

# Buying an Existing Business — What to Consider

**W**hether you are an entrepreneur looking to open your first business or an established business looking to expand into a new market, buying an existing business (also known as a “target business”) may be a viable alternative to starting one from scratch. However, before you sign on the all-important dotted line, you should make abundantly sure that the transaction is properly structured, that you’ve exhaustively investigated the target business, and that the contract for sale is properly drafted.

The benefits of buying an existing business are obvious. According to the Small Business Administration, approximately 50 percent of small businesses do not survive past the fourth year of operations. By taking over an existing business, you may significantly increase your business’s chance of survival. You can take advantage of a target business’s strong reputation and established clientele, which is commonly called “goodwill.”

The detriment lies in the fact that successful business owners take pride in the goodwill they’ve developed through their hard work, the calculated risks they’ve taken, and their attention to their customers. Hey - they’ve earned it! But as the purchaser, the value of that goodwill is explicitly or implicitly built into the purchase price.

One of the first issues to consider would be how to structure the transaction. The more information that you have about the possible ways to structure the purchase of the business in the early stages of your negotiations, the better off you will be in your negotiation of the ultimate purchase price.

The difference between purchasing the assets of a business versus buying the company itself could mean significant differences in tax liability or general liability to both the seller and the buyer. You should consult with your accountant about how best to structure the purchase of the business from a tax perspective, and consult

with an experienced attorney about how best to structure the purchase of the business from a legal liability perspective.

From a legal perspective, if you buy the stock in a company, you may be purchasing all of that company’s liability exposure along with its goodwill such as contract claims, consumer claims, consumer warranties, etc. If you only buy the business assets, you will probably be able to avoid that exposure, depending on the structure of the deal.

You should consider how to you want to structure the payments. Payments to the seller may be made in a lump sum at closing, in installments, or possibly earned by meeting future financial goals, which is called an “earn-out” clause.

“Due diligence” should also be built into the transaction, which is the process by which the buyer conducts an investigation of the target business. The buyer is often

entitled to pull out of the deal if it is not satisfied with the results of due diligence, with certain restrictions.

Once the transaction is structured, the question becomes whether or not the purchase price is justified. By purchasing the target business, along with the assets and the goodwill, you may also be purchasing the target business’ pre-existing warranty obligations, contractual obligations with vendors or customers, or even personal injury claims.

It therefore makes sense to spend the time and money on conducting thorough due diligence before purchasing the target business, as opposed to dealing with the ramifications after you’ve taken ownership. As to each issue that arises in due diligence, it helps to have an expert (legal, accounting, environmental, etc.) to guide you.

In due diligence, at a minimum, you

Personally serving Bucks, Mercer & Philadelphia counties.

Member  
FDIC

est friend wanted.

Community  
bank  
obsessed  
with green  
seeks small  
businesses  
obsessed  
with same.

**A**  
Calif  
Comm  
tions of  
est-ran  
cials.  
started  
The  
mally  
cian into  
lo's offi  
Del  
ing D  
ers ar  
as "T  
the  
dress

Main interests:  
+ Free Business Checking  
+ eDeposits & Online Banking  
+ Lines of Credit  
+ Cash Management  
+ Commercial Loans  
+ Merchant Services  
+ Excellent Business Money  
Market Rates  
+ Go Green!



**FEDERAL BANK**

For personal attention,  
please contact Kent Lufkin, CEO,  
at 267-757-8887.

[www.ThirdFedBank.com](http://www.ThirdFedBank.com)

Whether you're looking for space or have a property to lease or sell, we have the local expertise and global reach you can trust.



#### ▲ Town Center

For Lease – 70,000 S.F.

1 Union Street, Washington Town Center  
Washington Township, NJ

- Newly constructed along Washington Town Center Lake
- Divisible to 2,600 S.F.
- Easy access to Routes 33, 130 and NJ Turnpike Exits 7A and 8



#### ▲ Class A Office Space

For Lease – 31,000 S.F.; Divisible to 2,000 S.F.

- VanNest Office Park  
Quakerbridge Road, Hamilton NJ
- Attractive corporate setting overlooking the Van Nest Forest Reserve
  - Minutes from Hamilton Train Station (Northeast Corridor Line)
  - Restaurants, banking and shopping within walking distance
  - Close proximity to Robert Wood Johnson and other area hospitals
  - Located within minutes from downtown Princeton, I-95, I-295 and Route 1



#### ▲ The Neuman Building

For Lease – 14,000 S.F.

3575 Quakerbridge Rd., Hamilton, NJ

- Aggressively priced, call for details
- Ready for tenant build-out
- 4 cars/1000 S.F. parking
- 1.5 miles from Hamilton train station
- 1.5 miles from Route 295
- T-1 Lines in building

Ibis Plaza

3525 Quakerbridge Road

Suite 908 • Hamilton NJ 08619

609 520 0061

[www.fennelly.com](http://www.fennelly.com)

**NAI Fennelly**  
Commercial Real Estate Services, Worldwide.

should examine the target business's:

- Financial information: tax returns, profit and loss statements and budgets, to chart the business's performance;
- Corporate records: to ensure that the business has been properly managed in conformity with the law;
- Employment contracts and benefit plans: to see what the target business's obligations are to its employees;
- Intellectual property ownership or restrictions: to see what marks, domain names and the like are associated with the target business;
- Real estate documentation: to ensure proper title and ownership;
- Environmental history: to ensure that any real estate is not impinged by environmental concerns;
- Leases and major contracts: again, to understand the target business' obligations; and
- Major business contacts including vendors or any other companies with whom the target business has a relationship: consider whether you will be able to build on those relationships.

Finally, it is imperative that you pay close attention to the terms and conditions in the contract for sale of the business. I would strongly suggest that you only sign such a contract if it has been drafted or reviewed by a competent attorney representing you, who has sufficient experience in the type of deal that you are negotiating. Even if the terms are relatively simple, the contract itself will probably be dense. It is therefore worth the investment to have someone with the proper experience review the contract with you to make sure that you understand each and every clause to which you are agreeing.

At the very least, the contract for sale should explicitly set forth the following: the purchase price for the business; the terms of payment; the liabilities assumed by the buyer; and representations and warranties of the seller.

Representations and warranties are often heavily negotiated. For example, buyers typically seek representations and warranties from the seller, in which the seller:

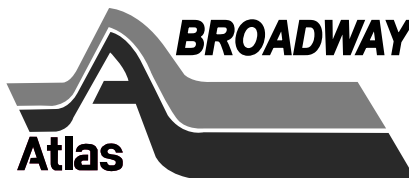
- Substantiates the assumptions made in valuing the business for the purchase;
- Indicates that it has the power and authority to conduct its business in the manner in which it is being conducted at the time of purchase;
- Agrees that its execution of the contract and the performance under the contract will not violate or conflict with any law or result in the breach of any other agreement;
- Agrees that the assets you are purchasing are free and clear of any debts, mortgages, security interests, or other liens or encumbrances (if any of the assets you are purchasing are so encumbered, they should be specifically listed in the contract and reflected in the purchase price); or
- Represents that there are no existing legal proceedings pending or, to the seller's knowledge, threatened against or affecting the seller or the business being purchased.

The seller should be held contractually responsible for any problems arising from any representations and warranties that turn out to be false. Ideally, you should make sure that you have some protection, via an escrow fund or some other holdback of the purchase price so that if you have problems you have recourse against the seller. You can also seek indemnifications that require the seller to defend any claims and pay for any attorney's fees or judgments incurred as a result of the seller's breach of its representations and warranties.

*Cary S. Kvitka is a member of Stark & Stark's Franchise Group and can be reached at 609.219.7434, or by email at [ckvitka@stark-stark.com](mailto:ckvitka@stark-stark.com).*

## MOVING YOUR OFFICE???

Serving Mercer County Since 1934



**CALL TODAY 1-800-842-8527**  
**FOR EFFICIENT, RELIABLE SERVICE**