GLOBAL FINANCIAL DUE DILIGENCE

CASE STUDIES

THE POWER OF BEING UNDERSTOOD
AUDIT | TAX | CONSULTING

RSM

A world leader in audit, tax and consulting services

ABOUT RSM

123
countries

860+
offices

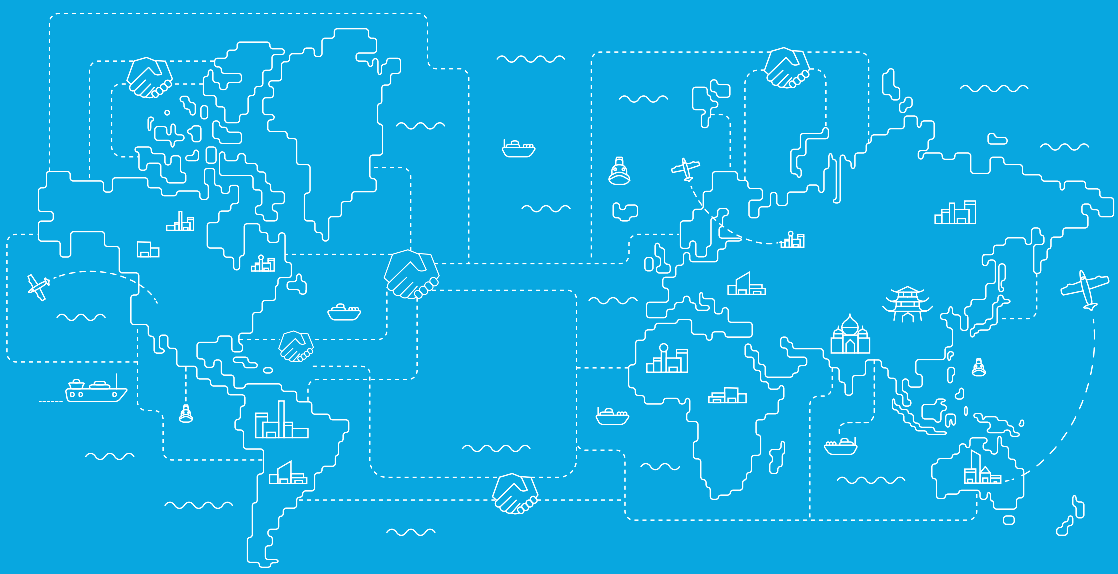
4,350
partners

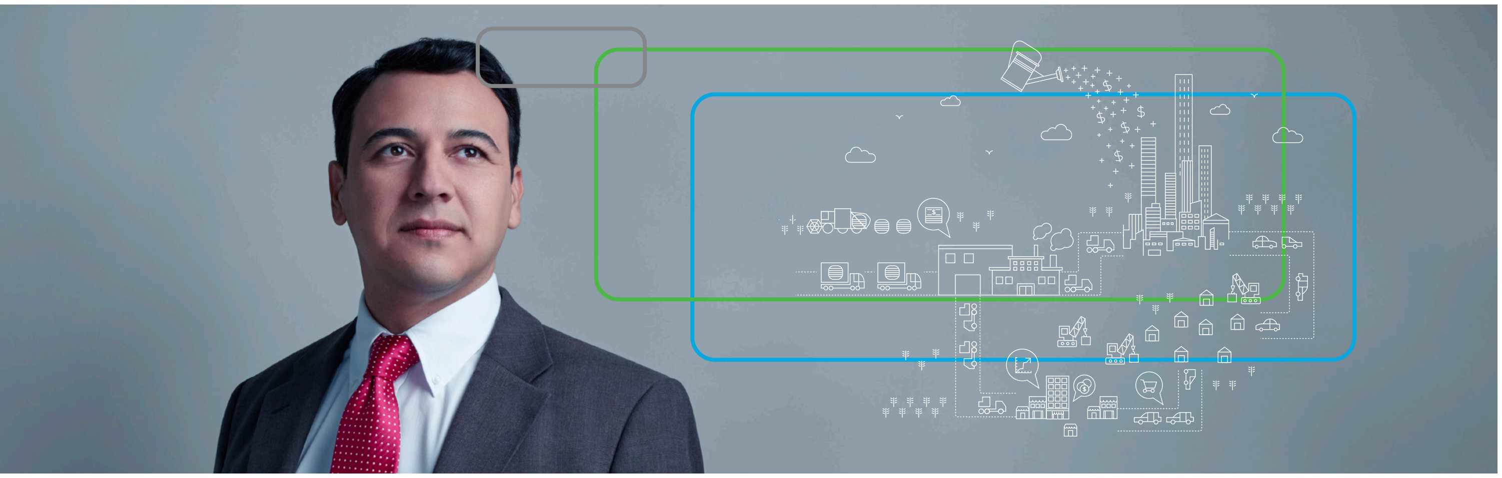
51,000+
staff

RSM is one of the world's leading audit, tax and consulting networks. We build strong relationships based on a deep understanding of what matters most to our clients. It is our strong, collaborative approach that differentiates us. We will strive to truly understand our clients, their strategies and aspirations in order to deliver insights tailored to their precise needs.

By sharing the ideas of our senior professionals, we empower clients to move forward, make critical decisions with confidence and take full advantage of the opportunities on the horizon for your business.

Understanding is what we do. This document outiines some examples of how we serve global clients across borders through the power of understanding.





CROSS-BORDER TEAM MARRIES LOCAL MARKET EXPERTISE WITH CLIENT AND INDUSTRY KNOWLEDGE

BACKGROUND

A U.S private equity client was purchasing an Australian-based family owned and operated business supplying and servicing manufacturing parts in the automotive industry. RSM provided financial due diligence services and assistance with the sale and purchase agreement and completion accounts, using a joint team of RSM US and RSM Australia due diligence professionals on-site in Australia.

FINDINGS

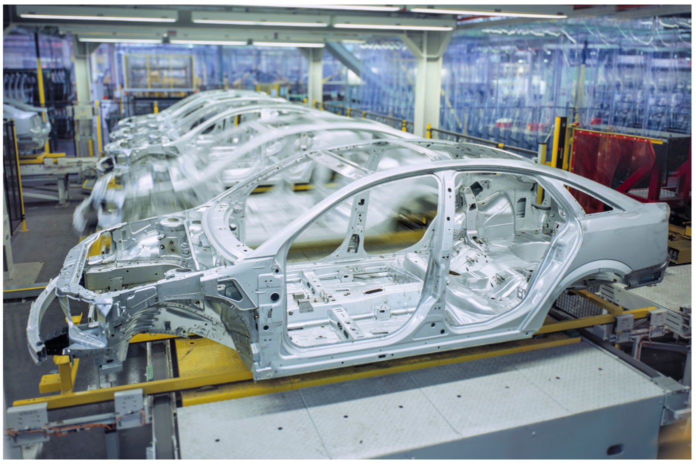
The target lacked accounting expertise resulting in a number of significant issues arising in relation to the quality of the financial accounts. Of specific concern, were the quantity and valuation of inventory and the accuracy of cost of sales and therefore profitability. Our team identified a large number of discrepancies in physical inventory to accounting records and numerous historical adjustments to inventory and cost of sales over the review period.

The RSM team spent time on site with the target's management to undertake walk throughs of the systems and procedures in place, run reports from the system to perform detailed testing and analysis and quantify, as far as possible, adjustments to inventory and Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA). RSM also attended a completion stock take to ensure that adequate procedures and controls were in place.

CLIENT OUTCOME

We identified due diligence procedures and analysis to quantify adjustments where possible and to provide a detailed understanding of adjustments and risks that could not otherwise be quantified.

The combined team from RSM US and RSM Australia leveraged client knowledge and continuity, industry proficiency, and local market expertise to seamlessly meet the client's needs. The insight we provided was invaluable to our client in negotiating the sale and purchase agreement and provided the client with the knowledge and confidence to complete the transaction.



MATERIAL PRICE ADJUSTMENT IN WORKING CAPITAL

BACKGROUND

A private equity backed business in specialist distribution was acquiring a regional company in the same sector. The target business did not have an internal finance department and produced only limited, unaudited financial information every half year. The rapid growth of the business meant that revenue had tripled over the course of 12 months and so agreeing a basis for valuation of the business was inherently complex.

FINDINGS

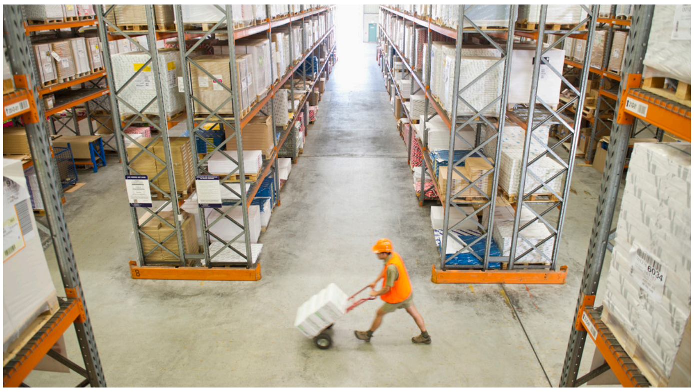
Our team assessed management's run rate calculation and identified flaws in the underlying assumptions which did not reflect the reality of the financial operations of the business.

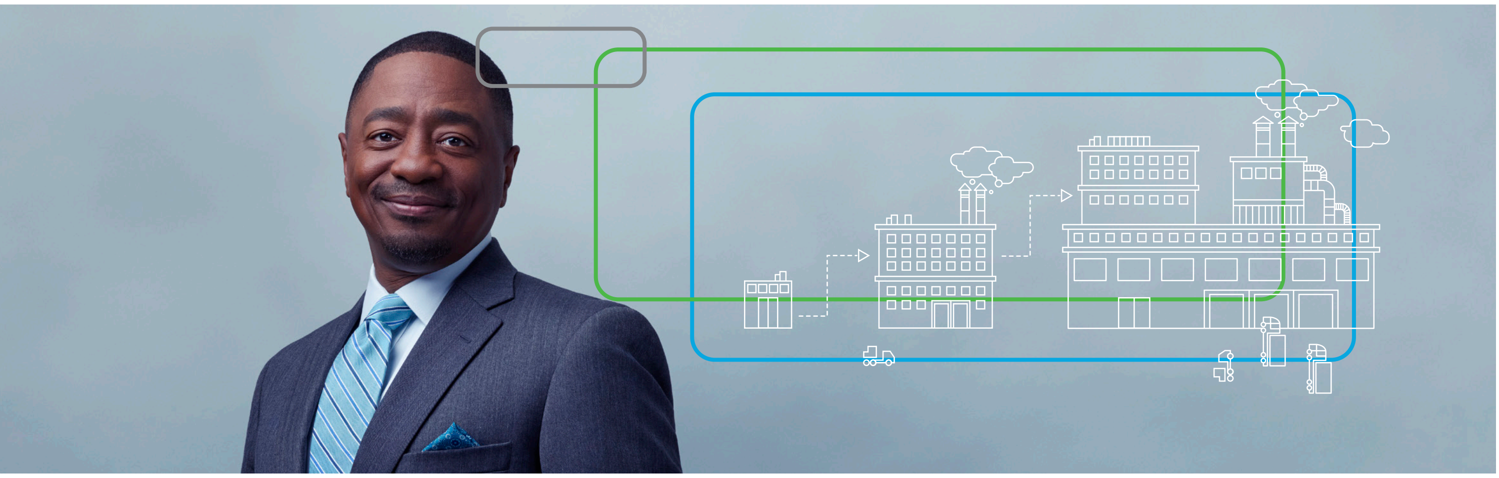
We developed a thorough understanding of the working capital dynamics of the business, to a level higher than the knowledge of both the vendors and their advisers. This allowed us to build a case to demonstrate that the working capital needs of the business were much higher than had been presented and successfully negotiated a highly positive outcome for the purchaser.

CLIENT OUTCOME

Our robust assessment enabled our client to negotiate a revision to purchase price terms.

The impact of adjustments to working capital represented a material reduction to consideration. Ultimately, the price paid was lower than what the vendors had initially indicated they were prepared to sell the business for.





DUE DILIGENCE WITHOUT MANAGEMENT ACCOUNTS

BACKGROUND

The target, a publishing business, had an unsophisticated back office and had never prepared management accounts. Financial control relied on active management by the key shareholders of the bank account and cash book with formal financial statements only prepared by the auditor at the year end. Our client, a private equity group, was reviewing the acquisition of the business but were unable to make an informed assessment without management accounts or detailed trend analysis to determine royalty income by product series over time.

FINDINGS

We performed substantial analysis of the group's cash book helping to validate the historical stability of the business's cashflows. This included key inflows in either annual or six-monthly cycles and outflows validated and assessed based on cash book analysis with verification of major items. This analysis was then used to provide validation of underlying profitability. We also identified the existence of certain source records which enabled an annual royalty analysis to be performed.

CLIENT OUTCOME

The transaction was successfully completed. Whilst the production of monthly management accounts has inevitably become a key operational tool post-completion, a large range of the analysis performed for the financial due diligence has become the form used for assessing ongoing performance of the business and in supporting strategic decision-making.

BACK OFFICE FAILURE IN A TECHNOLOGY BUSINESS

BACKGROUND

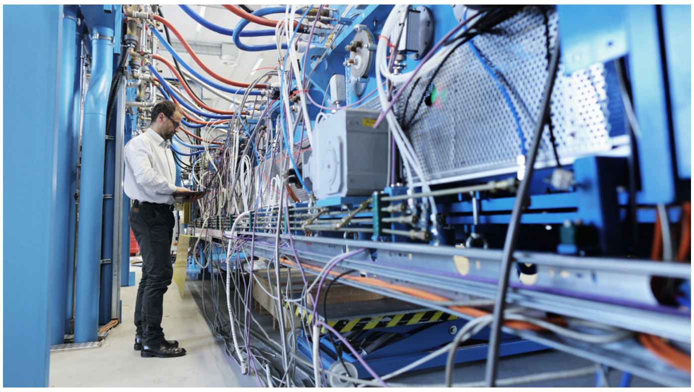
The target was a technology business seeking growth capital investment to help drive the business forward. The accounting systems were unrefined with a focus on growth in customer numbers and billing rather than back office support, not uncommon in businesses at a similar stage of development. The client was a private equity group looking at the investment opportunity and assessing value on trading run rates.

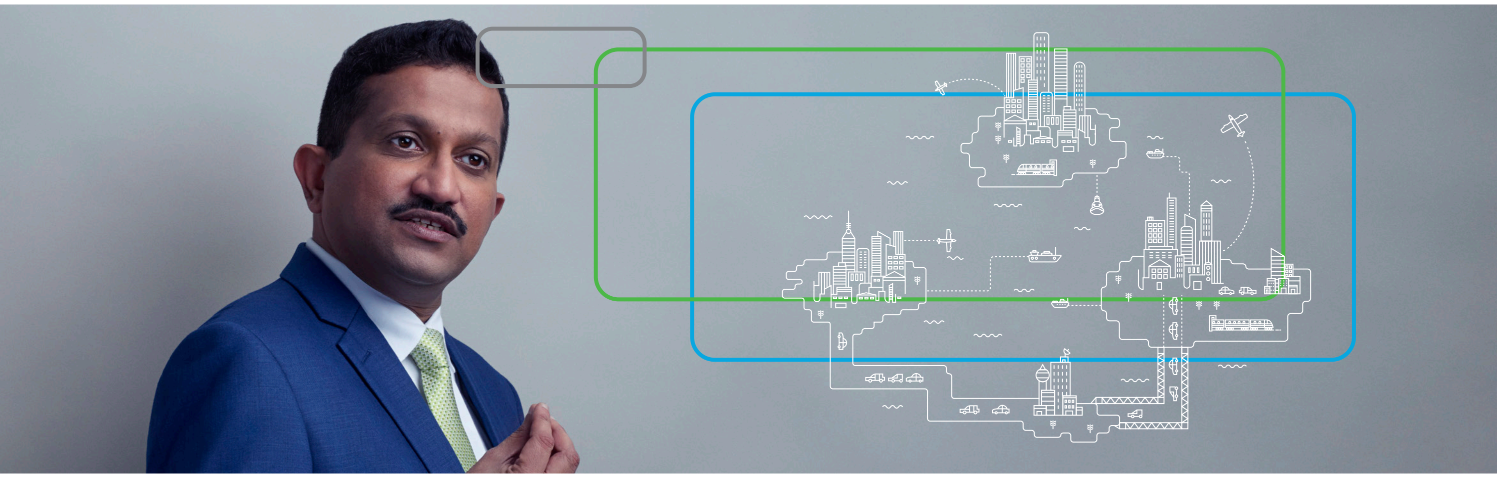
FINDINGS

In assessing the balance sheet and debtors, we identified that not only was there substantial ageing issues in the debtor's ledger, but that this systematic failure led to cancelled or lapsed clients continuing to be billed monthly even though earlier invoices had not been paid. The lack of credit control functions was a key failing and our analysis highlighted and quantified a significant working capital opportunity for the target business to rectify.

CLIENT OUTCOME

Our analysis of the run rate resulted in a material adjustment to the terms of the transaction with the buyer obtaining a higher proportion of the equity. A robust deal mechanism was also put in place to protect the buyer to the extent that clients represented as continuing by the vendor could be properly assessed and tested following the deal based on the successful cash collection of billings.





CARVE-OUT OF A DIVISION FROM A LARGE LISTED COMPANY

BACKGROUND

The buyer, a global logistics entity, was expanding its operations into the eastern half of the United States through the acquisition of the rail terminal division from a seller that wanted to shift its focus from logistics to supply chain solutions. The target division was a small portion of the seller's operations, and management did not historically prepare stand-alone financial statements for the division.
The client, the buyer, was focused on identifying any shared costs that were not reflected in the financial results of the division to be acquired.

FINDINGS

The corporate overhead that management assigned to the rail terminal division was found to be grossly understated. The seller did not consider operating costs such as human resources, information technology, customer service, financial reporting, or insurance. The RSM team's analysis uncovered the additional cost sources and worked with the client and target management to estimate more realistic amounts that the buyer could expect to incur, given the size and scope of the target operations.

CLIENT OUTCOME

Our analysis exhibited a number of additional costs that the client would not otherwise have considered. As the financial information provided the basis of the client's bid to acquire the target division, our work identified that operating costs were substantially understated. The buyer used our findings to revalue the transaction and was able to complete the acquisition at a substantially lower purchase price than initially contemplated.

AVOID TAX RISKS FROM VENDOR PLANNING

BACKGROUND

A large US public company was acquiring a UK-based services business. The target business was highly cash generative and, in a bid to reduce tax payments, had implemented a tax avoidance scheme using an Employee Benefit Trust (EBT) following advice obtained elsewhere.

FINDINGS

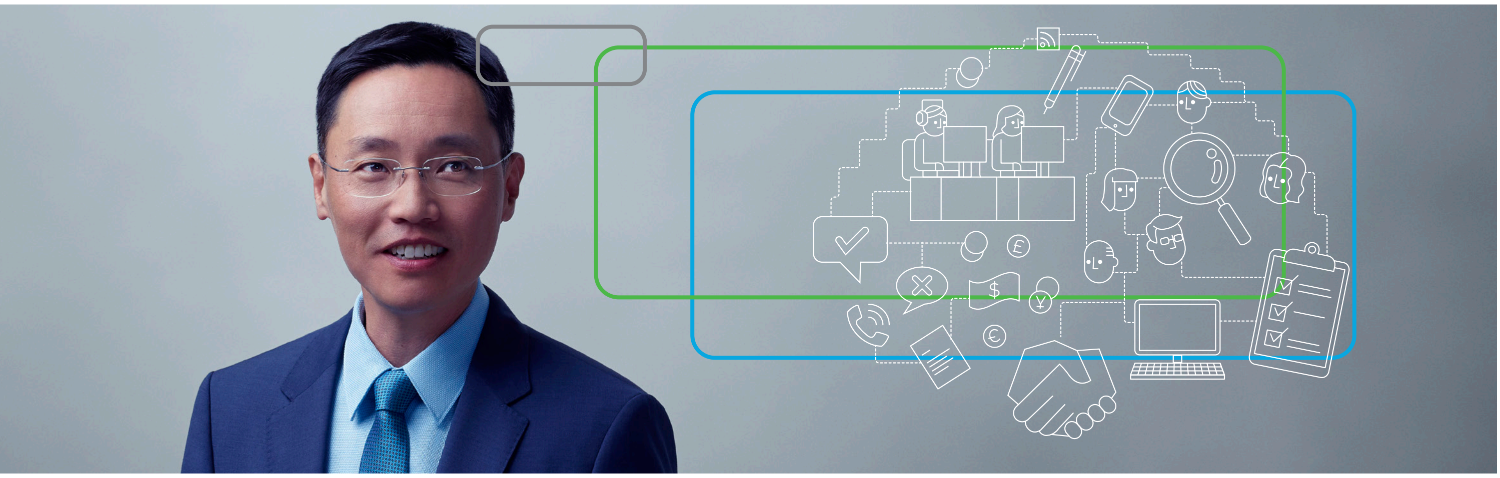
We identified that the use of the EBT structure created a contingent exposure in the target business. Indemnity protection was not satisfactory to the prospective buyer due to the nature of the exposure, the significant amounts involved in the context of the deal and the period in which the risk would remain. In its proposed structure, the transaction was unworkable.

With the purchaser concluding a need to abort the transaction, our team devised a structure to enable the planning to be unwound in a way that meant the tax risk was not transferred to the purchaser. The plan was set out to the vendors and their advisers who ultimately accepted the proposal.

CLIENT OUTCOME

RSM's lateral thought allowed the transaction to proceed. The client went from the abort position to implementing a successful acquisition of a profitable business which was then integrated into the buyer group.

Post-completion, the target business requested our continued support in helping to implement the processes required to resolve the tax issues relating to the tax planning structures.



INCOMPLETE DATA IN A LEVERAGED DEAL SCENARIO

BACKGROUND

The buyer, a private equity group, was looking to acquire a niche product distribution business. The vendor was looking to retire and had invested significant efforts in a sales process including the commissioning of sell-side vendor due diligence. The transaction had reached exclusivity with one party but the deal failed and RSM was asked to provide due diligence with a view to achieving a leveraged buyout.

FINDINGS

The vendor due diligence report had failed to emphasise the lack of orderly management information in the business with no routinely prepared management accounts. Our team invested significant time with senior management to understand the available data and the extent to which operational data might be used to enable trend analysis to be performed.

Substantial efforts in reconciling operational data to financial statements meant that we established integrity in the operational data which in turn, allowed us to make strong and robust conclusions on product-by-product trends.

CLIENT OUTCOME

Having invested the time in understanding the business, our due diligence report provided the crucial comfort level required by both private equity and financing debt providers to enable the transaction to complete where the previous buyer process had failed.

Challenges?
We see opportunities.

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