Key facts about...

Buying or Selling a Business

TOWNSENDS BUSINESS & CORPORATE LAWYERS

What I need to know about...
Buying or Selling a Business

When you buy or sell a business, what exactly are you dealing with? A 'business' is not a tangible asset as such – you can't pick it up or put it in a box or carry it down the street.

A 'business' is actually the collection of all the assets and rights the owner uses to earn revenue ... and hopefully turn a profit.

So when it comes to buying or selling a business it is essential to identify every asset or right individually so it can be effectively transferred from seller to buyer.

Those assets and rights could include:

1. business name
2. trade mark or logo
3. right to occupy premises (lease)
4. plant & equipment
5. fittings and fixtures
6. stock
7. goodwill
8. telephone number(s)
9. domain name
10. website
11. employees
12. supply agreements
13. current orders
14. database
15. licences

The seller must be prepared and able to give good title to all of the above. The seller must be sure this is possible before putting the business on the market.

The buyer must be prepared and able to accept good title. The buyer must check that it is receiving everything necessary for the proper, efficient and profitable running of the business.

Let's look at the important things that each side would have to think about as part of the sale process.

The Seller	The Buyer

The Agent

The agent is the seller's agent. What they tell others when acting as the seller's agent may therefore bind the Seller.	Unless the agent's representations are included in the sale contract, you may not be able to rely on them.

The Identity of the Seller

Make sure you know **exactly** who owns each asset of the business and therefore has the right to sell them all.	Make sure you know exactly who owns each asset of the business and therefore has the right to sell them all.
Do different parties own different parts of the business? Reduce the business to its elements and check ownership of each component.	Reduce the business to its elements - does the Seller own all these elements?
If you don't and the wrong person **sells**, the tax consequences could be disastrous (not to mention the problems you'll have with the Buyer).	If you don't check, you may not obtain good title to **all** of the business.

The Identity of the Buyer

If the Buyer is a company the Seller **may** need a personal guarantee from the people who operate the Buyer such as its directors, shareholders or senior management to ensure that the deal goes through.	The Buyer must make sure the right entity will own the business. This is absolutely vital from an income tax point of view. Should it be: • Individual(s) (in which case should partners be included?) • Company • Trust
Has the Buyer the financial capacity to complete the sale?	You may need to provide guarantees that the sale will be completed.

The Seller

The Buyer

The Price

Plant & Equipment ("Fixed" Assets

These are assets used in the Business itself: eg vehicles, machinery, office furniture etc. They are not the product the Business sells.

Produce an itemised list of the assets.

If these are sold above the depreciated book value, the Seller may be liable to tax on the excess.

The amount for which plant and equipment are purchased will be the opening value in the books of the Buyer and may only be depreciated from that opening book value.

Goodwill

The notion of goodwill is hard to define. Generally it is the totality of the opportunity and means to operate the Business.

Goodwill is capital in the hands of the Seller and therefore subject to capital gains tax if acquired after 19/09/85.
Regardless of the definition of goodwill the Buyer needs to ensure it buys everything even remotely concerned with the successful operation of the Business.

Payments for goodwill are capital payments by the Buyer.

Stock in trade

This consists of

- supplies used in the production of the goods for sale in the Business;
- goods being produced; and
- finished goods.

The Buyer will need the opportunity to value the stock immediately prior to settlement and even ensure that the stock is really saleable.

The maximum amount payable for stock should be agreed at the start to ensure the Buyer has enough funds available to complete the purchase.

Finance

The Buyer must have their finance organized before exchanging contracts for the purchase.

The Seller

The Buyer

The Premises

If you own the premises and they go with the Business, prepare sale documents ready for inspection.

If the goodwill depends on the Business' location in any way, proper transfer of the premises will be vital to a successful sale. No area has the potential to cause as much harm to the Buyer than this.

If you just lease the premises then check with your landlord **before** you put the business on the market so you **know** their attitude. REMEMBER: most leases give the landlord significant power when it comes to transferring a lease.

If location of business is associated with the goodwill, the Buyer MUST be sure he or she can obtain the legal rights to the premises by either -

- transfer of current lease
- new lease
- purchase of real estate

Make sure you have the lease document handy before putting business on the market, so that Buyers can inspect it.

If leasing, you need to spread the amount you pay for goodwill over the absolute minimum period of the lease and make sure the business can repay that amount in the necessary time **and** provide desired income for the Buyer as well.

The Seller	The Buyer

The Goodwill

.... or what it is about the Business that gives it a value above the value of the assets alone

Assess which names of the products/services contribute to the Business' goodwill.	Determine which names of products/services used in the Business contribute to its goodwill. Ensure registration of those names before or at sale.
Ensure each of these is registered before putting the Business on the market so you have maximised the Business' sale value.	Check the ASIC Business Name Register to see if name properly registered and if any similar names are around.
	Check other name registrations, other intellectual property rights that may be appropriate - • Design Registrations • Company name • Patents • Trade Marks
Make sure you are happy to transfer all communication links even if it means changing a private one. This includes domain names, email addresses, websites, telephone numbers, fax numbers, PO boxes and any other method by which clients or potential clients contact the business	Ensure you receive a transfer of all the communication links by which the clients or potential clients contact the business.

No Encumbrances

The Seller will be required to pay out any: • mortgages • charges • bills of sale • security agreements • other encumbrances over plant, equipment, fittings, fixtures and stock. Be sure you can do this easily and understand whether there will be any penalty interest.	The Buyer must check to ensure that there are no encumbrances that need to be paid out on settlement. Check: • PPSR • Bankruptcy search • Land titles search • ASIC
For those items the subject of hire purchase or chattel lease the Seller must ensure that the agreements can be transferred to the Buyer or be prepared to pay them out (which can sometimes be expensive).	Buyer must ensure that the Chattel Lease Company or Hire Purchase Company agree to transfer the leases or hire purchase agreements - otherwise the Seller may remain as the owner of the goods - or the Buyer may end up with goods which are encumbered.

The Seller	The Buyer

Restraint

The Seller will need to promise the Buyer that the Seller will not compete with the Business after the sale.	The Buyer will want a promise from the Seller that the Seller will not compete with the business after the sale.
But the Seller will need to ensure that the promise does not limit his future activities too much.	But the Buyer must ensure that this promise is not too restrictive on the Seller, or otherwise the Court will not enforce the promise.
The Buyer may also want a restraint from any key staff that are not remaining with the Buyer. If the key staff have not signed a restraint with the Seller already then the Seller may want to orchestrate that restraint prior to revealing to the key staff that the sale has been effected.	Key staff can drain clients as readily as the owner/seller so it may be necessary to ensure that key staff remain in the Business for as long as possible after the sale or arrange for them to provide the Buyer with a restraint.

Employees

Nothing the Buyer and the Seller agree on affects the statutory and award rights of the employees of the business. Various statutes ignore the sale of a business when calculating an employee's rights to entitlements such as long service leave, holiday pay, sick leave and the like. So ...

The Seller must ensure that the Buyer fulfills all obligations to the employees. If the Buyer defaults the Seller may become liable to the employees.	The Buyer must ensure that all obligations to each of the employees are known and perhaps that an amount to cover these have been accounted for in calculating the purchase price.
The Seller should also try to ensure that key staff remain with the business.	If the employment of key staff is truly important to the Buyer then the contract needs to make it a condition of settlement that those staff agree to stay and work for the Buyer.

Existing Contracts

If the Business includes work-in-progress, being the obligation to finish certain orders, the Seller needs to ensure those orders are properly filled or they may remain liable under those contracts.	If the Buyer is paying for work-in-progress as part of the purchase price he or she is in fact paying non-deductible capital for the right to receive assessable income. A discount factor should be applied in calculating that part of the purchase price relating to work-in-progress.
If the Business involves agreements with suppliers, the Seller must make sure that the suppliers will release the Seller from those agreements and accept the Buyer instead.	The Buyer must make sure that he or she has inspected all supply agreements so all rights and obligations under them are known, and that the Supplier will agree to supply the Buyer on the same terms and conditions.

The Seller	The Buyer

Tuition and Introduction to Client Base

The Seller should ensure that he or she provides enough tuition to the Buyer to enable the Buyer to run the business effectively when it is taken over.

The Buyer wants enough tuition so that the takeover of the business can occur as quickly and effortlessly as possible.

The Seller should also be prepared to introduce the Buyer to suppliers, clients etc to protect the Goodwill.

The Buyer needs to have the Seller's endorsement as the new owner. Consider a flyer and personal introduction to key clients.

Seller's Warranty on Takings

Sellers often do not want to give a warranty on recent year's takings as they consider this is a hard and fast promise that the Buyer will make that money. This is not so. The warranty is simply a statement of fact as to the Seller's takings in respect of the Business during the relevant period.

Wherever possible the Buyer should try to get a warranty as to the financial basis of the Business. This is not a guarantee that the Buyer will make that money, but provides a benchmark against which the Buyer's performance can be measured in order to justify the purchase price and ensure the Seller's representations about the Business have been accurate.

The Seller may not want to give a warranty because the actual takings of the business may not all have been put through the books.

Licences

If the conduct of the business or part of it involves holding a licence issued by government or a statutory authority the Seller should ensure that the Buyer is likely to be granted a new licence or have the existing one transferred.

The Buyer will need to ensure that the Buyer will be granted a new licence or a transfer of any existing licence necessary to be held before the Buyer can operate the Business. Completion of the contract must be conditional on that happening.

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