

Three Things to Prepare for When Selling Your Company

By Russell Stein on September 16, 2024



The M&A market has had a very nice run over the past several years, and more transaction activity will certainly continue as interest rates come down. As an attorney who has represented many sellers over the past 30 years, I thought it might be helpful to cover three things business owners contemplating a transaction should consider.

1.) Understand the tax cost of the sale. Typically, the sale of a business will take one of two forms:

- A sale of assets; which will most likely have both ordinary income and capital gain implications, or
- A sale of the equity of the business (stock or membership interests), which most likely will yield capital gain treatment, but may be treated as an asset sale for tax purposes if the buyer wants to depreciate the purchase price.

A seller should understand these implications as part of the pre-sale planning process. Discussing these tax implications with your CPA and attorney could result in pre-sale planning that could be advantageous for the seller and still meet the buyer's needs.

2.) Understand what third parties may need to consent to the transaction. Understanding this sooner rather than later in the process can eliminate or substantially reduce potential closing delays.

- Do you have any governmental licenses or permits that need to be assigned to the buyer or that the buyer must obtain to close?
- Do you have material contracts requiring consent to assign (in an asset sale) or a change of control provision that gets triggered (in an equity interest sale)?

A seller should start to review these provisions of their licenses, permits, and contracts as part of the pre-sale process. To the extent that you are negotiating new contracts, try to insert a provision not requiring consent in connection with a sale or change of control.

3.) Understand that your employees are critical assets of the company.

- Do you have agreements with your employees covering non-disclosure, assignment of inventions, and non-solicitation of customers and employees?
- If you have non-compete agreements with your employees, do they comply with Massachusetts law if they are based in Massachusetts (or the state where such employees work)?

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These will be critical to have in place before entering a sale process, or a condition of closing by the buyer could be that these agreements be entered into with your employees prior to the closing. For key employees, consider using transaction bonus agreements. These can be structured to give the employee a portion of the bonus at closing and a portion if the employee stays with the buyer for a certain period of time after the closing. These agreements can also serve as consideration for post-closing restrictive covenants with the buyer, which will also add value to your company.

Getting in front of these considerations early on can help a seller be as prepared as possible to sell his or her business when the time comes.

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