

# *Buying a Business*

**Buying a business can be a complex task. For the purchaser, there are many potential risks. This article outlines some of the main issues that purchasers should consider. By addressing these issues, the risks commonly associated with buying a business may be reduced.**

## **Assessment of the business**

Prior to buying a business, it is important to look at the past records and the current documents of the business. This includes monthly and yearly sale patterns for the past three years. Depreciation schedules and all the costs recorded for the business should be checked. Ensure that the records comply with tax requirements. Also verify the value and condition of any existing stock.

## **Deciding upon the Structure of the Business**

When buying a business, the purchaser should decide upon the structure of the business to be implemented. The three main structures a purchaser may choose are either a sole trader, partnership, or limited liability company.

- **Sole trader:** The business will be conducted by oneself and / or employees but with no joint owners. The owner is singularly responsible for all debts and providing the capital needed to do the business.
- **Partnership:** The business will be conducted by more than one person, dependent on the number of partners. Normally, up to 20 people may form a partnership. If no formal partnership agreement exists, all partners have equal powers under the law.
- **Limited Liability Company:** This structure allows for many owners by way of the issue of shares. The company is a separate legal entity to the individual shareholders and shareholder liability is limited to the amount that remains unpaid on their shares. A board of directors conducts decision making for the business.

## **The Contract for Sale of Business**

This contract is normally prepared by the vendor's lawyer pursuant to negotiations between the vendor and the purchaser of the business. The purchaser would engage their own lawyer to vet the documents, and often new clauses would be added to the contract. Normally, the assets would be listed and the -goodwill component of the business stated clearly. The liabilities to be assumed by the purchaser would also be set out.

The contract can include clauses that protect the purchaser. Examples include:

- **Restraint of Trade Clauses:** These prevent the previous owner (vendor) from setting up a similar business within a certain radius and for a certain amount of time from the settlement date of the transaction (*Restraints of Trade Act, 1976* NSW).
- **Training Clauses:** These clauses allow the purchaser to work in or observe the business prior to settlement, so that the purchaser can gain a greater understanding of the operation of the business.
- **Performance Clauses:** These state the minimum takings of the business over a certain period of time.
- **Clauses stating that payment of the agreed price will be made in stages.** This may give the purchaser greater bargaining power if a dispute arises after the transfer of ownership.
- **Clauses providing a guarantee from the vendor that all representations made regarding sales, costs and profits figures are correct.**

### Employment Issues & Workers' Compensation

When a business changes hands, it is the purchaser's decision whether to retain the employees of the previous owner. It is the responsibility of the purchaser to inform any employees if they are to be re-employed.

Often, new employment contracts are drawn up by the purchaser, as original contracts (with the vendor) are terminated. However, the original employment contracts may still be used, if the purchaser so chooses. Purchasers should be aware that the use of *original* employment contracts requires the full recognition of past services and therefore all accrued entitlements will be the responsibility of the new purchaser. On the other hand, if the new owner decides not to re-employ existing staff, the onus is on the vendor to provide employees with all their statutory rights and entitlements arising from a termination of employment.

### The Lease

Any existing lease between a vendor and their landlord may be assigned to a purchaser with the consent of the landlord. Alternatively, the purchaser can enter into a *new* lease with the landlord. Before the lease is signed, it is important to examine the terms and conditions of the lease. Alterations to the lease must be considered and put forward prior to its signing.

Special attention should be paid to any terms which restrict the type of business which may be permitted on the property. These restrictions are often strictly adhered to by the courts and may make it difficult for the purchaser of a business to diversify their business. To combat this, clear wording should be used, keeping future developments in mind.

### Stamp Duty

Stamp duty is payable by the purchaser. Stamp duty calculations for a purchase of business (conveyance) differ from stamp duty for a transfer of shares.

Stamp duty payable for the transfer of unquoted shares is 60 cents for every \$100 or part thereof, for example:

Value of Shares	Stamp Duty
\$1,000,000	\$6,000
\$1,500,000	\$9,000

The transfer of quoted shares (ie shares listed on the stock exchange) does *not* attract stamp duty.

Stamp duty payable for the conveyance of a business itself (like a transfer of land) is higher, for example:

Value of Business	Stamp Duty
\$1,000,000	\$40,490
\$1,500,000	\$67,990

### Other costs

Before buying a business, the purchaser should be aware of any permits or fees that must be paid in order to carry out the business legally. Often, required permits are not transferable to the purchaser, and a new fee must be paid.

Under the law, Workers' Compensation insurance must be taken out where there are employees. Public liability, fire and contents insurance would be useful and should be considered.

### Conclusion

This article addresses some of the more pertinent issues surrounding the buying of a business. It highlights matters that purchasers should consider before signing a contract to buy a business.

*Comasters has acted in many 'sale and purchase of business' transactions. The firm receives instructions from vendors and purchasers of businesses.*

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**Important:** This is not advice. Clients should not act solely on the basis of the material contained in this paper. Our formal advice should be sought before acting on any aspect of the above information.

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