



# Building and extracting the maximum value from your business

Wednesday, 30 August 2023  
10:30 – 11:30 am (ACST)

**Webinar will commence soon**



**David Montani**  
National Tax Director



**Hugh McPharlin**  
Partner - Forensic Accounting



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# Introduction

- Pandemic delayed planned business exits, in particular:
  - Baby Boomers ( $\approx 59$  yrs+)
  - Elders of Generation X (up to  $\approx 58$  yrs)
- Critical factor in maximising exit value:
  - Timing
  - Exit/succession ready
  - Tax planning
- Exit planning relevant at any stage in business lifecycle

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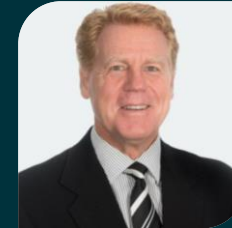
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# Today's session

- Factors that drive business value
- Compounding effect of improvements over time
- Different types of business exits
- Exit/sale/transition process
- Sell the assets or sell the company?
- Pre-sale restructuring
- Tax planning
- Maximising the after-tax sale proceeds

# Factors That Drive Business Value

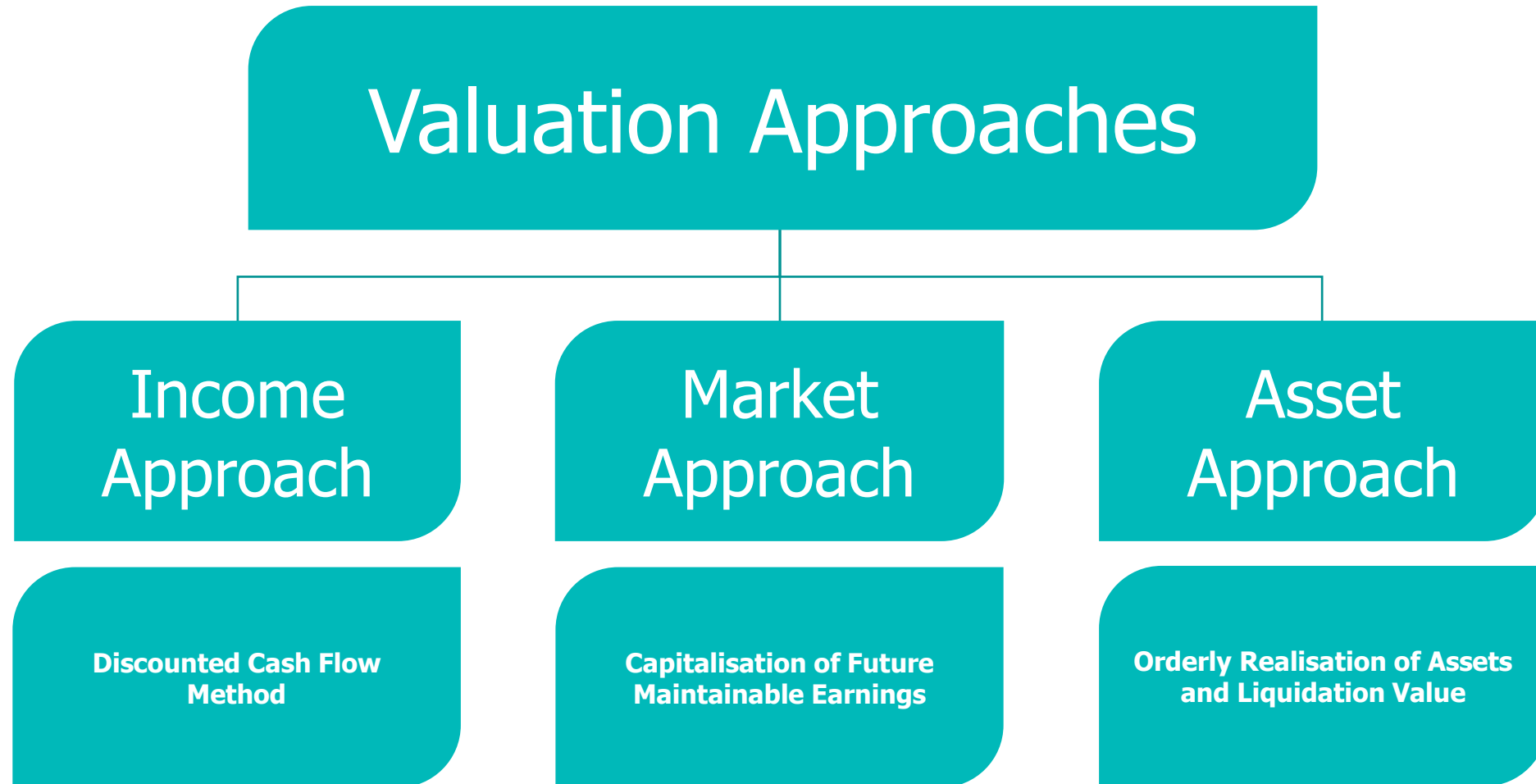
The background features a series of overlapping, wavy lines in shades of teal and pink, creating a sense of motion and depth against a dark teal gradient.

# What Drives Business Value?

- Cash flow and profitability, track record, and potential for growth
- Market position, sustainable competitive advantage(s), barriers to entry
- Management, systems and operating separation from owners
- Customers: quality, sustainability and spread
- Suppliers and other personnel: locked in, diversified, replaceable
- Factors that reduce risk



# Valuation Methodologies



# Normalised Earnings

- An important concept in Business Valuation
- Normalisation of:
  - Non-recurring/abnormal transactions (both income and expense)
  - Restating related party transactions to be commercial (remuneration, rent, etc)
  - Depreciation (subject to the measure of earnings)
- Actual method of funding probably ignored (subject to measure of earnings)
- Actual accounting policies of little relevance, valuation is a pragmatic/realistic/forward-looking process

# The Value Equation

## Market Approach



# How to Maximise Value

- Understand the business
- Be prepared (for the sale)
- Pick your moment
- Enhance features
- Cover-off on deficiencies
- Work on the factors that drive business value
- Be prepared to walk away

# The Roadmap to Success

- Indicative valuation
- Plan – now / where to / how
- Monitoring goals and objectives
- Work on factors which drive business value
- Get sale ready

# Benefits of Improvements - Earnings

	Base Case	Improvement	
Earnings (EBIT or EBITDA)	\$1.0m	\$1.1m	Increase revenue
Price Earnings Multiple (say)	4.0x	4.0x	Increase gross profit margins
Enterprise Value	\$4.0m	\$4.4m	Reduce overheads

# Benefits of Improvements – Price Earnings Multiple

	<b>Base Case</b>	<b>Improvement</b>
EBITDA	\$1.0m	\$1.0m
Multiple	3.75x	4x
Enterprise Value	\$3.75m	\$4.0m

Reduced working capital need

Better contract terms or quality of customers

Increased market share

Engagement with new technology

Enhance management team

Lock in supply arrangements.

# Types of Business Exits

## Common Exit Options

- Trade Sale – sale of business or shares/units
- Partial sale
- Management Buy Out (MBO)
- Initial Public Offering (IPO)
- Orderly realisation followed by deregistration or winding-up



# Exit, Sale & Transition Process

- Sale ready, marketing materials, transaction team & Non-Disclosure Agreement (NDA), data room
- Identify potential buyers
- Release of initial financial information
- Execute Non-Binding Indicative Offer (NBIO)
- Due Diligence (financial, tax and legal)
- Execute Binding Purchase Agreement (including warranties)
- Deal close, closing accounts / earnout

# Questions

# Taxation considerations

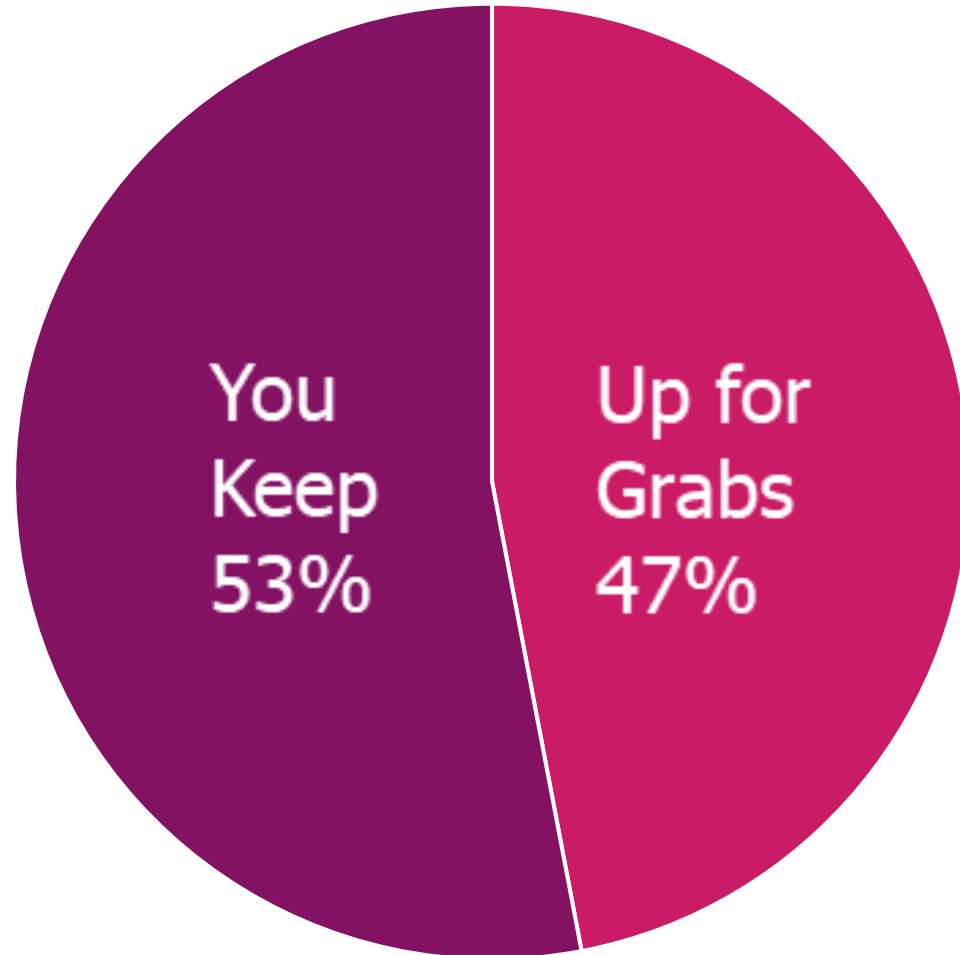
# Tax concessions

- 50% general discount
- Small business CGT concessions
- Number of taxing points
  - Single?
  - Multiple?
- Pre-CGT (pre-20 September 1985)

# Tax impost

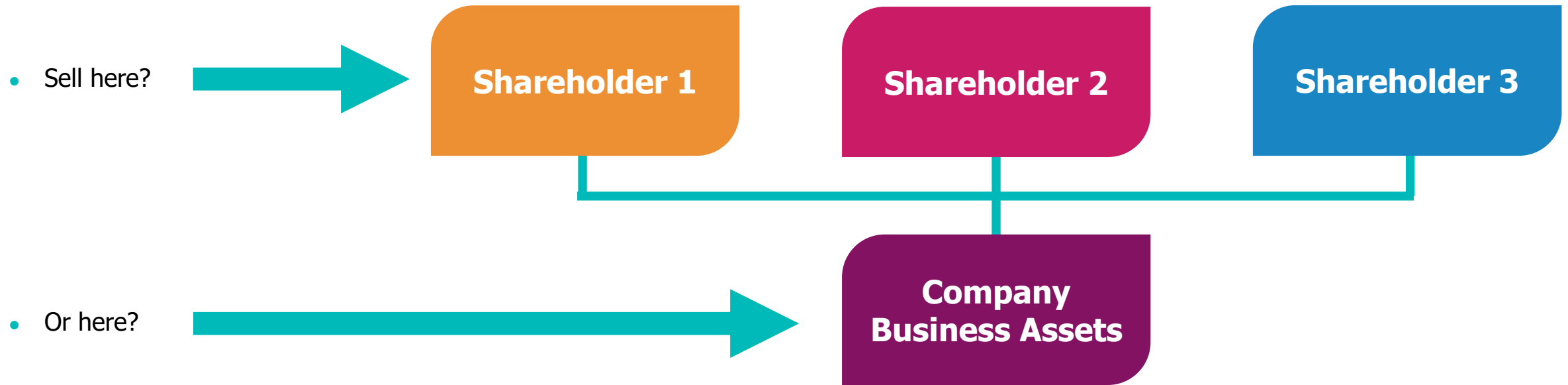
0% – 47%

- Concessions have numerous qualifying conditions
  - Just before sale
  - Years leading up to sale
- Integrity rules
  
- \$4 million x 47% = \$1.88 million



# Sell business assets or the company?

# Sell business assets or the company?



- Which will maximise the after-tax cash left in your hands?

# Sell business assets or the entity?

- Unit trust
  - Sell units might be feasible
- Discretionary trust
  - Sell assets is only option



# Sell business assets or the company?

- Which will maximise the after-tax cash left in your hands?
- Sale of company tends to achieve better result
  - But cannot assume will
- Model outcomes of each option
  - Two modelled piles of cash
- Seek to negotiate sale structure based on bigger one

# Company sells business assets

- No 50% CGT discount
- Small business CGT concessions
- Extraction from company
  - Additional taxing point

# Sell business assets

## Allocation of sale price

- Capital gain on goodwill:
  - Might be reduced by concessions
- Gain on depreciating assets:
  - No concessions
  - Taxed at full rates
- Tax law generally does not interfere with outcomes from parties dealing at arm's length
  - Cautionary tale

	<b>More allocated to:</b>	<b>Less allocated to:</b>
<b>Seller wants...</b>	Goodwill	Depreciating assets
<b>Buyer wants...</b>	Depreciating assets	Goodwill

# Transfer duty

- Still imposed on purchases of business assets:
  - QLD, WA, NT
  - $\approx 5\%$  business value
- Incentive for buyer to buy company/unit trust

# Sell the company

- Sale at shareholder level
- Possible pre-sale dividend
- Prepare the company, eg:
  - Remove non-business assets
  - Clear loans to/from related parties
  - Tax consequences
- Has company made an Interposed Entity Election?

# Pre-sale restructuring

# Pre-sale restructuring

- Separate part of business not being sold
- Not 100% sale – some owners staying on
  - Existing structure acceptable to incoming equity holders?
- Remove non-business assets
- Pre-sale dividend

# Pre-sale restructuring

## Where results in qualifying for a tax concession

- Discover after sale – too late
- Discover/act shortly before sale – anti-avoidance risk
- Discover/act well before sale – minimise risk



# Other issues



# Pre-CGT business

- Acquired/started before 20 September 1985
- Do not assume still has pre-CGT status
- Can be lost
  - Changes in business nature or character
  - Changes in ultimate owners
- After 38+ years, increasing risk

# GST

## Sell business assets

- GST-free?
  - Do not assume so
- Seller's risk
- Claw-back clause

# Pre-lodgement agreement ATO

- Engage with ATO before sale, or before lodgement
- Confirm tax treatment
- Provides practical certainty
- Virtually eliminates any likelihood of being selected for review

# Looking ahead for concession-ruiners

# Key tax concession-ruiner Time

- Primarily:
  - 50% discount
  - Small business CGT concessions
- Some qualifying conditions satisfied over time. Eg:
  - Active asset test – up to 7.5 years
  - 15-year exemption – 15 years+

# Key tax concession-ruiner Time

- If time-based condition not met before sale:
  - Too late
- Identify in advance
  - Mitigating action

# Business Concession Review

- Suitable anytime in business lifecycle
- Identify currently present concession-ruiners.  
eg:
  - Legal/equity structure
  - 50% discount
  - Small business CGT concessions
  - Pre-CGT status
- Asset protection
- Non-business asset extractions

Business Concession Review





# Ideal timing

- Tax advice – before sale/transaction
- Groom business for sale – 2 years minimum
- Business Concession Review – anytime (ie, now)

# Conclusion

# Conclusion

- Allow more time to maximise value
- What improvements can I make today?
- What will my exit look like?
- Exit options to suit circumstances
- Sell assets vs sell shares
- Pre-sale restructuring
- Look ahead for tax concession ruiners

# Talk to your trusted Nexia Advisors



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