In any M&A transaction, one of the first questions for the parties to the transaction is how the deal should be structured. Whether to provide for the buyer to acquire the assets or the stock (or other equity interests) of the target company will impact virtually every aspect of the deal. At times, the choice for the optimal structure is apparent and quickly agreed; other times, parties can spend significant time and resources working to agree on this threshold determination. When the time comes to draft the definitive purchase agreement, there will be significant differences in the agreement depending on the type of transaction structure agreed upon by the buyer and the seller.

This article does not address the tax considerations involved in pursuing an asset deal versus a stock deal; however, the choice of structure often is driven by tax implications that are complex and deal specific. Involving tax counsel and accounting advisors early in an M&A process, ideally before negotiating a letter of intent or other acquisition proposal, can save time and money in the long run.

**Asset Sale**

An asset sale transaction involves the sale of some or all of the assets used in a business from a selling company to a buyer. The purchased assets often encompass all or substantially all of the assets of the company; other times, the transferred assets include only those used in a specific division or certain selected assets of the company. In an asset deal, typically the buyer will assume only certain specified liabilities of the business from the selling company.

A benefit of an asset sale is that it allows the parties significant flexibility as to what assets and liabilities are included in the transaction. In particular, for a buyer this provides an opportunity to reduce its risk of assuming unknown liabilities of the acquired business. Additionally, an asset sale allows a buyer to avoid spending money on unwanted assets. For a seller, an asset sale is often not preferred over a stock sale, but in some instances it is ideal for allowing a seller to dispose of just a portion of its holdings. Asset sales often are used in connection with the sale of a distressed business, the sale of a business division, or in transactions where there are significant concerns regarding known and unknown liabilities of the business.

**Stock Sale**

A stock or equity sale transaction involves the sale of the equity interests in a target company from the equity holders to a buyer. In a stock deal, instead of choosing specific assets and liabilities to acquire, the buyer purchases an ownership stake in the entire business. In effect, the buyer acquires the entity instead of acquiring the business from the entity.

A stock sale is often favored by the owners of a selling company because, in general, all of the known and unknown liabilities of the business are transferred to the buyer, and therefore the sellers avoid ongoing...
exposure to such liabilities (other than as expressly agreed with the buyer). Buyers often resist a stock sale transaction unless the company to be acquired has a clean operating history or there are significant practical difficulties in completing an asset sale, such as restrictions on the transfer of certain assets from the selling company to the buyer or burdensome third party consents needed to transfer the assets.

Though this article has used the term “stock sale” to describe the primary alternative to an asset sale, it should be noted that another common M&A transaction structure, a merger, provides another alternative. A merger is, in many ways, similar to a stock deal in that the buyer acquires the entire entity operating the business, including all of the assets and liabilities of the business. However, if the company has a significant number of stockholders, the stockholders are not easily accessible or there is a risk that all of the stockholders will not support the transaction, then a merger may be preferable to a stock sale. This is due to the fact that a stock sale requires each and every stockholder to agree to sell such holder’s equity, while a merger usually requires approval of less than all of the stockholders. There are other considerations, including tax considerations, to attend to in opting for a merger instead of a stock sale and any party to a potential M&A transaction should discuss these with its legal and tax advisors.

**Drafting Considerations**

Depending on whether an acquisition is structured as an asset sale or a stock sale (or merger), there will be significant differences in the transaction documents. A substantial portion of an asset purchase agreement is used to identify the assets to be acquired and the liabilities to be assumed by the buyer. Typically, the buyer will want the asset purchase agreement to provide that the buyer disclaims any obligations other than those liabilities that are expressly assumed. If the provisions describing the acquired assets and assumed liabilities are carefully written, then the representations and warranties from the seller can be limited to focus on items that have or might impact such assets and liabilities. In addition to an asset purchase agreement, other ancillary agreements will be required to transfer the assets from the seller to the buyer. These might include a bill of sale, assignment and assumption agreements, intellectual property assignments and corporate name change filings, as well as agreements providing for the hiring of the employees of the business by the buyer.

In a stock sale, the purchase agreement will not describe specific assets and liabilities of the business to be acquired since the entire spectrum of assets and liabilities of the business will transfer to the buyer along with the entity that is purchased. As such, typically the representations and warranties in a stock purchase agreement from the seller to the buyer will be more comprehensive and broader in scope, covering all aspects of the acquired business and the historical operations of the entity. While additional ancillary agreements are required in a stock sale, often fewer are needed than in an asset sale and, typically, the number of third party consents needed to complete the deal is much lower.

**Conclusion**

Deciding on the best deal structure for an M&A transaction requires evaluation of a number of factors, some of which are complex or deal specific. The determination of the optimal structure should be made as early as possible, since the decision will impact virtually all of the transaction documents. If you are considering a significant M&A transaction, whether as the potential buyer or seller, you should consult with your legal counsel and tax and accounting advisors early in the process to avoid potential delays and unnecessary expense.
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