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Private Equity Lifecycle

Episode 5: Mid-cycle refresh – How to get back on track?

Continuing our series through the PE lifecycle, with a focus on driving growth and putting the strategy into action. This episode sets out the key points to be considered when a refresh is needed, either due to external or internal factors – often referred to as a mid-cycle refresh.

Deloitte's private equity specialists work with businesses throughout the PE lifecycle and beyond. This series of publications highlights the key points to be considered at each stage of the lifecycle, paying particular attention to how to effectively manage assets and add value ahead of an exit.

How to get back on track?

In Episode 4, we looked at driving growth. But what do you do when things don't quite go as planned? Although you may have a detailed plan and strategy in place, external factors can disrupt progress and a strategy refresh may be required to get back on track. This is a phase many businesses will be familiar with the given disruption caused by the COVID-19 pandemic, rapidly rising energy prices, and related economic measures.

In addition to refreshing its strategy, the business may need to strengthen its balance sheet through a refinancing of external debt, potentially involving non-traditional options, such as third-party investors, or the sale of non-strategic activities.

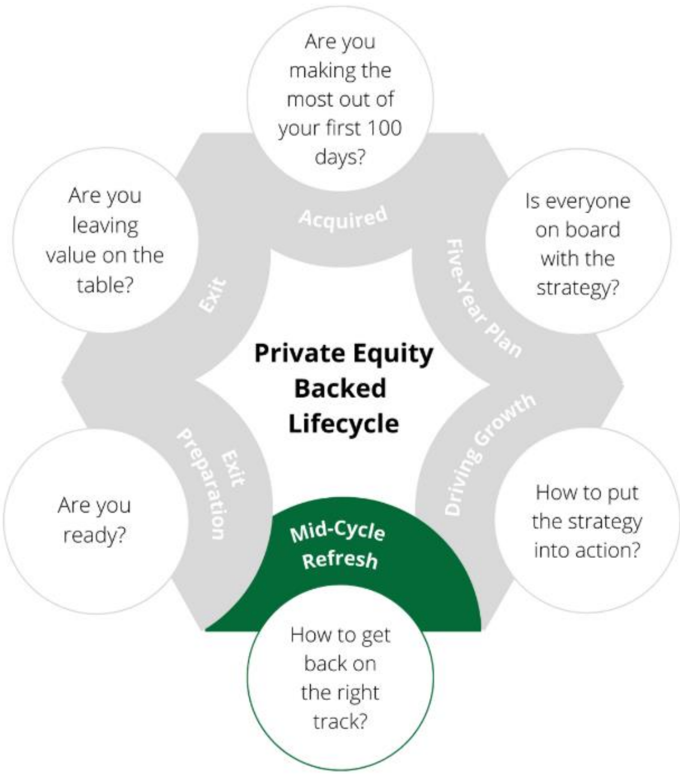
Below are some of the key points to be considered during this refresh phase for the business:

- Consider whether the original forecasts and tax plan are still fitting for the purpose. During this phase, a business should revisit its 5-year plan to assess if a) its tax strategy remains on track or whether this needs to be refreshed and b) the cash tax assumptions are still valid or need to be amended.
- Ensure all reliefs available to the business have been identified, and there is a plan to effectively manage these reliefs and drive value. This process should consider the tax impact, as well as the accounting (for example, the balance sheet position of any deferred tax assets or liabilities).
- Consider the impact of refinancing on accounting for net liabilities and also the interest deductibility of any new financing that is taken on by the company, including any additional debt drawn down from an investor. Debt provided by connected parties is subject to additional tax considerations, such as the anti-abuse, hybrid / ATAD 2 legislation, which makes it critical to understand the tax profile of the lender receiving any interest income, it enables the borrower to consider expense deductibility.
- Work with our advisers to assist with divesting activities. Strategic divestment transactions are often complex and will require legal, financial, and tax advice. It is important to consider any regulatory or banking restrictions while ensuring alignment with the overall strategy of the business. To that end, consider the tax impact of divesting certain assets, such as the application of a specific exemption, or certain exit reliefs that may be available in the seller's jurisdiction. There is also a need to consider the cash repatriation of any consideration received and any withholding tax obligations if cash is distributed to other parts of the business.
- As in previous phases, we recommend the business conducts an in-depth review from a financial and tax perspective. This should include a review of direct and indirect taxes, employment and wage taxes, as well as transfer pricing. This review should identify the risks and/or points of attention for future due diligence, but also the opportunities. Pay particular attention to any divestment planning or considerations, as any new warranties or agreements may be subject to increased diligence focus during an exit process.
- Cash repatriation: Ensure there is a tax-efficient cash repatriation strategy to service any new debt that may be held by new borrowers in different jurisdictions. This review will probably need to include the distributable reserves position, company law, and tax considerations.

Our specialist team provides advice to PE-backed companies, helping management address challenges faced during, a typically unplanned, mid-cycle refresh. If navigated appropriately, a business can continue to thrive and grow as it moves closer toward an exit process.

We understand this can be a new challenge for many businesses, especially after the intensity of a transaction. We offer our expertise and guidance to support businesses as they begin their journey on the PE-Backed lifecycle.

Discover all phases of the 'Private Equity Lifecycle' or get in contact with Dirk Baken or Sjoerd Hasselmann.



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