

Purchase Price

The Purchase Price in a Stock Purchase Agreement

ASimpleModel.com

DISCLAIMER: The information contained in this document has been made available on ASimpleModel.com and is subject to ASimpleModel.com's Terms of Use. This document is made available solely for general information purposes. ASimpleModel.com does not warrant the accuracy, completeness, or usefulness of this document.

PURCHASE PRICE

Purchase price, in the context of an acquisition, is not as simple as it might otherwise sound. To arrive at the purchase price for a target company the parties involved must first agree on the value of the company. This value will then be defined in the definitions of a stock purchase agreement as something similar to Base Purchase Price or Initial Purchase Price.

Using Base Purchase Price for the purposes of this example, a series of adjustments must then typically be made to arrive at Purchase Price. This is largely because most transactions are contemplated on a cash-free, debt-free basis, and because it is impossible to accurately measure net working capital in advance of or on the date of the transaction.

Consequently, to arrive at Purchase Price the Base Purchase Price needs to be adjusted for the following:

- (a) the amount of cash on the balance sheet;
- (b) indebtedness (to be defined later in this post);
- (c) working capital;
- (d) and transaction expenses.

Items (a) and (b) above, adjust the Base Purchase price for a cash-free, debt-free transaction. This means that the Seller is entitled to the cash on the balance sheet on the date of the transaction, and that the Seller is responsible for debts owed by the company (defined as Indebtedness). Item (c) is addressed in a post titled The Working Capital Adjustment in a Purchase Agreement. And item (d) is included to make sure that the Buyer is responsible for the fees and expenses associated with the transaction.

In summary, to arrive at Purchase Price the following adjustment are made:

- (a) the Base Purchase Price;
- (b) *plus* Cash;
- (c) *minus* Indebtedness;
- (d) *plus* the amount by which Net Working Capital is greater than the Net Working Capital Target;
- (e) *minus* the amount by which Net Working Capital is less than the Net Working Capital Target;
- (f) *minus* the Transaction Expenses.

In a purchase agreement all of the capitalized words in the bullets above require definitions. The definition for Indebtedness frequently covers half a page or more (we have included an abbreviated definition). To visualize how the definitions and the calculation of purchase price come together we have included a summarized example on the pages that follow.

Stock Purchase Agreement Language:

The pages that follow contain hypothetical language detailing the above sequence as it might appear in a stock purchase agreement.

STOCK PURCHASE AGREEMENT LANGUAGE

WHAT FOLLOWS IS A HYPOTHETICAL EXAMPLE PROVIDED SOLEY FOR GENERAL INFORMATION PURPOSES.

STOCK PURCHASE AGREEMENT

ARTICLE I DEFINITIONS

[Only definitions relevant to this post have been included. This is by no means a comprehensive example of the definitions that would otherwise be found in a stock purchase agreement. It is not uncommon to see a purchase agreement with 10+ pages of definitions.]

“Base Purchase Price” means \$XXX,XXX,XXX.

“Cash” means the aggregate amount of all cash and cash equivalents of the Company (including marketable securities, short term investments, liquid instruments and petty cash).

“Indebtedness” means (i) all indebtedness for borrowed money; (ii) obligations for the deferred purchase price of property or services; (iii) obligations evidenced by any note, bond, debenture, mortgage, or other similar instruments; (iv) capitalized lease obligations; and (v) all obligations with respect to any salary, bonus or deferred compensation. *[This is an abridged definition of Indebtedness.]*

“Net Working Capital” means (i) the current assets (excluding Cash and marketable securities) of the Company, minus (ii) the current liabilities (excluding Indebtedness, Transaction Expenses and property Tax) of the Company determined as of the Closing Date.

“Net Working Capital Target” means \$X,XXX,XXX.

“Transaction Expenses” means the fees and expenses incurred by the Company in connection with the preparation of this Agreement and the consummation of the transactions contemplated by this Agreement.

ARTICLE II PURCHASE & SALE

Section 2.1 Purchase and Sale. Subject to the terms and conditions set forth herein, at the Closing, Sellers shall sell to Buyer, and Buyer shall purchase from Seller, the Securities free and clear of all Liens, for the consideration specified in **Section 2.2.**

Section 2.2 Purchase Price. Subject to the terms of this Agreement, the aggregate purchase price for the Securities (the **“Purchase Price”**) shall equal the sum of:

- (a) the Base Purchase Price;
- (b) *plus* Cash as of immediately prior to the Closing;

STOCK PURCHASE AGREEMENT LANGUAGE

- (c) *minus* Indebtedness as of immediately prior to the Closing;
- (d) *plus* the amount, if any, by which the Net Working Capital is greater than the Net Working Capital Target;
- (e) *minus* the amount, if any, by which the Net Working Capital is less than the Net Working Capital Target;
- (f) *minus* the Transaction Expenses, to the extent not paid prior to the Closing and to be paid by the Buyer.