Monthly Newsletter

NOVEMBER 2015

Acquisition Financing – Part 1

A Short Course for Buyers and Sellers

First let's address choosing an agent. What does that have to do with financing you may ask? Because, an agent can't advise you on pricing your business if they don't know what would be acceptable to the various types of lenders. When thinking about listing your business for sale don't just go with the agent/broker who says they can get you the most money for your business. Why, because even if you and a buyer agree on a sales price, the lender will have the last say and if it doesn't pass their muster they won't approve the loan. That means starting the entire process over from the beginning. When trying to determine an agent's expertise about financing and its impact on the transaction, ask question such as:

- Will my asking price hold up to lender scrutiny and a bank ordered valuation?
- What's an acceptable down payment?
- Will I have to carry any of the financing?
- Based on the adjusted cash flow of the business what is the debt service ratio and what ratio is acceptable to a lender?
- Will any payments on a seller carried loan be subject to being deferred based on the total debt service?
- Will they find the buyer's qualifications adequate to run my business?

If a business isn't priced properly, not only will many buyers be reticent to pursue the opportunity, but it will have very little chance of ever getting to the closing table. Price it properly and the entire process will go much smoother and your chances of a successful transaction are greatly increased. Look at more than just price when choosing representation and hire an agent who understands the entire process… It gives you the best chance to sell your business.

Acquisition financing, a topic rarely discussed when putting a business on the market but one that can make or break many deals. When it comes down to it, it sometimes doesn't matter what you are asking for your business or even what a qualified buyer may be offering. It often times comes down to whether a lender is willing to come to the table and finance the acquisition. Lenders are going to look at every aspect of a deal and price is only one of the factors taken into consideration. A lender will look at any and/or all of the following:

- Price.
- Down Payment.
- Buyer Qualifications.
- Seller Carry and Terms.
- Company Performance and History.
- State of the Subject Industry.
- General Economic Conditions.
- Ability to cover personal obligations from the proceeds of the business (after debt service is deducted).

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Watch for our December Newsletter with Part 2 on Acquisition Financing.

Acquisition Financing – Part 1

Sources of Financing

SBA (Small Business Administration) – SBA guaranteed loans are the largest source of financing for business acquisitions under $5 million. Why do banks use the SBA… because they guarantee 70% of the loan amount, it's an insurance policy for the lender! This is also why you will see banks asking for 30% of the purchase price as a down payment, the bank's liability is fully covered. Be aware that the 30% can usually be a combination of buyer's cash down payment and owner carry, as long as it adds up to the 30% figure. The down payment figures are not set rules and can be negotiated, and will vary based on buyer background and qualifications. The stronger the buyer and the stronger the company being purchased the more likelihood there is of a buyer being able to negotiate favorable terms with the lender.

One negative to SBA guaranteed loans is the inclusion of a 2.0% loan guarantee fee (which can be included in the loan amount), this plus typical 1.5% average bank fees can make SBA guaranteed loans on the more expensive side. Regardless of the expense, SBA loans are often the only option for small business acquisitions. On the positive side the interest rates on SBA guaranteed loans are often lower than other types of financing because the lenders risk is offset by the government guarantee.

Commercial Bank Loans - Most banks will not consider doing a straight commercial loan for a business acquisition without a SBA guarantee but there are a limited number of banks who WILL use this type of financing. We at Tait Associates regularly interview a large number of lenders and are happy to set you up to interview different lenders before making a choice. One thing to consider on commercial loans is you don't have to deal with all the SBA paperwork and delays but you typically will pay a higher interest rate for loans without a SBA guarantee because this would be considered higher risk. Fees will vary by lender but as a general rule the fees are lower than a SBA loan because there is no 2% loan guarantee fee. Most of these types of loans will be available at smaller regional banks and credit unions, not the large national banks. This can be a very good option but, unfortunately it's not always available.

Be sure to check for the 2nd half of this article in the December issue where we will discuss five additional forms of more "non-traditional" acquisition financing.

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