

The Top 10 Mistakes We See In Sale & Purchase Contracts

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A sales and purchase agreement (SPA) is the most commonly used document in commercial transactions, from deals involving purchases of commodities, shares, businesses and real estate, these types of contracts are vital to business activity. To execute any deal successfully you need the protection of a well drafted SPA, but often buyers or sellers fail to take even the basic steps required to protect their own interests.

Below are the top 10 “red flag errors” we see when buyers or sellers consult us afterwards looking to salvage their money or assets, or otherwise engage in “damage control”.

1. Doing the Deal with the Wrong Person

The best drafted SPA in the world is no use to you, if you sign it with a fraudster or an incompetent.

2. Essential Parties Are Not Part of the SPA

Often buyers will sign an SPA with Company A, when in reality Company B (or a Shareholder in Company A), is the actual owner of all or part of the assets being purchased. On the sell side, sellers often engage in a contract under which Company C is buyer and makes significant final commitments to the seller, but seller does not realize until it is too late that Company C is merely a shell company with no assets to meet the commitments.

3. Failure to Identify and Address Essential Pre Conditions to the Deal

Conditions precedent are conditions and events which must be resolved before a transaction detailed in an SPA can be completed. Any buyer or seller has to identify all these preconditions and make sure they are all properly addressed in the SPA. Important conditions to include are clearance of the seller's debts, third party consents, transferring key employees, banking approvals, and clearances and approvals from the appropriate authorities

4. Failure to Specify a “Long Stop Date”

Commonly conditions have to be met before the deal can close. What if the time for satisfying conditions or obtaining approvals blows out from weeks to months? In this case buyers and sellers need to have a “Long Stop Date” in their SPA, so they can bail out of the SPA if the delay becomes untenable for them. If essential preconditions are not met by this long stop date, one or both parties can walk away from the deal.

5. Failure to Agree Necessary Financial Adjustments

In some deals, buyers seek to protect themselves by including a post acquisition price adjustment. Upon completion of the transaction, the buyer's accountants finalize the accounts and determine the net assets of the company to evaluate whether the price paid at completion was greater or lower than agreed for. If the price was greater than the value, the buyer will be granted a reconciliation payment. An alternative to the post completion price adjustment is the “locked-box” approach where the seller makes detailed and specific commitment as to the value of the business's net assets at closing. If the business suffers major losses or the sellers strip out dividends, any buyer without these safeguards will be financially exposed.

6. Failure to be Specific about Closing Requirements

An SPA should clearly identify all actions to be taken and all the documents to be provided at closing. Examples include discharge of banking facilities, handover of customer and financial records, change of bank and regulatory signatories, original documents, and obtaining regulatory approvals.

7. Failure to Protect Against Competition from the Seller

Any buyer should consider whether it is appropriate that the SPA contain contractual terms restricting the seller from competing with or soliciting customers, suppliers, and against poaching employees of

the business for a specified period of time after completion.

8. Failure to Change Signatories

Often buyers overlook the need to change the signatories to essential banking and business accounts. Third parties must be notified in a timely fashion of the new owners and accept the signatories.

9. No Simple and Effective Dispute Resolution

In the run up to closing, arguments over money and adjustment are common. The SPA can ease these problems by providing for independent experts to conduct valuations and provide their expert advice on (and if necessary determine) issues in dispute.

10. Skimping on Lawyers' Fees

Often parties download "ready made" contracts from the internet, adapt a form from the last deal or try to draft the contract themselves. Ensure you have a specialist lawyer review the SPA. Lawyers' fees for reviewing SPAs are often a tiny fraction of lawyers fees for litigation, or catastrophic financial losses from a deal gone bad or a deal which should never have been done.