

Notes on the acquisition of the Seven Stars

BACKGROUND

The freehold of the Seven Stars, Dinton (the “Pub”) was marketed for sale in May 2011. The vendor was a large corporate pub group who was in the process of restructuring their portfolio to focus on larger pubs which generally produced higher profit margins. Village pubs such as the Seven Stars were considered non-core.

The vendor had owned the Pub for the last decade. During that time there had been numerous tenants and managers none of who had been able to make a sustainable business from the Pub. Local residents were concerned that the Pub would prove more attractive to residential developers than pub operators and that a valuable village and community asset would be lost.

THE ACQUISITION TEAM

An initial group of 5 people (the “Acquisition Team”) began to canvass local residents to ascertain if there was sufficient appetite to acquire the Pub. This process involved lots of phone calls, leaflet drops and several meetings in the village hall. The Acquisition Team was purposely kept to a small group as it was considered that a larger team would be too unwieldy. The Acquisition Team shared all decisions and communications.

FORMING THE ACQUISITION VEHICLE

The Acquisition Team reviewed several types of structure which could be established to acquire the Pub. These included:-

1. a Limited Liability Partnership,
2. a Limited Company, and
3. a Co-Operative Society.

It was decided that a limited company would provide the best structure. This decision was based on the number of the potential shareholders, ongoing management and, to a lesser extent, taxation. The Seven Stars Dinton Limited (the “Company”) was established and the Acquisition Team became the initial directors. Bank accounts were opened and VAT registration was applied for. An application for the Company to be an Enterprise Investment Scheme was considered but not progressed due to the anticipated operating structure going forward.

THE BIDDING PROCESS

The vendor used a selling agent to market the Pub and to handle negotiations with interested purchasers. The Acquisition Team was in constant communication with the vendor’s agent to ensure that they understood the key drivers for the vendor. Whilst price was the main determinant, other factors such as timing of exchange and completion, no over reliance by the purchaser on bank loans etc were also important to the vendor. The bidding process lasted approximately two months, during which time the Acquisition Team made a series of bids. There were three other bidders and the vendors agent eventually brought the process to a conclusion by asking for best and final offers from all interested parties. The Acquisition Teams offer was successful due to a combination of price, a lack of conditionality and an offer of an immediate ‘non-refundable’ deposit. The non-refundable deposit showed the vendor that there was a real intent to complete the purchase. In exchange for this the Acquisition Team was able to secure an eight week exclusivity period in which to exchange contracts with the vendor. During this period the vendor was unable to discuss the sale or accept offers from under bidders.

RAISING THE MONEY

The money required to fund the purchase of the Pub was mainly raised from local residents and people from the surrounding areas. The Acquisition Team initially sought expressions of interest for an investment in the region of £5,000 to £10,000 per person. The concept was to include as many local people as possible in the purchase but this had to be balanced against raising the required money quickly and the administrative burden of agreeing and signing shareholder agreements. Until investors had actually transferred their funds to the nominated bank account, the Acquisition Team could not be certain of the total funds raised. To cover any potential shortfall, a finance broker was mandated to source debt funding. Many banks were approached but only a few were willing to lend to a situation where the borrower was a consortium of villagers that didn't have experience of running a pub. This was despite the requested loan to value being significantly less than 50%. Eventually a lender was secured and an offer of a bank loan was accepted. The lender was given mortgage security. The Acquisition Team ensured that the loan was drawn on commercial terms and that it did not contain any hard default financial covenants.

The availability of grants was also explored as a third source of capital. Over the course of the bidding process many forms were completed and the Acquisition Team were able to secure a grant from the Leader Programme.

The Acquisition team ensured that there was sufficient day 1 funding to cover not only the purchase price but also costs such as SDLT, legal and other professional costs, deferred maintenance items and a working capital reserve.

THE DUE DILIGENCE PROCESS

Once the offer was accepted, a third party professional team was established to ensure that the timescales detailed in the offer were met and that all contracts were properly documented. The professional team included lawyers, tax advisers, accountants, building surveyors and valuers. The Acquisition Team managed the professional team and ensured that the acquisition was completed on time and that the budgeted costs were not exceeded.

FINDING THE TENANT

The Acquisition Team realised that a suitable professional operator would be required to run the Pub going forward. Different types of operating agreement were considered, including:-

1. Management contract,
2. Tenancy, and
3. Lease

It was decided that a lease would provide the best solution for operating the Pub. No formal advertising was undertaken to find a lessee. The Acquisition Team selected and interviewed operators from other pubs based on their personal knowledge of these pubs. A shortlist of candidates was drawn up and these candidates were asked to provide their vision and business plan for the Pub. A preferred party was selected and detailed heads of terms were agreed before going into documentation. The heads of terms covered key points such as:-

1. The term of the lease and each party's ability to break the lease.
2. The rent charged together with any rent free periods and how the rent was to be reviewed.
3. Alienation provisions
4. Repairs and alterations
5. Fixtures and fittings.

The lease was completed simultaneously with completion of the acquisition.

POST COMPLETION MATTERS

Post completion a programme of works was created to cover deferred maintenance items and the Landlords ongoing maintenance obligations under the lease.

SUMMARY

The whole process took nearly eight months from conception to completion. The key stages can be summarised as follows:-

- **The Acquisition Team**
 - A small team comprising of individuals with the right skill set to complete the acquisition.
- **The Acquisition Vehicle**
 - Vehicle selected which best suited the situation having regard to the number of people likely to be involved, taxation and ongoing administration.
- **The Bidding Process**
 - Offer accepted due to an understanding of want motivated the seller.
- **Raising the Money**
 - Three sources of capital identified and utilised.
- **The Due Diligence Process**
 - Timescales and budgets met due to the right professional team being selected.
- **Finding a Tenant**
 - Tenant selected with a vision and business plan which was most aligned with the Acquisition Team.
- **Post Completion**
 - The Pub is the Company's only asset and needs to be maintained to a good standard.

If you would like to discuss any of the above in more detail please do not hesitate to contact:-

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