ab4g

Social Firms Scotland

Acquiring Business 4 Good

An Introduction to business acquisition for third sector organisations

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BIG LOTTERY FUND

ACKNOWLEDGEMENTS

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Social Firms Scotland is grateful to all those individuals and organisations that have shared their knowledge and experience of business acquisition with us. We are particularly grateful to Social Firms Scotland's members who participated in the AB4G Programme and to our professional advisers who provided invaluable advice and guidance to Social Firms Scotland.

SOCIAL FIRMS SCOTLAND

Social Firms Scotland is the only support agency in Scotland providing multi-level support to the development of Social Firms. Our purpose is to grow the Social Firm sector in Scotland to support employment opportunities for people who are severely disadvantaged in the labour market. At a policy level we work to ensure that the political and legislative climate is conducive to Social Firm development in Scotland. At a delivery level we provide development support, training and consultancy to individuals and organisations seeking to start or grow a Social Firm. www.socialfirms.org.uk

SOCIAL FIRMS

Social Firms are a distinct type of social enterprise. They are recognised internationally as market-led enterprises, working in a wide range of sectors with a specific social mission to create employment for people most disadvantaged in the labour market. This includes people who have disability, a history of mental health problems as well as others who face major barriers to employment, for example because they have a criminal record or a drug or alcohol dependency.

ACQUIRING BUSINESS 4 GOOD (AB4G) PROGRAMME

AB4G was devised and delivered by Social Firms Scotland (2009-2012) and funded under the Big Lottery's Dynamic Inclusive Communities Fund. We worked across the third sector delivering business acquisition training and support.

DISCLAIMER

This paper cannot and does not purport to replace professional advice.

January 2013.

Contents

1. Introduction

Acquiring Business for Good (AB4G) is a programme managed and delivered by Social Firms Scotland (2009-2012) and funded under the Big Lottery's Dynamic Inclusive Communities Fund.

Recognising the potential benefits of supporting third sector organisations to acquire profitable private business and convert them to social enterprises, our aim was to raise awareness of and provide support to third sector organisations that were looking to grow through acquisition as opposed to other methods, such as start up or replication.

The programme worked across the third sector delivering business acquisition training and support. One of our key areas of support was to assist social enterprises and charities to acquire profitable private businesses and convert them to social enterprises/social firms. We also supported organisations looking to work together, develop partnerships or merge, either within the third sector or across sectors.

Purpose of this publication

The purpose of this publication is to provide some practical information based on Social Firms Scotland's experience and learning from delivering the AB4G Programme. It provides information on the acquisition process and some useful hints and tips to any organisation considering growth through business acquisition. It is not intended to be an evaluation of the AB4G programme; rather, we have collected some useful elements from the delivery of the programme in order to:

- Encourage enterprising third sector organisations to consider business acquisition as a method of growth
- Provide a framework for approaching business acquisition
- Highlight some of the common pitfalls in order to give some guidelines for risk management during the business acquisition process

This is not intended to be a handbook for conducting mergers and acquisitions in the Third Sector, but aims to provide an understating of the acquisition process. Bear in mind that every acquisition deal is different and every deal requires assistance from professional advisors who have relevant expertise.

Who might find it useful?

The paper is aimed at enterprising third sector organisations (including social enterprises, housing associations, charities, community groups, development trusts and social firms) who are interested in acquisition as a route to growing their organisations.

2. AB4G Programme Experience

Social Firms Scotland embarked on the AB4G programme in 2009 and worked across Scotland providing advice and training on mergers and acquisitions, bespoke organisational growth support and direct deal support to third sector organisations.[1]

Whilst the Programme focused primarily on supporting the acquisition of profitable private businesses by third sector organisations, we also supported a variety of partnership, merger and joint venture processes across the third sector. Social Firms Scotland worked with a pool of trusted professional advisers from the private sector who provided support to our acquisition deals, delivered training sessions alongside the AB4G team and delivered professional advice as required. The breadth of the advisers who worked with the programme is listed at AB4G website[2].

Support delivered through the AB4G programme

Social Firms Scotland engaged with 120 third sector organisations during the four years of the programme. In addition, we also delivered intensive support to 73 organisations who expressed an interest in growing through acquisition. Our support covered all stages of the acquisition process, from business planning, working with professional advisers from the private sector to support valuation, due diligence through to accessing funding and finance. A series of Business Acquisition Master Classes and 'Getting Ready to Buy' workshops were also delivered with the support of our professional advisers.

We worked with a range of third sector organisations across Scotland, including Social Firms, development trusts, housing associations, community groups and charities. At programme closure (Dec 12), we supported 11 deals in Scotland which included business acquisitions, mergers, joint ventures and partnerships. Further information on deals supported is given in Chapter 16.

Useful resources

As part of AB4G, Social Firms Scotland produced a range of useful resources and reading materials relevant to business acquisition in the third sector, many of which are available on AB4G website. These include:

- Case studies of deals we have supported to completion
- A short film with testimonies from third sector organisations who received support as part of the programme[3]
- An independent interim lessons learned report
- A series of acquisition blogs and online vlogs available at YouTube channel[4],
- Template documentation relevant business acquisition

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[1] The AB4G programme delivered some support outside Scotland, including in England and Jersey but these assignments were not within the direct focus of the programme and so have not been counted in the various figures in this section.

[2] http://www.acquiringbusiness4good.com/partners/

[3] http://youtu.be/_GHdmChwFfM

[4] http://www.youtube.com/user/ab4gscotland

3. Strategic Organisational Growth

Business acquisition can be described as one method of growing a business or third sector organisation but there are a variety of methods of growth. A corporate acquisition occurs when one business buys another and ends up controlling it. Along with merger and franchising, acquisition is a typical route to business growth that doesn't involve building up a new business from scratch.

The following section provides a brief overview of various growth strategies and highlights some points of comparison.

Reasons for growth

The first step in deciding how to grow an organisation is to determine and agree what it is seeking to achieve. For third sector organisations, this will be a strategic board decision and should be aligned with the organisation's mission. Some reasons for growth are outlined below:

Increased income; Improved or increased social outcomes; Improved and measurable social impact; Eliminate competition; Achieve economies of scale & efficiencies; Reach new geographic areas; Reach new clients; Reach new supporters; Reach new beneficiaries.

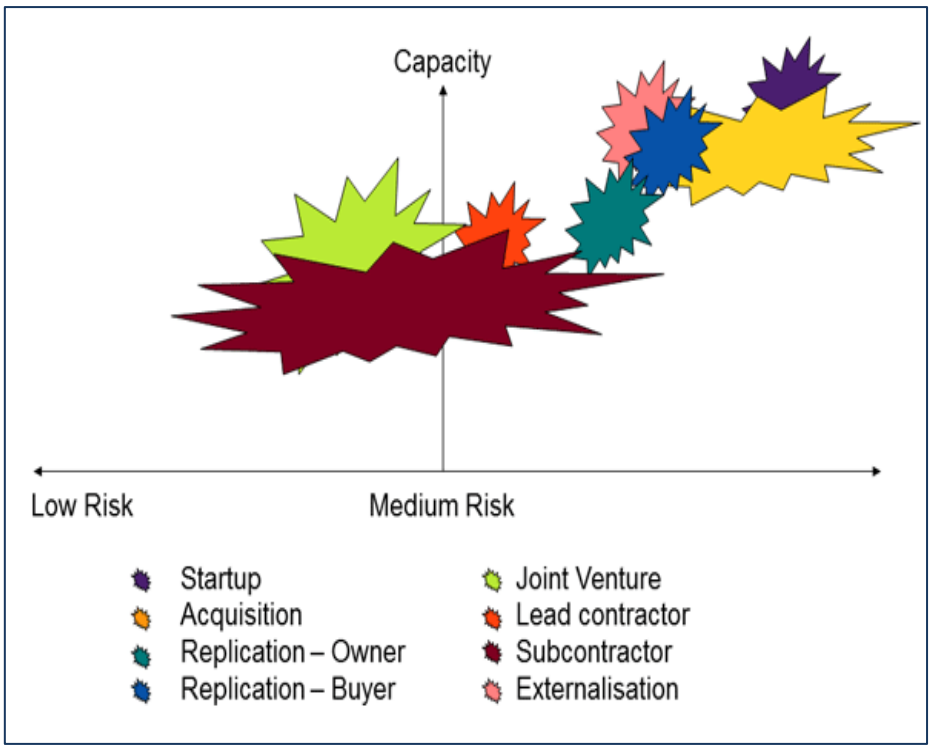
Once the **aim** has been agreed then the organisation can assess its operating environment and circumstances and consider which growth strategy would work best to achieve the desired aim. Third sector organisations will be presented with different **opportunities** for growth at different times and a SWOT (Strengths, Weaknesses, Opportunities and Threats) analysis can be a helpful starting point when assessing an organisation's options around growth plans, and importantly when thinking about how to identify and manage any associated risks.

Growth options

Figure 1 below compares various growth methods on axes of Capacity and Risk. The various options are defined in this section. Some points of comparison to consider when reviewing various growth options are:

Access to funding and finance; Internal resources required; Support available; Timescales and impact creation; Control & Ownership; Delivering a known service versus creating something new.

Figure 1: Growth Options



Some Useful Definitions

Start-up is the creation of a new social enterprise from nothing but an idea. There is a strong focus on start-up within the third sector with funders and intermediaries providing support for organisations to do this effectively.

Acquisition is the purchase of a business or parts of a business from its owners. This paper provides more information on this growth method and how the AB4G programme has supported acquisition in Scotland.

Replication is the copying of one organisation's business idea by another. Historically informal replication has occurred in the third sector where organisations share their processes and ideas with each other. More recently there has been recognition that the 'sharing' activities cost the **Owner** organisation time and money, leading to some charges for supporting replication paid by the **Buyer** organisations. More formal replication models are licensing and franchising, each of these provide progressively more support from the Owner to the Buyer and usually incur a greater cost for the provision.

Some third sector organisations choose to buy a private sector **license or franchise**, for example Ben & Jerry's[5]or O'Briens[6]. These can be provided in a social partnership model (like Ben & Jerry's) or in the usual private sector method. Replication whether through informal sharing or licensing or franchising does not deliver a *business in a box* but is a useful way of growing where the new organisation can benefit from best practice, tools and

[5] http://www.benjerry.com/activism/peace-and-justice/partnershops

[6] http://www.obriens.ie/franchising.html

ideas that have been developed by another organisation[7].

Joint Venture is when two or more organisations choose to work together within a new venture in partnership[8]. Often each organisation contributes to a joint venture from an area of activity where they have a good track record of delivery, allowing the other organisations to contribute complementary experience and resources. The joint venture could be a joint project, partnership (formal or informal) or a new organisation which is jointly owned and legally constituted. Different types of partnership are discussed in this Guide.

Contracting together is one method of partnership delivery that is becoming more common. Sometimes organisations use a joint venture to deliver a contract in partnership, or they can work together purely in relation to a contract. In this case, one organisation needs to be the **Lead Contractor** who leads and manages the complete contract delivery; other organisations in this model become **Sub Contractors** who are accountable to the Lead Contractor for delivering their activities under the contract.

Externalisation is a third sector process where a project or division is spun-out of a local authority, NHS trust or charity to create a social enterprise. It has been a popular method of creating social firms in the UK.

[7] There are a number of organisations working on the use of replication in the third sector more information can be found at: http://www.socialfranchising.coop/ , http://www.socialenterprise.org.uk/uploads/files/2011/11/social_franchising_manual.pdf , http://www.the-icsf.org/ , http://www.socialfirmsuk.co.uk/resources/library/can-franchising-and-replication-grow-number-social-firms..

[8] The iSE (http://www.i-se.co.uk/) toolkit on partnership and consortium delivery is a useful tool for organisations considering contracting together or joint venture creation. It can be found at http://www.acquiringbusiness4good.com/2012/06/successful-partnerships-and-consortiums/ise-toolkit/.

4. Pros and Cons of Business Acquisition

The experience developed by AB4G suggests that, for the third sector, there can be many good reasons why buying an existing company can make good business sense. There are also a number of downsides, however, that must be fully considered.

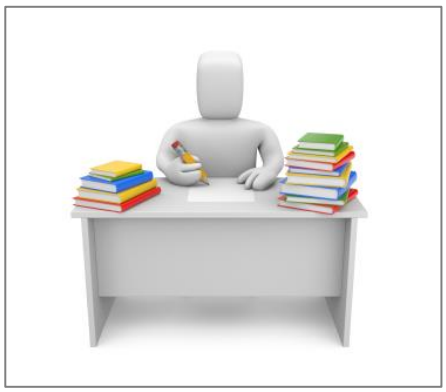
PROs

- A market for the product or service will have already been demonstrated.
- There may be established customers, a reliable income, and a reputation to capitalise and build on.
- There is the ability to acquire the valuable industry knowledge, experience and contacts that exist within existing employees.
- Most of the groundwork to get the business up and running will have been done, and many problems discovered and resolved.
- There is the opportunity for economies of scale through shared marketing budgets, increased purchasing power and lower costs.
- Strategic acquisition can assist the speed of entry into a new market through established channels.
- Buying up new intellectual property, products or services can eliminate important sources of competition.
- The acquisition of new products or services can improve and enhance the existing offering to customers.
- It may prove easier to obtain finance as the business will have a proven track record.

CONs

- Substantial upfront investment will be required to purchase a successful business, and professional fees can be high.
- Additional investment in the business together with sufficient working capital may be required to ensure success.
- The acquired company may not perform as expected or there may be undisclosed liabilities, risk factors, or contingencies.
- The role of the previous owner and their reasons for selling up must be considered and may impact upon takeover.
- The transition to a new management culture, if handled poorly can, lead to uncertainty and employee attrition.
- The departure of the former owner manager can lead to a loss of key connections and clients, leading to a drop in turnover.
- Many acquisitions result initially in above normal levels of client attrition.

5. Preparing for Business Acquisition



As a result of working with a variety of organisations across Scotland, Social Firms Scotland identified key questions to be considered prior to starting a business acquisition process.

- **Is your organisation looking for a risk free growth mechanism?** There is no risk free growth mechanism, but then doing nothing is often risky too. A SWOT analysis and business planning will help an organisation to assess and mange risks.
- **Is your organisation ready to run a business if you are considering acquisition?** Organisations may need time to work through their strategic plans and evaluate how their board and staff are aligned to these before embarking on running a new organisation.
- **Is your organisation looking for a quick fix?** Expect a Business Acquisition to take at least 6 months to complete[9], and in many cases, much longer. There are also always integration[10] costs and/or time involved before an organisation starts to see the benefits of an acquisition.
- **Are you online?** During the AB4G programme, we found that efficient storage and sharing of information is useful for facilitating acquisition deals. Inevitably trustees and directors, members of staff, advisers and the seller are seldom available at the same time, and as a result online document management[11] is useful for sharing information, emails and deal status. It is also helpful to store information related to a deal in a secure online forum where it can be both tracked and accessed by everyone authorised to support the transaction[12].
- **Is your organisation ready to commit the time and resources required to make an acquisition work**? It is considered good practice to create a deal team at the start of an acquisition process. This usually includes a deal champion (Board member), a lawyer, an accountant, a project manager and an administrator. This team is usually given clear parameters within which it can operate and when it should bring issues to the board for decision making.

  In our experience of supporting third sector organisations at the initial stages of acquisition, between £5k and £10k has been required to cover the costs of an initial valuation (of a target company), planning, advice, surveys and early stage due diligence. Depending on the size of the deal, its industry and any growth plans.

  Additional finance will be required to support the costs of the transaction to completion, for example for due diligence costs, for purchasing the business, and to cover any investment needs in the newly acquired business.

[9] "complete" / "completion" – when the deal is legally completed. At this stage all the contracts are signed, the agreed initial **consideration** (payment) is made to the **vendor (seller)** and the business belongs to the new owner. Until completion occurs there is no deal agreed, and the deal may **abort (fail)** at any stage.

[10] **Integration** – the process of taking any business that has been acquired/merged with and developing new synergistic ways of working. The first 6 to 12 months after completion are more likely to cost extra money than to generate cost savings.

[11] AB4G used Basecamp for this support as it was cost-effective. (http://basecamp.com/) However there are many online project management tools.

[12] AB4G blog on this topic: http://www.acquiringbusiness4good.com/2012/04/onlinedealmanagment/

6. Business Acquisition Process

Once an organisation has decided to acquire a business, there are some key steps in the process shown in **Figure 2** below**.** This process is well documented and includes all the steps for completing an acquisition, both essential steps and additional ones which might be specific to an acquisition deal.

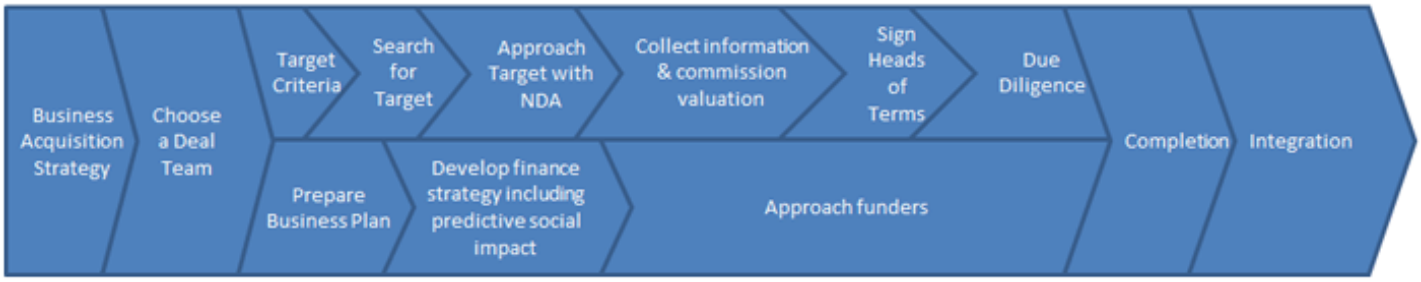
Figure 2: Key Steps in the Acquisition Process

Essential Steps	Additional Steps – deal specific
• Valuation • Heads of Terms • Due diligence • Completion and Integration	• Business Acquisition Strategy • Target Criteria • Preparing a Business Plan • Developing a Finance Strategy including predicting Social Impact and Approaching funders

For example, where an organisation has not specifically planned for buying a business but a seller approaches them with a possible target, the purchasing organisation usually ends up skipping a number of steps i.e. developing Target Criteria. The organisation will review the opportunity against their overall strategic business plan and mission. The organisation is still following the essence of the framework by considering the strategic value of the opportunity rather than simply embarking on a Valuation.

Another example of how the process may not be followed step by step is if an organisation is investing its own reserves in a Business Acquisition therefore a full acquisition specific Finance Strategy may not be required but a predictive social impact assessment may be included to support the business plan. However it is **critical** for an organisation to review the **forecast financials** to see whether the deal would be a good investment.

Businesses and organisations (including the Third Sector) are accountable to their stakeholders for managing the organisation prudently and using the process below as a framework will be helpful.



7. Preparing a Business Plan - Acquisition and Finance Strategy

Process and planning are integral to business acquisition that can deliver the financial and/or social aims of the purchaser. The main areas of planning that should begin as soon as an organisation decides to pursue an acquisition strategy are:

- Create a deal team
- Understand the deal process
- Develop a business plan with clear acquisition target criteria
- Start to investigate where the finance for the deal will come from

Acquisition Business Planning

Developing a comprehensive business plan to support an acquisition and the raising of finance to fund the acquisition are inextricably linked. The business plan provides a clear path for integrating the business into the purchasing organisation, supports managing the new business to achieve the organisation's aims and provide a basis to support any investment requirements.

Social Firms Scotland produced a Business Plan Template that explains what is important to be included in each section when seeking funding or support for a business acquisition.

Funding and Finance

The greatest learning around funding and finance for business acquisition from AB4G has been that both social funders and third sector buyers are learning how it works. The difference between funding a business acquisition and a project is that a business acquisition could abort at any stage, having spent time and money but not actually completed. In addition to this issue it is important to consider funding of the various stages within a matrix of different types of finance.

When considering finance and funding of a business acquisition it is important to consider the resource requirements for different part of the acquisition process, including any implications of State Aid[13].

Social Impact

In the third sector, measuring the social impact of activities is very important. When thinking about social impact in terms of measurement you will need to consider the change that happens as a result of an action or activity. Many organisations and agencies (including funders, government and commercial businesses), wish to maximise the positive impact their activities have on society. There are a variety of methodologies and tools to support organisations to measure their social impact, Social Accounting and Social Return on Investment being some of these. Contact Social Firms Scotland if you require further information on measuring social impact.

As part of the AB4G Programme, Predictive Social Impact Assessments were completed to support a number of organisations' business and financial strategies. A predictive assessment also allows an organisation to consider the impact buying a new business will have; what they wish to achieve; what is likely to change and how they will measure and evaluate these changes.

[13] A brief introduction to State Aid by one of our advisors has been included in Appendix 3.

8. Creating a Deal Team

There are various skills, knowledge and expertise required in a deal team to manage an acquisition deal from start to finish, including reporting to the purchaser's board or trustees. It is important that the deal team has clearly defined roles, responsibilities and the authority to move the deal forward in a timely manner. It is recommended that a deal team is established as soon as possible to make the flow and management of information much easier and effective.

It is **essential** that staff members who are part of the deal team are **kept up-to-date** during all stages of the deal.

Key roles in an acquisition deal team are:

1. **Deal Champion** – a board member/trustee with the authority to lead and oversee the deal, whilst ensuring that the board is kept up to date on progress. This would include making sure that the board is included where necessary in any decision making that require board approval.
2. **Project Manager** – a member of staff/consultant who is responsible for co-ordinating and managing the deal transaction from start to finish. Developing appropriate action plans/business plan etc, to support the deal process, allocating/delegating tasks where necessary to other members of the team.
3. **Administrator** – member of staff or consultant who is responsible for managing documents and information flow.
4. **Financial accountant** –conducting valuation and full due diligence, advising on deal structure and documentation
5. **Corporate lawyer** – advising and drafting all documentation, managing due diligence and contract management

It is important that the professional advisers you choose are lawyers and accountants who process SME (small and medium sized enterprise) deals on a regular basis. For example it is recommended that you use an accountant who regularly values businesses and conducts financial due diligence of acquisition transactions rather than an accountant who specialises in auditing accounts.

There are certain 'specialist' advisers that you may need to engage for specific aspects of a deal (not part of the deal team), for example: *Employment lawyer; Tax and VAT adviser; Pensions adviser; Surveyor; Architect; Other specialist professionals e.g.: environmental surveyor*.

When seeking **specialist advice** please be aware that there will be **cost implications** to consider.

See Blog - http://www.acquiringbusiness4good.com/2012/01/building-your-deal-team/

9. Identifying and Approaching the Target

More often than not the purchasing organisation needs to seek out a target company that meets its acquisition criteria but occasionally a seller will make a direct approach to a potential buyer.

How to find Target Businesses:

1. **Identify Target Criteria.** These can be as simple as preferred location, size (by turnover or employees), or industry sector, profitability and whether the business has a strong asset base. Sometimes you might be looking for products and services or particular knowledge or skills in the employees that would make a business fit with or adds value to your current organisational aims.
2. **Check out your neighbourhood.** Once you know what you are looking for you can start to make a list of suppliers, customers, businesses in your community and even competitors that match the list.
3. **Approach potential targets.** It is possible that you can approach potential target organisations yourself with an opening like "We are looking to grow and develop our organisation through acquisition, your business fits our criteria and is a good ethical and cultural match with ours - would you consider selling?"
4. **Request an approach.** If a direct approach is considered inappropriate then professional advisers might offer to approach businesses on your behalf. This is usually on an anonymous basis; they introduce the enquiry on behalf of a client who might be interested in buying the target.
5. **Ask for a search.** Some professional firms have a list of businesses for sale. On the basis of your criteria they could potentially do a search for you to find out if any businesses are on the market that meets your criteria. This may or may not be a chargeable service.
6. **Brokers and Estate Agents.** During the AB4G programme working with buyers in the third sector, we have found this the least effective method of finding a target.

Once you have identified a target business which is open to discussing selling, it is recommended that you **resist asking** for sensitive information regarding the business until a **mutual confidentiality agreement** sometimes called a **Non-Disclosure Agreement (NDA)** has been signed. Only then should you start requesting commercial information which is necessary to evaluate the business and its value.

10. The Importance of Confidentiality

The importance of **confidentiality** cannot be underestimated in a business acquisition context.

A Confidentiality Agreement (also called a non-disclosure agreement or NDA) is a legally binding document in which a person or business promises to treat specific information as a trade secret and promises not to disclose the secret to others without proper authorisation.

Any profitable business depends on retaining key competitive advantage in the market and trade information should be legally protected through contracts and agreements to ensure that any prospective buyer does not use any information accessed during deal discussions to their advantage without further thought about the loss to the rightful owner.

Not all information in the business will be considered confidential. A confidentiality agreement allows the parties involved the opportunity to establish clearly defined levels of information security. As such, both parties agree on which information falls within the confidential arena and which information is commonly known.

Deals may involve buyers and sellers who live in the same community and who will continue to live in the same community after the deal is complete. One question often asked is how to move from the casual chat about a possible sale to a more formal enquiry? The use of a 'Mutual Confidentiality Agreement' between both parties shifts the deal from that of a 'casual' conversation to a more 'formal' process and often establishes whether a seller is indeed interested or ready to sell.

A confidentiality agreement not only enables the purchaser to gain access to sensitive business information but minimises any potential uncertainty for employees who may be alarmed to know that the business they work in is possibly being sold. At this early stage of the potential deal it is crucial that any discussions are contained and limited i.e. to key individuals - the buyer, the seller and adviser(s). It is important to remember that a good business relies on a loyal and skilled workforce to achieve success and any buyer would wish to retain valuable employees within the business going forward.

11. Valuation

It is **essential** that purchasers request an **independent valuation** of the target business from an experienced adviser who conducts business valuations on a regular basis. This is important both to funders and to the various stakeholders to whom your organisation is accountable.

During the AB4G programme, our professional advisers have been able to complete an initial valuation for between £500 and £1,500 (plus VAT), depending on the size and complexity of the business. It is possible to keep the cost of valuations down by collecting relevant information from the seller and making it readily available to the deal team/advisers. This then allows the adviser to spend a minimum amount of time on the actual valuation, rather than spending their time chasing information from the sellers.

The **minimum requirement** for a valuation is the full accounts and management accounts by month for at least 2 years. However Social Firms Scotland introduced a standard **Valuation Checklist** which was provided by a core adviser, Gareth Magee from Scott-Moncrieff. It includes a number of items to consider for a valuation and also allows some early stage due diligence to be completed. For example, knowing the number of staff and whether they have contracts may or may not assist in the valuation directly but will help with business planning, and also assist in demonstrating how ready to the seller is to proceed.

In our experience of working with sellers, if a seller has made sure that all their agreements are reflected by signed contracts, who has good management information figures readily available and, who has all their paperwork up to date is someone who is ready to sell. The benefit to the seller is that by demonstrating that their business is transferrable they can potentially achieve a quicker sale and sometimes a higher valuation.

See Blog - http://www.acquiringbusiness4good.com/2012/02/ideal-seller/

When **assessing value** there are three main approaches:

1. Asset based value
2. Turnover based value
3. Enterprise value (combines asset and turnover based value).

A professional who advises on the value of a business regularly will not only know the most appropriate method of valuation for your target company but will also apply various formula to the initial value to reflect the current state of the industry, the current deal market, and the size of this particular business. In addition to providing a valuation based upon analysing historical results and 'normalising' them where necessary and reviewing projections from the target, your financial adviser(s) may also assist you in developing your business plan and identifying the value by:

1. Adjusting figures for any synergies or economies of scale the deal will offer the purchaser*
2. Adjusting the resultant combined group figures*
3. Completing group projections*.

*These services have not been provided by advisers through the AB4G programme, but are offered as additional services with associated costs.

12. Heads of Terms

Once you have a valuation from a professional adviser and have your initial business plan prepared, you are ready as a purchasing organisation to approach the seller with an offer in the form of a Heads of Terms (sometimes called Heads of Agreement). The Heads of Terms provides a framework to reach an agreement on; **what is being purchased, at what price, how it will be paid for and a purchase date.** This then allows due diligence to progress. Heads of Terms are not binding documents except for their confidentiality[14], exclusivity[15] and legal country[16] clauses.

In corporate deals, reaching Heads of Terms can be a lengthy process involving many advisers; however the size of deals that were supported through AB4G were generally less complex and so the drafting of a Heads of Terms was introduced early on in the process as a starting point for negotiations.

It is recommended that a draft Heads of Terms is completed by the purchaser, detailing as much information as possible but most importantly their **offer price and how they intend to pay.** The purchaser should then present this document to the seller at a joint meeting where the negotiations usually begin.

The benefit of a meeting is that both parties begin to develop a relationship that will assist with moving the deal forward. The legalities of a deal are of course important but equally, being able to agree a price and the terms of payment face to face is also important. It is recommended that professional advisers are involved where necessary.

It is also **important to note** that the price agreed in the Heads of Terms is the starting point for negotiations and is subject to the due diligence process. During due diligence the purchaser may **discover extra value**, or they could **discover liabilities** which they would use to 'price chip'. (Price chipping simply means reducing the price based on the possible costs that any liabilities would create in the business). Sometimes price chipping is not the best method of protection, and further due diligence, changing the deal structure, warranties[17], insurances or indemnities[18] could also protect the purchaser any liabilities uncovered during due diligence.

Deal Structure

The deal structure covers the type of deal, as well as the timing and type of finance.

Important questions to be answered:

- What is it you are actually buying?
- What does this actually mean?

[14] Continuation of the mutual confidentiality agreement.

[15] Guaranteeing a period of exclusivity during which the vendor will not negotiate with another potential purchaser.

[16] This specifies under which country's legal system the transaction will be completed.

[17] Warranties are provided by the seller to the purchaser to reassure them that the business has no hidden liabilities. In order to get re-imbursed for a breach of warranty the purchaser needs to prove in court the breach caused a monetary loss.

[18] Indemnities are similar to warranties in that they are provided to reassure the purchaser by the seller, however should an indemnity be breached then the seller is under legal obligation to reimburse the purchaser pound for pound for the cost of liability.

One thing for certain is that **all the employees' transition over to the new owner with the business**, regardless of the deal struck.

Types of purchase

- **Share Purchase**

The simplest method of buying a business is purchasing the shares of a company. In essence the purchaser pays the shareholders for their shares and receives the entire company in return. All legal entities that do not have shares are excluded from this form of acquisition.

For shareholders, selling their shares means only **paying tax once** on the money received.

For purchasers, historic liabilities are purchased along with the assets and income, creating additional risk which needs to be managed through due diligence and legal advice relating to the purchase agreement. An additional consideration is whether everything you, as a purchaser, expect to be included in '*The Business'* is actually owned by the company? For example, we have found that on occasion, vehicles or website domain names can be owned by private individuals and not the company. If this was the case then these items would need to be specified and acquired separately from the shares.

There are other types of businesses that do not have shares, e.g. sole traders and partnerships and there are occasions where you may not want to buy everything that belongs to the company or business. Also a business may be contained in different entities. In these instances you would buy the elements of the business that you wanted through an Asset Purchase.

- **Asset Purchase**

For sellers this type of purchase can entail **tax implications** – the purchaser buys the chosen assets from the entity who owns them, usually requiring tax to be paid on the profit, and then the sellers receive their money from that entity with the possibility of a second tax payment being due. For purchasers an Asset Purchase entails inheriting less liabilities and therefore it can require less rigorous due diligence, but **hidden liabilities** can be attached to various assets too. In this case, the purchaser may be faced with owning a business, which may or may not be '*The Business'* as initially offered for sale or detailed in the Heads of Terms.

Finance and structuring the deal

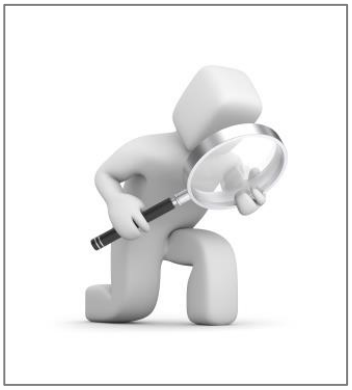
This section is about how much the purchaser is paying the seller for the business and when the payment(s) will be made.

It is quite common for an amount of the purchase price to be kept back for post-completion accounts. This depends on the size of the deal and the type of business – it can be as simple as reviewing stock in a business, for example. Your professional advisers can assist with the deal structure which best protects the buyer's interests.

There are a number of other instances where the seller does not receive the full payment on completion. For example an amount may be retained for future payment against the business reaching performance targets – this is known as an 'Earn out'. *Earn out is* a contractual provision stating that the seller of a business is to obtain additional future compensation based on the business achieving certain future financial goals. The financial goals are usually stated as a percentage of gross sales or earnings.

The value of a business is part based on its **future potential earnings**; sometimes a purchaser will only be willing to pay a price based on historical earnings and **not** a seller's asking price based on projected earnings. An 'Earn out' provision structures a deal so that the seller receives an amount over and above an agreed price **only** if the business achieves a certain level of earnings over an agreed period of time.

13. Due Diligence



When buying a business, 'due diligence' refers to the process of reviewing all of the available information related to that business so could be described as 'getting under the bonnet of the business'. The aim of conducting due diligence is to make sure that all legal and financial issues pertaining to the business are in order and that there are no unpleasant surprises i.e. hidden liabilities, should you decide to go through with the purchase.

Generally lawyers and accountants conduct due diligence on behalf of the purchaser. The amount of money spent on due diligence should be in proportion to the value of the business being acquired but this is not always the case. Experienced professionals will conduct an initial due diligence on the target business and advise if further investigation(s) are required based on their findings, industry knowledge and expertise. It is important to be able to discuss how much you would like to spend on due diligence in order to protect the deal, and what the risk of not doing further due diligence could be.

Due diligence Checklist

The importance of Due diligence and what this process might throw up for the buyer cannot be underestimated since post-due diligence, the purchaser should be ready to make a decision on whether to move to completing the acquisition.

As part of AB4G Programme, our legal professional advisers at bto solicitors produced a Due Diligence checklist which captures all the key pieces of information that should be collected from the seller. This checklist includes but is not limited to the following sections:

- Fixed Assets
- Intellectual property
- Current Assets
- Liabilities
- Banking
- Competition law
- Employees, trade unions, pensions
- Contracts
- Insurance
- Insurance
- Charges and mortgages
- Facilities and licences
- Litigation
- Corporate authority
- Stamp duty
- VAT
- Grants
- Business name, printed stationary
- Trade associations

Please contact Social Firms Scotland for further information.

14. Completion

At completion a 'Share Purchase Agreement' (SPA) or 'Business Purchase Agreement' (BPA) is signed together with all the other documentation required (see below) to finalise the transaction and the agreed consideration is paid. At this stage all the required signatories must be present from both parties and all the required consents must be signed.

Share Purchase Agreement[19]

The Share Purchase Agreement (SPA) forms the main part of the transaction completion and includes the following areas:	In addition to the SPA there are two further key documents which are needed:	Finally there are additional documents which may be required to complete the transaction. These could include:
• Details of shares being sold • Price of shares and agreed adjustments (if any) post completion • Restrictive covenants placed on the seller preventing them from competing with the purchaser after the sale • Any warranties the seller gives the buyer • Any conditions necessary to the completion of the deal – e.g.: competition law clearance. • Arrangements for the transfer of the pension fund.	1. Tax Deed This provides that if the target has unexpected tax liabilities prior to completion the vendor will compensate the purchaser for them 2. Disclosure Letter The seller's opportunity to reveal to the buyer any possible issues relating to the target, once these issues are disclosed they cannot form the basis for a claim by the purchaser in the future.	• New employments agreements for the seller/key employees • On-going agreement for supply of services between the seller and the target • New lease • Administrative documents including: board minutes, resignation from the board of those stepping down at completion, stock transfer forms and other forms required to register the transaction at Companies House.

Business Purchase Agreement[20]

A business purchase is the transfer of the assets and liabilities relating to a target business. Usually more documents are required for a business purchase as there is more choice of what is being acquired, in contrast to a share purchase agreement where everything owned by the company is automatically acquired. We have described some of the most important aspects of a Business Purchase in this section however; the various ancillary documents and necessary sections of an agreement will differ with each deal.

[19] "Mergers and Acquisitions", Consultant Editor Jonathan Reuvid, Kogan Page, London and Philadelphia, 2007 Jonathan Reuvid, Chapter 4.4.

[20] Ibid. Jonathan Reuvid, Chapter 4.5.

Documents required completing a Business Purchase:

Disclosure letter	Business Sale Agreement including:	Ancillary documents could also include:
The seller's opportunity to reveal to the buyer any possible issues relating to the target, once these issues are disclosed they cannot form the basis for a claim by the purchaser in the future.	a) Details on what comprises the business including tangible assets, intangible assets and liabilities. b) Agreement of the price and structure of any adjustments to the price post completion c) Warranties from the seller to the buyer about the business being sold d) Conditions of the completion of the deal e) Transferring employees f) Pensions considerations g) Tax – both stamp duty and VAT.	• Agreement to transfer intangible assets • Agreement to transfer book debts • Register all assets transferred.

Finally the acquisition process if complete and integration can begin.

15. Integration

KPMG[21] identified ten keys for successful integration which are a valuable report line for achieving business acquisition success, even for those transactions moving private businesses into the third sector.

The keys are:

1) **Director involvement** – directors and senior staff must be seen to be involved in all stages of the integration. This leads naturally from the Deal Champion being part of the deal team from the start of the business acquisition process.

2) **Clarity of Vision** – the strategy regarding the group including the newly acquired business should be settled and clearly communicated to staff from both the original purchasing firm and the newly acquired company.

3) **Develop momentum** – management need to identify and act on opportunities to demonstrate the benefit of combining the two organisations as quickly as possible, whilst bearing in mind any long term opportunities there may be in the future.

4) **Timing** – the first 100 days should be used to gain momentum with integration and its benefits.

5) **Adopt "best practice"** – the deal should be used as an opportunity to develop best practice rather than adopting the better practice from the two original organisations.

6) **Address emotional and political issues** – fear, uncertainty, lack of commitment, hidden agendas need to addressed as they can easily undermine the integration process. When in doubt communicate clearly confronting potentially emotive and political issues.

7) **Maximise staff involvement** – involve staff at all levels from both organisations in planning and implementing the integration.

8) **Communication** – on-going communication from management and directors will assist in keeping staff committed. Remember the deal team has lived with this transaction for a while so they are likely to assume that everyone knows what they know, or sees the deal the same way that they do. It is important to realise that most employees and stakeholders in both organisations need to be reassured through the provision of clear messages about the deal and the subsequent integration.

9) **Clarity of structure and roles** – prevent uncertainty and despondency by announcing the structure and roles which will apply to both organisations as soon as possible after completion.

10) **Operational involvement** – staff from operations should have been included in the purchaser's deal team to help with developing the business and integration plan.

[21] Unlocking Shareholder Value; the Keys to Success – A Global Research Report on Mergers and Acquisitions by KPMG [1991]

16. Deal Support Summary

From January 2009 to November 2012, the Acquiring Business 4 Good programme has worked with many organisations. As a pilot programme the initial target of completing 10 deals was in line with the funding of one full time deal manager supported by the Social Firms Scotland team.

Map of Engagement

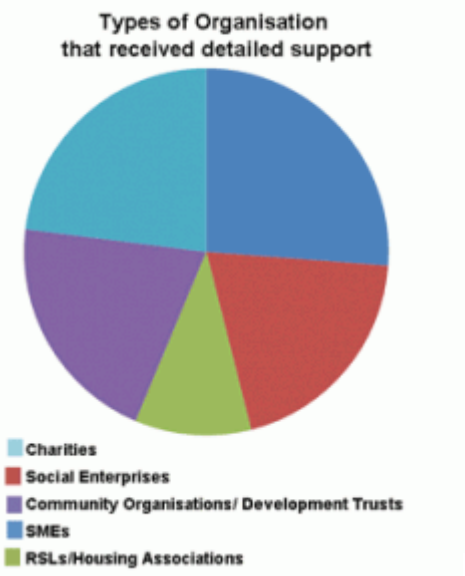
The map of our engagement shows the many places we have worked delivering general and bespoke training on business acquisition for the third sector. We have certainly covered the length and breadth of Scotland with our free support.

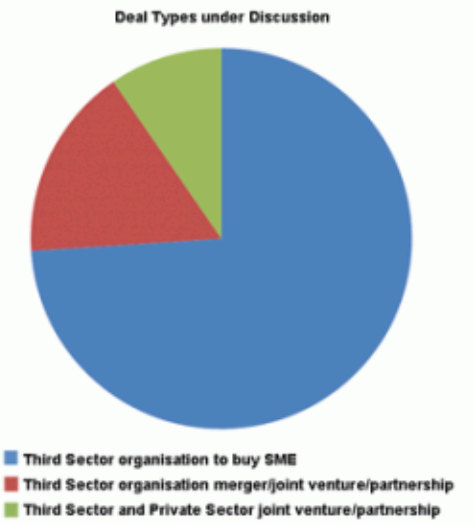
In addition to these training sessions we have handled many initial enquiries about the programme and mergers and acquisition; from these calls we delivered direct support to over 120 organisations. From these we engaged in direct deal support with 73 organisations.

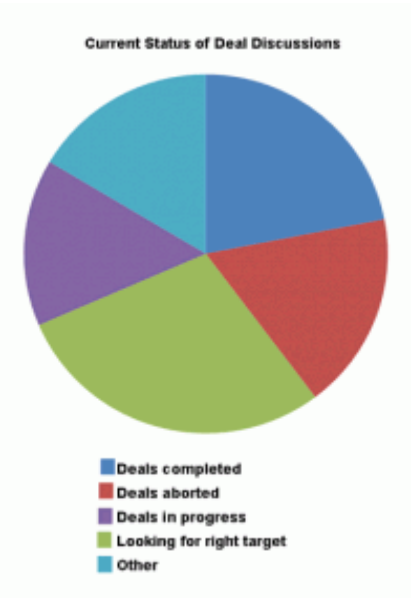
We have worked with many types of organisations and the chart on the right shows the mix of charities, community organisations, housing associations, social enterprises and small and medium sized enterprises (SMEs) that have received detailed support.

Of those organisations which chose to utilise the programme for detailed support the mix of deal types was overwhelmingly focused on a third sector organisation looking to buy a private sector SME. This split of deal type is reflected in the chart below.

The final chart demonstrates the various outcomes of programme support at the end of the funded pilot period. We have completed 11 deals which are detailed in the next section. The deals that are in progress are all progressing with a mixed package of support from various organisations including Social Firms Scotland.







17. Deals Completed

Where possible we have named the organisations involved in the deals, however some deals are by their nature confidential and therefore we have only shared the project name.

i. Project Bananas

(CFINE acquired The Fruitmart) - acquisition of a private fruit and vegetable business providing training and employment by a charity in the North East (2010).

This charity with a social enterprise trading subsidiary bought the Fruitmart. The Fruitmart was owned and managed by a private individual who provided placement opportunities for individuals with disabilities alongside the business of selling fruit and vegetables in a small village. In addition to buying the business, CFINE offered the previous owner a position as manager of the shop. This she accepted as it was not running the shop that had caused the owner to want to sell, but rather managing the business and all that entailed.

The new business immediately extended its number of placement opportunities and also served as a base for local fruit and vegetable deliveries for the school and local groups. Some of these schemes were funded through the organisation's charitable arm and some were subsidised.

The deal started in late Quarter 3 2009 and was completed by Quarter 4 2010. The deal consisted of the actual property of the shop plus goodwill for the business. It was an asset purchase rather than a share purchase.

It was funded by a mixture of local redevelopment funding and small loans. The new business was then used as the hub of a local development for which the Big Lottery provided funding.

AB4G provided negotiation support by helping the vendor to understand the deal, introducing advisers to support the process in addition to those who the vendor and purchaser already used, providing tax support to both sides, facilitating the Heads of Terms meeting where the deal details were agreed, assisting with bridging finance and finding further funding.

ii. Project PEA

Pentland Housing Association acquired Community Energy Advice – acquisition of a project from a community charity by a Housing association and its conversion into a trading business. The project employed 4 people and provided services to local housing and businesses (2011).

Pentland Housing Association took over the project by creating a subsidiary company under its Social Enterprise arm, Pentland Community Enterprises. The key aspects of the deal were the transfer of the processes and TUPE relating to staff.

For PHA the acquisition provided the opportunity to retain an important service that can tackle the fuel poverty faced by tenants, protect valuable employment within a deprived rural community, and to grow a business with significant potential. For the staff at PEA, now under the wing of the Housing Association, this provided the organisational back-up required to bolster operations and addressing 'growing pains', offered increased job security, and provided a platform for future business growth. PEA continues to grow and now works across the North Highlands including Caithness, Sutherland and Rosshire, with some contracts in Orkney and Shetland. As a CIC, all of PEA's profits and assets will be used for community benefit through the Housing Association.

PHA approached AB4G in Quarter 3 2010 and the deal completed by Quarter 2 2011. Our support was firstly to help the deal team review the process that was needed to successfully transfer the business, identify funding for facilitating the process and supporting the deal team to work with advisers who were implementing the technical aspects required.

Whilst there was not a payment to the original parent charity, funding was still required and Pentland Housing Association sourced this from a variety of sources to ensure the organisation both transferred successfully and had some working capital. The new venture has already developed new services and also employed a further member of staff. Initially this was a funded placement but when the placement ended the social enterprise was ready to employ this individual and fund their driver's training and licence, which enabled this person to be more responsible for client delivery.

iii. Project Together

This was an asset acquisition of inventory and intellection property as a charity was merged into two other third sector organisations (2011).

In Quarter 2 2011, Acquiring Business 4 Good was approached to support the merger of two charities. One was a charity with a social enterprise subsidiary and the other a charity coming to the end of a funded project. Initially the plan was to create a new subsidiary for the former organisation creating a new home for the latter. Over the next few months, due diligence and negotiation lead by the social enterprise/charity supported by AB4G brought to light a number of risk factors which resulted in two separate an asset acquisitions by the social enterprise/charity and another charity. These acquisitions supported the original organisation to windup.

iv. Aspire and The Breadmaker

This was a joint venture between a golf club and a social enterprise to run a café onsite (2011).

The Bread Maker in Aberdeen is expanding its catering services by taking over the catering at the Aspire Golf Centre, Aberdeen. The Bread Maker will run the eatery independently at the golf centre, which boasts a nine-hole course, state of the art driving range and golf shop. The Bread Maker has been running an award winning coffee house and artisan bakery in Aberdeen since 2006. The move comes after a two-year search by the charity for a new outlet to operate from within the city.

The AB4G programme provided initial investigation and contract negotiation support to this joint venture development. The new joint venture at Aspire will allow for continued growth and give the charity a second base to offer its produce across the south side of Aberdeen City and Deeside as well as providing more opportunities for adults with learning disabilities. The Bread Maker currently employs 17 staff and provides some 24 placements for adults with learning disabilities. Over the coming year, the move is hoped

to create real job opportunities for adults with learning disabilities who have developed real work skills through training at the Bread Maker.

v. Project Combo

This project was a merger between 2 charities in order to allow the two organisations to deliver more support to their clients (2012).

AB4G was approached in Quarter 3 of 2011 to support this merger which had been agreed in principle by the organisation's respective boards. It completed in Quarter 2 of 2012, the time scales were partially driven by the new financial year starting and partially by the timings imposed by the Office of the Scottish Charity Regulator (OSCR).

The focus in this deal was managing the OSCR requirements alongside the organisations' reciprocal due diligence. It is important that charities considering merging and acquisition read the relevant guidance[22] from OSCR and consult legal professionals. AB4G worked as a facilitator and a deal manager, reminding the parties of the various essential activities and legal deadlines associated with them.

vi. Ready for Business LLP

This was a joint venture created between Senscot, CEiS and Social Firms Scotland which then was the lead partner in a bid with MacRoberts and KPMG as partners to deliver a Scottish Government contract (2011). AB4G was involved in reviewing the various forms of joint venture and liaising with the legal professionals involved in the process.

vii. Bigton Community Shop

Bigton Community Enterprise, a local community co-operative, purchased their village shop from a private businesswoman, (completed Quarter 2 2012).

AB4G was approached in Quarter 2 of 2011 to support the acquisition process. The programme was involved in:

- community meetings - helping to manage expectations and confidentiality
- valuation – facilitating an independent valuation process with a programme adviser
- business plan and funding – reviewing and advising
- Heads of Terms and completion – drafting the Heads of Terms and managing the completion.

The programme worked alongside Shetland Islands Council, Highland and Islands Enterprise, Business Gateway, the Big Lottery and The Co-operative Enterprise

[22] http://www.oscr.org.uk/managing-your-charity/reorganisation-in-scotland/charity-reorganisation/

Hub to support this community acquisition. The community bought shares in the co-operative and this provided the funds to buy the business and start with the new developments that are planned. An official launch was held on 23rd June attended various local dignitaries including the MSP Tavish Scott.

viii. ACE Partnership

ACE received funding through the Scottish Government's Enterprise Growth Fund to develop partnerships. The first stage of this was with Kibble Works and Aberdeen Forward (2012).

The partnership created various jobs at the different partners' sites as well as expanding the recycling reach and capabilities of all three organisations.

Acquiring Business 4 Good supported this transaction by assisting in drafting the partnership agreement and with the various meetings required to reach completion.

ix. Roadwise

Aberdeen Foyer purchased Roadwise Driver Training (2012). This deal was completed over 5 years through Aberdeen Foyer buying out one partner in the business and then the other.

Whilst the deal started prior to Acquiring Business 4 Good's programme start, the programme worked with Aberdeen Foyer to complete the deal. This support covered both the operational aspects of the change in ownership and the legal requirements of completion.

As a result of this deal Aberdeen Foyer now own the largest independent driver training provider in the North East of Scotland. The business has been running since 1994. It is also became the first social enterprise driver training provider. Aberdeen Foyer owns the business through its trading arm Foyer Enterprise. Profit generated by Roadwise directly supports the work of Aberdeen Foyer and means the social impact of the organisation extends well beyond the existing work of creating a safer road environment for all road users.

x. Catalyst Catering

CEiS Ayrshire acquired an existing business to create its trading subsidiary, Catalyst Catering (2012)

Acquiring Business 4 Good was approached in Quarter 1 2012 to support this deal which completed within 6 months. The programme support was focused on the various legal documents required for completion.

Catalyst Catering is based in Marathon House, Dundonald and services the business park occupants; with future expansion planned to a second site in Kilmarnock and a contract catering operation. Catalyst Catering will offer meaningful employment and training opportunities for young people aged 18-24 within the café from food preparation, sales, budgeting, customer service and front of house experience to providing a contract catering service. Clients will come from the employability programmes managed by CEiS Ayrshire on behalf of North Ayrshire Council and the Community Planning Partnership.

Initially the intention is to service Marathon House and the surrounding areas. As the model develops, the venture will explore the potential to expand its external catering operations and customer base to new

areas in a small goals/steps approach. Albeit designed to enhance the individual work ethic, social interaction, technical skills, entrepreneurial ability and personal planning and development, this is a venture aimed at income generation and it will function as a sustainable social enterprise.

xi. Thurso Harbour Trust Deal

Pentland Housing Association completed their second deal in December 2012, by acquiring Caithness Sports Facilities Ltd (CSF) from the Thurso Harbour Trust who set up the company to develop a watersports centre in Thurso.

Acquiring Business 4 Good supported Pentland Housing Association with this deal during 2012. The support focused on ensuring that the transfer met OSCR requirements and positioned the organisation for future developments.

Following talks with CSF, the Highland Council and Caithness Partnership it was felt that Pentland Community Enterprises, a subsidiary of Pentland Housing Association, could provide much needed support in developing the funding bid. CSF has been registered as a Community Interest Company (CIC) and a wholly owned subsidiary of Pentland Housing Association Ltd. CSF have now submitted a bid to the Coastal Communities Fund which will facilitate the re-development of the slipway at Thurso harbour. The outcome of the bid is pending.

Map showing Deal Location in Pentland.

17. Some Key Learning Points from AB4G Programme

Lack of clarity about what you are buying

It is usually assumed that what the seller thinks they are selling and the buyer thinks they are buying are the same thing. However this is seldom the case. It is very useful to clarify assumptions and expectations as early as possible – e.g. what is actually included in the deal and what is not included. The most effective way of clarifying this is at the valuation process which should include a list of what is actually being purchased. Even when you are buying shares in a company and you expect to get **everything** the business uses to trade, there are often items which are not included e.g. vehicles might be owned by the seller's wife, or the web developer owns the web domain name[23].

Buying the business (assets) or the company (shares)

When buying a business there are two main methods: buying the shares or buying the assets and business. The first separation of methods is whether shares are available for purchase: only when you are buying a company limited by shares is this an option. If you are buying a business from a sole trader or a company limited by guarantee or a division of a company, then the shares are not part of the deal. There are different implications to buyers and sellers depending on whether you are buying the business (asset transaction) or the company (shares). Make sure you know what the seller is offering for sale. Often the word 'business' can be used to cover various legal entities and assumptions.

Mutual Confidentiality / Non-Disclosure Agreements (NDA) are important

The primary purpose of a Mutual Confidentiality Agreement or NDA is to prevent either the buyer or seller from prematurely disclosing anything about a deal during the process. This is why it should be signed when a target business is first approached by a purchaser. The secondary purpose of an NDA is to assist the purchaser in demonstrating to the seller that they are familiar with the acquisition process, and that any resulting transaction will be managed in a professional way. The signing of an NDA early on sets out clearly the expectations around confidentiality on both sides. If a seller refuses to sign an NDA and walks away prior to valuation, it has saved the purchaser time and money.

The purchaser drives the deal

In our experience; we have found that purchasing organisations are surprised to discover that they are expected to lead the deal process. Even if a seller has approached your organisation, it is up to you as the purchasing organisation to manage the transaction. The buyer usually presents the non-disclosure or confidentiality agreement, and then requests information for the valuation, and then drafts the heads of terms etc. The consequence of this is that the purchaser's costs are generally higher than the sellers.

The right professionals in your deal team are key to a successful acquisition

Throughout the AB4G programme we have seen that experienced professional advisers who regularly conduct SME acquisition deals are essential to completing acquisitions effectively and efficiently. This is due to their familiarity with both the legal requirements of business acquisition and the practical reality of completing deals, both large and small. Identifying a deal team with the right professional advisers and most appropriate staff members should be an early step in the process of business acquisition. Appointing

[23] See vlog - http://youtu.be/e2va_J-XSvc

advisers who are not familiar with acquisition deals can often cause delays, add complexity and additional costs to the process, which either causes the deal to fail or to cost much more than it should[24].

Underestimating the duration of the acquisition process

A common question at our Business Acquisition Master Classes workshops is: *How long does it take to buy a business?* It is recommended that a purchaser plan for a deal to take at least six months, however some deals can be completed quicker and some take much longer. Every acquisition deal is different and there can be a variety of factors which can affect the duration of the process.

In the deals supported through AB4G Programme, there have been two main reasons for delays:

- The **seller is not ready** or geared up to sell. For example, some sellers do not have the detailed information about their business that is required for a robust valuation and due diligence and this can causes unnecessary delays.

- The **purchasing organisation is not ready to buy**. Third sector organisations, because of their governance structures, need to ensure that both their trustees (and staff) are fully behind the decision to acquire and that they understand the process. If the board of the purchaser are not fully convinced of acquiring a business then this can lead to delays in the process. The importance of an acquisition strategy signed off by the board is critical to the organisation being able to proceed with an acquisition and in managing risk.

Both examples above demonstrate why, in our experience, it is important to include everything from agreeing an acquisition strategy to integrating the business into a process framework. It is useful for the purchasing organisation to have a clear understanding of the deal process and its requirements before initiating a target search.

TUPE always applies

The Transfer of undertakings (Protection of Employment) Regulations (TUPE) always applies in an acquisition deal. The simplest explanation of TUPE is on the ACAS website: "Employees of the previous owner when the business changes hands automatically become employees of the new employer on the same terms and conditions. It's as if their employment contracts had originally been made with the new employer. Their continuity of service and any other rights are all preserved. Both old and new employers are required to inform and consult employees affected directly or indirectly by the transfer[25]".[26]

VAT & Tax Issues

We have a detailed blog[27] on this issue however if you are buying a business that is VAT registered then in order to avoid paying VAT on the entire amount you pay for the business then your organisation must be VAT registered before completion. We recommend that purchasing organisations consult a TAX expert where appropriate.

[24] See Vlog - http://youtu.be/wadKNIEGPWM

[25] http://www.acas.org.uk/index.aspx?articleid=1655

[26] see blog - http://www.acquiringbusiness4good.com/2012/10/tupe-beyond-the-legislation/

[27] see blog http://www.acquiringbusiness4good.com/2012/06/transfer-of-a-going-concern/

Don't mention price (too early)

The price you intend to pay for a business depends on many issues (e.g. initial valuation) but the price may be subject to change within the acquisition process, e.g. after due diligence has been completed and/or during negotiations with the seller. We have found it unhelpful to discuss the price you intend to pay or the seller's expectations of the value of their business too early in the process. Key to your offer will be an independent valuation of the business you are buying, so discussing the possible offer/price with the seller in advance of receiving a valuation is not recommended. Sellers usually want more for their businesses than purchasers are willing to pay. It is recommended that you **always highlight** to the seller that your organisation will base your offer on an independent valuation.

Not knowing when to let go.

Many of our advisers cite this as the key reason for deals being completed that cost too much or don't achieve the profit margins or efficiencies expected. Sometimes the buyer can become emotionally attached to a particular target business or the buyer concludes that they have spent so much money on a deal that they should complete regardless of issues or liabilities uncovered. The process around business acquisition provides a route map for a journey of discovery about a target business. The due diligence undertaken by your advisers will provide you with detailed information pertaining to the business in its entirety and it is prudent that you do not ignore anything this throws up. Due diligence is to help purchasers identify the value and the liabilities in the target company and weigh them up, to see whether the deal will be a good one. It is foolish to ignore the evidence that this process provides and pursue a deal against advisers' advice and commercial logic[28].

[28] See blog: http://www.acquiringbusiness4good.com/2012/04/acquiring-a-business-know-what-youre-getting/

Glossary

Advisers	Professionals who assist businesses with legal, commercial, financial and other issues.
Adjustments	The difference between the price an acquiring company pays to purchase a target company and the net original cost of the target company's assets. An acquisition adjustment is the premium paid for acquiring a company more than its tangible assets or book value[29].
Ancillary documents	Documents that are required to completion in addition to the Purchase Agreement.
Asset Purchase Agreement	Document to complete a business acquisition where the assets (rather than the shares) are transferred to new ownership.
Business Acquisition	The transfer of a business from one owner to another, either through a share or asset purchase agreement.
Capital Gains Tax	Capital Gains Tax is a tax on the gain or profit you make when you sell, give away or otherwise dispose of something. It applies to assets that you own, such as shares or property[30].
Completion accounts	These are the final accounts for the target business prior to the acquisition being completed. These are usually compiled after the acquisition has been finalised and will include all transactions up to the date of signing the Purchase Agreement. These are important as often a portion of the consideration is withheld until the Completion Accounts are finalised as the price paid can be directly linked to the business value on the day of the transfer.
Compromise agreement	A **compromise agreement** is a specific type of contract, regulated by statute, between an employer and its employee (or ex-employee) under which the employee receives consideration, often a negotiated financial sum, in exchange for agreeing that he or she will have no further claim against the employer as a result of any breach of a statutory obligation by the employer[31].
Consideration	Something with monetary value that is paid for the business to the seller by the buyer, usually this is cash but it could be shares.
Debt finance	Any finance provided through a loan of some sort, this could be an overdraft or a lease. The amount of money loaned is required to be returned and usually with an agreed interest payment calculated over time.
Deferred consideration	Part of the payment for the business that has been withheld by the purchaser for a specific period of time or until a certain milestone has been met. The

[29] http://www.investopedia.com/terms/a/acquisition-adjustment.asp#ixzz2LLiiiEkF

[30] http://www.hmrc.gov.uk/cgt/intro/basics.htm

[31] http://en.wikipedia.org/wiki/Compromise_agreement

	seller agrees to deferred consideration during the deal negotiations and the conditions for it are included in the deal documentation.
Disclosures / disclosure letter	Part of the completion documentation, where the seller details information about the business to the purchaser. The purchaser is considered to have been legally notified of an issue through this letter.
Due Diligence	Process of investigation of the target business by the purchaser and their advisers. The purpose of due diligence is to identify and protect the value of the target whilst identifying any potential risks in the transaction.
Earn-out	Payment of the consideration (or part of the consideration) to the seller that is deferred and paid, as the business achieves agreed milestones. Earn-outs are often variable and linked to the proportional achievement of the milestones.
Equity	Shares in a limited company.
Goodwill	Goodwill is seen as an intangible asset on the balance sheet because it is not a physical asset like buildings or equipment. Goodwill typically reflects the value of intangible assets such as a strong brand name, good customer relations, good employee relations and any patents or proprietary technology[32].
Heads of Terms	The Heads of Terms provides a framework to reach an agreement on; **what is being purchased, at what price, how it will be paid for and a purchase date.** This then allows due diligence to progress. Heads of Terms are not binding documents except for their confidentiality[33], exclusivity[34] and legal country[35] clauses.
Indemnities	This is a contractual agreement within the documentation signed at completion. Indemnities give the purchaser the right to recover from the seller their exact losses in specified circumstances[36].
Intellectual Property	Intellectual Property (IP) results from the expression of an idea. So IP might be a brand, an invention, a design, a song or another intellectual creation[37].
Retentions	A term referring to amounts of the consideration that are kept back for payment later, for example a retention could be made to cover any changes the completion accounts reveal to the purchase price.
Share Purchase Agreement	Document to complete a business acquisition where the shares of the business are transferred to new ownership.

[32] http://www.investopedia.com/terms/g/goodwill.asp#ixzz2LLoQPRJn

[33] Continuation of the mutual confidentiality agreement.

[34] Guaranteeing a period of exclusivity during which the vendor will not negotiate with another potential purchaser.

[35] This specifies under which country's legal system the transaction will be completed.

[36] http://www.inhouselawyer.co.uk/index.php/ireland/7833-warranties-and-indemnities-whats-the-difference

[37] http://www.ipo.gov.uk/

Target	The company being acquired.
Tax deed	A tax deed is one of the documents dealt with when a buyer purchases a company or group of companies. It sits alongside the share sale and purchase agreement, and will sometimes be drafted as a schedule to that agreement rather than as a separate deed. When a buyer purchases shares in a company and takes over responsibility as owner of that company, it also becomes responsible for the tax liabilities which arise in that company. The purpose of the tax deed is to protect the buyer of a company from any tax liabilities that are referable to the period *before* the buyer purchased, and became responsible for, the company[38].
Transfer of a going concern	Business acquisition where the new owner intends to continue the business trading as under its previous owner.
TUPE	The Transfer of undertakings (Protection of Employment) Regulations (TUPE) always applies in an acquisition deal. The simplest explanation of TUPE is on the ACAS website: "Employees of the previous owner when the business changes hands automatically become employees of the new employer on the same terms and conditions. It's as if their employment contracts had originally been made with the new employer. Their continuity of service and any other rights are all preserved. Both old and new employers are required to inform and consult employees affected directly or indirectly by the transfer[39]".[40]
Valuation	The process of calculating the value of the target business.
Warranties	These are contractual assurances from the seller to the purchaser. They are included as subsidiary provisions to the Purchase Agreement. A breach of warranty claim means the purchaser must bring an action for breach and prove loss and damage that is foreseeable as a result of the breach. The seller is only liable for the loss resulted from the breach[41].

[38] http://www.out-law.com/en/topics/tax/tax-for-entrepreneurs/tax-deed-and-tax-warranties/

[39] http://www.acas.org.uk/index.aspx?articleid=1655

[40] see blog - http://www.acquiringbusiness4good.com/2012/10/tupe-beyond-the-legislation/

[41] http://www.inhouselawyer.co.uk/index.php/ireland/7833-warranties-and-indemnities-whats-the-difference

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Appendix 1 – Business Plan Template

Appendix 2 – State Aid

Appendix 3 – Non-Disclosure Agreement

Appendix 4 – Valuation Checklist