Ask a VR Intermediary?

What is the Difference Between Stock vs. Asset Purchases?

Lee Osterland
Provo, UT

Perhaps the most fundamental issue in structuring the acquisition of a target business is whether the transaction will be an asset or stock purchase. Each form has its respective advantages and disadvantages, depending on the facts and circumstances surrounding each transaction. The buyer and seller should consider the following factors before determining the kind:

STOCK PURCHASES

The Buyer's Perspective – Advantages

- Tax attributes carryover to buyer – ie., net operating loss and credit carry forwards.
- Avoids many of the restrictions imposed on sales of assets in loan agreements and potential sales tax.
- Preserves the right of the buyer to use seller's name, licenses and permits.
- No changes in corporation's liability, unemployment or worker's compensation insurance ratings.
- Nontransferable rights or assets can usually retained by the buyer – ie. license, franchise, patient, etc.

The Seller's Perspective – Advantages

- Taxed only on the sale of stock.
- All obligations (disclosed, unknown and contingent) and nontransferable rights can be transferred to the buyer.
- Gain/loss is usually capital in nature.
- If stock held by individuals is IRC Section 1244 stock and is sold at a loss, the loss is generally treated as ordinary.
- May permit sellers to report gains from sale of stock on an installment basis.
- Does not leave the seller with the problem of disposing assets, which are not bought by the purchaser.

The Buyer's Perspective – Disadvantages

- Less flexibility to cherry pick key assets of seller.
- The buyer may be liable for unknown, undisclosed or contingent liabilities (unless adequately protected in the purchase agreement).
- No step up in basis (ie., seller's basis is carried over to the buyer at historical tax basis).
- Normally does not terminate existing labor union collective bargaining agreement(s), and generally results in the continuation of employee benefit plans.
- Dissenting shareholders have a right of appraisal for the value of their shares with the right to be paid appraised value or remain a minority shareholder.

The Seller's Perspective - Disadvantages

- Offer and sale of the company's securities may need to be registered.
- Seller cannot pick and choose assets to be retained.
- May not use the corporation's net operating loss and credit carry forwards to offset gain on sale.

- Loss on sale of stock may not be recognized by corporate shareholder who included the company in its consolidated income tax return.

ASSET PURCHASES

The Buyer's Perspective – Advantages

- The buyer can be selective as to which assets of target will be purchased.
- The buyer is not liable for seller's liabilities unless specifically assumed under contract.
- Step-up in basis of assets acquired equal to purchase price allowing higher depreciation/amortization deductions.
- Buyers are generally free of any undisclosed or contingent liabilities.
- Normally, results in termination of labor union collective bargaining agreement (s) and employee benefit plans may be maintained or terminated.
- Buyers may elect new accounting.

The Seller's Perspective – Advantages

- Seller maintains corporate existence.
- Ownership of nontransferable assets or rights is retained – licenses, franchise, patents.
- Corporate name and goodwill can generally be maintained.
- Corporation's tax attributes are retained – net operating loss and credit carry forwards.

The Buyer's Perspective – Disadvantages

- No carryover of seller corporation's tax attributes – net operating loss and credit carry forwards, etc.
- If a bargain purchase, step-down in basis of assets.
- Non-transferable rights or assets cannot be transferred to buyers – license, franchise, patent, etc.
- Transaction more complex and costly in terms of transferring specific assets/liabilities – title to each asset transferred and new title recorded; state sales tax may apply.
- Lender's consent may be required to assume liabilities.
- Loss of corporation's liability, unemployment or workers' compensation insurance ratings.

The Seller's Perspective - Disadvantages

- Double taxation if the corporation also liquidates.
- Generates various kinds of gain or loss to sellers based on the classification of each asset as capital or ordinary.
- Transaction more complex and costly in terms of transferring specific assets/liabilities – title to each asset transferred and new title recorded; state sales tax may apply.
- Bill of Sale must be comprehensive with exhibits attached in order to ensure that no key assets are overlooked; and as a result, not transferred to the buyer.
- A variety of third party consents will typically be required to transfer key tangible and intangible assets to the buyer.
- Seller will be responsible for liquidation of the remaining corporate "shell" and distributing the proceeds of the asset sale to its shareholders, which may result in a double taxation, unless a Section 338 election is made.
- Asset acquisition requires compliance with applicable state bulk sales statues as well as state and local sales and transfer taxes.