CHECKLIST FOR SALE OR ACQUISITION OF A SMALL BUSINESS
(This is not intended to be exhaustive, only helpful)

The following points are items to consider when handling a business sale. Please note, however, that the enumerated points are not necessarily in order of importance to any particular transaction or the sequence they might arise in practice.

1. Avoid becoming involved as an attorney where you have any kind of interest in the transaction. (See ORPC 1.8 and Exclusion 8 of the PLF Coverage Plan, including the 10-day notice to PLF requirement.)

2. Determine and make absolutely clear who you are representing – who is your client and who is not. Closely-held companies with multiple shareholders/members can present scope of representation issues unless the representation is made clear from the outset. Document your representation in writing, both in an engagement letter and in correspondence where appropriate.

3. Beware of giving legal advice (or even detailed information that could be construed in the mind of the recipient as advice) to parties who are not your clients. Encourage people to get independent counsel, and, if there is potential confusion as to your role, make sure to clarify your role in writing so there is no confusion as to which party you represent.

4. Beware of the client who never seems to get all the information to you or fails to do the necessary footwork because they want to save money. Double-check and even threaten not to handle the matter unless you have all the information.

5. Be extremely careful about letting the client handle filings and recordings. Follow-up with a letter or an email to the client indicating that they have accepted the responsibility for this. The better practice is to not allow the client to do it. If a client insists on performing material aspects of the transaction, consider entering into a limited engagement. (See ORPC 1.2(b).)

6. If the client acts against the advice of the attorney, the attorney should follow up with a letter or an email indicating the actions are against the advice of counsel. Consider terminating the relationship.

7. Follow up phone calls and conferences when action is taken or discussed, or advice is given, with a letter or email confirming the discussion or a memo to the file. In situations where the issue is critical or legal advice is rejected, a memo to the file is a less ideal solution because it does not give notice of the importance of the subject matter or reinforce the points raised by the attorney.

8. When forwarding documents to any party that is not your client, send a letter or email, as applicable, indicating you are representing another party and the non-client should have the documents reviewed by their own attorney if they so wish. If a proposed contract is included in the transaction or is being tendered to escrow, there should be some writing with an acknowledgement provision for the other party that indicates you are representing your client and the other party can seek independent legal advice concerning the agreement.

9. When emailing counsel for other parties, do not copy or even blind copy your client. There is a risk that your client might “reply all,” disclose information your client intended only for you, and potentially waive attorney-client privilege as to the communication and subject matter. The better practice is to send an email to the other party’s attorney and then send a separate copy to your client.

10. Keep some kind of file, even a miscellaneous one, when only asked to review documents. Document in writing the limited scope of your engagement. A good practice is to recite the documents considered in providing the legal advice based on the review.

11. In deciding whether the buyer should purchase equity or assets, key points to consider are what liability will be assumed by the buyer (i.e., the potential for contingent or undisclosed liabilities) and how much of the value of the business lies in nonassignable contracts, licenses, or leases. The possibility of undisclosed or contingent liabilities might suggest
purchasing assets while the existence of valuable nonassignable contracts, licenses, or leases could lead a buyer to purchase equity (make sure nonassignable contracts are not breached on a change of control).

12. Look at all tax aspects when making the decision as to whether to sell or purchase the stock or the assets of the company. The choice of a stock sale versus an asset sale often significantly changes the tax consequences to buyer and seller; the same price for either deal should be assumed. Check the applicability of ORS 305.330, potential liability of purchaser of assets for seller’s tax liabilities. Document in writing who is undertaking the tax analysis to advise your client about the income tax aspects of the transaction, whether it is you, a tax accountant, or another tax expert. Be aware of personal property taxes and real property taxes that may have accrued but not become due as to the target company’s assets.

13. When an accountant is involved, make sure that the client understands what functions you are performing and not performing. Clarify your scope of work in writing to the client and, possibly, to the accountant, and if the accountant has not clarified their scope of work, find a way to do so for the protection of your client and yourself. Particularly, watch out for sub-chapter S elections. When you are forming a corporation, send a confirming letter or email to the accountant indicating who (you or the accountant) is responsible for filing the election, and copy the client.

14. In any business sale, verify the status of the buying and selling entities through the appropriate division of the Secretary of State of each company’s incorporation/organization state and any state in which the company is registered to conduct business.

15. Document your due diligence if stock is being purchased or notes are being issued by your client. See, Considerations in the Sale or Acquisition of a Small Business, infra. In all other cases, confirm responsibility for due diligence review. Do not undertake blanket due diligence on behalf of your client. Instead, determine what the client, their accountant, any other professional advisors, and you will do and document your scope of work (and exclusions) clearly.

16. If real estate is part of the transaction, investigate the environmental status of the real estate and whether the real estate can be used for its intended purpose (be extremely cautious, however, about providing an opinion on permissible land uses unless this is your area of expertise). Be sure you obtain and review all encumbrances and any other exceptions on a Preliminary Title Report.

17. Check for interests of other parties or liens, whether real or personal property. Conduct relevant state UCC searches on the target company whether you represent the seller or the buyer.

18. Check for balloon payment and amortization schedules on senior contracts and notes when handling the resale of a business. If the seller is paying senior installment encumbrances and buyer is paying seller in installments, be sure the senior encumbrances will never exceed the unpaid balance of the purchase price. Check all underlying instruments in a transaction to make sure the sale in which you are involved does not trigger a due-on-sale clause, an interest rate adjustment, or run contrary to a non-assignability provision.

19. Determine what third-party consents (including from lenders, landlords, and key suppliers/vendors/contractors or customers) are necessary to complete the transaction, and make closing the transaction contingent on obtaining all of the necessary consents.

20. Be sure amendment or revision of documents does not destroy prior security interests or prior assignments unless intended.
21. If any of the seller’s employees will become employees of the buyer, determine what, if any, of seller’s obligations to these employees (including contractual compensation, paid time off (“PTO”) or other leave, or other obligations) will be the responsibility of the buyer and make sure the documentation reflects this responsibility. Often, as a practical matter, even if the seller retains liability for prior employee benefits, the buyer/new employer might credit certain benefits (often PTO balances and accrual rates) to preserve employee loyalty. The cost of crediting new obligations should be considered in the purchase price. Review applicable employment law. If the sale includes a mass layoff or plant closing, as defined in the WARN Act, comply with its requirements.

22. If assets are being purchased, the contract of sale should contain a provision allocating the purchase price among the assets, which should be prepared or approved by the client’s accountant.

23. If the business being purchased could be adversely affected if the seller or any principals of the seller compete with the buyer, the transaction should include a covenant not to compete, which prohibits those individuals from competing with the buyer. ORS 653.295, which governs noncompetition agreements in the employer-employee context, does not apply to noncompetition covenants given solely in relation to sale of a business.

24. For security of a purchase price paid over time, make sure to evaluate the credit-worthiness of any guarantors or the soundness of pledged security. For a stock pledge to be perfected, you must have possession of the stock, or the stock must be pledged and held in a third-party escrow (please note that the rules for perfecting a pledge of LLC membership interests are different and vary based on whether the membership interest is certificated).

25. Be sure you have a security agreement if there is a sale of assets involving seller financing, and then be sure to file a UCC-1 Financing Statement to perfect it. With regard to fixtures, for perfection, the filing must be in the deed records of the county where the property is located. ORS 72A.3095.

26. As seller’s attorney, recommend the seller take a security interest in the seller’s interest in any leased property that is being assigned to the buyer (and extensions of the lease). A default in either the lease agreement or the purchase agreement should also constitute a default in the other agreement. Moreover, any default on an underlying mortgage or encumbrance should also constitute a default under the lease and purchase agreement.

27. Make sure the escrow is properly set up if the matter is to be closed in escrow and use a disinterested third party. BEWARE OF ACTING AS ESCROW AGENT.

28. Docket UCC filing deadlines. Be sure to advise the client in writing when a UCC filing will expire and the importance of renewal.

29. Beware of preparing documents in strict accordance with earnest money receipts without checking the reasons and explaining the consequences. Follow up with a letter or email setting out the final agreements and why.

30. Check current rules, regulations, and procedures on transfer of licenses and permits. Do not rely on it being the same as the last time you did it. Determine what licenses and permits are required for the business.

31. Obtain verification of items on financial statements or ensure that the client is obtaining such verification from an accountant or other source. The responsibility for such verification should be clarified in writing and is best delegated to the client’s accountant. Help a buyer client consider what financial statement information is most critical for the buyer’s success (e.g., gross sales, net income, or sales from a particular division) and tailor the seller’s representations in the purchase agreement to protect the buyer’s interest in the accuracy of such information.
32. Determine if any party is required to comply with any federal or state securities laws for an equity sale or payment of the purchase price over time.

33. Ensure each company obtains proper authorization to enter into and consummate the sale transactions—e.g., board, shareholder, manager, or member consents.

34. Verify that all intellectual property assets, including trademarks, service marks, copyrights, works of authorship, trade secrets, patents, and “know how” are included in the sale of the business. Request from seller representations that such intellectual property assets do not infringe the rights of others. The seller will often want such representations limited to only knowledge or notice of infringement.

35. DOCUMENT YOUR DUE DILIGENCE. If stock is being purchased or notes are being issued, be mindful that ORS 59.115 imposes liability on persons who sell or solicit the sale of securities in violation of ORS 59.135(1) or (3) (re: fraud and deceit with respect to securities or securities business) or “by means of an untrue statement of material fact or an omission to state a material fact.” The liability may also attach to nonsellers that control the seller, occupy a certain status in relation to the seller or perform certain functions for the seller or who “participated or materially aided in the sale of the security” unless the nonseller can prove “the nonseller did not know and, in the exercise of reasonable care, could not have known, of the existence of facts on which the liability is based.” This is a substantial burden and providing legal advice to the seller during an offering has been held to constitute providing material aid in the sale of a security. Document your due diligence to show that you did not know and could not have known such facts.

36. The contract of sale should specify what obligations of the seller are being assumed by the buyer and what obligations of the seller are not being assumed by the buyer. The contract should also contain an indemnification provision protecting the buyer from obligations of the seller not being assumed. Indemnification provisions are often highly negotiated and include different caps (maximum dollar limits), baskets (deductibles to be reached before indemnification liability commences), and survival period.

37. In seller-financed transactions, if you represent the seller, be sure the buyer’s ongoing covenants which protect the value of the security (such as limitations on borrowing or minimum debt/equity ratios) have built-in monitoring/enforcement mechanisms, such as requiring the buyer to provide the seller with quarterly financials and allowing seller access to buyer’s books.

38. Check, and double check, all documents for consistency, signatures, and dates.

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