6S Sale of Stock

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II. Annotated Stock Purchase Agreement

II. ANNOTATED STOCK PURCHASE AGREEMENT

A. [6S.4] Heading, Table of Contents, and Introductory Material

Add after the second paragraph on p. 6-7:

When there are more than a few shareholders and the shareholders do not constitute all or a majority of the directors or management of the target company, the target company (Moonlight is our example) is often added as a party to the Agreement. Two purposes are served by adding the target company as a party. First, the buyer may require the target company to take various actions between signing and closing and, accordingly, desires the target company to contractually agree to take such action rather than rely on an indirect commitment of the shareholders "to cause" the target company to take certain action. Second, for purposes of giving the representations and warranties regarding the target company, the target company's management, on behalf of the shareholders, often makes representations and warranties regarding the target because the management is usually more familiar with and more comfortable giving factual representations regarding the target company than passive shareholders. As discussed below, the shareholders, and not the target company, will retain all of the liability for an incorrect or inaccurate representation.

B. [6S.5] Article 1: Transactions at Closing; Working Capital Adjustment; Escrow

Add at the end of the second paragraph on p. 6-8:

Alternatively, the parties pick a balance sheet date as of a sensible date prior to the closing (for example, the last day of the month prior to the closing date) and provide for restrictions on transactions that the company may engage in during the period between the balance sheet date and the closing date plus an amount of company cash on hand at the closing that is easily verifiable at the closing (by obtaining a bank statement). This method provides the parties with sufficient time to review the balance sheet and reduces the need for post-closing adjustments.

Add after Section 1.5(A)(2) near the bottom of p. 6-9:

Cutoff date for receivables. When calculating working capital, it will be important to negotiate the receivable cutoff age that will be included as working capital. The parties should review the company's collection history and, if possible, industry comparisons to determine a fair cutoff date for receivables. For example, in some transactions, it makes sense to state in the agreement that any receivables older than 90 days are not to be included in the calculation of working capital. In other transactions, that number may go up to 120 or 180, depending on the nature of the business.

Section 1.5(E)(1) near the middle of p. 6-10 is revised:

(1) be in cash (or, for payments owed to Big Fund, from the escrow reserve);

The last sentence of the paragraph titled Interest *on p. 6-10 is deleted.*

D. [6S.7] Article 3: Shareholders' Representations and Warranties

Add after the last paragraph on p. 6-12:

When there are more than a few shareholders, and the shareholders do not constitute all or a majority of the directors or management of the target company, buyers often desire that the target company's management, on behalf of the shareholders, make representations and warranties regarding the target. In this case, management is much more likely to be more familiar with, have a greater knowledge base concerning, and feel more comfortable giving factual representations regarding the target company than passive shareholders. The shareholders, however, and not the target company, will retain all of the indemnification liability for an incorrect or inaccurate representation as if they personally gave the representation and warranty, as explained in the preceding paragraph.

At the end of Section 3.2(B), the phrase **and each Subsidiary** *is deleted.*

Items 1 – 3 at the top of p. 6-15 are revised:

1. U.S. domestic transactions valued below $59.8 million do not require notification.

2. U.S. domestic transactions valued above $239.2 million require notification, regardless of the size of the parties.

3. U.S. domestic transactions valued between $59.8 million and $239.2 million must meet an additional size-of-person test before the Act requires notification. The size-of-person test is met if one transaction party's ultimate parent entity has $12 million in total assets or annual net sales and another transaction party's ultimate parent entity has $119.6 million in total assets or annual net sales. 72 Fed.Reg. 2693 (Jan. 22, 2007) (updated annually and posted on the FTC Web site at www.ftc.gov).

F. [6S.9] Article 5: Obligations Before Closing

Section 5.1(C) is revised:

(C) to maintain its equipment and machinery in good repair and operating condition, normal wear and tear excepted;

G. [6S.10] Article 6: Noncompetition and Related Covenants

Section 6.1(A) is revised:

(A) For three years after the closing date, a Shareholder — whether directly or indirectly — must neither engage in nor be interested in any business whose products or activities compete in any way with Moonlight's or a Subsidiary's products or activities, in existence as of the closing date or at any time during the 24 months prior thereto, anywhere in the United States.

I. [6S.12] Article 8: Indemnification

Add after the first sentence in the paragraph titled Indemnification *at the beginning of the section:*

When the target company gave the representations and warranties on behalf of the seller, the indemnification section would clearly provide that the shareholders are liable for indemnification claims and not the target company. For further protection, the buyer may request that the seller indemnify the buyer for any claims or causes of action arising from company actions taken (or omitted to be taken) prior to the closing date, regardless if there is a breach or inaccuracy of a representation or warranty in the agreement. The buyer may also be required to indemnify the seller for any claims or causes of action arising from company actions taken (or omitted to be taken) after the closing date.

Add after Section 8.2(A)(1) and renumber Section 8.2(A)(2) accordingly:

> **(2) any action taken by or on behalf of the Company or any Subsidiary prior to the closing date; or**

Add after Section 8.3(A)(1) and renumber Section 8.3(A)(2) accordingly:

> **(2) any action taken by or on behalf of the Company or any Subsidiary after the closing date; or**

J. [6S.13] Article 9: Ending the Agreement

Add at the end of the section:

Willful breach. The parties will often limit post-termination liability to "willfully breaching" its obligations under the agreement. Since the seller has many representations, warranties, and covenants under the agreement, the seller will want to limit its liability for unintentional breaches of representations and warranties.

K. [6S.14] Article 10: Miscellaneous Provisions

Add at the end of the paragraph titled Amendments to the agreement *near the middle of p. 6-45:*

If there are multiple shareholders, it may make sense for amendments to be made effective by shareholders owning a threshold amount of the outstanding shares (for example, 75 percent) unless the amendment directly adversely affects the non-amending shareholder.