



Mergers and Acquisitions

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M&A Matters To Consider Before Embarking on a Sale or Purchase of a Business

Whether you are a Buyer or Seller, there are special issues you should consider before you enter a term sheet or letter of intent with an interested party (even non-binding letters of intent).

1. Structure of Transaction

1. Asset v. Equity /Stock Sale
2. What buyers prefer and what sellers prefer, and why

2. Your Current Entity Structure/Special Considerations

1. Are you an LLC, Corporation, S. Corporation?
2. Do you have any special qualifications: size, certifications?

3. Due Diligence

1. Special considerations for government contracts
2. Compliance issues
3. Assignment and Novation issues
4. Tax issues

1. Structure of Transaction

1. Asset Sale

1. Buyer purchases certain assets of the Seller and assumes certain contracts and liabilities
2. Assumes certain contracts, but not all
3. Simpler transaction documents; asset purchase agreement, bill of sale, and assignment documents

2. Equity/Stock Sale

1. Buyer purchases the stock or membership interest of the Seller entity, so the entity goes through a change of control/ownership
2. All contracts and liabilities are assumed, except as negotiated by the parties (in limited circumstances)
3. Stock or equity purchase agreement

Structure of Transaction (Cont'd)

Asset v. Equity Sales — Considerations for Buyers and Sellers

1. Seller: Typically prefers an equity/stock sale, while a Buyer prefers an assets sale.
2. Buyers favor an assets sale
 1. Liability: because of less liability issues with an asset sale, as they avoid inheriting existing liabilities issues with the Seller entity, especially contract disputes, employee lawsuits, employee benefit issues
 2. More robust/costly due diligence process
3. Sellers favor stock/equity sale
 1. Liability: Buyer takes on all company's contracts, risks, liabilities, employees ... etc.
 2. Practical considerations: Most contracts include assignment provisions that require consent in an "assignment" situation, however, few require consent or notice in a change of control or ownership, so easier assumption of Seller existing contracts

Structure of Transaction (Cont'd)

Asset v. Equity Sales — Special Tax Considerations

1. Buyer (why an asset sale):

1. Buyer can allocate part of the purchase price to depreciable assets, providing for a post-closing tax benefit
2. Can negotiate the allocation of the purchase price of certain assets and allocating higher values to assets that depreciate quickly and lower values to assets that amortize slowly
3. More flexibility and simpler structure of transaction

Structure of Transaction (Cont'd)

Asset v. Equity Sales — Special Tax Considerations

1. Seller (why an equity sale):

1. All gain of stock/equity sale is taxed at the lower capital gain rate
2. For an asset sale, Buyer's allocation of purchase price to certain assets may trigger depreciation recapture for the seller, which is considered ordinary income
3. More complex structure in certain circumstances, if Seller is an S. corporation for example, there are certain requirements for ownership of an S. corporation (must be an individual owner not an entity, only certain number of individual owners, no foreign owners ... etc.)
4. May require certain restructuring of transaction or conversion of Seller entity into a different form pre-closing such as F. Reorg.)

2. Entity Type and Special Considerations for Parties

1. Seller Entity types:

1. Limited liability company ("LLC"). Is it a single-member LLC, or multi-member. Any special tax treatments?
2. Corporations ("Corp.") C. Corp. or S. Corp. How many shareholders/stockholders. Any option holders?

2. Special Qualifications of Seller Entity:

1. Provided by U.S. Small Business Administration ("SBA")
2. Allows certified business to access and complete for government contracts, as well as private sector contracts
3. Ability to form joint ventures with other businesses with similar certifications to compete for certain contract

Special Considerations (Cont'd)

1. Special Qualifications of Seller Entity (Cont'd):

1. 8(a) Small Business Certification ("SDB"). Business owners who are "socially or economically disadvantaged."
2. HUBZone Business certification ("HUBZone"). Historically underutilized business zone.
3. Women-owned Small Business ("WOSB"). Must be owned 51% by women who are US citizens.
4. Minority-owned business certification ("MBE"). Must be at least 51% minority owned.
5. B-corporations ("B. Corp"). For profit but driven by a social missions. Typically, uses profits to impact social change.
6. Veteran-owned business ("VBE").
7. LGBTQ+ business certification ("LGBTBE").

Special Considerations (Cont'd)

1. Special Qualifications of Seller Entity (Cont'd)

- How the qualifications affect Buyer
- Is Buyer able to keep qualification post-Closing, especially if Buyer is private equity buyer ("PE")
- Multi-year contract issues
- Future contract awards and profit considerations
- Other issues

3. Due Diligence and Disclosure Schedules

1. Process looks the same whether stock or asset sale; however, Buyers tend to conduct a more robust diligence process with stock or equity purchase
2. Due diligence v. disclosure schedules
3. Assignment and change of control provisions
4. Consent issues and timing of Closing
5. Regulatory issues
6. Late disclosure of audits, investigations, or litigations issues
7. Anti-corruption provisions and disclosures
8. Foreign operations of Sellers and tax implications
9. Operations between signing and closing of transactions; obligations to disclose

Questions?

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