

There are steps that selling care operators can take which, if tackled early, can create deal and financial efficiencies to ensure a smooth transaction. **Paul Krivosic**, corporate lawyer at Mills & Reeve, considers the steps



# Rationalising your portfolio

**Health and social care remained a fairly robust sector during 2023 where we saw sale mandates of strong health and social care businesses continuing to attract buyers whose appetites for acquisitions remained apparent, if not at quite the same level as in previous years. However, the macro-geopolitical economic events that dominated the landscape encouraged, or forced, care home businesses to seek internal efficiencies and reassess their future growth.**

As a result, interest in divestments and a rationalising of portfolios increased, with operators either looking to return to their core business activities or releasing cash to fund future growth.

## Adopting the right approach

Any sale process, whether it's a divestment by an auction process or simply a bilateral transaction, will always benefit from both parties carrying out some of the inevitable heavy lifting up front. As such, operators should always consider several pre-sale steps.

## Getting your data room in order

A buyer is going to need to undertake a certain level of due diligence on the assets up for sale. For the sell side, giving a buyer a starting point by creating and populating a comprehensive and well-ordered data room should always lead to a smoother transaction.

Obtaining a due diligence question-

naire from your legal advisers, which has been tailored to your business and the type of transaction, will help a seller navigate the questions a buyer is likely to raise and search for documentation that supports a seller's responses.

The key benefit to taking the above steps is that a 'buyer's eye' review of the data room provides an excellent opportunity for your legal advisers to review the information collated to find any red flags, key issues that a buyer might have issues with, or any obstacles to the transaction closing without delay. In doing so, it gives a seller the advantage of getting ahead of what might turn out to be contentious negotiating points with the buyer and to carry out an in-depth analysis of the issue, its materiality and what impact it could have on the buyer's willingness to progress with the acquisition or how it might impact price. It also, to the extent possible, gives a seller an opportunity to rectify the issues in advance or to take steps to minimise its potential impact on the transaction (which, in turn, helps maintain the deal timetable if any such steps are not immediate quick fixes).

Additionally, often a well signposted and comprehensive data room made easily accessible will help a seller negotiate the position that the data room is deemed disclosed to the buyer, and to the extent a seller is conducting an auction process, it's always best to set this position out in any process letter to manage expectations.

Clearly there is a cost and time impact to a seller taking these steps prior to any certainty of a transaction (for example, having agreed heads of terms

with a buyer in place or sellers having granted exclusivity to a buyer) and maintaining confidentiality is always a high priority. Not all businesses keep a central record and approaching staff for information might unintentionally set hares running so sellers do need to use their best judgement and, with the help of their advisers, decide when, and how, to start this process.

## Ensuring regulatory compliance

Assess and review your current approach to regulated processes to identify any short comings. This should include reviewing your registrations, investigations, enforcement action as well as internal quality controls, watch lists and policies.

## Summary of your contractual commitments

Understanding the material commercial contracts and what novations or change of control consents are required to close the transaction is key to understanding how, and when, to approach third parties.

## Property portfolio

Reviewing your property portfolio and, in the case of leases, understanding any landlord consents required or planning conditions which might restrict or have an impact on a buyer's willingness to acquire or be subject to further negotiation between the parties e.g. dilapidations.



## Other issues to consider

- **Discovering any lender or finance consents that might be required and/or the release of security over assets**
- **Reviewing template employment contracts/staff handbooks and understanding the profile of pensions operated by the business**
- **If the deal is structured as an asset transaction where central functions are retained, a seller should always consider whether a Transitional Services Agreement is likely to be required by a buyer; although this may also be true for a seller where it is divesting a group company that supports others in its group**

On asset transactions, both buyer and seller will need to consult with regulators to ensure all registrations are in place for closing. Whilst this is necessary, it has in the past been viewed as an uncontroversial process for the parties to follow.

In 2023 we saw this issue become less straightforward, especially where there is a cross border element (even domestically) to the transaction; and we have seen regulators expecting to be notified

of the deal at a much earlier stage. However, there is a delicate commercial balance to strike between fulfilling that expectation, and the risk of a potential breach of confidentiality, against keeping regulators onside.

This uncertainty has caused more complexity in transactions that are structured as a split signing and closing for parties trying to agree a suitable 'material adverse change' clause and, where there is a warranty and indemnity insurance policy in place, with any substantial delay increasing the possibility that coverage may not extend to the warranties given at closing. It will be interesting to see if this continues to be an approach taken by regulators in 2024.

## Asset sale tax considerations

Very commonly on asset sales, the sale of the assets of a business will qualify as a 'transfer of a going concern' (TOGC) and that means that no supply takes place for VAT purposes and no VAT is chargeable. Perhaps counter-intuitively, for certain businesses in the health and social care sector, particularly charities, this structure isn't always desirable.

If a care business has construct-

ed properties such as care homes, it is common for the business to have applied VAT zero rating treatment on those costs. If the business has applied zero rating treatment in constructing the site(s) less than ten years from a seller's intended disposal of the freehold property, it will normally result in the business needing to account and pay VAT by reference to the construction costs (known as a self-supply charge), which could be a very large number.

If the sale can be structured so that the TOGC conditions are not met then a seller may be able to treat the VAT due under the self-supply charge as fully recoverable (though likely only if it can zero rate the non-TOGC sale of the property). There are a few ways to achieve this, but most will hinge on the VAT position of a buyer, and also what the buyer is willing to do; and the larger the number the bigger the impact on price which in any process means that this is not an exclusive problem for a seller to solve.

In the context of TOGCs, it is also worth being aware upfront on whether the buyer is a taxable person, or becomes one, as a result of the transfer of assets. If a seller is a taxable person for VAT purposes, the TOGC will fail if the buyer is not registered/registrable for VAT. Parties should always ensure that specialist tax advice is obtained.