

Deal Structure and Financing the Transaction

Deal Structure Alternatives

The structure of the deal is often more important than the actual purchase price of the business. For instance, if it is important for you to cash all the way out now, you may take considerably less for a cash offer than another offer that requires owner financing. In fact, there are numerous ways for you to get paid in the sale of your business. Some of these ways include:

- Cash - the most certain way to collect the entire sales price, but has some immediate tax consequences;
- Secured notes - the seller is paid over time out of the cash flow from the business, and has the right to foreclose as a secondary repayment source if the buyer defaults;
- Assumed Liabilities
- Unsecured notes - riskier than secured notes and limited secondary repayment source if the buyer defaults;
- Shares in the purchasing company - typically only included as part of the package when selling to a public company or a private company that can substantiate its internal valuation;
- Consulting agreement - seller is required to stay involved for a fairly short period of time (usually six months to two years) in exchange for a lower purchase price;
- Employment contract - seller is required to stay involved on a longer-term basis (usually three to five years) to help transition to the new owner;
- Leases on assets retained by the seller - the most common leases are with real estate or equipment. If you agree to this, you should require the buyer to sign a long-term lease (five years or more);
- Non-compete agreement - the seller receives payments over a period of time (usually three to five years) in consideration for agreeing not to open a competing shop down the street;
- Royalty program - the seller receives part of the sales price based on future sales generated by the business; and

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- Earnout - the seller receives part of the sales price based on future earnings generated by the business. This can be problematic if profits decline after the sale.
 - Retention of a portion of the selling business: this allows the seller to have a “second bite of the apple” at some negotiated point in the future.

Case Study that demonstrates the issues of alternative forms of consideration.

Valuation Considerations: Not all offers are “cash-only”. An example of various deal structures, demonstrating valuations by class of acquirer

- A project that was worked by Grand Avenue Capital had four offers for the company. This was for a niche private manufacturer of custom lighting products: single location, with JV in China, \$20+m revenue, \$2.5+m adjusted EBITDA
- Four offers were developed for this client:
 - **Strategic Domestic Acquirer:** Public company, cash and capped earnout term sheet: 6.5X EBITDA. No equity rollover or future upside other than capped earnout
 - **Hybrid Acquirer:** Private equity backed strategic company in a parallel market, cash, 20% retained with formula buyout on year 3 EBITDA, note and uncapped earnout: 8X EBITDA
 - **Hybrid Acquirer:** Private equity backed strategic company is identical market, cash, note and equity in acquiring company, 6+X EBITDA : 3 year horizon to sell rolled equity.
 - **Financial:** Pure play financial investors / private equity funds without platform, cash and capped earnout, 5X EBITDA

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