Guide to: Completion Accounts

A key aspect of any share purchase is the mechanism used to establish the price to be paid for the target shares. One method is to calculate the final purchase price after completion of the transaction has taken place, by reference to accounts of the target company drawn up to the date of completion. These are known as “completion accounts”, and allow the buyer to test, and ultimately adjust, its initial valuation by reference to the actual balance sheet that is delivered by the target.

Although this can be a useful mechanism to arrive at a fair price, buyers and sellers also need to be mindful that completion accounts can also be the cause of protracted and expensive disputes if insufficient attention is given to the relevant clauses of the Share Purchase Agreement.

The particular assets and liabilities that are taken into account and measured under a completion accounts mechanism will vary depending on the circumstances of the transaction. The most commonly adopted price adjustments based on completion accounts include:

- a net assets adjustment - where the purchase price is adjusted to take account of any difference between the target's actual net asset value at completion and an agreed target figure;
- a working capital adjustment - where the purchase price is adjusted to take account of any difference between the actual working capital in the target at completion and an agreed level of "normal" working capital; or
- a cash free/debt free (or net debt) adjustment - where the parties agree an enterprise value for the target before completion (typically a multiple of EBITDA), which excludes the target's cash and debt. Following completion, the price for the target's shares will be determined by adding the cash and deducting any debt as shown in the completion accounts.

Because completion accounts are not regulated by the same legislative framework that governs the target company's statutory accounts, the format, content and basis for preparing completion accounts need to be agreed by the parties and reflected in the acquisition agreement. The key issues to be addressed include:

- The form and content of the completion accounts;
- The accounting principles to be applied in their preparation;
- The process for drawing up and agreeing the completion accounts;
- The procedure for resolving any disputes; and
- How the price will be adjusted by reference to the financial information shown in the completion accounts.

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All of these issues are capable of having a material impact on the purchase price and it is, therefore, vital that the parties' accountants and solicitors work together from the outset to draft, negotiate and agree the completion accounts provisions.

Although a dispute resolution procedure will normally be included in these provisions, this will often be costly and time-consuming to invoke and it is, therefore, far better to ensure that everyone fully understands (and agrees!) on the completion accounts provisions from the outset.

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