



Entrepreneur

How to Buy a Business

Starting from scratch isn't the only way to get started. Buying an existing business can help you hit the ground running. Here's what you need to know to find a great deal.

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When most people think of starting a business, they think of beginning from scratch--developing your own ideas and building the company from the ground up. But starting from scratch presents some distinct disadvantages, including the difficulty of building a customer base, marketing the new business, hiring employees and establishing cash flow...all without a track record or reputation to go on.

Buying an Existing Business

In most cases, buying an existing business is less risky than starting from scratch. When you buy a business, you take over an operation that's already generating cash flow and profits. You have an established customer base, reputation and employees who are familiar with all aspects of the business. And you don't have to reinvent the wheel--setting up new procedures, systems and policies--since a successful formula for running the business has already been put in place.

On the downside, buying a business is often more costly than starting from scratch. However, it's easier to get financing to buy an existing business than to start a new one. Bankers and investors generally feel more comfortable dealing with a business that already has a proven track record. In addition, buying a business may give you valuable legal rights, such as patents or copyrights, which can prove very profitable. Of course, there's no such thing as a sure thing--and buying an existing business is no exception. If you're not careful, you could get stuck with obsolete inventory, uncooperative employees or outdated distribution methods. To make sure you get the best deal when buying an existing business, be sure to follow these steps.

The Right Choice

Buying the perfect business starts with choosing the right type of business for you. The best place to start is by looking at an industry with which you're both familiar and which you understand. Think long and hard about the types of businesses you're interested in and which best match your skills and experience. Also consider the size of business you are looking for, in terms of employees, number of locations and sales. Next, pinpoint the geographical area where you want to own a business. Assess labor pool and costs of doing business in that area, including wages and taxes, to make sure they're acceptable to you. Once you've chosen a region and an industry to focus on, investigate every business in the area that meets your requirements. Start by looking in the local newspaper's classified section under "Business Opportunities" or "Businesses for Sale". You can also run your own "Want to Buy" ad describing what you are looking for. Remember, just because a business isn't listed doesn't mean it isn't for sale. Talk to business owners in the industry; many of them might not have their businesses up for sale but would consider selling if you made them an offer. Put your networking abilities and business contacts to use, and you're likely to hear of other businesses that might be good prospects.



Contacting a business broker is another way to find businesses for sale. Most brokers are hired by sellers to find buyers and help negotiate deals. If you hire a broker, he or she will charge you a commission--typically 5 to 10 percent of the purchase price. The assistance brokers can offer, especially for first-time buyers, is often worth the cost. However, if you are really trying to save money, consider hiring a broker only when you are near the final negotiating phase. Brokers can offer assistance in several ways.

- **Prescreening businesses for you.** Good brokers turn down many of the businesses they are asked to sell, whether because the seller won't provide full financial disclosures or because the business is overpriced. Going through a broker helps you avoid these bad risks.
- **Helping you pinpoint your interest.** A good broker starts by finding out about your skills and interests, then helps you select the right business for you. With the help of a broker, you may discover that an industry you had never considered is the ideal one for you.
- **Negotiating.** The negotiating process is really when brokers earn their keep. They help both parties stay focused on the ultimate goal and smooth over any problems that may arise.
- **Assisting with paperwork.** Brokers know the latest laws and regulations affecting everything from licenses and permits to financing and escrow. They also know the most efficient ways to cut through red tape, which can slash months off the purchase process. Working with a broker reduces the risk that you'll neglect some crucial form, fee or step in the process.

A Closer Look

Whether you use a broker or go it alone, you will definitely want to put together an "acquisition team"--your banker, accountant and attorney--to help you. These advisors are essential to what is called "due diligence", which means reviewing and verifying all the relevant information about the business you are considering. When due diligence is done, you will know just what you are buying and from whom. The preliminary analysis starts with some basic questions. Why is this business for sale? What is the general perception of the industry and the particular business, and what is the outlook for the future? Does--or can--the business control enough market share to stay profitable? Are raw materials needed in abundant supply? How have the company's product or service lines changed over time?

You also need to assess the company's reputation and the strength of its business relationships. Talk to existing customers, suppliers and vendors about their relationships with the business. Contact the Better Business Bureau, industry associations and licensing and credit-reporting agencies to make sure there are no complaints against the business.

If the business still looks promising after your preliminary analysis, your acquisition team should start examining the business's potential returns and its asking price. Whatever method you use to determine the fair market price of the business, your assessment of the business's value should take into account such issues as the business's financial health, its earnings history and its growth potential, as well as its intangible assets (for example, brand name and market position).

To get an idea of the company's anticipated returns and future financial needs, ask the business owner and/or accountants to show you projected financial statements. Balance sheets, income statements, cash flow statements, footnotes and tax returns for the past three years are all key indicators of a business's health. These documents will help you conduct a financial analysis that will spotlight any underlying problems and also provide a closer look at a wide range of less tangible information.

Following is a checklist of items you should evaluate to verify the value of a business before making a decision to buy:

1. Inventory. Refers to all products and materials inventoried for resale or use in servicing a client. Important note: You or a qualified representative should be present during any examination of inventory. You should know the status of inventory, what's on hand at present, and what was on hand at the end of the last fiscal year and the one preceding that. You should also have the inventory appraised. After all, this is a hard asset and you need to know what dollar value to assign it. Also, check the inventory for salability. How old is it? What is its quality? What condition is it in? Keep in mind that you don't have to accept the value of this inventory: it is subject to negotiation. If you feel it is not in line with what you would like to sell,



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or if it is not compatible with your target market, then by all means bring those points up in negotiations.

2. Furniture, fixtures, equipment and building. This includes all products, office equipment and assets of the business. Get a list from the seller that includes the name and model number of each piece of equipment. Then determine its present condition, market value when purchased versus present market value, and whether the equipment was purchased or leased. Find out how much the seller has invested in leasehold improvements and maintenance in order to keep the facility in good condition. Determine what modifications you'll have to make to the building or layout in order for it to suit your needs.

3. Copies of all contracts and legal documents. Contracts would include all lease and purchase agreements, distribution agreements, subcontractor agreements, sales contracts, union contracts, employment agreements and any other instruments used to legally bind the business. Also, evaluate all other legal documents such as fictitious business name statements, articles of incorporation, registered trademarks, copyrights, patents, etc. If you're considering a business with valuable intellectual property, have an attorney evaluate it. In the case of a real-estate lease, you need to find out if it is transferable, how long it runs, its terms, and if the landlord needs to give his or her permission for assignment of the lease.

4. Incorporation. If the company is a corporation, check to see what state it's registered in and whether it's operating as a foreign corporation within its own state.

5. Tax returns for the past five years. Many small business owners make use of the business for personal needs. They may buy products they personally use and charge them to the business or take vacations using company funds, go to trade shows with their spouses, etc. You have to use your analytical skills and those of your accountant, to determine what the actual financial net worth of the company is.

6. Financial statements for the past five years. Evaluate these statements, including all books and financial records, and compare them to their tax returns. This is especially important for determining the earning power of the business. The sales and operating ratios should be examined with the help of an accountant familiar with the type of business you are considering. The operating ratios should also be compared against industry ratios which can be found in annual reports produced by Robert Morris & Associates as well as Dun & Bradstreet.

7. Sales records. Although sales will be logged in the financial statements, you should also evaluate the monthly sales records for the past 36 months or more. Break sales down by product categories if several products are involved, as well as by cash and credit sales. This is a valuable indicator of current business activity and provides some understanding of cycles that the business may go through. Compare the industry norms of seasonal patterns with what you see in the business. Also, obtain the sales figures of the 10 largest accounts for the past 12 months. If the seller doesn't want to release his or her largest accounts by name, it's fine to assign them a code. You're only interested in the sales pattern.

8. Complete list of liabilities. Consult an independent attorney and accountant to examine the list of liabilities to determine potential costs and legal ramifications. Find out if the owner has used assets such as capital equipment or accounts receivable as collateral to secure short-term loans, if there are liens by creditors against assets, lawsuits, or other claims. Your accountant should also check for unrecorded liabilities such as employee benefit claims, out-of-court settlements being paid off, etc.

9. All accounts receivable. Break them down by 30 days, 60 days, 90 days and beyond. Checking the age of receivables is important because the longer the period they are outstanding, the lower the value of the account. You should also make a list of the top 10 accounts and check their creditworthiness. If the clientele is creditworthy and the majority of the accounts are outstanding beyond 60 days, a stricter credit collections policy may speed up the collection of receivables.

10. All accounts payable. Like accounts receivable, accounts payable should be broken down by 30 days, 60 days, and 90 days. This is important in determining how well cash flows through the company. On payables more than 90 days old, you should check to see if any creditors have placed a lien on the company's assets.

11. Debt disclosure. This includes all outstanding notes, loans and any other debt to which the business has agreed. See, too, if there are any business investments on the books that may have taken place outside of the normal area. Look at the level of loans to customers as well.

12. Merchandise returns. Does the business have a high rate of returns? Has it gone up in the past year? If so, can you isolate the reasons for returns and correct the problem(s)?

13. Customer patterns. If this is the type of business that can track customers, you will want to know specific characteristics concerning current customers, such as: How many are first-time buyers? How many customers were lost over the past year? When are the peak buying seasons for current customers? What type of merchandise is the most popular?

14. Marketing strategies. How does the owner obtain customers? Does he or she offer discounts, advertise aggressively, or conduct public-relations campaigns? You should get copies of all sales literature to see the kind of image that is being projected by the business. When you look at the literature, pretend that you are a customer being solicited by the company. How does it make you feel? This can give you some idea of how the company is perceived by its market.

15. Advertising costs. Analyze advertising costs. It is often better for a business to postpone profit at year-end until the next year by spending a lot of money on advertising during the last month of the fiscal year.

16. Price checks. Evaluate current price lists and discount schedules for all products, the date of the last price increase, and the percentage of increase. You might even go back and look at the previous price increase to see what percentage it was and determine when you are likely to be able to raise prices. Here again, compare what you see in the business you are looking at, with standards in the industry.

17. Industry and market history. You should analyze the industry as well as the specific market segments of the business targets. You need to find out if sales in the industry, as well as in the market segment, have been growing, declining, or have remained stagnant. This is very important to determine future profit potential.

18. Location and market area. Evaluate the location of the business and the market area surrounding it. This is especially important to retailers, who draw the majority of their business from the primary trading area. You should conduct a thorough analysis of the business's location and the trading areas surrounding the location including economic outlook, demographics and competition. For service businesses, get a map of the area covered by the business. Find out, based on the locations of various accounts, if there are any special requirements for delivering the product, or any transportation difficulties encountered by the business in getting the product to market.

19. Reputation of the business. The image of the business in the eyes of customers and suppliers is extremely important. As we mentioned, the image of the business can be an asset, or a liability. Interview customers, suppliers and the bank, as well as the owners of other businesses in the area, to determine the reputation of the business.

20. Seller-customer ties. You *must* find out if any customers are related or have any special ties to the present owner of the business. How long has any such account been with the company? What percentage of the company's business is accounted for by this particular customer or set of customers? Will this customer continue to purchase from the company if the ownership changes?

21. Inflated salaries. Some salaries may be inflated or perhaps the current owner may have a relative on the payroll who isn't working for the company. All of these possibilities should be analyzed.

22. List of current employees and organizational chart. Current employees can be a valuable asset, especially key personnel. Evaluate the organizational chart to understand who is responsible to whom. You must also look at the management practices of the company and know the wages of all employees and their length of employment. Examine any management-employee contracts that exist aside from a union agreement, as well as details of employee benefit plans; profit-sharing; health, life and accident insurance; vacation policies; and any employee-related lawsuits against the company.

23. OSHA requirements. Find out if the facility meets all occupational safety and health requirements and whether it has been inspected. If you feel that the seller is "hedging" on this and you see some things you feel might not be safe on the premises, you can ask the Occupational Safety and Health Administration (OSHA) to help you with an inspection. As a prospective buyer of a business that may come under OSHA scrutiny, you need to be certain that you are not buying an unsafe business. Some sellers may perceive your asking for OSHA's help as a dirty trick. But you must realize that as a prospective, serious buyer, you need to protect your position.

24. Insurance. Establish what type of insurance coverage is held for the operation of the business and all of its properties as well as who the underwriter and local company representative is, and how much the premiums are. Some businesses are underinsured and operating under potentially disastrous situations in case of fire or a major catastrophe. If you come into an underinsured operation, you could be wiped out if a major loss occurs.

25. Product liability. Product liability insurance is of particular interest if you're purchasing a manufacturing company. Insurance coverage can change dramatically from year to year, and this can markedly affect the cash flow of a company.

No decision is more emotionally charged than deciding upon a price for an existing business. The owner has one idea of how much the business is worth, while the buyer will typically have another viewpoint. Each party is dealing from a different

perspective and usually the one who is best prepared will have the most leverage when the process enters the negotiating stage.

Keep in mind that most sellers determine the price for their business arbitrarily or through a special formula that may apply to that industry only. Either way, there usually aren't very many solid facts upon which to base their decisions.

Price is a very hard element to pin down and, therefore, is for the buyer to assess. There are a few factors that will influence price, such as economic conditions. Usually, businesses sell for a higher price when the economy is expanding, and for a much lower price during recessions. Motivation also plays an important factor. How badly does the seller want out? If the seller has many personal financial problems, you may be able to buy the business at a discount rate by playing the waiting game. On the other hand, you should never let the seller know how badly you want to buy the business. This can affect the price you pay adversely.

Beyond these factors, you can determine the value of a business using several different methods discussed below.

Multipliers

Simply put, some owners gauge the value of their business by using a multiplier of either the monthly gross sales, monthly gross sales plus inventory, or after-tax profits. While the multiplier formula may seem complex and quite accurate to begin with, if you delve a little deeper and look at the components used to arrive at the stated value, there is actually very little to substantiate the arrived at price.

Most of the multipliers aren't based on fact. For example, individuals within a specific industry may claim that certain businesses sell at three times their annual gross sales, or two times their annual gross sales plus inventory. Depending on which formula the owner uses, the gross sales are multiplied by the appropriate number, and a price is generated.

For instance, if the business was earning \$100,000 a year and the seller was using a formula in which the multiple of gross sales was 30 percent based on industry averages, then he or she would generate a price using the following equation:

$$100,000 \times .30 = \$30,000$$

Of course, you can check the monthly sales figure by looking at the income statement, but is the multiplier an accurate number? After all, it has been determined arbitrarily. There usually hasn't been a formal survey performed and verified by an outside source to arrive at these multipliers.

In addition, even if the multiplier was accurate, there is such a large spread between the low and high ends of the range that it really just serves as a ballpark figure. This is true whether a sales or profit multiplier is used. In the case of a profit multiplier, the figure generated becomes even more skewed because businesses rarely show a profit due to tax reasons. Therefore, the resulting value of the business is either very small or the owner has to use a different profit factor to arrive at a higher price.

Don't place too much faith in multipliers. If you run across a seller using the multiplier method, use the price only as an estimate and nothing more.

Book Values

This is a fairly accurate way to determine the price of a business, but you have to exercise caution using this method. To arrive at a price based on the book value, all you have to do is find out what the difference is between the assets and liabilities of a company to arrive at its net worth. This has usually been done already on the balance sheet. The net worth is then multiplied by one or two to arrive at the book value.

This might seem simple enough. To check the number, all you have to do is list the company's assets and liabilities. Determine their value, arrive at the net worth, and then multiply that by the appropriate number.

Assets usually include any unsold inventory, leasehold improvements, fixtures, equipment, real estate, accounts receivable, and supplies. Liabilities can be anything. They might even include the business itself. Usually, though, you want to list any unpaid debts, uncollected taxes, liens, judgments, lawsuits, bad investments--anything that will create a cash drain upon the business.



Now here is where it gets tricky. In the balance sheet, fixed assets are usually listed by their depreciated value, not their replacement value. Therefore, there really isn't a true cost associated with the fixed assets. That can create very inconsistent values. If the assets have been depreciated over the years to a level of zero, there isn't anything on which to base a book value.

Return on Investment

The most common means of judging any business is by its return on investment (ROI), or the amount of money the buyer will realize from the business in profit after debt service and taxes. However, don't confuse ROI with profit. They are not the same thing. ROI is the amount of the business. Profit is a yardstick by which the performance of the business is measured.

Typically, a small business should return anywhere between 15 and 30 percent on investment. This is the average net in after-tax dollars. Depreciation, which is a device of tax planning and cash flow, should not be counted in the net because it should be set aside to replace equipment. Many novice business owners will look at a financial statement and say, "There's \$5,000 we can take off for depreciation." Well, there's a reason for a depreciation schedule. Eventually equipment does wear out and must be replaced, and it sometimes has to be replaced much sooner than you expect. This is especially true when considering a business with older equipment.

The wisdom of buying a business lies in its potential to earn money on the money you put into it. You determine the value of that business by evaluating how much money you are going to earn on your investment. The business should have the ability to pay for itself. If it can do this and give you a return on your cash investment of 15 percent or more, then you have a good business. This is what determines the price. If the seller is financing the purchase of the business, your operating statement should have a payment schedule that can be taken out of the income of the business to pay for it.

Does a 15-percent net for a business seem high? Everybody wants to know if a business makes two, three, or 10 times profit. They hear price-earning ratios tossed around, and forget that such ratios commonly refer to companies listed on the stock exchange. In small business, such ratios have limited value. A big business can earn 10 percent on its investment and be extremely healthy. The big supermarkets net two or three percent on their sales, but this small percentage represents enormous volume.

Small businesses are different. The small business should typically earn a bigger return because the risk of the enterprise is higher. The important thing for you, as a buyer of a small business, is to realize that regardless of industry practices for big business, it's the ROI that you need to worry about most. Is it realistic? If the price is realistic for the amount of money you have to invest, then you can consider it a viable business.

Capitalized Earnings

Valuing a business based on capitalized earnings is similar to the return-on-investment method of assessment, except normal earnings are used to estimate projected earnings, which are then divided by a standard capitalization rate. So what is a standard capitalization rate?

The capitalization rate is determined by learning what the risk of investment in the business would be in comparison to other investments such as government bonds or stock in other companies. For instance, if the rate of return on investment in government bonds is 18 percent, then the business should provide a return of 18 percent or better on the investment into it. To determine the value of a business based on capitalized earnings, use the following formula:

Projected Earnings x Capitalization Rate = Price

So, after analyzing the market, the competition, the demand for the product, and the organization of the business, you determine that projected earning could increase to \$25,000 per year for the next three years. If your capitalization rate is 18 percent, then the value of the business would be:

$$\$25,000 / .18 = \$138,888$$

Generally, a good capitalization rate for buyouts will range between 20 to 40 percent. If the seller is asking much more than what you've determined the capitalized earnings to be, then you will have to try and negotiate a lower price.

Intangible Value

Some business owners try to sell goodwill as an asset. Normally, in everyday accounting procedures, most companies put down perhaps one dollar as the value of goodwill. There is no doubt that goodwill has value, particularly if the business has built up a regular trade and a strong base of accounts. But it is the financial value of the accounts, not their psychological value, that should be placed on any financial statements.

Goodwill as such is not an asset. You as a buyer would assess the business based on the return on investment. Certain rules of the game may change when you enter the fields of acquisition and merger. Suppose you buy out your competition, merge all your facilities, and double your volume. Now the labor and overhead factors are much lower. Thus, even if the seller was losing perhaps 5 percent a year, if you bring them into your company, which is making 15 percent a year, it might allow you to increase sales and end up making 20 percent.

Deciding on a price, however, is just the first step in negotiating the sale. More important is how the deal is structured. David H. Troob, chairman of Geneva Companies, a national mergers and acquisitions services firm, suggests that you should be ready to pay 30 to 50 percent of the price in cash, and finance the remaining amount.

You can finance through a traditional lender, or sellers may agree to "hold a note," which means they accept payments over a period of time, just as a lender would. Many sellers like this method because it assures them of future income. Other sellers may agree to different terms--for example, accepting benefits such as a company car for a period of time after the deal is completed. These methods can cut down the amount of upfront cash you need; Troob advises, however, that you should always have an attorney review any arrangements for legality and liability issues.

An individual purchasing a business has two options for structuring the deal (assuming the transaction is not a merger). The first is asset acquisition, in which you purchase only those assets you want. On the plus side, asset acquisition protects you from unwanted legal liabilities since instead of buying the corporation (and all its legal risks), you are buying only its assets.

On the downside, an asset acquisition can be very expensive. The asset-by-asset purchasing process is complicated and also opens the possibility that the seller may raise the price of desirable assets to off-set losses from undesirable ones.

The other option is stock acquisition, in which you purchase stock. Among other things, this means you must be willing to purchase all the business assets--and assume all its liabilities.

The final purchase contract should be structured with the help of your acquisition team to reflect very precisely your understanding and intentions regarding the purchase from a financial, tax and legal standpoint. The contract must be all-inclusive and should allow you to rescind the deal if you find at any time that the owner intentionally misrepresented the company or failed to report essential information. It's also a good idea to include a no compete clause in the contract to ensure the seller doesn't open a competing operation down the street.

Remember, you have the option to walk away from a negotiation at any point in the process if you don't like the way things are going. "If you don't like the deal, don't buy," says Troob. "Just because you spent a month looking at something doesn't mean you have to buy it. You have no obligation."

Alternatives to Cash

Short on cash? Try these alternatives for financing your purchase of an existing business:

- **Use the seller's assets.** As soon as you buy the business, you'll own the assets--so why not use them to get financing now? Make a list of all the assets you're buying (along with any attached liabilities), and use it to approach banks, finance companies and factors (companies that buy accounts receivable).
- **Buy co-op.** If you can't afford the business yourself, try going co-op--buying with someone else that is. To find a likely co-op buyer, ask the seller for a list of people who were interested in the business but didn't have enough money to buy. (Be sure to have your lawyer write up a partnership agreement, including a buyout clause, before entering into any partnership arrangement.)
- **Use an Employee Stock Ownership Plan (ESOP).** ESOPs offer you a way to get capital immediately by selling stock in the business to employees. If you sell only non-voting shares of stock, you still retain control. By offering to set up an ESOP plan, you may be able to get a business for as little as 10 percent of the purchase price.
- **Lease with an option to buy.** Some sellers will let you lease a business with an option to buy. You make a down payment, become a minority stockholder and operate the business as if it were your own.



- **Assume liabilities or decline receivables.** Reduce the sales price by either assuming the business's liabilities or having the seller keep the receivables.

Don't be too anxious when you're looking to buy a business. As we've mentioned already, if you're too anxious, this can affect the price.

Tremendous mistakes are made by people who are anxious. Business consultants called in by anxious buyers can sometimes salvage the situation, but oftentimes consultants are not called until a deal has been closed. And once your signature goes on that dotted line, you're stuck with the purchase. So keep in mind that anxiety or impatience isn't going to help you buy a business. Take your time. Recognize that there's always time to reflect on the business that's for sale. No matter what a business broker, a business seller, or any other person may tell you, there's always time. Nine times out of 10, the business that's up for sale is going to be around for awhile. And if it's not, then it's the seller who is going to be the anxious one; and the seller's anxiety, of course, is something that can be manipulated to your advantage as buyer.

Some of the more common mistakes are:

- **Buying on price.** Buyers don't take into account ROI. If you're going to invest \$20,000 in a business that returns a five-percent net, you're better off putting your money in stocks and commodities, the local S&L, or municipal bonds. Any type of intangible security is going to produce more than five percent.
- **Cash shortage.** Some buyers use all their cash for the down payment on the business, though cash management in the startup phase of any business, new or existing, is fundamental to short-term success. They fail to predict future cash flow and possible contingencies that might require more capital. Further, there has to be some revenue set aside for building the business via marketing and PR efforts. So, if you have \$20,000 to invest, make sure you don't invest the entire amount. Keep some of the capital. Though figures vary from industry to industry, a common contingency is 10 percent. Additionally, you may want to set aside a sum that you regard as your working capital, which in a number of businesses is enough to cover about three months' worth of expenses.
- **Buying all the receivables.** It generally makes good sense to buy the receivables, except when they are 90 or 120 days old, or older. Too often buyers take on all the receivables, even those beyond 90 days. This can be very risky because the older the account, the more difficult it'll be to collect against. You can protect yourself by having the seller warrant the receivables; what's not collectible can be charged back against the purchase price of the business. For receivables beyond 90 days, give those to the owner, and see if he or she can collect.
- **Failure to verify all data.** Most business buyers accept all the information and data given to them by the seller at face value, without the verification of their own accountant (preferably a CPA, who can audit financial statements). Most sellers want to get their cash out of the business as soon as possible, and buyers frequently allow them to take all the quick assets such as receivables, cash, and equipment inventories, and sometimes bring in equipment. The seller talks the buyer into virtually anything, knowing that the buyer wants the business badly.
- **Heavy payment schedules.** Novice business owners often overestimate their revenue during the first year and take on unduly large payments to finance the buyout. Generally, however, revenue rarely pans out. During the first year of any operation, the owner experiences numerous non-recurring costs such as equipment failures, employee turnover, etc. For this reason, it makes sense to have a payment schedule that begins fairly light, then gets progressively heavier. This is something that can be negotiated with a seller and should not be difficult to arrange.
- **Treating the seller unfairly.** People think that, because they are buying a business, the seller is at their mercy. All too often, the buyer will be cold, rigid and hard-headed. Sellers with savvy will throw such people out and tell them not to come back. Just because you have some money and may be interested in purchasing the business, that doesn't mean that you aren't going to have to give a little in the process of negotiation.

Transition Time

The transition to new ownership is a big change for employees of a small business. To ensure a smooth transition, start the process before the deal is done. Make sure the owner feels good about what is going to happen to the business after he or she leaves. Spend some time talking to key employees, customers and suppliers before you take over; tell them about your plans and ideas for the business's future. Getting these key players involved and on your side makes running the business a lot easier.



Most sellers will help you in a transition period during which they train you in operating the business. This period can range from a few weeks to six months or longer. After the one-on-one training period, many sellers will agree to be available for phone consultation for another period of time. Make sure you and the seller agree on how this training will be handled, and write it into your contract.

If you buy the business lock, stock and barrel, simply putting your name on the door and running it as before, your transition is likely to be fairly smooth. On the other hand, if you buy only part of the business's assets, such as its client list or employees, then make a lot of changes in how things are done, you'll probably face a more difficult transition period.

Many new business owners have unrealistically high expectations that they can immediately make a business more profitable. Of course, you need a positive attitude to run a successful business, but if your attitude is "I'm better than you," you'll soon face resentment from the employees you've acquired.

Instead, look at the employees as valuable assets. Initially, they'll know far more about the business than you will; use that knowledge to get yourself up to speed, and treat them with respect and appreciation. Employees inevitably will feel worried about job security when a new owner takes over. That uncertainty is multiplied if you don't tell them what your plans are. Many new bosses are so eager to start running the show, they slash staff, change prices or make other radical changes without giving employees any warning. Involve the staff in your planning, and keep communication open so they know what is happening at all times. Taking on an existing business isn't always easy, but with a little patience, honesty and hard work, you'll soon be running things like a pro.

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