

SCORE[®]

Counselors to America's Small Business

BUYING A BUSINESS

- **Checklist for Buying a Business**
- ▮ **Checklist for Buying a Franchise**

BEWARE OF THE “GOTCHA’S” IN BUYING A BUSINESS

1. Are you buying assets or stock?

2. What's the price?

- Fixed amount
- Fixed amount plus assumption of liabilities
- Other

3. What are you buying?

- Inventory -- is it obsolete?
- Raw materials -- are they usable?
- Accounts Receivable -- are they collectible?
- Equipment -- is it in good working order and sufficient to operate the business?
- Lease -- is it assumable on the same terms?
- Is the name included?
- Franchise rights and other contracts rights.
- Non-competition agreement/goodwill.

4. What liabilities are you assuming?

- Liens on equipment -- better do a UCC search.
- Outstanding contracts -- are they assumable?
- Contingent liabilities.
- Employment agreement.
- Warranty work or refund claims on past sales.

5. Tax Aspects of buying a business.

- Price allocation can substantially affect your write-offs.
- Sales tax clearance from State Board of Equalization.

6. Other compliance areas.

- Bulk sales notice if asset purchase
- Securities consent if stock purchase.
- Fictitious Business Name Statement.

7. Continuing liability after the purchase

- Indemnification.
- Personal guarantees -- where purchaser is corporation.

8. Do your homework before you buy.

- Review financial statements.
- Talk to customers.
- Talk to suppliers.
- Can you live with the purchase agreement?

Buying a Business

Basic requirement - Management capability - 75% chance of success

1. Basic knowledge of business - get job for a short period of time. -
2. Compatibility to type of operation indoors or out - enjoy what you are doing.
3. Limited capital and available financing
4. Potential of industry - competition

Sources -

1. Business brokers - check reputation with Better Business Bureau - Trade ` associations
2. "Business Opportunities" column - Local Newspapers
3. Trade Associations - Banks - Product Suppliers

Evaluation

1. Reason for selling - Health - Retirement
2. Divorce - Financial bind
3. Business failing - Increased competition - Obsolete inventory
4. Highway re-route - closing off-ramp - Expiring lease or Franchise Agreement Lack of energy or incentive
5. Financial statements - Accountant
6. Contact adjacent businesses
7. Foot and auto traffic - Parking
8. Customer count

Purchase Price

1. Merchandise - Count - Cost or market value Condition - Obsolescence Consigned stock
Fixtures - Cost less depreciation - "Used " dealers -Appraiser
2. Physical condition - Leased? Liens?
3. Accounts receivable - Collect for Seller - Trust a/c
4. Insurance & Property Tax - Pro-rate
5. Goodwill - Evaluation - Allocate to fixtures & leasehold improvements (depreciable)
6. Accounts payable - guarantee
7. Suppliers - Contact re continuation
8. Store lease - Transferable - period - renewal option

Escrow

1. Collection of accounts receivable
2. Assigned leases
3. Tax clearances
4. Guarantee of liabilities not shown
5. Covenant not to compete
6. Pro-ration of P. P. tax and insurance
7. Transfer of name

Making offer known

1. Brokers - Newspapers (Business Opportunities)
2. Trade Associations - Suppliers

Sellers check list

1. Financial information - Good points
2. Screen prospects - Capital - Background

Selling price

1. Merchandise - count & price
2. Insurance - Taxes - pro-rated
3. Receivables - collected for you or guaranteed
4. Fixtures - Cost less depreciation vs. market
5. Goodwill computation

Salary for owner/operator

Yearly net profit

Extra earning power

Multiple factors

1. Young - 1 - 2 - 3
2. Established 5 to 10
3. Unique 15

Closing Sale

1. Attorney Escrow Company or bank
2. Landlord - transfer of lease
3. Equipment lease transfer
4. Notify unpaid creditors to submit bills
5. Tax clearances - Sales - Soc. Sec. - Unemp.

FRANCHISING CHECKLIST

QUESTIONS TO ANSWER AFFIRMATIVELY BEFORE GOING INTO FRANCHISING

Check if answer is YES

THE FRANCHISOR

- Has the franchisor been in business long enough (5 years or more) to have established a good reputation?
- Have you checked Better Business Bureaus, Chambers of Commerce, Dun and Bradstreet, or bankers to find out about the franchisor's business reputation and credit rating?
- Did the above investigations reveal that the franchisor has a good reputation and credit rating?
- Does the franchising firm appear to be financed adequately so that it can carry out its stated plan of financial assistance and expansion?
- Have you found out how many franchises are now operating?
- Have you found out the "mortality" or failure rate among franchises?
- Is the failure rate small?
- Have you checked with some franchisees and found that the franchisor has a reputation for honesty and fair dealing among those who currently hold franchises?
- Has the franchisor shown you certified figures indicating exact net profits of one or more going operations which you have personally checked yourself?
- Has the franchisor given you a specimen contract to study with the advice of your legal counsel?

Check all that apply. Will the franchisor assist you with...?

- A management training program?
- An employee training program?
- A public relations program?
- Obtaining capital?
- Good credit rating?
- Merchandising ideas?
- Designing store layout and displays?
- Inventory control methods?
- Analyzing financial statements?
- Does the franchisor provide continuing assistance for franchisees through supervisors who visit regularly?
- Does the franchising firm have an experienced management trained in depth?

- Will the franchisor assist you in finding a good location for your business?
- Has the franchising company investigated you carefully enough to assure itself that you can successfully operate one of its franchises at a profit both to it and to you?
- Have you determined exactly what the franchisor can do for you that you cannot do for yourself?

THE PRODUCT OR SERVICE

- Has the product or service been on the market long enough to gain good consumer acceptance?
- Is it priced competitively?
- Is it the type of item or service which the same consumer customarily buys more than once?
- Is it an all-year seller in contrast to a seasonal one?
- Is it a staple item in contrast to fad?
- Does it sell well elsewhere?
- Would you buy it on its merits?
- Will it be in greater demand five years from now?

If it is a product rather than a service:

- Is it packaged attractively?
- Does it stand up well in use?
- Is it easy and safe to use?
- Is it patented?
- Does it comply with all applicable laws?
- Is it manufactured under certain quality standards?
- Do these standards compare favorably with similar products on the market?
- If the product must be purchased exclusively from the franchisor or a designated supplier, are the prices to you, as the franchisee, competitive?

THE FRANCHISE CONTRACT

- Does the franchise fee seem reasonable?
- Do continuing royalties or percent of gross sales payment appear reasonable?
- Are the total cash investment required and the terms for financing the balance satisfactory?
- Does the cash investment include payment for fixtures and equipment?
- If you will be required to participate in company sponsored promotion and publicity by contributing to an advertising fund, will you have the right to veto any increase in contributions to the "fund"?
- If the parent company's product or service is protected by patent or liability insurance, is the same protection extended to you?

- Are you free to buy the amount of merchandise you believe you need rather than being required to purchase a certain amount?
- Can you, as the franchisee, return merchandise for credit?
- Can you engage in other business activities?
- If there is an annual sales quota, can you retain your franchise if it is not met?
- Does the contract give you an exclusive territory for the length of the franchise?
- Is your territory protected?
- Is the franchise agreement renewable?
- Can you terminate your agreement if you are not happy for some reason?
- Is the franchiser prohibited from selling the franchise out from under you?
- May you sell the business to whomever you please?
- If you sell your franchise, will you be compensated for the good-will you have built into the business?
- Does the contract obligate the franchiser to give you continuing assistance after you are operating the business?
- Are you permitted a choice in determining whether you will sell any new product or service introduced by the franchiser after you have opened your business?
- Is there anything with respect to the franchise or its Operation which would make you ineligible for special financial assistance or other benefits accorded to small business concerns by federal, state, or local government?
- Did your lawyer approve the franchise contract after he studied it paragraph by paragraph?
- Is the contract free and clear of requirements which would call upon you to take any steps which are, according to your lawyer, unwise or illegal in your state, county, or city?