

Got Business Questions? SCORE Has Answers

By Willy Campbell

Do Your Homework Before Buying A Business

Not every would-be entrepreneur wants to start a small business from scratch. There is a certain attraction to coming into a business that already has a location, name, permits, customers and cash flow. Moreover, compared to a start-up there is a lower level of risk and a greater likelihood that lenders will help you with financing.

However, none of this guarantees that the going will be smooth. The risks you encounter can be many. Consider the following ten questions regarding the purchase of a business; many of them also apply to purchasing a franchise.

1. If I am actively considering a specific business opportunity, have I assembled an acquisition team comprising my attorney, banker and accountant?
2. Why does the owner really want to sell the business?
3. Is the owner willing to show me projected financial statements plus the last three years' balance sheets, income statements, cash flow statements and tax returns?
4. What assets convey with the business? Do there seem to be more fixed assets than it warrants?
5. How much inventory is there? For a business that sells a product, excessive inventory is a red flag!
6. Will the owner help me learn the business and give initial operating help?
7. How much cash does the owner need up front?
8. What is the best way to finance the purchase? Will the owner assist, for example, through leveraging the buyout?
9. Has the company or its principals been involved in bankruptcies or lawsuits?

You must establish your independent valuation of the business. This value is usually a function of its earnings, not its tangible assets. There are three approaches to valuing a business. The "Asset Based Approach" arrives at a value through the costs to replace tangible assets in like-kind condition. The "Market Approach" derives a value using ratios or factors derived from past transactions or similar businesses. The "Income Approach" converts future earnings or cash flow into a value using a capitalization or discount rate. I strongly recommend this method and direct you to www.score.org/article_business_valuation.html.

There is also valuation software for purchase on the web. And there are a number of companies and brokers that will perform business valuation.

A number of web sites provide information for prospective buyers and sellers of private businesses. They include www.onlinebusadv.com, www.score.org, and www.buysellbiz.com.

If you would like to discuss this or other business issues, contact the Sandhills Chapter of SCORE “Counselors to America’s Small Business”. SCORE is a nationwide nonprofit association of expert business counselors who provide free and confidential business counseling to small business owners. Your local Sandhills Chapter is very active in counseling, mentoring and presenting free business seminars. Volunteers to expand these efforts are urgently required. Please contact the Chapter via the web at www.sandhillsscore.org or at 910-692-3926.

Remember – send your business questions to me at www.info@sandhillsscore.org and don’t forget to provide a way to contact you. I may not be able to answer all of them in this column but every one will receive a personal answer from one of our Sandhills SCORE counselors!