seller blindly follows what their solicitor says then there are times you just can't get a deal done because the solicitor effectively talks the owner out of it. We want to keep the seller on our side.

Use the four phrases – that's what your solicitor's for; it's a big chunky contract; it would ruin my reputation; it's guaranteed – and you can also say, 'If you feel that we wouldn't pay you, don't do the deal, because I don't think you should be selling your business to someone that you feel about in that way,' and a motivated seller will probably never raise the question again.

You've planted the seed of an ultimatum – if you're going to push for this then you clearly are showing that there's no trust in us and we don't think we should buy a business from someone who doesn't trust us. It's not really a logical argument, but this is more emotional than logical.

## Personal guarantees

Let me just explain the nature of a personal guarantee. It means if there's a company default then the seller can come to you as an individual to get their money. If you say you're not going to pay, they can sue you personally. They will most probably be successful, and you're forced to pay up if you've got the cash or sell assets to raise it if you don't. The that everyone always gives is you're forced to sell your house. Now, that's like our absolute worst-case scenario and there's a lot leading up to that, it doesn't happen overnight.

When it comes to personal guarantees, you can add a clause to your heads of terms agreement to explain that the directors are not in a position to offer a personal guarantee. Then, when the solicitor says they need a personal guarantee, you say we've already agreed that we're not going to do that. Now, most of the heads of terms document isn't legally binding, so it doesn't really mean anything, but you both put your signature to a piece of paper and you play the card that the seller is going back on what was agreed.

You can also say that both directors, let's say there's you and someone else, would have to guarantee and one of you can't, which makes it not fair on the other one. It's either both or neither and one can't do it.

You might also want to explain that your assets are pledged elsewhere. For a personal guarantee to be effective there needs to be assets standing behind it. You might say, 'I bought a couple of businesses recently, as you know, and we have given personal guarantees and effectively our assets are therefore pledged to those other businesses. If I gave you a personal guarantee it wouldn't mean anything.' Now that's both true and not true. With personal guarantees there is no hierarchy like there is with a loan, for example, where you have a first charge, a second charge, a third charge and everyone knows the third charge probably won't get anything. Again, archaic system. There's also no official way of releasing a personal guarantee in the UK; an email saying you've paid the debt, we no longer are going to call on the personal guarantee is actually all you need to get. But if you explain that your assets are pledged elsewhere then you're being very upfront about it, you're showing that you're happy to give a personal guarantee but explain it would mean nothing, and therefore they want something that means nothing. Again, it's a bit of a false argument but again, this is an emotional negotiation. Also, it's a corporate purchase, it's not a personal one.

A favourite answer I use is, my lawyer won't let me. You can leave this issue to the very last moment so everyone's forgotten about it, you've conveniently ignored that paragraph in any emails that you've received, and then suddenly you're completing tomorrow, they say, ‘Oh my goodness, we need the personal guarantee,’ and you say, ‘My lawyer won't let me. If that's what you really want, we can't do the deal.’ They're so emotionally connected to ‘tomorrow's my day of freedom’ that they say let's just do it. Every seller gets to the point where they'll sign anything just to sell that business. I know, because I have myself. You just want to get it done and you start to you start to concede on points that you wouldn't have conceded on before.

Alternatively, you might just sign the personal guarantee. It depends how confident you are about the business, your attitude towards risk and whether you can handle it. I signed a personal guarantee on a lease recently and it was a tiny lease, it was £12,500 a year. I can handle that, that doesn't terrify me. Everyone has different sense of what's a big number and a small number, so it's always going to be down to the individual.

## Key points

**Eight ways to buy a business without using your own cash:**

1. You buy the company for £1
2. The consideration for the business is 100% deferred
3. You pay only a percentage of the consideration on completion
4. You use the money in the business to fund the initial consideration
5. You use retained profits to fund the initial consideration
6. The property strategy
7. The earn-out
8. The director's loan strategy

**You don't:**

- pay all the money on day one
- issue personal guarantees