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# “Changing Ownership”

Presented by GKH Corporate Practice Group  
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# Introduction

Knowing when to involve your attorney

- a.k.a., worthwhile “ounces of prevention”
- how to achieve cost savings in concluding a deal

# Before The Handshake

- A. Non-Disclosure Agreements
- B. Letters of Intent, Term Sheets --  
and unintended consequences
- C. Haggling over price and apportionments



# Before The Handshake

NDA's - Keeping confidential your confidential info

- Defining “confidential”
- Defining penalties for breach
- Stating mechanism for dispute resolution

# Before The Handshake

Letters of Intent, Term Sheets --  
and unintended consequences

- Essential deal terms
- Binding or nonbinding
- Brevity versus completeness

# Before The Handshake

Haggling over price and apportionments

- Price term in order to “complete” an agreement
- Real estate assets as special circumstances
- Tax consequences of price allocation IRS 8594
- Asset versus entity sale

# Preclosing

## Sizing up the Buyer

- Confirm that the third party is genuinely interested in buying
- Might be just industrial spying
- Broker's role
- Consider requiring nonrefundable earnest money to cover seller's time and expense of responding to an expression of interest
- How much lead time (Phase I and appraisal)

# Preclosing

## Asset v. Interest Sale

### Asset Sale

- Better liability protection
- Allocate purchase price
- Bulk sale issues



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# Preclosing

## Interest Sale

- To co-owners
  - If you don't own 100% of the business, then, obviously, you can only sell your interest, unless all the owners are selling
  - Controlled by shareholder, operating or partnership agreement
  - Redemption or cross-sale
- To outside party
  - NOL's and other tax issues may add value
  - Insurance history (workers' comp and unemployment comp) may be available as extra value
  - Buyer inherits liabilities

# Preclosing

- Securities Law Analysis - Asset Sale v. Interest Sale
  - Does the sale involve a “SECURITY”?
  - Determination of applicable Securities laws?
  - Available EXEMPTION(S)?



# Preclosing

## COMMON TYPES OF SECURITIES

- Stock
- Certain Promissory Notes
- Certain LLC interests
- Certain limited partnership interests
- Bonds
- Evidences of indebtedness
- Certificates of interest or participation in any profit-sharing agreement
- Warrant or right to subscribe to the above

**CAUTION:** This is a non-exhaustive list. The definition includes “in general, any interest or instrument commonly known as or having the incidents of a security.”



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# Preclosing

## SECURITIES LAWS- WHICH APPLICABLE?

- Federal Laws
  - Securities and Exchange Commission (“SEC”)
- Pennsylvania Securities Laws
  - Department of Banking and Securities
- Laws of various other States
  - Each State has its own regulatory body

# Preclosing

## EXEMPTIONS FROM REGISTRATION

- Sales to Principals (Regulation 203.184)
  - Sales to Principals- “Principals” Defined
  - No \$ limit
  - No PA issuer requirement
- Small Issuer Exemption (Regulation 203.187)
  - Sales to no more than 10 persons inside or outside PA
  - No \$ limit
  - PA issuer requirement
- Isolated Transaction Exemption (Regulation 203.189)
  - 2 PA residents every 12 months
  - No \$ limit
  - Generally, a PA issuer requirement



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# Preclosing

## EXEMPTIONS FROM REGISTRATION CONT.

- Section 203(a)- Any non-issuer transaction except where directly or indirectly for the benefit of an affiliate of the issuer.
  - “Non-issuer Transaction” Defined
  - “Affiliate” Defined
- Section 203(b)- Any non-issuer transaction that would directly or indirectly benefit an affiliate, which is exempt pursuant to certain federal exemptions.

# Employment Considerations

- Notifying your current employees
  - Ensure that your communication with current employees or the general public abides by any agreements with the purchaser
  - Potential issues: Key employees may leave prior to sale; morale issues/production issues
  - Limited requirement to notify employees due to plant closing or mass layoffs



# Employment Considerations

- Stock sale: Buyer generally assumes all liabilities of the Company
  - This includes liabilities arising under employment agreements, pension plans, health benefit plans, deferred compensation plans, matters related to employment litigation (including ongoing matters) and court orders
- Asset Sale: Buyer has more flexibility to choose which assets it will assume

# Employment Considerations

- Determine who has responsibility for the following:
  - Continuation of any applicable professional liability insurance for the seller, e.g. tail policy;
  - Employee litigation for events occurring before sale; and
  - Notices to applicable agencies and transfers of licenses

# Employment Considerations

- Ensure compliance with federal and state regulations prior to sale and document compliance, *e.g.*:
  - I-9 immigration law
  - OSHA
  - Independent contractor agreements
  - Pension and benefits -ERISA

# Restrictive Covenants

Restrictive covenants may contain prohibitions against the seller from:

- Competing with purchaser, doing business in the marketplace;
- Disclosing confidential information and trade secrets;
- Soliciting current or former customers and vendors; and
- Soliciting current employees
- Non-disparagement



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# Closing

Simple cross-purchase or redemption

- No bank involvement
- No real estate conveyance

Documentation

- simple agreement
- resolutions of company authorizing the transfer
- joinder of company agreement if buyer is new owner
- may still require bank consent or refinance

# Closing

## Full-throated

- 3<sup>rd</sup> party buyer
- new financing
- real estate involved

## Logistics

- challenge to coordinate all the parties and all the transactions

## Documentation

- *Next page example of document checklist*

# Closing Sample of Closing Document Checklist

REAL ESTATE  
AND  
LOAN CLOSING AGENDA  
ZZ  
TO  
ZZ

LENDER ("L")	
LENDER'S COUNSEL ("LL")	
BORROWER ("B")	
GUARANTOR ("G")	
BORROWER'S AND GUARANTOR'S COUNSEL ("BL")	
SELLER ("S")	
SELLER'S COUNSEL ("SL")	
TITLE COMPANY ("TC")	
FINANCING	(a) YLL Commercial Mortgage Loan (b) ZZZ Line of Credit
PROJECT/PREMISES	
ESTIMATED CLOSING DATE (* -document to be recorded)	

NOTICE: Unless indicated as "received and approved" in the "Status" column, all submissions and documents are subject to review and approval of Lender and Lender's Counsel.

**I. REAL ESTATE DOCUMENTS**

#	DOCUMENT/TASK	PARTY TO PREPARE OR SUBMIT	STATUS/COMMENTS AS OF ZZ
1.	Agreement of Sale ("AUS")		

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2.	Amendment Addendum to AOS		
3.	Notation		
4.	Clear and Open documents		
5.	Deed		
6.	WCDM		
7.	TRC Binder		
8.	Affidavit for title insurance		
9.	Assignment of Lease		
10.	UCC's		
11.	Payment		
12.			
13.			

**II. LOAN DOCUMENTS**

#	DOCUMENT/TASK	PARTY TO PREPARE OR SUBMIT	STATUS/COMMENTS AS OF ZZ
1.	Commitment Letter	L	Issued by L and accepted by B
2.	Loan and Security Agreement by and between L, B and G	LL	
3.	YLL Mortgage Loan Note issued by B	LL	
4.	YLL Line of Credit Note issued by B	LL	
5.	Disclosure for Commission/Judgment for Notes from B	LL	
6.	First Lien Open-end Mortgage in the principal amount of YLL secured by the Project Premises from B*	LL	
7.	Second Lien Open-end Mortgage in the principal amount of YLL secured by the Project Premises from B*	LL	
8.	Assignment of Lease and Accts from B*	LL	

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9.	Environmental Indemnity Agreement from B and G	LL	
10.	UCC's Security Agreement between L and B	LL	
11.	UCC Financing Statements from B*	LL	
12.	Guaranty and Surety Agreements from G	LL	
13.	Disclosure for Commission/Judgment for Guaranty and Surety Agreements from G*	LL	
14.	Affidavit of Disposition Purpose from LL	LL	
15.	UCC's Security Agreement from LL	LL	
16.	UCC's Security Agreement for Liqueur License from LL	LL	
17.	UCC Financing Statements from LL*	LL	
18.	Assignment of LAR Insurance	B	
19.	Landlord's Waiver from B	LL	
20.	Subordination Agreement by Shareholders of B subordinating loans to Financing	B	
21.	Certified copies of Authorizing resolutions, Organizational Documents and amendments for B and ZZ	BL	
22.	UCC Pledging Certificates for B and LL	BL	
23.	Title Insurance Commitment with copies of all exceptions and an Insured Closing Protection Letter	TL	
24.	Phase 1 Environmental Site Assessment of Project Premises	B	
25.	Approval of Project Premises	L	
26.	Copy of Liqueur License	B	
27.	Financial Statements and Tax Returns of B/G	B/G	
28.	Written detailed course of action regarding funding of ESOP Obligations	B	
29.	Legal Opinion of Counsel to B and G	BL	

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30.	Copy of signed Lease Agreement between B and LL	B	
31.	Insurance: (i) public liability insurance, naming Bank as additional insured (Accord 23 certified); (ii) builder's all risk insurance or fire and theft insurance naming Bank as additional insured (Accord 23 certified); (iii) worker's comp (full statutory employer or liability); (iv) business interruption and rental loss insurance; all to include thirty (30) day notice to Bank of non-renewal or non-renewal	B	
32.	Establishment of Escrow Account	LB	
33.	Filed Assent Certification for Project Premises	L	
34.	Settlement Sheet	TL	At Settlement
35.	Payment of Bank's Commitment Fee	B	At Settlement
36.	Payment of Bank's Counsel Fee	B	At Settlement
37.	Mailed-off Title Insurance Commitment with documents required by Lender	TL	At Settlement
38.	Title Policy within thirty (30) days of closing	TL	Post Closing

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# Closing

## Financing

- Lender approval if sale to co-owners
- Subordination to commercial lender if seller financing

## Protecting Seller Financing

- Collateral on assets
  - not sufficient – you sold the business, you don't want it back
  - Will have to subordinate to commercial lender
  - May be crammed down in bankruptcy



# Closing

## Financing

### Protecting Seller Financing (Con't)

- Collateral on unrelated assets
  - Make sure there's equity in any collateral
- Guaranties
  - Personal
  - Will have to subordinate to commercial lender

### Documentation

- Confessed judgment note
- Mortgage
- Financing statement (UCC-1's)
- Guaranties
- Bank subordination agreement

# Transferring The Brand

- A. Your name, brand, trademark, identity
- B. Transferring it to a buyer with low risk
- C. PA DOS vs USPTO

# Transferring The Brand

Your name, brand, trademark, identity

- Intellectual property
- How memorialized, recorded, and defended/defensible
- Valued as “goodwill” for financial reporting
- Registered trademarks
- Company names and D/B/A's



# Transferring The Brand

Transferring it to a buyer with low risk

- Reversion of rights
- Recordation of assignment of trademark
- Payment for transfer completed
- Security collateral in the TM rights going forward

# Transferring The Brand

## PA DOS vs USPTO

- Parallel registration mechanisms
- PA DoS is NOT USPTO
- USPTO is federal
- Trademark office practice

# Post Closing Seller As Consultant

- Seller possesses valuable knowledge and intangible skills which purchaser may want to utilize post sale
  - Determine:
    - Length of time
    - Amount of compensation
    - Scope of duties
    - Whether seller will be considered an employee or independent contractor

# Post Closing

WHAT HAPPENS WHEN REPRESENTATIONS & WARRANTIES FAIL?

- Included Reps. and Warranties in Purchase Agreement
- These Reps. and Warranties fail
- Now what? Remedies for Breach involving securities laws

# Post Closing

## ANTIFRAUD PROVISIONS UNDER THE ACT

It is unlawful for any person, in connection with the offer, sale or purchase of any security in this State, directly or indirectly:

- (a) To employ any device, scheme or artifice to defraud;
- (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading; OR
- (c) To engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person.

# Post Closing

## ANTIFRAUD PROVISIONS UNDER THE ACT CONT.

Does the Seller have a duty to disclose? One Party has it and the other Party is entitled to it.

Does the Purchaser have the information? Perhaps the Party entitled to the information has it.

Is the fact “Material”? Material if there is “**a substantial likelihood** that the disclosure of the omitted fact would have been viewed by **the reasonable investor** as having significantly altered the total mix of information made available.”

# Post Closing

## Default on Seller Financing

- You don't want the business back
- Bankruptcy
- Collateral
- Guaranties

## Enforcement Venues

- Common Pleas
- Bankruptcy
- Self Help



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# Post Closing

## Court of Common Pleas

- Action on the Note
- Foreclosure on Mortgage
- Action on collateral - Replevin
- Action on guaranties

# Post Closing

## Bankruptcy

- Chapter 7 or 11
- Cram down
- Preference claims

# Post Closing

## Self Help

- Art. 9 of UCC
- Ejectment
- Replevin

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QUESTIONS & ANSWERS

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