Planning ahead

How to avoid pitfalls and missteps in business acquisitions and sales

tructuring, implementing and closing a business acquisition or sale is a complex process fraught with unanticipated consequences for the unwary.

"Proper planning and an experienced team of advisers is essential for a successful transaction," says Jill M. Bellak, Esq., a member of Semanoff Ormsby Greenberg & Torchia, LLC.

Smart Business spoke with Bellak about how to ensure an acquisition or sale is implemented in a cost effective and timely manner.

What factors into the transaction structure?

The transaction structure can take many forms. The tax consequences to the buyer and seller have a significant impact on determining the structure. For example, if net operating losses are available on the seller side, a stock transaction or merger may be desirable for the buyer to take advantage of these losses as an offset against future income. Similarly, if the seller has significant customer contracts that may be terminated or subject to renegotiation upon a change of control, a stock sale would be more favorable than an asset sale. On the other hand, if the buyer is concerned about liabilities during the seller's operation of the business, a sale of assets may be the preferable structure.

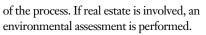
Why is due diligence important?

The buyer and its team of advisers must review the books and records of the seller's business, including financial statements, tax returns, employee benefit plans, union contracts, customer and vendor contracts, employment agreements, leases, stock records and minute books. In addition, inspection of the seller's real estate, facilities, equipment, inventory, vehicles and other personal property is a key part

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A lien search is undertaken by the buyer's counsel to determine if there are security interests encumbering the equity interests or assets being sold. Third-party loans must be paid off by the transaction's close.

A careful and thorough review of the documents and property will flush out issues that must be addressed by the parties and could result in further price negotiations.

What documentation is needed?

A letter of intent is often used by the buyer and seller to outline the principal terms, including purchase price, timing of due diligence and closing, and to restrict the seller from negotiating with or selling to other parties for a specified time period. Typically, the obligation to consummate the acquisition or sale arises when the parties enter into a definitive agreement, which specifies the price, terms and conditions that govern the deal.

The buyer will typically insist on confidentiality, non-solicitation and non-compete provisions in the definitive agreement that restrict the seller from operating a similar business, calling on customers or hiring away the employees. The seller makes extensive 'representations and warranties' in the definitive agreement relating to the business operations, title to

the stock or assets being sold, compliance with laws, payment of taxes, claims or pending litigation and similar matters.

Disclosure schedules provide detailed information to the buyer regarding the business and typically identify: the owners of the business and the capital structure, the business assets, customer and vendor contracts, leases, employee matters, benefit plans maintained by the seller, debt obligations, violations of laws or regulations and other information that is provided or discovered during due diligence.

While a thorough due diligence investigation is critical, equally important are accurate and complete disclosure schedules, which impact the representations and warranties made by the seller.

What is involved in closing the transaction?

To close the acquisition or sale, the buyer may need to line up financing if it has insufficient cash on hand. Typically, the lender will take a lien on the stock or assets being acquired by the buyer. Other aspects include the transfer or issuance of licenses and permits to the buyer, obtaining consents of landlords, customers and vendors if contracts are being assigned, transfer of title to real estate and motor vehicles, payoff of the seller's debt obligations, and transfer/hiring of employees. An experienced team of advisers is key to a successful closing. •