

# Sale of Business

By Owen Vaughan

If you are selling your business, there is a high chance that the contract will be prepared using the standard form Agreement for Sale and Purchase of a Business developed by the Auckland District Law Society and the REINZ. This form has recently been updated and a new edition released, updating the 1995 form in many regards. There are many issues to be addressed in the sale of a business and set out below are some of the more important matters which will need consideration.

## Apportionment of purchase price

The total purchase price needs to be apportioned between tangible assets, intangible assets (which includes goodwill) and stock. Accounting advice must be taken before agreeing to these apportionments. Depreciation is recovered and tax payable in respect thereof by a vendor on any increase over book value for tangible assets, whilst on the other hand, a purchaser will wish the value apportioned to tangible assets to be as high as possible, to gain the maximum depreciation benefit.

## GST

Providing all of the assets of the business are sold, including provision of premises from which the business is to be carried out by lease or otherwise, then the sale will constitute a sale as a "going concern" for GST purposes. This means that the vendor does not have to account for GST on the sale and the purchaser does not need to fund GST on the purchase price pending a refund becoming available from the IRD. The transaction is zero rated for GST purposes.

## Stock

It is important for a purchaser to have a clear idea of the value of stock to be paid for on take-over. The contract requires the "in store" cost of stock to be inserted in the contract as at the date of the agreement. On settlement, a stock take takes place and the value established with allowance to be made for obsolete or damaged stock. For some businesses, there are established practices for agreeing on a valuer e.g. dairies/superettes use wholesale merchants, pharmacies use drug companies. It is important for the parties to agree on just who is to carry out the valuation and in some cases, the parties may agree that they will carry this out together. The agreement provides for a maximum percentage stock value adjustment. For example, if stock is valued at \$5,000.00, then the purchaser can elect which stock the purchaser wishes to acquire and the vendor will be required to remove any additional stock. On the settlement date, the purchaser pays to the vendor the estimated in store value of stock in trade and in addition, will need to lodge with the purchaser's solicitor a sum which is equivalent to the maximum percentage stock value adjustment. The purchaser's solicitor will be required to undertake to pay any additional sum for stock up to the maximum of this amount, once the stock value is known.

## Work in progress

The standard form does not cater for work in progress. The drafting committee discussed how work in progress could be incorporated into the standard form agreement, but after many hours of debate, it was finally agreed that as each business is unique, the parties need to specifically agree how work in progress is to be dealt with. There are no obvious differences between a manufacturing company and a retail business, which rendered it impossible to formulate a standard provision for work in progress.

## Vendor's assistance

The standard form agreement provides for the vendor to provide a period of assistance to the purchaser. The old agreement provided for this period of assistance to be following settlement, but is common for the parties to agree that the purchaser can have access to the business prior to the settlement and the period prior to settlement will then constitute the vendor's period of assistance.

## Restraints of trade

As a purchaser is invariably paying goodwill for the vendor's business, it is usual for a vendor to enter into a restraint of trade with the purchaser. The period of time and the area within which the vendor may not carry on a similar business, depends upon the nature and extent of the business. It is a matter for negotiation between the parties. If the vendor is a limited liability company, the standard form agreement provides for directors and shareholders to enter into a similar restraint. The agreement has provision for the

names of those persons who wish to be excluded from the restraint to be inserted.

## Approval of lease

More often than not, a business occupies leased premises and the lease is to be transferred to the purchaser in conjunction with the sale. There are comprehensive provisions relating to approval of the lease and for obtaining the landlord's consent. The provisions in the agreement relating to this contain specific timeframes and the parties' solicitors must pay careful attention to ensure that the agreement does not fail through inattention to these time restraints.

## Warranties

The vendor is obliged to provide a number of warranties on which the purchaser is entitled to rely on relating to the business and premises.

As between the vendor and purchaser, there will be any number of incomings and outgoings to be adjusted as at the settlement date. However not all outgoings are apportionable and it is only those outgoings which related to goods or services supplied to the vendor, where such goods and services have not been supplied in whole or in part by the settlement date. Consequently, pre-paid advertising, telephone listings or trade listings, may be apportionable whereas matters such as one off payments for trade association subscriptions are not. Over all, it is important to stress that both vendors and purchasers need to carefully consider the terms of any contract before signing same and heed the warnings on the standard form agreement to take professional advice before signing the contract. A few hundred dollars spent on professional advice may well be the difference between fully understanding just what the implications of the various contract terms are, and discovering these too late to escape the consequences.

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