

## **Buying and Selling a Small Business: Analyzing the Purchase Agreement**

This article is the first in a series analyzing the basic provisions of purchase agreements for the sale of a small business.

Buyers and sellers of businesses can effectuate the sale of a business in two basic ways: a stock sale or a sale of assets. While an examination of the differences between these transactions is fodder for other articles, the overly simple distinction is that, in a stock sale, the buyer is getting the "whole" business whereas in an asset sale, subject to negotiation, the buyer is picking and choosing the assets and liabilities of the business that it will keep and the seller is retaining the rest. Put another way, in a stock sale, the seller is generally washing its hands of the business at closing while in a sale of assets, the seller will still be intertwined with the business for a period of time. In actuality, stock purchases still require the seller to be on the hook in various ways, including indemnification provisions, earnouts, and holdbacks, all of which will be discussed later. In a very general sense, however, a stock sale can be thought of as more of a wholesale divestiture of the business.

Stock Purchase Agreements ("SPAs") and Asset Purchase Agreements ("APAs") will differ in numerous ways, but both will address similar major issues. Throughout this series, we will look at eight clauses that appear in both types of agreements and, where appropriate, review the differences between the two. This article outlines the eight provisions at issue and initiates analysis by looking at the Introduction to an agreement for the sale of a business. Over the next few weeks, we will inspect one or two clauses per article as we work our way through these essential agreements.

**1. Introduction.** Establishes the names of the parties, the nature of the agreement, and notes the factual background that is the subject of the agreement.

**2. Sale and closing.** Defines the terms of the sale, the price to be paid, and the manner in which it will be paid. This section also sets the time, place and circumstances of the closing, which is the time when title will transfer from the seller to the buyer and consideration will transfer from the buyer to the seller.

**3. Representations and warranties.** In this generally lengthy section, the parties set forth the representations and warranties on which the parties are relying for the basis of the sale. Representations are statements made by one party at the time the contract is entered into, regarding a fact which is influential in bringing about the agreement. A warranty is a promise that a statement of fact is true.

- 4. Preclosing covenants.** This section states the parties' promises to do or not do certain things prior to closing. The seller bears the bulk of the responsibilities here, and will generally be required to operate the company in the ordinary course of business, among other promises.
  - 5. Preclosing conditions.** Unlike a covenant, which is a promise, conditions are things that must be satisfied prior to closing. If any required condition does not occur, a party may walk away from the deal.
  - 6. Postclosing covenants.** As with preclosing covenants, these are things that the parties are required to do, or must refrain from doing, after the closing and may include employee issues, continuing assistance of the seller, noncompetition issues and further assurances, among others.
  - 7. Remedies and indemnification.** This section will set forth the amount of time after closing that the representations and warranties will survive. It will also specify how the parties will indemnify each other for breaches of the Agreement.
  - 8. Miscellaneous.** The "boilerplate" section which, nonetheless, contains important provisions related to assignment, governing law, jurisdiction, and parol evidence, among others.
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**1. Introduction.** As the name implies, the introduction is the basic introductory paragraph setting forth the names and addresses of the parties, the date of the agreement and the types of entities entering into the contract.

The introduction will also likely set forth Recitals, or the underlying facts on which the agreement is based. While not necessary for an effective contract, the recitals provide background and make for easier reading of the contract, especially for someone who was not privy to the contract negotiations. A typical recital may state, "Buyer desires to purchase from Seller and Seller desires to sell to Buyer, subject to the Terms and Conditions of this agreement, all the business and properties of Seller in exchange for [price]. Therefore, in consideration of the mutual covenants set forth herein, the parties agree as follows..."

Our next article will look at the Sale and Closing Provisions.

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