Buying a Business out of Receivership

Buying a business out of receivership involves vastly different features to customary business purchases. This article discusses the issues for a purchaser that are unique to a target company that is in receivership.

Good Faith

Central to any business acquisition is the need to obtain clear and unencumbered title to the target assets. Where the vendor is in receivership:

a. charges over the assets will have become fixed. Releases of all charges having priority to that pursuant to which the receiver has been appointed must be released;

b. you need to be certain of the validity of the receiver's appointment (and any limitations on it);

c. licences to intellectual property may have terminated, requiring new licences in the names of the purchaser (an assignment of licences will not suffice as you cannot assign something that has ended);

d. long term contracts may likewise have terminated and will have to be dealt with separately rather than dealing with them under the umbrella of business contracts, as is usually the case.

Caveat Emptor

All assets will be acquired on an "as is where is" basis, ie no warranties will be available. This demands that the purchaser make its own enquiries about the assets and the existence of any encumbrances against them and to place sole reliance on those enquiries.

Hand in hand with this is the absence of a warranty that all material information has been provided. Nor will time permit an extensive due diligence to be carried out. The solution is to factor all risks into the price and/or agree on an escrow arrangement for part of the purchase price being placed in a solicitor's trust account for a period that establishes a low risk of claims against assets.

Escrow arrangements are popular amongst purchasers but are strongly resisted by receivers, as agents for the vendor whose interests are predicated on an uncomplicated and quick recovery for the creditor who has appointed them. Where an escrow arrangement is not available, again the bargain becomes one that is dictated solely by price.

Goodwill

Goodwill in the business may have been irreparably damaged. Purchasers need to satisfy themselves that key suppliers will continue to supply the business and/or that they do not have the right to repudiate the contract. Purchasers should also ascertain whether key employees will remain.

Banking Arrangements

Existing banking arrangements will invariably terminate. Purchasers therefore need to have finances at the ready for working capital purposes including (and especially) immediate rent and salaries.

Debtors

The purchase of debtors in a business centres on:

a. their collectability;

b. managing their collection so as not to determine business with the customer.

In the case of a company in receivership, collectability concerns are often high. That is sometimes because the debtor has a competing claim for the supply of late or defective product. Because of this it is generally best for a purchaser not to acquire debtors of a company in receivership and to manage any fall out with the customer that may accompany the vendor's approach to collection.

Non-Compete Clauses

These are generally not available where businesses are acquired from a receiver.

Time Frames

Usually there is no time for extensive due diligence as there is strong elasticity between the period to completion of the sale and retention of value in the business (the risk of lost customers and employees).

The Landlord

If use of the premises is desired, a discussion with the landlord to gauge its support will be needed. Time frames won't permit a formal assignment of lease to be obtained by completion and it will be a breach of the lease where, absent a landlord consented assignment, the tenant affords the purchaser access to the premises.

If you are interested in pursuing a purchase of a business where a receivership prevails, feel free to contact me. I would be glad to help.