

Management Buy-Outs

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In my last column I described how employees may be the best buyers for your business (this is commonly referred to as a Management Buy Out or “MBO”).

Successful business purchases are made by people who understand the key drivers of a business; often its employees. MBO’s provide an opportunity for key employees to take their first step into business ownership. However, MBO’s will only work if the following conditions are met.

1. **Hunger.** Your employees must have a burning hunger to being a business owner. Employees often underestimate the difference between a “9 to 5” mindset and the psyche of a business owner. Business owners never stop thinking about their business and often this goes hand in hand with high stress levels. MBO participants must learn to integrate an increased business focus with their family and other commitments.
2. **Debt.** Employees will almost certainly need to borrow from a bank (and perhaps the vendor) to fund the purchase of a business. Banks will demand security over employees’ homes and other personal assets, which can cause significant additional stress.
3. **Diverse personalities.** If a number of employees combine to form an MBO team, they must be certain that their different personalities can successfully combine to manage the business. Often, a strong leader is required to provide direction and vision.
4. **Ability.** Don’t invite employees to participate in an MBO merely because they’ve served the firm for a long time. Choose employees with the ability and energy to move the business forward. Others may be best suited to their current roles.
5. **Motive.** MBO’s will appeal to people driven by their ego, who have a desire to “be the boss”. Often, these individuals become so focussed on this aspect of their role, they lose sight of the basics. Exclude these people from your MBO team.

The focus of an MBO team in the first 5 years will be to reduce bank debt as fast as possible, by maintaining or increasing the earnings of their business. Only in later years will dividends be available for satisfying personal financial goals.