

# Selling your business

## How to maximise your profits

By Alan Zeffertt

**This fact sheet will assist owners of small to medium sized business in preparing for a sale. It applies to most types of businesses including shops, restaurants, service industries, pubs, newsagents, bars and nightclubs.**

### Getting started

If your business is run through a limited company, your first decision is whether to have a share sale or an asset sale.

With a share sale, you are selling not only assets, but also any liabilities of the company. This means that any buyer will usually ask you for warranties and indemnities. Transferring assets is a simpler matter.

Either way, the type of sale is usually determined by tax considerations. The big question is how to avoid the tax 'double whammy' for individual shareholders - corporation tax on the chargeable gain on the sale of the business, on top of income tax on the distribution of the net proceeds as dividends

There is a way round this. Business asset taper relief is available for most disposals of shares in owner-managed businesses. This is very attractive for individual shareholders selling shares in a private trading company.

Talk to your tax adviser before you even market the business for sale, so that you don't end up paying more tax than you need to.

### Capital v Income

You should consider whether to sacrifice income now for a potentially larger capital sum later. A Seller's willingness to continue in a consultancy or employment role after sale may assist in maximising the price which a purchaser is willing to pay.

Although to many people 'cash is king', you may be able to achieve a greater sum overall if you are prepared to consider deferred payment of the consideration over a period of time.

Consider also taking non cash consideration, usually in the form of shares in the purchasing company.

### Which assets are you selling?

You will first need to identify the assets used in the business. These will usually include any lease of the property occupied, goodwill, intellectual property rights, equipment and stock. The next step is to clarify which of those assets you are selling and which ones won't be included in the sale. This is particularly important where a division of a larger business is being sold. Consider re-structuring so as to separate two distinct businesses.

Only those assets which are necessary for the smooth running of the business need be included as part of the sale. For example, consider excluding a freehold property the full value of which may not be reflected in the price for the business which may be based on a multiple of profits. A seller might also exclude any intellectual property rights and licence their use to a purchaser thereby maximising the return on such rights.

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### Which legal documents will your solicitor need?

Once you have decided to sell part or all of your business, it will save time, and money, if you provide to your solicitors those contracts and other documents which they will need to see, including:

- All HP or leasing agreements
- Contracts with customers
- Contracts with suppliers
- Employment contracts
- Property title deeds and leases
- Software licensing agreements

### Apportioning the sale price—save tax by getting it right

Your tax adviser can guide you as to the best apportionment or split of the sale price between the various assets being sold. The way the price is apportioned could have significant tax consequences, so it needs to be decided on as early as possible.

For example, if capital allowances have been claimed, there will be a balancing allowance in the year of disposal, to reflect depreciation not accounted for. If the price apportioned to fixed assets exceeds their written-down value in the books of the business, there may be a balancing charge on the difference, which could increase your tax bill.

The disposal of assets, other than trading stock, is liable to capital gains tax. You will therefore need to consider available reliefs such as rollover relief on re-investment in permitted qualifying assets, business assets taper relief for disposals after 5th April 1998 and indexation allowance for disposals after 5th April 1998.

### Valuation of stocks

Another factor to take into account is the value of stock. It is in your interest to keep stock values low, since you will be taxed on the sale price of the stocks. Your buyer, on the other hand, will usually want a higher acquisition cost for stock, in order to claim stock relief.

You may be able to agree the stock price in advance of completion. If this is not possible, a valuation may be necessary. This may simply involve a joint stock-take on the day of completion. The total stock price would then be determined by reference either to acquisition cost (which can be verified from invoices), or to the basis used for valuing stocks in the accounts. Few allowances are generally made for old or slow-moving stocks, which may then be worth less than their acquisition cost.

There is another alternative, but it is a more expensive one. You and your buyer can nominate a third-party valuer to carry out the valuation on completion.

You could consider providing for a pre-estimate of the stock value to be handed over at completion, with the balance to follow when the valuation has been agreed.

### Is VAT on the sale avoidable?

If the sale of the business is treated as the Transfer of a Going Concern, or TOGC, it will be outside the scope of VAT. While you do not pay VAT on the sale, you are not prevented from deducting input taxes on related expenses as a general business overhead.

TOGC applies where a business is transferred either whole or in part as a going concern, and the assets are to be used by the buyer in continuing the same type of business as the seller.

However, your buyer needs to be registered for VAT at completion of the sale, or must be liable to be registered, if the turnover exceeds the existing registration limit immediately before the transfer. There must be no significant break in the normal trading pattern before or immediately after the transfer.

What if one of the assets transferred is property? If you have elected to waive exemption but your buyer has not, you must charge VAT on that part of the property which falls outside the TOGC.

For the property to be included in the TOGC, your buyer must notify Customs and Excise of his or her election to waive exemption. This needs to be done before the 'time of supply', which is either on exchange of contracts (if there is a gap between exchange and completion and a deposit is paid to the Seller's solicitors as agents) or if vacant possession is given before completion.

### Employees' rights and unfair dismissal

The rights of employees are protected under the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), in the case of a 'relevant transfer'. A relevant transfer is the transfer of an economic entity which retains its identity. This includes the transfer of a business or part of a business.

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The rights of those employed immediately before the transfer will automatically be transferred to the buyer, thus preserving continuity of employment. Any action you as the seller may have taken towards your employee before the sale is now deemed to have been taken by the buyer. What this means in practice is that any claim an employee could have brought against you—race discrimination or harassment, for instance—may be brought against the buyer instead.

There are exceptions to these conditions. In cases where there is an 'economic, technical or intending change to the workforce' (ETO) before or after the relevant transfer, the employee will not be deemed to have been unfairly dismissed.

Yet it is important to note that the fact such a change has occurred, resulting in the loss of a job, is not enough on its own to avoid a claim for unfair dismissal. The reason for the ETO must also involve changes to the workforce i.e. the number of employees involved. Genuine redundancy would be a valid economic reason. A technical reason might be a lack of appropriate skills, while an organisational one would perhaps be the need for a reduced combined workforce.

And even if there is an ETO reason entailing changes in the workforce, an unfair dismissal claim might still arise if the employer does not act reasonably in dealing with the procedural aspects of the dismissal, such as failing to give employees the opportunity to apply for suitable alternative employment. Meanwhile, paring down the workforce to achieve a sale, for example at the buyer's request, or to obtain a better price, would not usually be considered an ETO reason and the employee would again have a valid claim against the buyer for unfair dismissal.

#### Restrictions on the seller

Your buyer will be concerned to protect the goodwill and name of the business against the risk of you setting up in competition or soliciting customers. No restrictive covenant is implied, so consider offering an express clause in the sale contract.

Restrictive covenants will be enforced, but only to the extent that they are not an unreasonable restriction to trade.

The reasonableness of a restriction will be tested against the geographical area to which it applies. This is based on the geographical distribution of the business's customers at the time of purchase, not what it is expected to be in the future. The period the restriction is to apply and the nature of the restricted activities are also taken into account when considering whether a restriction is reasonable or not.

#### For further information, please contact:-

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