

Share and Asset Purchases

Overview

The two principal means of acquiring a business are by way of an asset or share purchase. An asset purchase may involve the purchase of some or all the assets of a business, usually without the assumption of historical liabilities. In the case of a share purchase, the company is purchased with all assets and liabilities within it. The purchaser will not be direct owner of the assets or be subject to the liabilities. He will own the shares but the value of the shares will depend on the assets within the company, net of the liabilities.

Sometimes, a particular business within a company may be packaged into a new company by way of re-organisation and that company will then itself, be sold. This is commonly called a **hive off** or **hive-down** and is often undertaken in the context of insolvencies of existing companies. Stamp duty and other tax reliefs are generally available on transfers between UK companies although the relief may be lost on subsequent disposals to third parties.

The law and practice in relation to share sales and purchases in England and Wales is broadly similar to that in Ireland. The standard Share Purchase Agreements and Asset Purchase forms used in Ireland are largely derived from equivalent English documentation. Many similar issues arise due to broadly similar Company law and taxation issues.

The purchaser of a company takes it lock, stock and barrel, subject to all existing liabilities and claims (within the company). Accordingly, the warranties and indemnities required in a share purchase will be substantially greater. An asset purchase may be preferable in that there may be concerns about past unquantifiable and unknown liabilities. With an asset purchase, it may be possible to cherry pick assets.

With an asset purchase, only the selected assets and liabilities are acquired. An asset purchase may involve the transfer of separate assets making up the business. It is more likely that the consent of third parties will be required in the case of an asset sale than in the case of a share purchase. Properties held under leasehold or business contracts with third parties, will generally require the consent of the third party to the change of identity occurring upon sale of the assets.

Tax will always be a consideration. The classes of assets subject to stamp duty in the UK are narrower than in Ireland. The top rate of Stamp Duty Land Tax is 4%. The rate of stamp duty or stamp duty reserve tax applicable on sale shares is 0.5%. See our separate note by way of general outline of the issues involved.

Regulation of Share Promoters

The Financial Services Promotion legislation in the UK was substantially reformed in 2000. It is similar to, but a more modernised version of, that applicable in Ireland. There is a general prohibition on financial promotion. A person must not, in the course of business, communicate or invite anyone to engage in investment activity unless he is authorised. Invitations and inducements by any methods whatsoever are caught.

This issue is separate to the requirements for a prospectus in marketing shares to the public. This regulation deals with the regulation of intermediaries as opposed to requirements that may apply to the company. See our separate chapter on the public sale of shares and exemptions from the requirements for a prospectus.

Financial promotion can only be undertaken by persons authorised under the Financial Services legislation. There are exemptions available which are relevant to private share purchase and sales. There is an exemption for a share transaction between a single seller and buyer in which the buyer will obtain at least 50% of the voting shares in the target. The financial promotions restrictions do not apply to an asset purchase.

Due Diligence

Due diligence is an information gathering process, where the buyer endeavours to find out as much as possible about the company or assets being purchased. The aim is to obtain a picture of the target in terms of strength, weaknesses and potential liabilities.

Due diligence is an essential preliminary to contractual protection in the form of warranties and indemnities based on an identified level of protection needed and any risks which the buyer should completely avoid. The level of due diligence will be greater for share purchases, because of the greater level of risk undertaken.

Due diligence will generally comprise an assessment of the financial, legal and commercial status of the buyer. It will usually be undertaken by the buyer's financial and legal advisers in conjunction with the buyer's own personnel.

The financial due diligence will usually be undertaken by the parties' accountant or financial adviser. It will involve inspection of the working papers of the seller's accountants and lengthy discussions with management and his accountants.

Legal due diligence will usually be carried out by way of questions and responses on a wide range of matters. The seller usually collates information and documentation requested by the buyer's legal advisers who will analyse it.

Typically, a first draft of the Share Purchase Agreement will be circulated before due diligence is completed. The buyer's solicitor will examine the warranties required in the light of due diligence and suggest amendments as appropriate.

Due diligence is only as good as the seller's will to co-operate. However, if a seller believes that a buyer is seriously intent upon purchasing, it will have an incentive to co-operate. There is no legal obligation on a seller to respond. This would not cover dishonest concealment of facts which is not permitted.

Share Purchase Agreement

The Share Purchase Agreement is the principal contract regulating the acquisition of the shares of a company or a group of companies. It is the key agreement and contains the terms and conditions of sale. Depending on the complexity and the size of the transaction, the agreement can often run to more than 100 pages. It will typically contain conditions precedent that the sale may be subject to lists of matters to be delivered and indemnities and warranties. The agreement is traditionally drafted by the buyer, except in an auction type sale.

Typically, the Share Purchase Agreement will be accompanied by a number of documents, including the Disclosure Letter and the Tax Deed. The Disclosure Letter will seek to limit the extent of the warranties by disclosing matters to which the warranties are subject e.g. known problems, qualifications or deviations from the standard warranty.

The Tax Deed is an indemnity to the company and the acquirers in respect of unexpected tax liability.

Asset purchase agreement

An asset purchase agreement is the contract dealing with the purchase and sale of assets. Asset purchase agreements are usually shorter than share purchase agreements. The asset purchase agreement may provide for a simultaneous exchange and completion or it may provide for an interim period. The latter will be significantly more complex as it will have to preserve the position in accordance with the deal in the interim period.

The business will generally be expressed to be sold as a going concern. This will allow exemption for VAT and will provide that employee contracts are automatically transferred under the TUPE regulations.

The agreement will specify the price and other commercial terms. It may be payable in cash shares or stocks option. It might be fixed or may be linked to assets or future profitability.

This Guide is intended as an overview and broad outline of the matters covered in it. Its purpose is to inform and raise awareness. We are happy to offer specific legal advice on particular circumstances.

This Guide should not be relied on as a substitute for comprehensive legal advice with reference to the particular circumstances.

While we have taken due care in the preparation of this publication, we do not accept legal liability as a result of any reliance placed on anything in this Guide. The reader should rely only on specific legal or taxation advice.