Corporate

Burges Salmon

Burges Salmon Guide to acquiring a UK company or business

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Introduction

This Guide provides an overview of what the overseas investor can expect of the legal process when acquiring a UK private company or business. In this Guide, UK refers to England and Wales, but we have lawyers who are qualified to work in all three legal jurisdictions in the UK – England and Wales, Scotland and Northern Ireland.

Common law system

In the UK (England and Wales), we have a common law system where the judiciary are at the heart of interpreting and creating the law. Common law is based on case law – decisions of the court made relying on established precedent (previous decisions) laid down by higher courts. Key features of UK law are the principles of freedom of contract and "caveat emptor" (meaning, "let the buyer beware").

Although there are some established principles which restrict what the buyer and seller can include in the contractual arrangements, essentially the parties can agree their own terms and price. This freedom has benefits in terms of flexibility but makes it essential for a buyer to carry out appropriate due diligence and have adequate contractual arrangements in place to protect its position.

Structuring the sale and purchase

The choice of structure will be driven by various factors, including what the buyer wants or does not want to acquire, the practicalities involved in the transfer of control and the tax implications for both the buyer and seller.

On a **share purchase** the buyer acquires the target company with all its assets, employees and the benefit of contracts, but also the historic liabilities and obligations of that company. From the outside, very little will appear to have changed and customers and suppliers may well be happy to continue dealing with the company as before. Third party consent to a change of control may however be required in relation to certain contracts (for example, financing contracts and other long term agreements).

On an **asset purchase** only the assets and liabilities which the buyer specifically agrees to take are acquired and generally everything else stays with the selling company. The exception to this general rule is the employees – under UK law, employees will often automatically transfer to the buyer on their current terms of employment and there may be obligations to inform and consult with them in relation to the acquisition plans. Contracts, real estate and certain intellectual property rights will all need to be formally transferred and the consent of significant customers and suppliers, landlords, licensors and others is likely to be required. There may be more disruption to the business than on a share purchase and the buyer may need to build confidence with the customers and suppliers of the business to maintain existing trading relationships.

Due diligence

Due to the fundamental principle of "buyer beware", a buyer will want to gather as much information as possible through the due diligence process to understand what it is taking on.

The information obtained will help the buyer decide whether to go ahead with the acquisition, evaluate the strengths and weaknesses of the business, establish the right price, identify liabilities or risk areas which may impact on deal-structuring or contractual protection and identify any third party consents or approvals which may be required.

Legal due diligence. Typically the buyer's lawyers prepare a detailed information request covering all aspects of the target including its constitution, employees, contracts, licences, real estate, intellectual property rights and IT systems. The degree of focus on any particular area will depend on the nature of the target business or company, perceived high risk areas and assets of particular significance. The use of electronic data rooms as a means of storing and accessing the information collated is increasingly prevalent, particularly in international transactions. The buyer's lawyers will typically evaluate the information provided and produce a report, highlighting issues of concern and suggesting protective measures where appropriate.

Financial due diligence. Financial due diligence will be carried out by the buyer's accountants and will focus on assessing the historic trading performance of the company or business to check that the assumptions the buyer is making about its future are supported.

Other specialist reports may also be required as part of the wider due diligence process, for example, commercial/market due diligence, real estate surveys, environmental audits, IP/IT reviews, insurance analysis, health and safety investigations or pension actuarial valuations.

Warranties, indemnities and disclosure

Warranties are contractual assurances in the sale and purchase agreement about the target company or business designed to protect the buyer against liabilities which may exist. If any of these assurances are untrue the seller may be liable to pay damages to the buyer under a breach of warranty claim. Warranties are usually one of the most negotiated aspects of the sale and purchase agreement – the buyer will be keen to

ensure that the warranties are as wide as possible whilst the seller will try to limit their scope. Warranties also perform the dual function of encouraging the seller to provide further information about the company or business through the disclosure process.

The seller will prepare a **disclosure letter** qualifying the warranties with factual information setting out the true state of affairs. To the extent that the seller properly qualifies a warranty by a disclosure it cannot be sued for a breach of that warranty. If a significant issue is identified through the disclosure process, assuming it does not stop the transaction completely, it will generally be dealt with through a price adjustment or an indemnity in the sale and purchase agreement.

It is also common for the seller to be required to give certain **indemnities** (promises to reimburse) to the buyer. These are more specific in nature than warranties and are generally used to protect the buyer against specific risks or identified liabilities. Typical examples include a series of tax indemnities on a share purchase (standard UK market practice) or indemnities to cover problematic issues identified during due diligence. The main distinction is the basis of any claim by the buyer for breach. Damages on a warranty claim are assessed by the courts and are based on the buyer's loss of bargain – is the company/business acquired worth less than the buyer paid for it because the warranty was untrue? Where an indemnity is breached the seller will be required to reimburse the buyer on a whole cost basis (regardless of whether it has affected the value of the company/business).

Other issues

Overseas buyers should be aware that certain issues may add to the complexity of the contractual arrangements and, as a consequence, prolong negotiations and increase the internal and external costs of the acquisition. Examples of such issues include:

- Regulatory or other third party consents or clearances, e.g. from the competition, tax, industry or pension authorities or regulators.
- Complex specialist matters, e.g. significant tax structuring, historic environmental contamination (regardless of whether the target company caused the damage) or problematic pension issues (usually arising from deficits under defined benefit pension schemes).
- Deferred consideration or external financing arrangements.

How we work with you

Burges Salmon is the independent UK law firm whose unique model and collaborative culture delivers the best mix of advice, service and value.

We have built a progressive service culture based on collaboration and teamwork that is shaped around the needs of our clients to deliver a fantastic service and experience.

We work in selected markets where our knowledge, experience and skills deliver highly effective solutions to our clients' complex needs.

Key contact

If you would like further information please speak to your usual contact at Burges Salmon or:

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