BUYING A BUSINESS - LET THE BUYER BEWARE

Buying an existing business can be an excellent way to become a business owner or to expand your present business. You can save the time and effort of building a customer and supplier base. You might also save the trouble of locating suitable equipment and hiring and training employees. However, before buying an existing business, you should abide by the Latin slogan *caveat emptor* (let the buyer beware). If you are not careful, acquiring an existing business can lead to disaster. This article discusses how to avoid those pitfalls.

Do You Really Want the Business? Before you actually look for an existing business to buy, decide whether that type of business fits your needs, both financially and emotionally. The process you go through to make this decision depends on your experience. For example, if you want to purchase a retail flower shop, but you have never sold flowers (or if you are reentering the industry after a long absence), educate yourself about the retail flower industry. Many local community colleges and libraries (especially the Harold Washington Library) have good resources.

After studying the retail flower industry, try working in a flower shop for at least one month. Select a shop that seems to be a good one-successful, attractive, with a good location. If the shop is not hiring, tell the owner that you want to someday own a shop and offer to work for free. The experience will be invaluable. For one thing, you may find out whether you truly want to work in a retail flower shop.

The next step is to prepare a business plan. The business plan will help you decide such things as the location and size of the shop you want to purchase. Again, many local community colleges and libraries have good resources that can help you learn how to prepare a business plan.

If you already have experience working in the type of business you want to buy, your decision will be easier. Presumably, you already know you like working in that industry. However, whether you want to acquire your first business or expand your existing business, you should still make sure you really want to take on the added responsibility. Preparing a business plan and perhaps studying the industry will help you decide whether you really want to do so.

Locating A Business For Sale. You have several choices for locating a business, such as through business brokers and classified ads. If you are using a broker, interview several to find one you think will respect your interests. The Sunday classified ads list many businesses for sale. You might consider running an ad yourself. Finally, you can ask owners of existing businesses if they would consider selling or if they know of a competitor who wants to sell.

Pricing the Business. There are many ways to determine the price for a business. Often, the price is set at some multiple of the value of the assets or the amount of the earnings. An accountant who is experienced in business acquisitions can assist you in determining a fair price. Again, many local community colleges and libraries will have helpful resources.

Deciding Whether to Purchase Stock or Assets If the business you want to buy is incorporated; you must decide whether to buy the stock or the assets. The stock of a business is similar to the title of a car or the deed to a house. Buying the title or the deed automatically gives you the entire car or the entire house. The assets of a business are like the various parts of a car or the contents of a house. Buying one asset does not necessarily give you other assets.

If you buy the stock of a business, you become responsible for all the debts the business incurred before the sale because you are automatically buying the entire business. These debts include those that neither you nor the seller anticipate. For example, the business's income or payroll taxes that the seller inadvertently failed to pay or unexpected customer credits for returned or rejected goods or services could all be unanticipated debts. (You can require the seller to repay you for all prior debts, but you will still owe them if the seller does not pay you.) If you only buy the assets of a business, you will not be responsible to pay the debts of that business (unless you expressly agree to do so) because you are not automatically buying the entire business.

Most purchasers of an existing business do not want to become responsible for the debts the business incurred before the sale, especially unanticipated debts. Therefore, purchasers usually buy the business's assets, not the stock. Purchasers usually only buy the stock if that is the only way to acquire a desired asset. For example, a travel agency may own a license granting access to an airline reservation service. This would be the key asset if the agency can't conduct business without access to that service. Depending on the terms of the license and the airline's rules for granting new licenses, acquiring the existing license by purchasing the business's stock may be only practical approach.

Do Your Due Diligence. After you have decided whether to buy the stock or the assets, you need to conduct a thorough examination of the business (often called the target). This review is necessary to make sure that you are getting what you will be paying for. This examination process is called due diligence. Your due diligence investigation should cover the following general areas:

Financial. You should have your accountant examine the target's tax returns and financial statements for the past five years. Your accountant should probably also spot check the target's bookkeeping records, especially if an item in a tax return or financial statement seems suspicious.

Condition of the Assets and Inventory. You should examine the assets and inventory (if any) to make sure they are in proper condition and quantity. Unless you are an expert, you should hire one to conduct this review. In any event, your attorney should make sure that there are no liens on any asset. If the assets include real estate, your due diligence should include a review of potential environmental hazards; a search to verify that the target owns clear title to the property; and a survey to verify the boundaries of the property, to make sure your neighbors are not encroaching on the property, and to make sure that all structures are within the building and lot lines.

Contracts. Your attorney should review the target's contracts to make sure it has no hidden liabilities. Also, if you want to assume, or take over, the target's rights under any contracts, you will want to make sure that the contracts permit you to do so.

Employment. If the target has employees, your attorney should review the target's books and records to make sure that there are no hidden employment agreements, union contracts, unpaid fringe benefits, or underfunded retirement plans.

Governmental Regulations. Your attorney should review all licensing requirements, zoning regulations, and the rules of all other pertinent authorities to make sure that no unexpected rules or fees exist.

General Books and Records. Your attorney should review the target's general books and records to make sure that there are not (or have not been) any adverse claims against the target or other problems associated with the business.

The Contract. Your attorney should prepare a written contract containing all the terms and conditions of your deal. You and the seller can sign the contract before you finish your due diligence, and the contract could provide that you do not have to purchase the business if your due diligence review discloses anything unsatisfactory about the target. You could also try to get the seller to agree to refrain from offering the target to anyone else until your due diligence is completed. Finally, the contract should cover your financing. For example, if you are obtaining commercial financing, the contract should enable you to walk away from the deal if you cannot obtain a loan. If the seller is providing any financing, those terms should be in the contract.

Conclusion. Buying an existing business is a major undertaking and is not a do-it-yourself job. To avoid a possible disaster, you should commit yourself to sufficient study and planning, and you should retain experts for proper guidance