

ASSET SALES VERSUS SHARE SALE

One of the most important questions to ask in the purchase or sale of a business is whether or not it is the assets that are being sold or the shares in the company that owns the assets that are being sold. The answer to that question can have profound implications to both buyer and seller.

In the sale of assets the parties can choose the assets that are subject to the acquisition and the obligations and liabilities, if any, to be assumed by the purchaser. In a share sale transaction all of the assets and liabilities of the company are, in effect, the indirect subject matter of the transaction because by buying all or a majority of the shares of the company, the end result is that the purchaser owns the company that owns the assets and has all of the liabilities and obligations. In general terms it is usually more advantageous for the purchaser to buy assets while it is, conversely, more advantageous for the vendor to sell shares.

The resolution of this conflict is usually done through pricing and other negotiated terms. Quite often, it is the income tax and other tax consequences that will be determinative of the way the transaction proceeds.

Each method of transferring ownership has its own advantages and drawbacks. For example, conveyancing costs, that is to say the costs of hiring a professional (lawyer or notary) to actually transfer the ownership of the assets, is much higher in an asset transfer.

Similarly, there are also registration costs such as Property Transfer Tax on land, Social Services tax on chattels and GST on things like trademarks. There may also be commission costs (for example, realtor's fees on land sales) incurred in an asset transfer. If land has to be transferred, the seller may have to pay a hefty commission while the buyer will have to pay for the property transfer tax of 2 percent of the first \$200,000 and 1 percent thereafter. These costs can make a substantial difference.

If you are buying the company that owns the land, instead of buying the land itself, you usually only have to register the transfer of the shares in the minute book and make a few filings with the company's branch, all of which is much less expensive than full conveyancing and registration costs that would otherwise be incurred.

On the other hand, share purchases may cause problems if you have to give minority shareholders their rights of first refusal or if there are other restrictions on the sale of shares. Minority shareholders may even oppose the sale of shares and hold up a transaction in the courts, with great legal expenses as a result. In some sales government approvals, for example those required under the Forestry Act or the Liquor Control and Licensing Act, may also be required. It may also require third party consents, which often take quite a bit of time to secure.

There is also the trouble of undisclosed or underestimated liabilities. In most cases it will be the share purchaser who takes on these problems while the asset purchaser usually avoids them. However, some liabilities, such as income tax reassessments or environmental liabilities, will follow the transaction and "flow through" the asset purchase. In the case of pollution, previous owners may be held responsible years and even decades later for pollution that occurred while they were the owner of the land.

Another important consideration in determining which way is the best is to consider what happens to the employees of the business and the obligations of the employer to the employees. In the share purchase, the new owner takes the company subject to the claims of the employees of the business. It sometimes comes as a shock to new owners when they go to fire an employee (who worked for the former owner for years) and they find out that they owe the employee a year or more of severance pay even though the employee may have only worked for the new owner for a few weeks or months.

In an asset purchase the employees are not the subject of the sale. For purchasers who intend on downsizing or automating or merging the business with an existing business, this can have a considerable impact on the way the sale is structured.

If there's a collective bargaining agreement, it may not be possible to avoid it in an asset purchase if an application is made under the Labor Relations Code by the union. Similarly, things like pension plans and employee benefit plans may also have to be acquired or assumed and that can be particularly costly in some situations.

In the end result, this is one of those situations where it pays to get good advice before you start negotiating a purchase or sale. Although it may cost you a few hundred dollars to talk to your accountant and your lawyer beforehand, chances are very good that you'll more than pay for the cost of their services with the amount of money you save by structuring the purchase or sale appropriately.