

BASIC DEAL STRUCTURES – ASSET PURCHASE VS SHARE PURCHASE

While the current economic situation has brought about a number of significant challenges for some businesses, for other businesses it has presented the opportunity to make acquisitions. At the very heart of any discussion concerning business acquisitions is the much debated question of whether such transactions should be effected by purchasing the company's shares or assets.

This article addresses the key differences between an asset and a share purchase. Both methods have benefits and the final decision about which method to adopt will ultimately be determined by the commercial needs of the parties.

ASSET PURCHASE

The basic reason for an asset sale is that the disposition of some or all of the assets by the vendor company does not result in the transfer of ownership of the corporate entity. The implications of this are far reaching and underlie much of the following discussion.

From a purchaser's point of view, certainty is the key benefit gained from purchasing the assets of a company. The purchaser can effectively specify the assets they wish to purchase and the liabilities they wishes to assume. Because the vendor retains ownership of the company, the purchaser does not assume the risk of any unknown or contingent liabilities, such as tax, product liability and employment obligations. Accordingly, the due diligence required can be more focused and often undertaken with reduced cost and time. This is particularly so in the case of large companies where many of the liabilities may be unknown or unascertainable.

However, because the transfer of individual assets often needs to be effected under separate documentation, transactions requiring the transfer of a large number of assets can be complicated and time consuming, with the final settlement prolonged.

The extent to which the assets of the vendor company are sold will determine whether the transaction may be classified as a going concern for tax purposes, and thus be zero rated. Although the requirements to be classified as a going concern are too numerous to include in this short article, it is important to note that assets sold which do not meet the going concern requirements will attract GST.

SHARE PURCHASE

In a share purchase, the purchaser takes a transfer of the vendor's shares in a company, thereby enabling the purchaser to essentially step into the shoes of the vendor. Logistically, this streamlines the transfer of ownership of all the company's assets and liabilities, as well as ensuring the company's corporate identity is retained. For this reason a share sale is generally less complex and legal settlement is typically achieved more quickly.

However, a significant disadvantage is that the purchaser of all the shares in a company also assumes all of the company's liabilities, including those unknown at the time of settlement. Accordingly, due diligence required for share sales are more involved given the wide ranging liabilities potentially being transferred. Purchasers should remember that they can take warranties or guarantees from the vendor to protect against some surprise liabilities.

Another challenge associated with a share sale is reaching agreement on a valuation for the entire business, including intangible assets such as goodwill, the difficulty of which is often compounded by the lack of publicly available information.

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CONCLUSION

Vendors will often prefer share sales as it allows them to completely step away from the business and all future obligations. Purchasers, on the other hand, will often prefer asset sales because it provides a far greater degree of certainty as to what is being acquired. It is important to ascertain the parties' objectives from the outset and determine the extent to which the parties wish to transfer the entire business as an operating entity or just key pieces of plant and equipment.

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