

BUYING A SMALL BUSINESS

Thinking about buying a small business? It can be a great idea, **if you do your homework**. This is a complex decision that requires a careful analysis of physical properties, financial statements, and the relationships between the business and its customers, its community, and its competitors. Don't try to do this analysis alone-**get professional help to evaluate and price the business, particularly if you don't have at least three years of experience in owning and operating a similar enterprise**. Some advantages and disadvantages of purchasing an existing business include the following:

Advantages

- The business has an existing established relationship with both customers and suppliers.
- Financing will be easier to obtain providing the business has a good profit history.
- Operations can begin right away; current inventory can be sold to produce immediate cash flow.

Disadvantages

- The cost may be higher than starting from scratch as often you are buying "goodwill."
- Existing problems can be hidden until after the sale.
- Inventories may be obsolete due to their age; equipment may be faulty.

Recommendations

I. Require the seller to put in writing and warrant every essential part of the business, including:

- that the financial statements which should be attached as exhibits are true and correct
- that there are no hidden liabilities of any kind (tax claims, lawsuits, or supplier bills).
- a complete list of everything being purchased: leases, contracts, amounts owed to suppliers, amounts owed by customers, inventory, fixtures, equipment, signs, computer hardware and software and anything else that will contribute to the success of the business.

2. If the financial statements have not been audited by a certified public accountant, have it done. If the seller won't pay the cost, you should do so in order to make sure your investment is a wise one.

3. Determine whether there is an industry association that can provide you with "normal" financials to be used to compare against the financials of the business you're buying.

4. Fairly safe investments will return 5% annually. Consider this when reviewing the selling price. There are companies that do business valuations for a fee; it's probably worth paying the fee to do the valuation to avoid paying too much for the business.

5. If you are paying more for the business than the assets are valued, recognize that you are buying "goodwill" -- an intangible asset that may be amortized over a 15-year period.

6. Make sure to involve your banker. The purchase and sales agreement state the agreed upon price, lists what is being bought, indicates what actions are required by the seller (such as an environmental study) and by the purchaser (such as seeking financing), and sets the time the agreement is binding on both parties. Your banker needs this agreement to determine how he or she can help you finance the selling price, and whether the down payment is adequate. The bank also needs to know what is being purchased as some of it may be considered collateral.

7 Determine why the seller is selling the business

8. Determine how long this business can be expected to last. Are there factors that could terminate the business, such as a road being built that destroys the business location?

9. If there is a lease, talk to the owner of the property to be sure the terms of the lease will remain the same. This is an excellent time to discuss renewal terms and termination possibilities.

10. Ask the owner to let you work in the business prior to making a decision to buy. There is no better way of judging whether the business volume is satisfactory, whether you will enjoy working in that business and whether there are any problems you need to straighten out before the sale is finalized.

11. A business is often successful due to the personality of the owner. If this is the case, you have to decide whether you will be able to make the business as successful with your personality.

12. Make sure the seller signs an agreement not to compete for the next 10 years or so. This is especially important if you feel his or her personality was the reason for the success of the business.

13. Investigate neighborhood businesses that are not direct competitors to learn what they have to say about the growth of business in your area, what problems they see for the future, and how they feel about the business you're buying.

14. Have a credit check done on both the owner-seller and the business itself.

15. Check with suppliers to determine if the inventory you are buying is valued correctly.

16. If there are employees, talk to them about whether they will remain if you buy the business. Get any other information they are willing to provide.

17. Talk to some of the customers. Find out if they are satisfied with the business as it is now.
18. Determine if this business' prices are competitive. Visit every competitor to see if there are any changes underway that might influence your business.
19. Check with government agencies. Local agencies can tell you about licensing, environmental requirements, zoning rules, and whether there are taxes due for any local or state agency (licenses, personal property tax, franchise tax, income tax, and property tax). Federal agencies can tell you whether income tax, social security, Medicare, and unemployment tax payments are up to date.
20. Prepare a business plan. If you need help, consult your local SCORE/SBDC office. Your business library might have an actual business plan for your industry for you to study and utilize to prepare your own.