Understanding Exit Strategy Terms— Business Blueprint Interview

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Intro:

Kerry Boulton is Australia's most respected exit strategy advisor and CEO of the Exit Strategy Group. Welcome to this week's segment.

Dale Beaumont:

What are the terms that we should be looking for, you know, in terms of, because I know sometimes you actually get paid in cash. Sometimes you get paid in stock. Sometimes you have to stay on for a year or two years. There's so many variables. What are some of the things that are the best-case scenario that you should aim for?

Kerry Boulton:

Well, best-case scenario is, "Here's the cash, and I'm out of here." Walk out the door.

Dale Beaumont:

Correct. We'll deal with everything that you can leave behind.

Kerry Boulton:

Yes, if you can. That's the least risk for you as the seller. But nine times out of 10, that isn't going to happen. A lot of the intellectual property in the business is caught up in you, the owner. Even though you may have done your best to get it all out and systemised, there'll be a perception from the buyer that they need you around for a while. That may change after two or three months, but there are different scenarios.

Dale Beaumont:

So there could be an earn-out where a portion of your payout is tied to the future profits of the business?

Kerry Boulton:

Correct. We're paying you a million dollars—here's $500,000 now, and we'll pay you the rest if the business hits these goals.

Dale Beaumont:

Right, and then you're going to stay connected to the business, coach the people to get the results, and get your own money out.

Kerry Boulton:

Correct, you've still got your skin in the game.

Dale Beaumont:

So what's that called?

Kerry Boulton:

That's called earning out. It could be any combination of upfront—high, upfront—low, whatever. It could be over any period of time—six months, two years, five years—all negotiable.

Dale Beaumont:

Are there other things that buyers may want to throw in there? And then it's up to you to decide, ultimately, are you going to negotiate on price to get the terms you want?

Kerry Boulton:

They may. Depending on the business that's buying you, you could get stock, for instance, shares. If you're being bought out by a listed company, they may give you a certain amount of cash and a certain value in shares. So you're punting on the value of those shares increasing or not going down.

Dale Beaumont:

Now, can you sell those shares instantly, or are they sort of escrowed or put on ice for a while, maybe a year?

Kerry Boulton:

Usually, they'll be on ice for a little while. Again, the term is negotiable.

Dale Beaumont:

So they'll say, "Here's the shares, but you can't sell them for a year." That way, you want the company to grow so you can increase your value too.

Kerry Boulton:

Right, they still want your skin in the game.

Dale Beaumont:

Got it. On the other hand, they might say... Sometimes people want to hold onto a little bit of equity in the business.

Kerry Boulton:

Yes, that could happen. Say, for instance, you're selling to a private equity group, which we haven't talked about yet. They have a very short timeframe. They see great opportunity with your business, and they're going to grow it—usually three to five times—in the next three to five years and then sell it. That's how private equity works.

Part of their deal might be that you retain a small percentage. That's a really good outcome for you because you unlock the wealth you created, you get a cash payout, and you still have a little bit of skin in the game for the future.

Dale Beaumont:

But often, they don't want you around, do they? They want you out because they're bringing in a different management style and new key people to exponentially grow the business.

Kerry Boulton:

Correct, and they don't want you influencing the staff or still hanging around.

Dale Beaumont:

Right.

Kerry Boulton:

It's very difficult in an earn-out situation. Say you're in an earn-out, and you've been the boss, calling the shots, and now all of a sudden, you're answering to someone else. You've got to do management reports that you're not used to doing.

Dale Beaumont:

It's got to be done by Friday—chop, chop.

Kerry Boulton:

Yes, exactly, otherwise, chop, chop! It's very difficult to be in that position.

Dale Beaumont:

If you don't have a copy of Kerry's new book, ***The Uncensored Truth About Exit Strategy***, please visit freeexitstrategybook.com.au.