



Buying a Business

Buying a business or a franchise is one of the many ways you can become a business owner. The decision to buy a business or franchise can be easily rushed. For such a significant decision you need to take time to consider some important factors before you sign any purchase or franchise agreement.

Buying a Business – The Seller and You

Before making the big decision to buy a business, make sure that you are comfortable with:

- ✓ The reason for the sale of the business;
- ✓ The level of cooperation from the current business owner;
- ✓ The type and size of business, in relation to your needs, experience, financial capacity and future plans; and
- ✓ The business performance during the trial period.

Check the Operations of the Business

Sales

- ✓ Check monthly and yearly sales patterns, from previous three years financial statements.
- ✓ 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.
- ✓ Find out if you are able to continue to buy from existing suppliers.
- ✓ Find out if there are any local developments that may affect the business' sales.

Costs

- ✓ Identify all fixed and variable costs.
- ✓ 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.
- ✓ Ensure that records have been kept well and comply with tax requirements.

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.

Putting Pen to Paper – The Purchase Agreement

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

- ✓ Includes all assets including goodwill that are being purchased; and
- ✓ Clearly states all liabilities that you will assume upon buying the business; and includes clauses that will protect you as a buyer and covers issues of obtaining finance, inspecting all records,

receiving necessary licences and rights and ensuring a minimum trading level during trial period.

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 must be registered, or required to be registered for GST;
- ✓ The supply is for consideration;
- ✓ The supplier must carry on the business until it is sold;
- ✓ All things required for continued operation of the business must be supplied; and
- ✓ Both parties must agree in writing that the supply is of a going concern.

Buying a Franchise

A franchise is a type of business ownership where an individual, partnership or company can operate a business under a banner of an already established business.

Benefits of a franchise can include:

- ✓ Support of the franchisor;
- ✓ Flow-ons from the franchisor's advertising, buying power, established goodwill and trade marks;
- ✓ Use of an already established business name;
- ✓ Access to the franchisor's management systems and industry knowledge;
- ✓ Reduction of business risk.

Some of the drawbacks of a franchise can be:

- ✗ Less independence through franchisor control of management techniques, possibly supply sources and product/service range;
- ✗ Reputation of franchise may be affected by factors beyond franchisee's control;
- ✗ Could have an unreliable franchisor;
- ✗ Sale of head franchise;
- ✗ Defined/ limited geographical market.

Before you commit to the Franchise

Before enter into a franchise agreement, you should obtain the following information.

- ✓ A complete description of the business.
- ✓ The track record of the franchisor and current motives for franchising.
- ✓ Evidence of the franchisor's strategic plan – where is the business heading.

- ✓ What the franchisor offers under the agreements, such as name, product, reputation/goodwill, site location, advertising budget and back-up assistance.
- ✓ Fees involved, including up-front capital and percentage of taking payable to the franchisor.
- ✓ Terms of sale of goods supplied by the franchisor and if you can purchase from outside the franchise network.
- ✓ Success/failure of other franchisees in the same business.
- ✓ Obligations upon termination of franchise.
- ✓ Guidelines for sale of the franchise;
- ✓ A franchise Operations Manual, if available.
- ✓ The franchise agreement document and the period of franchise.

The Franchise Agreement

A franchise agreement is a written document outlining the rights and obligations of both the franchisor and the franchisee. It is a legal contract and binds both parties. The content of a franchise agreement will regulate, to a certain extent, the way you operate the franchise.

Operations Manual

The Operations Manual details how the franchise is to be run. Every member of the franchise operates their business according to the Operations Manual. The Operation Manual ensures that each franchise operates consistently, under the one banner.

Regulation

All franchise businesses are required by law to comply with the Franchising Code of Conduct. This Code protects the rights of franchisees and sets out obligations of franchisors. The Code also provides a mediation procedure where disputes cannot be resolved within the franchise system.

The Office of the Mediation Adviser (OMA) helps franchisors and franchisees resolve their problems and disputes without going to court. For further information contact OMA on 1800 150 667 or website www.mediationadviser.com.au.

Contacts

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

Solicitors and Business Law Specialists

in your area can be located through the Law Society on (02) 9926 0305 / (02) 9926 0383, or refer to the Law Society of NSW website at www.lawsocnsw.asn.au.

Accountants in your area can be located through the following peak accounting bodies:

- CPA Australia, phone (02) 9375 6200 or website: www.cpaaustralia.com.au.
- Institute of Chartered Accountants in Australia, phone (02) 9290 1344 or website: www.icaa.org.au.
- Association of Taxation and Management Accountants, phone (02) 9799 6255 or website: www.atma.com.au.
- National Institute of Accountants, phone (02) 9299 3052 or website: www.nia.org.au.

Franchise Council of Australia

For information on franchising matters, contact the Industry Association, phone (02) 9264 4077, fax (02) 9264 4966 or website at www.fca.com.au.

For More Information:

Contact your local Business Advisory Service on 1300 650 058 to talk over business management issues.

You can also visit the Small Business Website of the Department of State and Regional Development at www.smallbiz.nsw.gov.au.