As the Seller of an operating business, you need to make sure that you accurately describe the business and that you can follow through on any promises or warranties. You do not want to give the buyer an excuse to believe that any failure Buyer suffers results from some fraud on your part. If you are taking any part of the purchase price in a promissory note, you also need to be sure the Buyer has the ability and intent to pay it. Finally, you need to make sure you comply with all applicable laws and regulations governing the dissolution of a business. Here are a few things to keep in mind when preparing to sell a business.

**Asset or Stock Sale:** Most business sales today are asset sales, because a Buyer can avoid most of the liabilities of the Seller, and thus does not have to concern itself with what debts or liabilities may be lurking. However, even in an asset sale a careful Buyer will require representations about existing or potential liabilities and will want to review the Seller’s books and records. These two types of transactions have different tax consequences that vary depending on the Seller’s circumstances.

**Down Payment:** You should always require a down payment. It will show the Buyer’s commitment to the purchase, and will protect you if the Buyer walks away after all contingencies are satisfied. All or a portion of the down payment can become non-refundable under certain conditions, such as the passage of time.

**Timing:** As Seller, you will want the sale to close quickly once you have committed to it. It becomes difficult to keep customers and employees on track when they know a change of management is imminent. Therefore, you should build deadlines into any purchase agreement to keep the Buyer moving on its pre closing obligations.

**Buyer’s Financial Ability to Pay:** If the Buyer will pay part of the Purchase price as a promissory note to you, you need to determine that Buyer is credit worthy, and get adequate security. If you are relying primarily on the cashflow from the business to pay the loan, remember that once you sell the business, you give up control. You will want limits on the amount the Buyer can pay him/herself (and family members, etc.) before calculating profits available to pay you. You want to assure yourself that this Buyer can run the business at a profit. You may want to require periodic financial statements, and have the ability to call the loan if certain thresholds aren’t met.

The Note should be callable (i.e. you can force payment at your option) or automatically come due upon certain events, such as: (a) Buyer sells all or a substantial part of the assets to an unrelated third party; (b) Buyer sells more than a fixed percentage of ownership in Buyer (typically 25% - 49%); (c) Buyer materially defaults in the performance of a covenant in any of the sale documents, not limited to making prompt payments under the Note.)
You want to get appropriate security for any loan you hold. Types of security include a deed of trust (mortgage) on real estate, security agreement on the assets sold, personal guarantee, security interest in other assets. Remember that a second place lien position has serious drawbacks – to foreclose your lien, you must pay off (or take the property subject to) any prior lien. Also, if the person giving the guarantee is married, you should have the spouse guarantee the loan as well.

**Information you provide:** Make sure all the information you give is accurate, to the best of your knowledge after due inquiry. You do not want Buyer to have a claim against you for inaccurate information. Specify the date of financial information, and do not exaggerate the good or hide the bad.

**Accounts Receivable:** The Buyer may want to buy the accounts receivable, and pay the Seller a percentage of their value, or may want Seller to retain them so the Seller can worry about collecting them. If you sell the A/R, are you getting fair value for them? If you keep them, how will you collect them, without the assets of the business to back you up?

**Work-in-progress:** How are you going to divide the cost and benefits of WIP? You may have spent money in labor, raw materials and overhead to get the work partially completed; you should recoup that cost in the Purchase price.

**Inventories:** Prior to the closing date, you will need to provide a detailed list of the furnishings, fixtures & equipment being sold. Have you included items held for sale or rent; items held for use in jobs; the A/R; other assets? Are all listed assets actually owned by the company? If not, by whom, and how does company hold the assets? Also, make sure you let the Buyer know of any items you intend to retain.

**Allocation of purchase price:** The IRS requires you to allocate the purchase price among the various classes of assets. The allocation must make sense factually, and should have the minimal negative tax consequences for both sides. Often, the tax implications differ for the Buyer and the Seller. Make sure you understand the consequences of the allocation you choose.

**Titles and Evidence of Ownership:** If you are selling vehicles, you need to have the certificates of title to transfer to the Buyer. Other assets also may have specific evidence of title you will need to transfer: stock certificates, registration statements for software, etc.

**Existing Liens and Leases:** Buyer will likely require the Seller to list all liens that encumber any asset of the company. Buyer may choose to take the assets subject to the liens or may insist that you pay them off at or before closing. If you have any personal liability, you should make sure you get a release, either through an early pay off or the creditor’s agreement to an assumption and release. You do not want to remain on the hook for any obligation that is out of your control. Equipment leases may be costly to terminate/transfer. Who will pay those costs? Make sure you allow sufficient time. The Buyer will likely require that funds be escrowed to pay any lien remaining at closing.
**Generally, liabilities not specifically assumed remain with Seller:** In an asset purchase, Buyer generally assumes few liabilities. Make sure you know the actual balance of any liabilities you will be left with so that you know you are getting sufficient purchase money to pay them off.

**Tax issues:** Make sure company is up to date on all tax filings, especially employee and sales taxes (horrendous penalties if not). Tax issues can come back to haunt you years later, so be sure you take care of all taxes. Buyer will likely require a certificate from the taxing authorities that all employment and sales taxes are up to date.

**Employees:** Buyer will want to know what agreements the company has with any employees, written or oral, formal or informal. (Vacation, pension plans, 401-Ks, health insurance, sick leave, other benefits, pay rates or raises, special conditions, terms of employment, etc.) Does the company have written employment handbook, policies? You will likely have to allocate employee expenses and accrued vacation, etc. You will terminate the employees as of the sale date. Buyer may or may not choose to rehire them. If you have more than 100 employees, special rules apply.

**Licenses:** Does the company have all required licenses and permits? Are any licenses currently held by the business transferrable?

**Good Will and Trade Names:** In an Asset sale, the Seller usually sells all of the business’s good will and intangibles, such as trade names, phone numbers, web sites and URLs, intellectual property rights such as patents and copyrights, insignia and logos, as well as customer lists, contact lists, marketing brochures and other information, etc. You will no longer be able to use these assets, and may need to change its registered name.

**Covenant Not to Compete:** Buyer may want to restrict your right to compete after the sale. Generally, any covenant must be reasonable in time and geography. Five years is usually as long as a buyer can require non-competition, but lenders often like a longer period to match the term of any loan. The geographical boundary depends on the geographical scope of the business. In most cases, a court would enforce a clause preventing competition within the state of Utah, the Wasatch Front, or specific counties. You should negotiate for as narrow a restriction as you can get, and insist on being paid for the valuable rights you are giving up.

**Consulting Agreement:** Often, Buyer will want to be able to consult with you for a period following closing, to assure smooth entry into the business. How much assistance will the Buyer need? The value of your time to consult should be built into the purchase price, or expressly calculated separately. Make sure you put specific limits on your time, or you may find yourself working for free.

**Environmental Issues:** Any time you sell real property, the Buyer (or its lender) will likely require a Phase I Environmental Assessment, because all property owners are jointly and severally “potentially responsible parties,” liable under federal law for ALL clean up costs (even if the owner had nothing to do with the pollution). Buyer will ask you specific questions about hazardous materials, discharges, and other environmental issues, and will require representations and indemnities in the closing documents. If you think some
environmental issues might exist, you should go ahead and get a Phase I now, because you are already on the hook for whatever is there, and you can more accurately apportion cost and liability if you know the situation.

**OSHA compliance:** If you handle hazardous chemicals, or use machinery, this could be an issue that Buyer will ask about. You should know the company’s compliance history, and have the required safety/emergency equipment and procedures in place. Disgruntled workers are a primary source of complaints to OSHA and other governmental agencies. Keep your employees happy!

**Litigation:** You will have to disclose all existing or threatened litigation, regulatory actions, violations, etc. You may need to disclose the existence of disgruntled customers and employees (complaints, warranty claims, etc.). Investigate whether any potential claims are lurking before you make a “No litigation” representation.

**Real Estate Lease:** Your landlord may want to keep you on the hook. Begin negotiating for a release early. The landlord may want the Buyer to enter a new lease, or may want to have Seller sublet, depending on the market conditions.

**Restrictions on Sale:** Are there any restrictions on the sale of the company’s stock or assets – either imposed by law (SEC or IRS rules) or by agreement (by laws, shareholder’s agreement)? Make sure you are not violating any restrictions, by reviewing the by-laws, any shareholder agreements, stock subscription agreements, and stock certificates. Make sure everyone who has a right to vote on the transaction does so, and that Seller has followed all required corporate formalities.

**Dissolving Your Company:** In a stock sale (or sale of limited liability company membership interests), the shareholders/member get the money directly, the company stays in business, now owned by the Buyer. In an asset sale, the money goes to the selling company, and after the asset sale is completed, you still own the company and all it owns is the cash (and note) proceeds. You will need to dissolve the company and distribute the assets to the shareholders/members. There are a number of filings required to terminate a company. You want to make sure you do it correctly, so you don’t find yourself personally liable for a forgotten company debt, or having to answer nasty letters from the IRS claiming you have not filed some tax return.