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# Lawyers Weekly Masterclass

## Business growth through acquisition, new capital and sale preparation, value and risk (Part 2)

WORKBOOK

*Presenters*

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## CASE STUDY: Sarah's Designer Masks



### Recap

In February 2020, Sarah watched in horror as the COVID-19 pandemic gripped the world. Many news sites showed images of health workers and everyday citizens wearing masks to protect themselves against this new untamed virus. It seemed only a matter of time before similar scenes were common in Australia.

Motivated by a passion to ensure all Australians were prepared for the virus, and in a fashionable manner, Sarah saw an opportunity for a bespoke mask-making service. Sarah decided to set up a new company, No Challenge Too Large Pty Ltd to pursue this venture.

Sarah contacted Darian, a peer from university with a degree in information technology, to develop an application for the new pursuit whereby customers could design their own fashionable masks from fabrics and templates created by Sarah. Darian delivered a great app with many features, including a function for customers to choose various fabric combinations, the layers of fabric (minimum 3) and designs. The app also collected vital customer information for communicating receipts and ensuring swift dispatch and delivery of the product. Sarah was impressed and brought Darian on as a 20% shareholder in No Challenge Too Large Pty Ltd.

Sarah also put to use her business skills to line up prospective arrangements with suppliers, manufacturers and delivery partners. It was vital that the bespoke masks could be swiftly delivered within 1 – 5 days of ordering.

Sarah got in touch with Ming, another university peer with a major in marketing, to oversee the online and television marketing of the product as 'Sarah's Designer Masks'. Ming also has the brilliant idea of marketing to organisations looking for bespoke masks.

Miraculously, Sarah and Darian's hard work was paying off, with all systems online upon Australia's lockdown in March 2020. By May 2020, the company continued to run at a small loss, although Sarah was more concerned with growth than immediate profitability and wanted to leverage the ongoing lockdowns to distribute Australia-wide.

## Present

Meanwhile, a small Western Australian company, WA Designer Masks, has enjoyed great success providing a similar consumer product in the Wildflower State. Sarah convenes a shareholder meeting to discuss the prospects of No Challenge Too Large Pty Ltd seeking to acquire WA Designer Masks to accelerate growth. The company approaches Big Bank to fund the acquisition.

Simultaneously, the company's growth has caused stress to its liquidity, as the company continues to run at a loss. Sarah approaches Zee, an investor known for putting money into early stage and promising businesses, to seek equity funding. Sarah is negotiating what stake Zee may acquire in the company in return for funding.

As of September 2021, a major US clothing company, Big Fashion Company Pty Ltd, having watched Sarah establish a strong brand, a business with strong prospects in Australia, and the unique functionality of the mask-customisation application, sees potential to apply it to broader fashion purposes. They reach out to Sarah to begin acquisition negotiations for the App or company in full. Hearing rumours of this acquisition, an international pharmaceuticals and health supply company, Prestige Health Holdings Ltd, makes an unsolicited competing offer to acquire No Challenge Too Large Pty Ltd.



# 1 GROWTH THROUGH ACQUISITION

**Recap of relevant key facts:**

- Sarah's Designer Masks is set up under No Challenge Too Large Pty Ltd
- The Business has achieved strong results in the Victorian and NSW market, with expansion into the broader Australian market
- A competitor with similar application and product offering has emerged in the Western Australian market.

# 1.1 Key commercial considerations: Growing Organically vs M&A

## Opportunities and Challenges of M&A



**Notes**

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## 1.5 Negotiating Transaction Documents



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## 2 FINANCING AND DEBT

### Recap of relevant key facts:

- Sarah's Designer Masks has borrowed money from Big Bank to finance its acquisition of WA Designer Masks
- The company is continuing to run at a narrow loss, with an emphasis on growth and solidifying its position in the market
- It is a relatively new business, with less than 2 years operation
- The business is customer heavy, with revenue continuing to grow with the need for masks only increasing for the short-medium term future



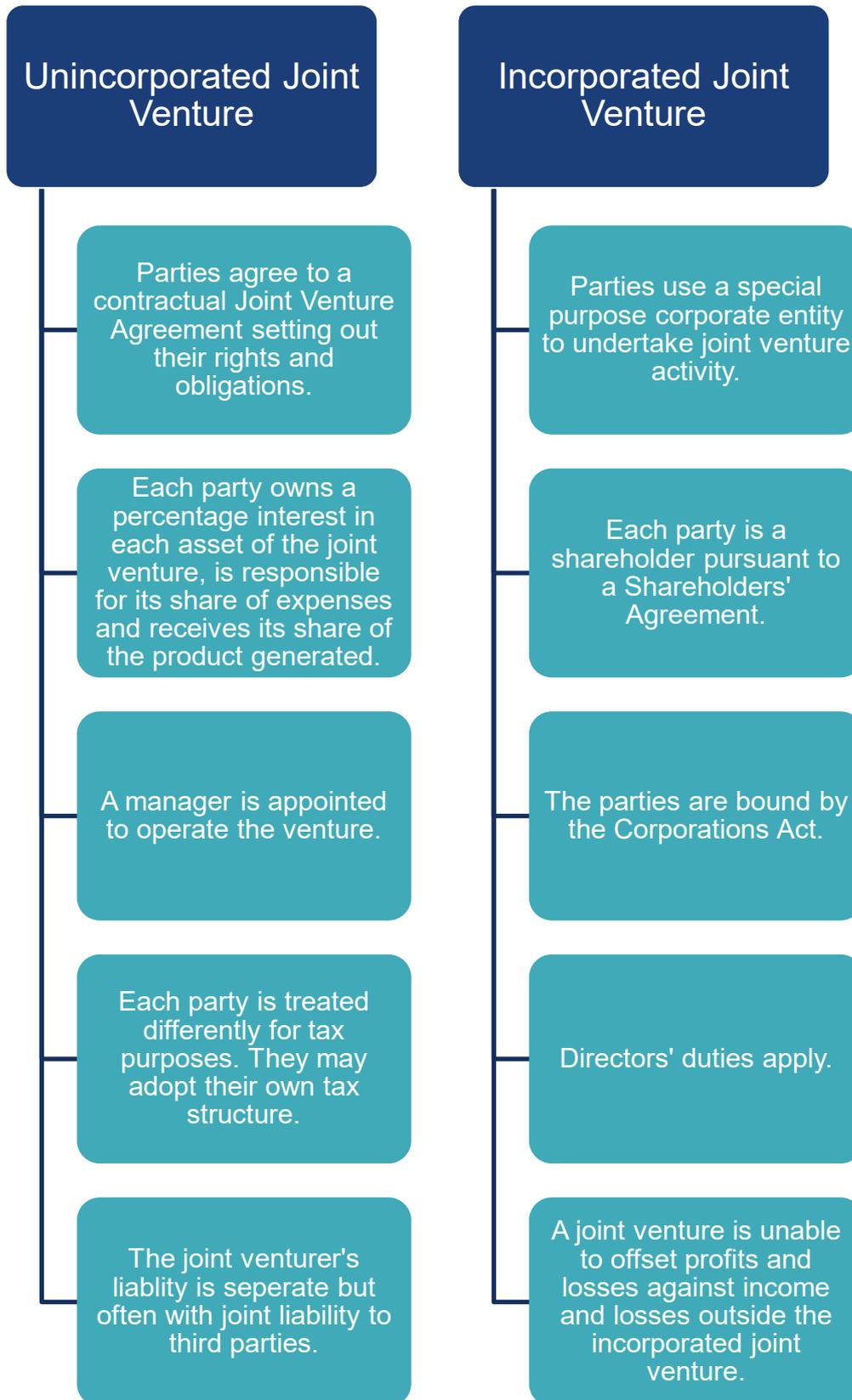


### 3 BUSINESS PARTNERS AND EQUITY INVESTORS

**Recap of relevant key facts:**

- Sarah presently holds a 70% stake in the company.
- Sarah brought on Steven as a business partner in No Challenge Too Large, due to his IT knowledge and special skills.
- Sarah approached Zee seeking equity investment, whereby Zee could acquire a stake in the company.

### 3.1 How to bring partners on (different structures)?



# 3.2 Key points to think about in shareholders' agreement

-  How many investors?
-  Valuation?
-  Class of Shares?
-  Investor decision making powers?
-  Critical business matters and special majority resolutions?
-  Drag-along rights?
-  Seed Preference Shares?
-  Put and Call Options?
-  Indemnities and Warranties?
-  Safe-guard mechanisms (how to exit agreement)?
-  Exclusivity and Confidentiality?

**Notes:**

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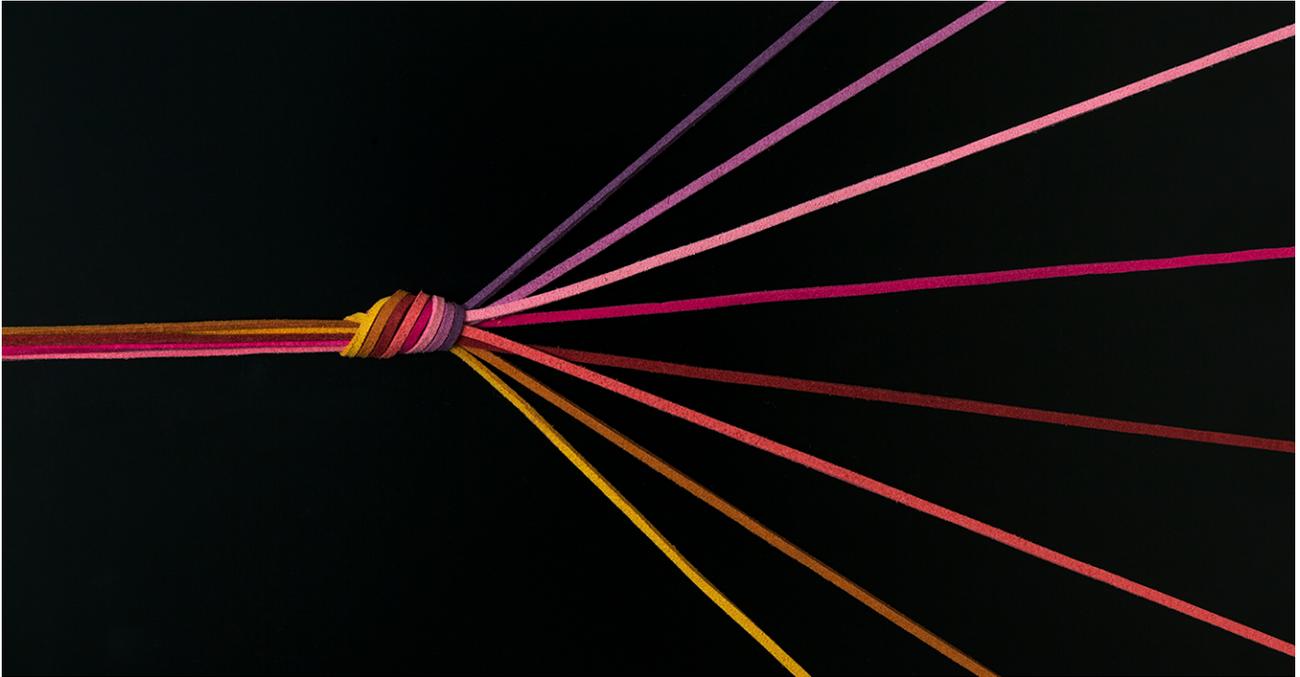
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## 4 PREPARING FOR SALE

### Recap of relevant key facts:

- No Challenge Too Large is an Australian company that has enjoyed success in Australia whilst targeting expansion via a settle acquisition of a WA company.
- Sarah's Designer Masks are a strong consumer good although are yet to yield a profit for the company.
- Big Fashion Company is a large US-based global player in the fashion industry.
- Prestige Health Ltd is another international player although in the pharmaceuticals and health supplies sector.
- Presuming the WA acquisition is completed, No Challenge Too Large's shares are held by Sarah (70%), Steven (20%), Zee (TBA%) and an employee incentive trust (10%).



## 4.2 Maximising sale value for the business

Maintaining competitive tension

Running multiple bidders

Completion accounts adjustments

How to adjust for risk

Deferred or upfront consideration

Retaining key employees

Performance hurdles

**Additional notes**

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## Presenter profiles



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Rebecca Maslen-Stannage is one of Australia's leading M&A and Equity Capital Markets lawyers, and a repeat winner of the Lawyers Weekly Dealmaker of the Year award.



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Malika Chandrasegaran is a Partner at Herbert Smith Freehills. She is an experienced corporate lawyer specialising in public and private mergers and acquisitions, foreign investment, joint ventures and other commercial transactions.

She has advised on leading cross-border and Australian transactions across a wide range of industries, including technology, media and consumer products.