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GUIDE 5: THE 4 SUCCESSION OPTIONS

Through the hundreds of deal structures, valuation and acquisition models, the complexities of share transfers and the challenge of value transfer and tax, there are essentially four primary succession options:

Enterprise third party

- Selling the assets of the firm or the equity of the legal entity to an enterprise style firm.
- Enterprise in this context means a large business with a clear strategy, dedicated management and significant resources to fund growth.
- Executives in these firms are responsible for budgets and are therefore unlikely to be spending their own money.
- Typical deal structure will include an initial consideration and an earn-out element, the final quantum of which will be determined by the performance of the firm over the earn-out period.

Owner/operator third party

- Selling the assets of the firm, or the equity of the legal entity, to a firm that is owned and operated by an individual or small group of people, who own a significant proposition of the firm.
- Although individuals in these firms are also responsible for budgets and the resources of the legal entity, their ownership brings them much closer to the consequences of their behaviour.

- Until recently, typical deal structures would focus on deferred consideration, however capital is now available to allow these firms to offer significant initial considerations along with deferred consideration with limited adjustments.

Employees via trust

- Selling the legal entity to a trust for the benefit of the employees.
- This is an HMRC approved scheme and a firm must satisfy qualification criteria.

Management/Adviser buyout

- Selling the assets of the firm, or the equity of the legal entity, to some or all of the individuals working in the firm.
- As with a sale to an owner/operator firm, until recently typical deal structures for internal succession would focus on deferred consideration, however, capital is now available to allow these firms to offer significant initial considerations, along with deferred consideration with limited adjustments.
- Management experience should be considered along with leadership qualities and adviser capability.

Key decision criteria

While there are potentially myriad factors that contribute to a final choice of succession option, the following criteria frequently play an important role in the process:

1. Motivation – of the buyer and the seller.
2. Valuation – the approach used and the difference between a valuation and an offer.
3. Tax – the difference between selling assets and selling equity (under current rules).
4. Initial consideration – the amount payable at completion and the proportion paid in cash.
5. Deferred consideration – the balance payable after initial consideration and the terms.
6. Owner's post-transaction situation – staying on, retiring or a combination as well as the terms.
7. Transaction events – due diligence, commercial warranties, negotiation tactics etc.

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