

Buying a Business

There are many advantages in buying a business, but equally many disadvantages. If you thoroughly check the operations of the business, and ensure the purchase agreement contains safeguard clauses, many of the disadvantages can be minimised.

With an existing business there will always be surprises. You may never know the real reason why the business is up for sale, but you can reduce the potential for surprises by insisting on working in the business for a time prior to sale to see how staff and clients really view the business.

Sale of business and the GST

The supply of a business as a going concern is GST free if the following requirements are met:

- ❑ The purchaser and the vendor must both be registered for GST.
- ❑ The business is actually for sale with money changing hands.
- ❑ The vendor must carry on the business until the day of sale.
- ❑ All things required for continued operation of the business must be supplied.
- ❑ Both parties must agree in writing that the business is a going concern.

Advantages of buying a business

If you buy a business, you start with:

- ❑ An existing customer base, and existing contracts.
- ❑ Existing suppliers.
- ❑ Existing staff and management.
- ❑ Existing plant, equipment, stock and material.
- ❑ Knowledge of the business from the current owner.
- ❑ Premises that are set up.
- ❑ Goodwill associated with the name and location of the business.
- ❑ Financiers lending more readily to an existing business with a trading record.

Disadvantages of buying a business

The disadvantages of buying an existing business can include:

- ❑ Customers may link the goodwill to the previous owner, and leave when a new operator takes over the business.
- ❑ Staffing problems:
 - some staff may leave when the new owner takes over
 - some staff may be unsuitable for the job they are doing
 - some staff may resent the change to a new owner
 - you may inherit staff entitlements, such as impending long-service leave payments.
- ❑ Plant and equipment may be obsolete or faulty.
- ❑ The business may have no real intellectual property that is transferable.
- ❑ The business may have a bad image which is difficult to change.
- ❑ The cost of acquiring goodwill may be too high.

Checklist for buying a business

- ❑ Find out why the business is for sale.
- ❑ Decide whether the type and size of the business fits with your needs, skills and experience, financial capacity and future plans.
- ❑ Check the operations of the business including sales, costs, profits and assets. It is advisable to take independent financial advice from your accountant when reviewing the financial records of the business being considered.
- ❑ Investigate the WorkCover claim record of the business.
- ❑ Research current and potential competitors. It may be prudent to consider placing restrictions in the sale contract on the future trading activities of the vendor, where this is in direct competition with the business you are intending to purchase.
- ❑ Inspect contracts for current and future work with customers.
- ❑ Review the draft purchase agreement with your solicitor, and advise them to carry out all required searches.

The level of co-operation you receive from the current business owner is one indicator of whether you should go ahead or not.

Buying a Business

The purchase agreement

Decide whether, on the basis of the due diligence conducted and the risks involved, you are comfortable with the purchase price.

Closely review the draft purchase agreement as well as all the clauses in the agreement. Ensure the purchase agreement:

- ❑ Details all assets and liabilities to be assumed.
- ❑ States when the business is to be taken over.
- ❑ States whether the offer is conditional on:
 - obtaining finance.
 - inspecting all records.
 - receiving necessary licences and rights.
 - minimum trading levels being met during a trial period.

More Information

SOURCES OF INFORMATION

You can visit the NSW Department of State and Regional Development small business website for information on issues facing small businesses, at: www.smallbiz.nsw.gov.au

For publications, rulings and other general tax information for small business, visit www.ato.gov.au or phone 13 28 66.

WHO SHOULD I TALK TO?

For advice and protection in buying a business, you should seek the services of a solicitor, accountant or business adviser.

Your local Business Advisory Service can offer you one on one advice on buying a business. Call 1300 650 058

Checking the operations of the business

Sales

- ❑ Check monthly and yearly sales patterns.
- ❑ Compare sales trends with industry trends.
- ❑ Determine if the business is expanding, losing sales or remaining static.
- ❑ Value existing stock - ensure that it is not old or unsaleable and that there is sufficient stock.
- ❑ Identify the business customer base and percentage of sales from different customers. Check to see if the customers will stay with the business if you purchase it.
- ❑ Determine where each of the business products is on their respective life cycles.
- ❑ Determine whether you'll be able to increase sales with current resources.
- ❑ Find out if you are able to continue to buy from existing suppliers.
- ❑ Find out if there are any local developments that may affect trade.

Costs

- ❑ Identify all fixed and variable costs and include interest expenses on your borrowings for the business.
- ❑ Examine the costs recorded for the business and ensure costs are reasonable.
- ❑ Determine whether recorded depreciation costs are reasonable.
- ❑ Determine whether you will incur similar costs to the current business owner.

Profits

- ❑ Analyse financial records, including balance sheets, profit and loss statements, Business Activity Statements and sales records.
- ❑ Determine whether the business generates sufficient profit for a reasonable income.
- ❑ Look at effects of increased or decreased sales on your profit.
- ❑ Compare gross profits with industry trends.

Assets

- ❑ Identify all asset items that you are buying. Refer to an asset register/list, if available.
- ❑ Check depreciation schedule for equipment, fixtures, fittings, etc.
- ❑ Determine book value, market value and replacement value of fixed assets.
- ❑ Identify any current leases for fixed assets.
- ❑ Ensure equipment is in good working condition.
- ❑ Determine if any equipment is unnecessary for the business or obsolete.

Staff

- ❑ Determine whether existing staff will continue employment.
- ❑ Identify key staff, and review salaries, employment packages and FBT implications.
- ❑ Assess any outstanding holiday pay and/or long service leave liabilities.