

Anticipating M&A “Cerberus”

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What are the critical success factors when engineering a new incentive structure in anticipation of or immediately following an M&A transaction (including entrepreneur relief for managers)?

Most important thing

- It has to incentivise the staff
- Therefore they have to understand their targets
- KISS

Heads of Terms - Cerberus

- Before Heads
- During Heads
- After Heads

Before Heads of Terms

- EMI still possible
- Arrangements are not yet in place for the sale of the Company
- But watch out when you get close to agreeing heads

During Heads of Terms

- EMI now too late
- Can still allot shares
- Valuation arguments still exist but act quickly. Don't forget the Information Standard.
- Think about rolling up options but old and new must have same value. Can be tricky.
- Now is the time to examine existing EMI contracts but don't despair – Not all is lost

Faulty EMI contracts

- Must refer to Schedule 5
- Death plus one year
- Inappropriate Performance Conditions
- Cashless Exercise
- Hard First Exercise Date
- 1% of the company

- Must be in writing

Faulty EMI contracts

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After Heads of Terms

- EMI unlikely (Mark Ife has discussed)
- CSOP – Trap if more than one class of ordinary shares
- BVCA MOU
 - Most appropriate when large amounts of debt
 - But only really works once
- Growth Shares
 - HMRC expect projections
 - Ratchet down
- Unapproved Share Options

Entrepreneurs' relief

- 5% test.
- Ordinary Share Capital
 - “ordinary share capital”, in relation to a company, means all the company's issued share capital (however described), other than capital the holders of which have a right to a dividend **at a fixed rate** but have no other right to share in the company's profits”
- 4.99999%:- Rectification
- Trying to be too clever

DOTAS

- Where a class of share is created ... so that the shares in question carry voting rights and form part of the company's ordinary share capital, but do not carry an economic interest in the company which is **consistent with other classes of the company's shares**, holders of those shares may be entitled to ER - which would not otherwise be due - on other shares.

DOTAS exclusion

- For example, where the use of shares with anomalous economic rights to ensure entitlement to ER is part of a **larger scheme or arrangement to further the commercial interests of the company** then an informed observer may conclude that obtaining the tax advantage of ER is not a main benefit of including the new class of shares in the arrangements.

Questions ?

- But remember
- It has to incentivise the staff
- Therefore they have to understand their targets
- KISS

Caveat

- Tax is tricky and is a crucial part of share schemes. Therefore detailed advice is necessary before taking or omitting to take action and the author's remarks are only meant to be an introduction to this area. Any views / comments are not to be taken as advice relevant to any specific arrangements.

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