

Acquiring or Selling the Privately Held Company

By Christopher A. Karachale • Wood & Porter • San Francisco

There are important and subtle differences between sales and acquisitions of publicly held companies and of their privately held (and usually but not always smaller) brethren. The former are usually complex, sometimes involving teams of lawyers assessing securities, regulatory and tax issues. Private company deals should be simpler and staffed more leanly. Increasingly, though, even the simplest deals involving the smallest private companies require practitioners to assess the same issues as their larger cousins.

Luckily, a recent Practicing Law Institute seminar provides a helpful and thorough review of issues practitioners face in acquiring or selling privately held companies. Held in various locations in May and June, and available through PLI's Web site as a DVD, this seminar provides

valuable information for practitioners dealing with private company sales and acquisitions.

One refreshing aspect of this seminar was its wide scope. Almost all the financial and business aspects of these transactions were covered, at least in part. The faculty addressed intellectual property and environmental concerns, the fiduciary duties of directors and majority shareholders, as well as important contract points, including letters of intent and indemnification provisions. Of particular interest to us here at the M&A TAX REPORT were the sessions on tax considerations, plus coverage of executive compensation, when acquiring or selling privately held companies.

At the San Francisco seminar, Julie Divola of Pillsbury Winthrop Shaw Pittman LLP, presented the tax session, reviewing how tax

concerns dictate structure. Ms. Divola contrasted seller and buyer tax objectives, which sometimes align and sometimes conflict. And the stakes are high, impacting such fundamental questions as whether the seller will receive capital gain or ordinary income from the transaction. Other issues: Can the seller ensure it will be subject to only one level of tax based the structure of the acquiring and target entities? Can the seller defer gain?

There are equally important tax considerations from the buyer's prospective. The buyer may wish to deduct, depreciate or amortize the purchase price, preserve tax attributes of the target, avoid certain tax liabilities of the target or integrate the target with the buyer's tax structure. The consideration provided by the acquirer, whether cash, equity or debt, will affect these tax implications as will the various entities' structures.

Executive compensation issues are of increasing importance. Sharon Hendricks of Gunderson Dettmer, LLP, updated seminar attendees on Code Sec. 409A and Code Sec. 280G matters. In particular, she addressed the treatment of target company equity awards and other compensation arrangements. For example, if amounts thought to be purchase price for the target stock are in fact

compensatory in nature, they will likely be taxed as compensation. This disguised compensation issue can arise in payments on target stock where there has been additional value allocated to the common stock.

Ms. Hendricks also reviewed the special golden parachute rules applicable to privately held companies. In particular, she flagged Code Sec. 280G(b)(5), which provides an exception to the general parachute payment rules for private companies. This exception requires approval of 75 percent of the disinterested shareholders, but approval of the transaction cannot be tied to a Code Sec. 280G vote. Furthermore, all material facts must be disclosed to all shareholders entitled to vote, and the vote must determine payee's right to receive or retain the payments.

PLI's *Acquiring or Selling the Privately Held Company 2010* reviews many issues arising in the acquisition or sale of privately held companies. As these rules—and plain old economics—become increasingly complex, short and efficiently packaged seminars such as these make sense, avoid potential problems, and serve as a good resource for practitioners. Details are available at: www.pli.edu/product/dvd_detail.asp?id=63462 or (800) 260-4PLI.

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