BUYING AN EXISTING BUSINESS

If you're thinking about running your own business, buying a company that's already established may be a lot less work than starting from scratch. However you will need to put time and effort into finding the business that's right for you. This guide takes you through the steps of buying an existing business, including how to assess and value a business, your obligations to any existing staff and where you can get professional help.

Advantages and disadvantages of buying an existing business

If you get it right, there can be many good reasons why buying an existing business could be the right move for you. Remember though, that you will be taking on the legacy of the business' previous owner, and need to be aware of every aspect of the business you're about to buy.

Advantages:

- Some of the ground work will already have been done in getting the business off the ground.
- It may be easier for you to get finance as the business will have a proven track record.
- A market for the product or service will have already been demonstrated.
- There may be established customers, a reliable income, a reputation to capitalise and build on, and a useful network of contacts.
- A business plan and marketing method should already be in place.
- Existing employees should have experience you can draw on.
- Many of the problems will have been discovered and solved already.
- You can always re-sell the business.

Disadvantages:

- You often need to invest a large amount up front, and will also have to budget for professional fees for solicitors, surveyors, accountants, etc.
- If the business has been neglected you may need to invest quite a bit more on top of the purchase price to give it the best chance of success.
- You will need to honour or renegotiate any outstanding contracts the previous owner has in place.

Deciding on the right type of business to buy:

Ideally your business needs to fit your own skills, lifestyle and aspirations. Before you start looking, think about what you can bring to a business and what you'd like to get back.
List what is important to you. It is useful to consider:

- Your expectations in terms of earning - what level of profit do you need to be looking for to accommodate your needs?
- Your commitment - are you prepared for all the hard work and money that you will need to put into the business to get it to succeed?
- Your strengths - what kind of business opportunity will give you the chance to put your skills and experience to good use?
- The type of business - limited company, partnership etc - that you're interested in buying.
- The business sector you're interested in - learn as much as you can about your chosen industry so you can compare different businesses. It's important to take the time to talk to people already in similar businesses.
- Location - but don't restrict your search to your local area. Some businesses can be easily relocated.

Where to look for a business to buy:

Many national and local newspapers carry adverts for businesses and business premises.

Depending on what sector you're interested in, you could look in trade journals.

Or put in your own advert, saying what you are looking for. You can get contact details for most newspapers, magazines and trade journals from press directories available at your local library.
Some magazines - many of them with their own websites - specialise in buying and selling, like Exchange and Mart, Loot and Daltons Business.

Don't forget word of mouth. Ask around among trade contacts, business associates, and at exhibitions and conferences.

How to value a business:

Understandably, how to value a business is often the most worrying part of buying a new business. Remember, though, that what a business is worth to you will not be the same as to someone else with a different set of priorities and objectives.
To get a general idea of how healthy the business is, look at:
the history of the business

- its current performance (sales, turnover, profit)
- its financial situation (cash flow, debts, expenses, assets)
- why the business is being sold

The list below may help you spot areas where you could lose out financially.

How healthy is the business?

Stock:
- How much is there?
- What condition is it in?

Assets:
- Does the asking price take into account depreciation?
- Is anything leased or on hire purchase?

Intangible assets:
- How much goodwill comes with the business?
- Are any trademarks registered?

Products:
- What are the profit margins on each product?
- Which products account for the majority of sales?

Licences:
- Which ones are required to conduct the business?
- Are there any outstanding issues with the licences?

Debtors:
- How old are the debts?
- Which debtors owe the most?

Creditors:
- What does the business owe?
- What is its credit history like?

Suppliers:
- What are their prices?
- What's their credit policy?

Employees:
- Is the business adequately staffed?
- Is it over-staffed?
- Do employees have the necessary skills?

Premises:
- Do they need refurbishing?
- Are they lease or freehold?

Competition
What percentage of the market do the competitors have?

Valuation methods:

Your accountant can advise on how to put a specific value on the business and do the actual calculations. You can then decide how much you want to offer, or if you want to buy it at all.
If you do decide to make an offer, the research you do now will be verified in detail once you've agreed a purchase price with the vendor.

Make sure a business is worth buying: due diligence:

Having done your research, it is important to verify the information you have. A period of time is allowed for you to access the business' books and records to verify that all of the information that you have been told up to now is accurate, and this is known as due diligence. It should give you a realistic picture of how the business is performing now and how it is likely to perform in the future.

When to begin due diligence

Don't start due diligence until you've agreed to a price and terms with the seller. For a down payment they may agree to take the business off the market during your investigation.
The investigation period is negotiable - but most small businesses need at least three to four weeks.

Where to get help

You should get accountants and solicitors to help you identify risk areas but you can also get information about companies direct from the interent. Due diligence is about much more than the finances of a business. You need to come out of this period knowing exactly what you are getting into, what needs to be fixed, what the costs are to fix them and if you are the right person to take on this business.

Key areas to cover are:

- employment terms and conditions
- outstanding litigation
- major contracts and orders
- IT systems and other technology
- environmental issues
- commercial management including customer service, research and development, and marketing

Information sources

Dig as deeply as you can and use whatever documents are available. For instance, if you're looking at employee records, you could check out:

- payroll records
- staff files
- copy of retirement and profit sharing plans plus financial statements, if relevant
- employment contracts
- the staff manual
- union contracts, if relevant
- you may also need information from external sources such as the landlord, tax office or bank.

Step-by-step: how to buy a business

1 Get professional advice

Professional help is invaluable as you go through the negotiation, valuation and purchase process. You may find it useful to contact the professional organisations to get advice and help on finding a solicitor or an accountant.

2 Research

Research the sector you're interested in, including the best time to buy. Shortlist two or three businesses. See our page in this guide Make sure a business is worth buying: due diligence and verify any information you have been given. As well as checks on the business, your attorney will conduct searches in order to verify relevant licences etc.

If you're planning to arrange a loan, the lender will insist on carrying out their own survey and valuation at your expense, but you may want to pay for an additional independent survey and valuation.

3 Initial viewing and valuation

Be discreet - the owner may not want staff to know they are selling, but be thorough and record key findings.

4 Arrange finance

Lenders generally require:

- details of the business/sales particulars
- accounts for the last three years
- financial projections (if no accounts are available)
- details of your personal assets and liabilities

5 Make a formal offer

If you make your initial offer by phone, follow this up in writing. Head your letter **subject to contract** and include this phrase in all written communication.

6 Negotiation

Before completing the sale, try to negotiate an overlap period so you have time to become familiar with the business before taking over. Record all the main point agreed.

7 Completion

Even after you reach an agreement on the price and terms of sale, the deal could still fall through. You have to meet certain conditions of sale to complete, including:

- verification of financial statements
- transfer of leases
- transfer of contracts/licences
- transfer of finance

Looking after existing employees:

There are regulations that govern what happens to employees when someone new takes over a business. These apply to all employees when a business is transferred as a going concern, meaning employees automatically start working for the new owner under the same terms and conditions. For more information, check on your responsibilities to employees if you buy or sell a business.

Employment tribunal awards

When you buy an existing business, you might decide you need to employ fewer staff. But be careful about making any changes, as an employee might take a case to an employment tribunal for unfair dismissal or unfair selection for redundancy. It's best to consult your attorney before making any such changes.

Inform and consult employees

If you do want to discuss reducing numbers of employees or reorganising staff it's a good idea to do this once you've completed the due diligence period, but before you take over the business. As the new employer you should inform and consult all employees - including employee representatives - who may be affected.

Employee Retirement Plans

As their new employer, you do not have to take over rights and obligations relating to employees' retirement plans put in place by the previous employer. However, if you don't provide comparable retirement plan arrangements, you could theoretically face a claim for unfair dismissal.

Related guides on www.businesslink.gov.uk:

- Buy a franchise
- Reasons for going into business
- Choose and manage an accountant
- Use your business plan to get funding
- Loans and overdrafts
- Responsibilities to employees if you buy or sell a business
- Getting new workers started
- Dismissal
- Making an employee redundant
- Recognising a trade union - the issues

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Home > Buy or sell a business > Buying a business > Buy an existing business

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