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A Guide to Buying or Selling a Business



Introduction

In this note, we briefly explain the most common ways of buying or selling a business, the main points to consider, some differences between them and the process.

Most common options

When buying or selling a business, two options most commonly present themselves, which are:

1. a transfer of the shares in a company, which owns the business, by the shareholders; or
2. a transfer of the business itself.

A transfer of shares is conceptually straightforward. However, a business sale is not quite so obvious - it is a shorthand expression covering anything from the sale of the whole of the assets and undertaking of the seller (which could be a company, partnership or sole trader) to the sale of just a few assets, which are assumed to be capable of being operated as a separate business. One of these assets would generally be the goodwill attaching to the business, for without this, the transaction would constitute merely the transfer of assets, rather than the transfer of a business.

Early stage considerations

There are a number of key points to consider before buying or selling a business, including:

- deciding whether the transaction is to be a transfer of shares or the transfer of the assets comprising the business; and
- understanding the share transfer process or the business transfer process that in each case commonly gone through before the transfer agreement is produced.

The viewpoint of the seller and the buyer will be fundamentally different in each transaction. In practice, it will be the relative bargaining positions of each side which will determine the shape of the final agreement between them.



In the following sections, we explain the share transfer process and the business transfer process and the main issues to consider in more detail.

Transfer of Shares

Main issues to consider on the transfer of shares are as follows:

Continuity

A change in the ownership of the company effected by a transfer of its shares by the shareholders does not generally interrupt the company's business; its contracts with customers and suppliers remain in place, as do those with its employees, and its ownership of its assets is unaffected.

Simplicity

Since the company continues as a separate entity, with a transfer of shares, there is no need to deal with a number of third parties, such as landlords, debtors and customers, to seek their consent to the assignment of individual assets such as leases, debts and contracts.

Direct receipt of consideration

The payment for the transfer of shares goes straight into the hands of the selling shareholders. With a business transfer, the payment for the transfer of the assets comprising the business is to the selling company and it then has to make some form of distribution to get the proceeds of sale into the hands of its shareholders.

Tax on capital gains

A number of tax reliefs are possible with a share transfer, such as Business Asset Disposal Relief (previously known as Entrepreneurs' Relief). The availability of any relief and other tax considerations will often be central to the decision as to what type of transaction the parties are willing to agree to.

Employees

The company's contracts of employment with its employees will not be affected by a transfer of shares. In a business sale, much the same result is achieved, but by operation of the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), although in practice, TUPE can be wearisome, both in complying with the requirements and because of their inconsistent interpretation by the courts.

Stamp Duty

The rate of Stamp Duty applying on a transfer of shares is 0.5% and this is payable by the buyer.

On a business transfer involving the transfer of property or land, Stamp Duty Land Tax (SDLT) may be payable by the buyer. The rate payable will depend upon the amount being paid for the property or land and whether it is freehold or leasehold and will also depend upon whether the property or land in question is residential or non-residential or mixed use.

Regulated activities

With a transfer of shares, the advisors need to consider whether advice provided constitutes a regulated activity and whether the promotion of a share sale is subject to the legal controls on financial promotions.

Financial assistance

A private limited company may give financial assistance for the purpose of the acquisition of its own shares. A public company is prohibited in giving financial assistance, but there are some exceptions to this general prohibition.

Transfer of a Business

Main issues to be considered with the transfer of a business include:

Clean break

The buyer does not acquire the historic tax and trading liabilities of a company on transfer as it would do with a transfer of shares.

Cherry picking

With the exception that the buyer would take on the employees of the business pursuant to TUPE, the parties can otherwise decide which assets and liabilities should transfer to the buyer and which should remain with the seller. For example, a significant liability could be left behind with the seller.

Tax

A buyer will not have the benefit of capital allowances on the purchase of shares, but for the purchase of certain assets they will be available. A corporate buyer may be entitled to a tax deduction on the acquisition of goodwill.

As referred to earlier in this note, SDLT may also be payable by the buyer on the transfer of any property or land assets, if they are transferred as part of a transfer of business.

Share Transfer or Business Transfer Process

Whether you decide on a share transfer or a business transfer, the process is likely to include some or all of the following elements:

Non-disclosure agreement

The seller may wish the prospective buyer to agree that any information provided will be kept confidential, including the fact that negotiations are taking place.

Lock-out or exclusivity agreement

The buyer may wish the seller to agree not to enter into negotiations with any other party for an agreed period during which the parties hope the transaction will be completed.

Heads of terms

The parties may wish to sign short-form and, generally speaking, non-binding heads of terms, which confirm their agreement on the principal issues that the subsequent main agreement will provide for.

Due diligence

The buyer will want to ask questions about, and seek a more detailed understanding of, the company/business they are buying. The seller will normally provide that information by written response to a questionnaire with supporting documentation that is usually provided to the buyer and their advisors to view via a virtual data room.

Share/business transfer agreement

This is the principal document which will set out the detailed agreement between the parties as to the terms on which the shares or the assets comprising the business will be transferred, including what assurances about the company or the business will be given to the buyer by the seller.

Disclosure letter and bundle

The seller normally gives certain warranties about the company or the business to the buyer. Some of those warranties may be true, subject to specific exceptions. The seller can, by disclosing those exceptions to the buyer at the time of sale, prevent them from becoming the subject of a warranty claim after completion.

Ancillary documents

The parties will usually need to enter into various ancillary documents to put into effect the transfer of the shares or the business. These documents will vary from transaction to transaction and will depend upon the type of business being bought and sold.

Stamp Duty Land Tax (at rates of up to 5%) will be payable on the transfer of property assets if transferred as part of a transfer of business.

Summary of the main differences between a share transfer and a business transfer

	Share Transfer	Business Transfer
Ability to cherry pick?	When the shares in the company are sold, the buyer takes all assets and liabilities, known and unknown.	With the exception that the buyer is bound to take the employees of the business, the parties can otherwise decide which assets and liabilities should transfer to the buyer and which should stay. For example, a significant liability could be left behind with the seller.
Due diligence	The buyer will want to ask questions about, and seek a more detailed understanding of, the company they are buying. The seller will normally provide that information by written response to a questionnaire with supporting documentation provided to the buyer and their advisors via a virtual data room.	Generally, the due diligence is less with a business purchase as fewer liabilities will transfer with the assets.
Warranties and indemnities	As the buyer is taking on all liabilities of the company, the buyer will usually require extensive warranties and indemnities in the Share Purchase Agreement (SPA). As a guideline, a full form SPA runs to over 100 pages long.	Generally, less warranties and indemnities are required as the buyer can exclude most liabilities (for example, the buyer does not acquire the historic tax and trading liabilities of a company on a business transfer).
Disclosure	The seller normally gives certain warranties about the company to the buyer. Some of those warranties may be true, subject to specific exceptions. The seller can, by disclosing those exceptions to the buyer at the time of sale, prevent them from becoming the subject of a warranty claim after completion.	As there are normally substantially less warranties when the assets comprising the business are being transferred, the disclosure process will be greatly reduced compared with a share transfer.
Employees	The company's contracts of employment with its employees will not be affected by a transfer of shares.	In a business transfer, much the same result as a share transfer is achieved, but by operation of TUPE, although in practice, they can be wearisome, both in complying with the requirements and because of their inconsistent interpretation by the courts.
Continuity	A change in the ownership of the company effected by a transfer of its shares by the shareholders does not generally interrupt the company's business; its contracts with customers and suppliers remain in place, as do those with its employees, and its ownership of its assets is unaffected.	If contracts form part of the business assets being sold/acquired, these will need to be novated or assigned to the buyer and consent of the other contracting party is often required.

	Share Transfer	Business Transfer						
Taxation	<p>A Capital Gains Tax (CGT) may be payable by an individual seller if a number of conditions are met. The rate payable will be 10% or 20%, depending on individual circumstances.</p> <p>Business Asset Disposal Relief (previously known as Entrepreneurs' Relief)</p> <p>Disposals of shares in a trading company for which the individual works and holds 5% or more of the share capital may qualify for Business Asset Relief (BADR) if they have been owned for at least two years up to the date of sale.</p> <p>An individual will qualify for relief on all disposals until the lifetime total of such gains reaches £1m. The first £1m of the gains will be charged to CGT at 10% instead of 10% or 20%</p>	<p>A buyer will not have the benefit of Capital Allowances on the purchase of shares, but for the purchase of certain assets they will be available. A corporate purchaser may be entitled to a tax deduction on the acquisition of goodwill.</p> <p>For a seller, there may be a double tax charge, firstly on the seller company and secondly on the shareholders on distribution of the proceeds.</p> <p>Provided the transaction qualifies as a transfer of a business as a going concern, VAT is not chargeable.</p>						
Stamp Duty	<p>Stamp Duty is charged on the total consideration of the shares (paid by the buyer) if it is over £1,000.</p> <p>The rate of tax payable is 0.5%.</p>	<p>The buyer pays SDLT on increasing portions of the property price (or consideration) if the buyer pays £150,000 or more for non-residential or mixed-use land or property.</p> <p>The current rates of tax are:</p> <table border="0"> <tr> <td>Up to £150,000</td> <td>Nil</td> </tr> <tr> <td>The portion from £150,001 to £250,000</td> <td>2%</td> </tr> <tr> <td>The portion above £250,000</td> <td>5%</td> </tr> </table> <p>Please note, between 8 July 2020 and 31 March 2021, the threshold for residential property is £500,000 and the portions and rates of tax are different.</p>	Up to £150,000	Nil	The portion from £150,001 to £250,000	2%	The portion above £250,000	5%
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The portion from £150,001 to £250,000	2%							
The portion above £250,000	5%							

Legal fees

Legal fees are a significant but necessary expense in ensuring your interests are adequately protected when buying or selling a business. They should be discussed with your legal advisor at the outset.

At TWM, we understand that clients have different needs and priorities when it comes to legal advice and that each transaction is different. We, therefore, welcome an initial, no obligation discussion in confidence at the outset of any transaction to better understand your needs and requirements, rather than simply providing a one size fits all approach to our work and fees.

We are up front about our fees and can offer a flexible approach to the way that we work and our pricing. We can offer estimated fees, fixed fees, capped fees and are happy to discuss sharing the risk on fees with our clients.

If you would like to know more, please get in touch with us.



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For further information, please contact a member of our Business Law team, or get in touch with your usual solicitor at TWM Solicitors.

Disclaimer

Whilst we have made reasonable efforts to ensure this guidance note is accurate, it is only intended to be a brief introduction to buying and selling a business and it is for information purposes only.

This note does not constitute any legal or other advice. You should take detailed specialist advice before taking or refraining from any action as a result of the comments made in this publication.

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