

Making a Small Business Purchase Offer

Everything You Need to Know to Successfully Close a Deal!

by
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INTRODUCTION

According to various experts associated with the sale of privately owned businesses throughout the United States, there are approximately 1.2 million such enterprises for sale at any given time. It is also estimated there is somewhere in the neighborhood of twenty would-be buyers for every business for sale. This suggests there are approximately 24 million people actively looking for a business to buy.

Yet, it is also estimated that about four out of every five businesses for sale will *never sell!* This means something close to 99% of all the would-be business buyers will not succeed in their effort. The “business opportunity” market is probably one of the most inefficient markets there is. The sad fact is, the vast majority of both business buyers and sellers cannot seem to strike a deal.

There are a number of reasons for this situation, the principal one probably being the inability of sellers to figure out what their business is worth and price it accordingly. Most privately owned businesses on the market are notoriously overpriced. However, even in those cases where the seller’s asking price is reasonable, the manner in which businesses are being marketed is often so poorly orchestrated that buyers are either unaware these businesses are for sale or cannot make sense of the financial performance and other pertinent data presented.

Both the tasks of attempting to sell a business and of trying to buy a business are enormously difficult because the act of selling or buying a business is a very complex transaction. However, there are numerous resources available on the subjects of *How to Sell a Business* and *How To Buy a Business* such as books, seminars, journal articles and so forth as well as professional consultants and business brokers available to assist individuals in these efforts. Anyone contemplating either selling or buying a business would be well advised to avail themselves of one or more of these resources.

However, in all such how-to-sell or how-to-buy a business resources the focus is usually on the “big picture” and generally there is not enough nuts-and-bolts detail on actually making or interpreting a purchase offer once the parties get to this point in a transaction. It is my belief that many potential transactions that are right for both the seller and the buyer do not come together because the buyer just can’t figure out how to take the last big step in the process and *make an offer*. The purpose of this book is to provide that instruction and through this process, perhaps in some small way, pave the path for some buyers and sellers to make a deal that might not have otherwise come together.

Of course, any discussion on how to make or how to interpret a purchase offer for a business must, of necessity, overlap to some degree with the issue of how to buy or how to sell a business. For any reader who is not familiar with the business buying process, this book will be very instructive.

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The principal perspective of this book is one of providing advice to would-be buyers. However, it is just as instructive for sellers as well; maybe even more so because it will allow the seller to “walk in the other person’s shoes” so to speak and perhaps for the first time, begin to appreciate all the concerns a buyer typically has about buying a business. It is important for business sellers to realize that the act of buying a business is far more difficult, more time consuming, more stressful and much more fraught with risk than that of selling a business will ever be.¹

Indeed, one of the central themes built into the process presented here is one of *Risk Management*. That is to say, an attempt to more equitably allocate the risk involved in buying a business between buyer and seller. This fact will become abundantly clear through the course of this book. For the business seller, this effort may appear as an attack on his or her integrity—nothing more than a recurring series of innuendoes about the buyer’s presumption of the seller’s innate dishonesty. For a seller to view this process in such fashion would be a mistake. Were a buyer to truly believe the seller with whom he is dealing is fundamentally a crook, it is unlikely that buyer would ever make an attempt to buy the business at all. The best perspective for both buyer and seller to assume is that this process is simply one of risk allocation and, moreover, one that will be most productive when both parties strive for reasonableness, fairness and balance throughout. By keeping this fact clearly in view at all times, there is no reason why the process cannot proceed within a congenial atmosphere void of contention, hostility and mistrust. The process is going to be difficult enough without having to deal with those problems.

It is important to point out now that this book is *not* intended to be a “buying-a-business-made-easy” treatise because buying a business is not easy. For any one unfamiliar with the process—and this includes virtually every first-time buyer, it is imperative that you get some help. Hopefully, after reading this book you will better appreciate this advice. Furthermore, it is important that the help you seek comes from professionals properly qualified for this purpose. If you engage an attorney—which you should, engage one who is familiar with business purchase and sale transactions.

It should also become evident that you will need some help in determining what the business you wish to buy is worth. The advances made within the business appraisal profession concerning analysis techniques and resources have been substantial in just the last few years. It is highly recommended that you take great care to only engage someone who is up to date on these changes, which in most cases will be someone who makes

¹ **ADVICE TO BUSINESS SELLERS:** Sometimes business buyers will ask you what may seem to be unnecessary questions or request to see business records you feel are immaterial to making an assessment of your business. Almost certainly, requests for information will be made that will require some effort on your part to respond. This is all part of the process and should be expected. Resisting such buyer inquiries is *highly* likely to drive them off. Without question, buying a business requires a great deal of effort on the buyer’s part but it also requires a substantial effort on the seller’s part. If you’re not willing to make a reasonable, and perhaps a little bit more than reasonable effort to accommodate the requests of a buyer, don’t expect to sell your business!

Additionally, don’t take a buyer’s probing questions personally. Many, if not most, of a buyer’s concerns will revolve around fears of being deceived. Not only is this a natural fear of buyers, it’s a *reasonable* fear, because it happens to buyers all the time. Answer their questions as best as possible and, if need be, bite your tongue. If you become insulted or allow your feelings to become hurt while working with a buyer and feel compelled to tell that buyer where to get off, that’s exactly what the buyer will do—count on it.

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business appraisal an important aspect of their full time profession. The preceding statement can be interpreted to mean that not every business broker or CPA is qualified to assist you in this effort.

On the other hand, most professional business appraisers, although generally knowledgeable regarding the income tax regulations pertaining to the sale and/or purchase of a business, are not specialists in this area. Be aware that federal tax laws and regulations surrounding business sale transactions are voluminous and complex, thus in most cases it is wise to have an expert examine your proposed transaction from this perspective.

Before getting down to the brass tacks of how to make a purchase offer, it's a good idea to define exactly what a Purchase Offer is or should be. This may seem intuitively obvious but it really isn't. For example in the case of Canfield versus Gill (101 Nevada, 170 170 (1985) *Canfield v. Gill*) Jacqueline Gill made what she thought was an offer to purchase Rick Canfield's business. The purchase offer was contingent on Mr. Canfield training Ms. Gill in the operation of the business. During the training period prior to close of escrow, Ms. Gill decided she really didn't want to go through with the transaction. She notified Mr. Canfield of this decision and requested a refund of her earnest money deposit. Mr. Canfield refused, maintaining that Ms. Gill had already bought the business and had to go through with the transaction. Ms. Gill sued Mr. Canfield for return of her earnest money deposit and termination of the contract. At trial, the court concluded that the "Sales Agreement" was merely an "option to purchase" based on Ms. Gill's intent and instructed Mr. Canfield to return the deposit. Instead, Mr. Canfield appealed the lower court's decision and the case was ultimately heard by the Nevada Supreme Court. The Nevada Supreme Court reversed the lower court's decision on the basis of the precise wording in the Purchase Offer document itself. As it happened, the purchase offer was made on a standard Residential Purchase Offer and Acceptance Agreement which is intended to serve as both a purchase offer and a sales agreement for buying a home. The Nevada Supreme Court found in favor of Mr. Canfield, maintaining that the wording of the contract held more force than Ms. Gill's intention which was only implied in the contract and instructed Ms. Gill to consummate the transaction. Instead, Ms. Gill filed for bankruptcy and Mr. Canfield got his business back and resold it for significantly less than the price Ms. Gill had agreed to pay.

The moral of this story is to be absolutely sure you know what you're doing when you make an offer to purchase a business. The process may appear to the casual observer to be pretty much the same thing as making an offer to purchase a home but, in fact, it is altogether different. For starters, consider the Purchase Offer Form intended for the purpose of buying a business. Unlike the residential real estate sales industry which, within each regional market, typically uses a standardized printed form familiar to all agents and brokers, the purchase offer forms used by business brokers are almost always the unique creation of each business broker. Moreover, the differences apparent in the various Business Opportunity Purchase Offer forms in use is enormous.

Some Business Opportunity Purchase Offer forms are intended to serve as both the Purchase Offer and the Sales Agreement, just like the form used in residential real estate sales. On the other hand, some are not so intended. The one attribute nearly every Business Opportunity Purchase Offer form in use has in common, however, is that they are generally a *Seller Biased* contract. That is to say, the terms and conditions included in the contract and how they are worded favor the seller to the detriment of the buyer. But more importantly, many pro-buyer terms and conditions which could be included are never

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addressed. Thus, anyone who believes he or she is a careful reader and can effectively word-smith a printed form to appropriately adjust the nuances in a paragraph to lean more favorably toward the buyer, is committing the classic error of not seeing the forest because of the trees. Having said that, it is worth pointing out that the form presented here is an attempt to overcome this bias. That is to say, an attempt to present a more balanced contract.

Nevertheless, one should never assume that a printed Business Opportunity Purchase Offer form is safe to sign because it is “a printed form.” Nothing could be further from the truth. Never sign any contract associated with the purchase of a business without first having it reviewed by an attorney at the very least but also, in most cases, by a CPA, an insurance agent and, if you intend to use a third-party lender, that lender also and that includes the form presented here.

Perhaps a better way to go, albeit a more expensive route, is to have your attorney draft the purchase offer document in its entirety. Of course, if you have not already come to a reasonably close agreement with a business seller on the key issues of price and terms, the process of negotiating these matters by way of submitting purchase offers and fielding counteroffers can get very expensive. It’s best to have a verbal meeting of the minds on key issues before having them put into contract form by an attorney.

Assuming there is a meeting of the minds on price and terms, there are several contract development steps one can take. The route recommended here is (1) submit the Purchase Offer (2) get acceptance of the Purchase Offer, (3) conduct your “due diligence” investigation and clear the contingencies, (4) develop a definitive Purchase and Sale Agreement, Bill of Sale and, when appropriate, a Promissory Note, (5) sign the definitive agreements and close.

An alternative route is to submit a Letter of Intent as the first step instead of a Purchase Offer. Letters of Intent come in two varieties: Binding and Non-binding. There is little legal difference between a Binding Letter of Intent and a Purchase Offer, thus, if the LOI route is your preference, then it should be a Non-binding Letter of Intent. Once the letter of Intent has been signed by all parties to the proposed transaction, the “due diligence” investigation of the business begins. Upon completion of that step, a preliminary Purchase and Sale Agreement is drafted, the terms and conditions negotiated between the parties and put into final form. Only after the finalized Purchase and Sale Agreement has been signed by the parties has a legally binding commitment been entered into. This event typically precedes the close of escrow by several days or sometimes weeks or months. The closing may depend upon the buyer negotiating a new lease with a landlord or the parties accomplishing other tasks which must precede closing. On the day of closing, the buyer will require that all representations about the business the seller made in the Purchase and Sale Agreement are still true. This is accomplished by way of a “Bring-Down” Agreement which essentially says “every thing the seller said about the business in the Purchase and Sale Agreement is still true.” As the last step, the Bring-Down Agreement is signed and the transaction closes.

THE PURCHASE OFFER FORM

Notice: The Purchase Offer form presented here only *suggests* the kind of wording that may be employed. None of that which follows is represented as being “court tested,” otherwise consistent with generally accepted legal terminology or reflective of applicable case law. *Do not use this form without the advice of legal counsel.*

DEFINE WHO THE PARTIES TO THE AGREEMENT ARE:

Suggested contract wording:

| |
|---|
| <p>Whereas _____ hereinafter known as PURCHASER wishes to purchase the business and/or real property known as _____</p> <p>and</p> <p>Whereas _____ who is/are</p> <p><input type="checkbox"/> the owners</p> <p><input type="checkbox"/> the Corporation President acting on behalf of the stockholders</p> <p>hereinafter known as Seller wishes to sell this business and/or real property</p> |
|---|

Comment:

Who is making the purchase offer?

This may seem too obvious to even discuss. YOU are making the offer of course!

But, perhaps not!

It is my opinion that an individual should not make an offer to purchase a business. I believe the Purchase Offer and all contracts associated with the purchase of a business should be completed in the name of a legally formed corporation or Limited Liability Company, and it should be that company which is making the purchase offer. You will probably be the President of that company, but it will not be you as a private individual but you as *President* of a legally formed liability-limiting entity who signs the contract.

If you do not want to incur the expense of forming such an entity prior to completing the transaction, then at the very least, in the place where you indicate it is you who is making the purchase offer you should enter your name appended with the notation “or designated company owned by Purchaser.” This allows you to sign all subsequent transaction documents in the name of your corporation or Limited Liability Company if you so desire.

One more thing to consider here are the tax advantages of first forming a corporation or limited liability company and pursuing all acquisition activities under the aegis of that

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entity. If you pursue an acquisition as a private individual, then only those expenses such as legal, travel, financial analysis, etc. which you incur in connection with a business you ultimately buy are tax deductible. If you form a legal entity and pay all bills connected with your acquisition activities through that entity, then *all* of those expenses may be tax deductible, including any incurred searching for, negotiating and evaluating acquisition candidates you ultimately do not buy.

Who is the seller?

If the subject business is not a corporation, the owner either in his or her capacity as a “sole proprietor” (which can include husband and wife) or owners in their capacity as partners, are selling the company. If the business *is* a corporation, the *stockholders* are selling the company. In this instance, the corporation’s President is representing their interests (which in many small businesses may be that individual alone or a husband and wife team). In any case, however, the corporate President cannot sell the business without a *Corporate Resolution to Sell* which has been approved by a vote of the stockholders. Therefore, the buyer should know the legal form of the subject business and insure that whomever it they are dealing with has the legal authority to negotiate the transaction and sign the contracts.

THE DISCLAIMER:

Suggested contract wording:

Now therefore, PURCHASER herewith tenders an offer to purchase said business and/or real estate under the following terms and conditions. PURCHASER further stipulates and the parties herein agree that this Purchase Offer and Deposit Receipt is intended to represent an Exclusive Option To Purchase said business and/or real estate, for the time period specified hereunder and shall not be construed as a Purchase and/or Sale Agreement.

Comment:

So as to avoid any ambiguity about the intent of the buyer when making the purchase offer, the first step is to clearly define what is being presented which is an *offer* to purchase and not a definitive Purchase and Sale Agreement.

THE EARNEST MONEY DEPOSIT:

Suggested contract wording:

Received from _____ hereinafter designated as PURCHASER, the sum of: \$ _____ (_____ Dollars) evidenced by [] Personal [] Company [] Cashier’s [] Other check payable to _____ hereinafter designated as SELLER as an earnest money deposit to be applied toward the purchase of the business described herein.

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Comment:

Just as in the purchase of commercial or residential real estate, it is customary for the buyer to make an “earnest money” deposit upon submitting a purchase offer. There is nothing customary about the size of the deposit. In fact, it does not even have to be money; it can be anything of value such as jewelry, a watch, a car—anything really. As a practical matter, however, under all but very rare circumstances, the earnest money deposit will be a check drawn on the account of the party making the offer.

It is best that this check be made out to a neutral escrow company or an escrow attorney and *not* to the seller or the seller’s broker or attorney. To do otherwise is to put your chances of getting your money back at risk should you elect not to consummate the transaction. If the seller or the seller’s broker resists this approach and insists the earnest money check be made out to either the seller or seller’s broker, it is best to end the acquisition process right there and walk away.

THE PURCHASE PRICE:

Suggested contract wording:

| |
|--|
| The purchase price for the [] business [] business and real property described herein shall be \$_____ (_____ Dollars) |
|--|

Comment:

Clearly, the price you offer for a business is the single most important aspect of the proposed transaction and is most in need of very careful consideration.

Determining a Business’s Value: An Introduction to Business Valuation

There are three fundamental approaches used to estimate a business’s value. There is the *Asset Based Approach* which is a collective re-valuation of a company’s assets and liabilities, the *Income Approach* which establishes value based on a company’s earnings and there is the *Market Based Approach* which establishes value based on a comparison of the subject company with the known selling prices of similar companies. Within these fundamental approaches there exist numerous different methods (or techniques) which business appraisers employ. In a perfect world, each approach and method would result in the same value conclusion. In the real world they never do. Thus, an appraiser’s final opinion of value is usually a synthesis of several value conclusions derived using a variety of valuation approaches and methods.

As will become evident in this book, a buyer’s ability to determine the “goodwill” portion of value embodied in a purchase price will be central to an ability to make an intelligent

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purchase offer. As it happens there is one business valuation technique frequently used by business appraisers and business brokers designed specifically for this purpose. It is known alternatively as the “excess earnings” method and the “treasury method” and is formally defined in IRS Revenue Ruling 68-609. This method was originally developed in the 1920’s to calculate the value of goodwill for which the owners of breweries and distilleries needed to be compensated as a result of Prohibition. A skillful application of the “excess earnings” business valuation method will serve a prospective buyer well in an effort to determine a reasonable purchase price.

In addition to the application of any of the various business valuation methods available, it behooves a buyer to examine a possible acquisition from his or her unique perspective. No matter what a business’s “fair market value” may be, from *your* perspective a business must meet three key objectives.

1. It must provide you with a reasonable (e.g., “fair market value”) wage for all hours you work in the business.
2. It must generate a reasonable return on the up-front money you invest in it (i.e., the down payment and additional working capital you invest at start-up)
3. There must be sufficient cash flow (*after* an allowance for your wage) to service any debt you incur as part of the acquisition price (e.g., seller carry-back financing or a third party acquisition loan.)

If you carefully analyze a possible business acquisition from both a “fair market value” perspective and your unique “investment value” perspective, you should be able to determine a realistic price to offer the seller.

Having said that, one word of warning is in order. Occasionally, within the business brokerage industry and among business owners themselves, there is a tendency to estimate a business’s value based on a “rule of thumb.” There are many published as well as unpublished “heard-on-the-street” rule-of-thumb methods used to estimate a business’s value. For a business buyer to make a purchase price offer based on a rule of thumb is extremely foolhardy. As Shannon Pratt explains in his book *Valuing a Business: The Analysis and Appraisal of Closely Held Companies* (Irwin Professional Publishing, 3rd Edition, p. 249) “Rules of Thumb are usually quite simplistic. As such, they obscure much important detail. They fail to differentiate how differences in either operating characteristics or assets from one company to another affect valuation. They also fail to differentiate changes in conditions for companies in various industries from one time period to another...consequently, rules of thumb rarely, if ever, should be used [to estimate a business’s value] without other, more reliable valuation methods.”

If you are not absolutely certain you know how to determine a reasonable price to pay for a business, get some help! Probably the best place to seek assistance is a professional business appraiser. The business appraisal profession is just now coming into it’s own along with valuation techniques and business valuation resources which did not exist just a few years ago. Even the Certified Public Accountant (CPA) profession has come to realize that being a CPA in-and-of-itself is no longer considered adequate preparation for the task of business valuation.

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There are four professional associations in the U.S. that train individuals specifically for business valuation and confer a professional credential upon successfully meeting the association's requirements. There is the American Society of Appraisers which confers the designation: Accredited Senior Appraiser in Business Valuation (ASA/BV); the Institute of Business Appraisers which confers the designation: Certified Business Appraiser (CBA); the National Association of Certified Valuation Analysts, which confers the designation: Certified Valuation Analyst (CVA), and; the American Institute of Certified Public Accountants which confers the designation: Accredited Business Valuator (ABV). In addition to these training programs, there is the International Business Brokers Association which confers the designation Certified Business Intermediary (CBI)—a credential which also indicates substantial knowledge of business appraising.

Of course, availing yourself of this consultation is not inexpensive. On the other hand, any of the above identified individuals as well as any business transaction attorney, CPA or business broker can probably recall numerous accounts of people paying well over double what a business is really worth—because it happens all the time.

The “cagey” buyer who offers a seller half the asking price and makes a deal is not really so cagey when the asking price was three times what the business was worth. At the very least, read a book on valuing a small business or attend a seminar on how to buy or how to value a business.

Many business buyers already own their own business and therefore feel they know how to buy right. This may or may not be true. The fact is, the vast majority of business owners have no idea what their business is really worth—but many think they know. This can be dangerous when venturing out to buy another business. If you think your business is worth \$1,000,000 and want to buy another business about half the size and with about half the earnings of your business, you would probably be inclined to pay around \$500,000. But what if your business is really only worth \$700,000? By miscalculating the value of one's current business, a business owner may be in danger of substantially over-paying for a new acquisition.

STRUCTURING THE DEAL

Suggested contract wording:

Plus any additional contingency payment or “earn out” payment in an amount and/or payment method to be determined as follows:

Minus an adjustment to future payments in an amount and/or to be determined as follows:

Comment:

Not all business sell for a fixed price. On occasion a buyer and seller cannot agree on a firm price but still want to try to put a deal together. This can be accomplished through a deal structure known as an “earn out” or “contingency payment.” Essentially it means the buyer will pay the seller something extra in the future *if* the business meets specified sales or earnings goals. The precise formula used to determine the “earn out” portion of a purchase price is limited only by the imagination of the buyer and seller. There are no doubt thousands of different methods by which a future event could be defined that would trigger an additional payment.

There are some strong positive and negative aspects of this approach to establishing a purchase price. On the positive side, it makes possible a transaction that otherwise may never have gone together. On the negative side, such a plan can be difficult for the seller to monitor and enforce. For example, if it is a gross sales based formula, the buyer can simply skim cash, dishonestly under-report the real gross sales revenue and never pay the seller his due. If it is a profit based formula, the buyer can distort the operating costs of the business and under-report the true profitability of the firm.

Also, the Federal Income Tax reporting procedures associated with gains-on-sale emanating from an earn-out deal can be very complex and thus could become very expensive for the seller.

Decrements to future Promissory Note payments are also occasionally built into a purchase transaction. This feature is very prevalent in the professional services businesses such as medical, legal, dental, accounting, and bookkeeping practices as well as engineering, architecture and management consulting firms. It can also appear in businesses that take on certain attributes of practitioner goodwill such as real estate brokerage firms, beauty parlors and travel agencies.

The most common use of this technique is to adjust promissory note payments for the loss of clients within a specified time period after ownership changes hands. This can range anywhere from twenty-five percent to one hundred percent of the revenue the seller received from the departing client during the twelve months preceding the sale.

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Suggested contract wording:

for the business known as _____
situated in the State of _____ City of _____, County of _____
located at _____

Comment:

Many businesses will have two names: the common name by which it is known in the community—that is, it’s “d/b/a” (“doing business as” or it’s “fictitious name”) and its legal name if it is a corporation. For example, “Joe’s Bar and Grill” may only be the “d/b/a” under which Joe Johnson does business, however the legal name of the company could be “Johnson Enterprises, Incorporated.” Additionally, Joe Johnson may have multiple operations with different d/b/a’s all held within the same corporation. Unless you propose to buy the stock of the company (more on this to follow) it’s wise to identify what you propose to buy using the company’s d/b/a, and if you are acquiring multiple locations, to identify each by their unique d/b/a’s.

Suggested contract wording:

This transaction shall be a purchase of the seller’s [] assets; [] corporate stock

Comment:

In an “asset sale” the buyer essentially acquires selected company assets individually which typically consist of the company’s equipment, inventory and “goodwill.” For purchase price allocation purposes, “goodwill” is defined as “that portion of the total purchase price not allocated to anything else being acquired.” In an “asset sale” the seller typically keeps the company’s cash and accounts receivable and retains responsibility to pay off all debts at the time of sale.

In a “stock acquisition” the buyer buys the company’s stock and with that acquires *all* the company’s assets and liabilities including it’s cash and accounts receivable *and* assumes responsibility to pay *all* the company’s debts *and* assume all “off book” liabilities as well. Of course, the option of buying the corporate stock or buying the company’s assets exists only when the subject business has been legally formed as a corporation. If the company is not a corporation, the transaction can only be a purchase of the company’s assets.

Sellers prefer to sell their stock and buyers prefer to buy the assets. By selling stock, sellers typically will enjoy a tax-on-sale advantage by avoiding the “depreciation recapture tax.” Buyers, on the other hand, prefer to buy the assets because of their ability to “step-up” the value of the fixed assets as they presently appear on the seller’s books and thereby acquire a larger “depreciation tax shelter.”

Additionally, buyers generally are loath to buy a company’s stock because of the “off book” liability issue. For example, if a company is sued for any reason immediately after

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being sold for reasons attributable to actions of the seller, that lawsuit remains the seller's problem if the buyer bought the company's assets. However, if the buyer bought the company's stock, that lawsuit becomes the buyer's problem. Also, the buyer will become liable for any back taxes assessed in a post-purchase audit (including penalties and interest) that the seller may have inadvertently failed to pay prior to selling out.

Most small businesses are acquired as an "asset sale" for the reasons described. If a sale must be consummated as a stock transaction, it is a wise buyer who seeks legal counsel on how to provide protection from the additional legal risks inherent in the transaction. Moreover, it is a wise business owner who seeks professional counsel regarding the best legal entity within which to own his or her business given the tax and legal ramifications inherent in those different forms.

Suggested contract wording:

This purchase price shall include all the seller's furniture, fixtures and operating equipment currently used in the business but specifically excluding the following:

Comment:

A buyer needs to get a list of the tangible assets to be included in the purchase price. Ideally, this list would include every item to be sold including its cost new, when it was purchased, its current book value and an estimate of its current fair market value defined as "the replacement cost for a like-piece of equipment in the same condition and age, delivered and installed." Unfortunately, almost no business owner is capable of providing this kind of detail. But, at the very minimum, get a list of the equipment.

Even though an effort has been made to list all the equipment and other hard assets that are to be included in the transaction, the best way for a buyer to protect themselves is to require that all assets *not* included in the transaction be specifically identified as such. Remember, there will almost never be a business offered for sale where the owner will be able to list every tangible asset used in the business even though it will be your assumption this is what you are paying for. Put the onus on the seller to identify those assets *not* included. Then, you will be in the driver's seat if there are any post-transaction disputes over "misunderstandings" regarding whether something is included in the sale, or not.

Suggested contract wording:

The purchase price shall include all the seller's goodwill comprised of everything customarily included in such definition such as (but not limited to) Company d/b/a name, trademarks, all phone numbers, fax numbers, e-mail address, customer lists, customer accounts, computer data bases, current files, current operating records, contacts, proprietary software, secret processes/recipes, patents, distributorship rights and agreements and all other such assets with the exception of the following specific exclusions:

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Comment:

A company's "goodwill" is an element of a business transaction that can cause a great deal of confusion for buyers and sellers. There are two aspects of "goodwill" to consider: (1) what is it? And (2) what is it worth?

The first question is the easier of the two to answer. "Goodwill" is sort of a blanket term used to describe all the *intangible* assets a company owns. Those assets described above represent only a partial list of the many things which can be part of a business that could be included on an exhaustive list. If there are certain particular intangible assets which a buyer views as central to the success of the business and its future growth potential, it is best to add those items to the above description.

As for their value, well, that is a much more problematic question. Sellers almost always view the value of their company's goodwill in terms of the *cost to create it*. They will point to the time, effort and money they have invested in building their company's name and reputation and often reflect as well on all the blood, sweat and tears they have poured into the business to make it what it is today. All of that notwithstanding, a business's "goodwill" altogether may or may not have any monetary value. In fact, it can even have a *negative* value. This is because the value of "goodwill" from the market's perspective (i.e., the combined wisdom of all business investors) will be its *profit generating capability*.

One possible logistical challenge which may present itself in acquiring a company's goodwill is acquiring the company's name. If a company is a corporation and the "common name" by which a company is known by its customers, that is, its d/b/a, is the same as its legal corporate name and the buyer proposes to buy the assets of this company (as opposed to acquiring its stock) then the buyer *cannot* buy that name directly. This is so because the seller will retain the corporate shell which *must* include the corporate name. The solution to this obstacle is to provide, as a condition of sale, that the seller *change* the legal name of the corporation as registered with the Secretary of State during the escrow period while the buyer simultaneously reserves that name and then acquires it immediately thereafter.

Suggested contract wording:

This purchase price also:

[] includes; [] does not include the real property in/on which the business operates which is also owned by the seller (if applicable).

Comment:

If you are also buying the real property in which the business is situated, it is probably best to make this an entirely separate transaction. The forms, procedures and methods of financing appropriate for the purchase of commercial real estate are entirely different from those for business transactions. Thus, by attempting to combine these two different acquisitions within one purchase transaction may be inviting enormous complexity and with that great potential for something to go awry.

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Additionally, it is almost always best for a business owner who also owns the real estate in which the business operates to hold them within separate legal entities and charge the business rent. This for two reasons; first, by so doing, both the business and the real estate should be easier to sell in the future. Most investors who want to buy a business do not want to also buy the real estate and most investors in commercial income property do not want to own the business which operates in and on the property. Thus by owning them separately and strategically calculating the ideal rent to charge the business, the market value of each entity can be optimized and thereby the combined value of both investments can be maximized. Additionally, they can be sold separately and at different times.

Secondly, by holding real estate in a separate entity, the business owner then has the option of selecting which of the two to use as the principal method to extract an income. For example, by charging the business with an above-market rent the owner can draw cash out of the business by way of that rent as opposed to wages and bonuses paid by the business thus avoiding both federal and state employee and employer wage taxes. Of course this tactic has not remained undiscovered by federal and state taxing authorities. Any use of this technique should only be done under advisement of a CPA.

Suggested contract wording:

| |
|---|
| [] includes; [] does not include an allowance for salable inventory valued at \$_____ ; said value to be determined as stipulated in item number 4 below. |
|---|

Comment:

Many business carry some inventory of goods available for sale that will be included as part of the bundle of assets a buyer acquires. In the case of retail outlets and distribution companies the inventory will probably represent the largest portion of the purchase price. When these businesses are marketed, the asking price sometimes includes the inventory and sometimes it does not. It is important when developing your valuation opinion for the business that you specifically address the issue of whether such opinion is including or excluding the business's inventory.

It is a fairly straight forward process to transform an "including inventory" value opinion into an "excluding inventory" opinion and vice versa such that you can make your offer in a format most suitable to the seller. Be careful not to make an "including inventory" purchase price offer and then agree to pay extra for that same inventory. You could easily end up paying nearly double what a company is worth by making this mistake.

There is also a logistical consideration when making an "including inventory" purchase offer. That is, it is impossible to know what the value of the inventory will be at the close of escrow. Thus, the appropriate method is to determine the business's average inventory level and make your offer based on that value with a proviso that a portion of the purchase price be adjusted to reflect the actual value at close of escrow. (This will be discussed in more detail later).

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Suggested contract wording:

[] includes; [] does not include an allowance for work in progress and finished goods valued at \$_____ ; said value to be determined as stipulated in item number 6 below.

Comment:

There are many manufacturing type business which will have “work in progress” which will be included as part of the bundle of assets a buyer acquires. When these businesses are marketed, the asking price sometimes includes the work in progress and sometimes it does not. It is equally important when developing your valuation opinion for the business that you specifically address the issue of whether such opinion is one including or excluding these assets.

It is a fairly straight-forward process to transform an “including work in progress and finished goods” value opinion into an opinion excluding them and vice versa, such that you can make your offer in a format most suitable to the seller. Be careful though not to make an “including work in progress and finished goods” purchase offer and then agree to pay extra for those same things again. Just as the with-or-without-inventory purchase offer option, you could easily end up paying nearly double what a company is worth by making this mistake.

There is also a logistical consideration when making an “including work in progress and finished goods” purchase offer. It is impossible to know now what the value of that work will be at the future close of escrow. Thus, the appropriate method is to determine the business’s average work in progress and finished goods on hand level and make your offer based on that value with a proviso that that portion of the purchase price be adjusted to reflect the actual value at close of escrow. (This will be discussed in more detail later).

Suggested contract wording:

[] includes; [] does not include an allowance for accounts receivable valued at \$_____.

Comment:

The sale of most small businesses excludes the seller’s accounts receivable and are generally marketed this way. Typically the seller retains the right to collect the money due from customers for sales and services provided on credit prior to close of escrow.

However, from a strategic point of view, it can be to a buyer’s advantage to include the seller’s accounts receivable as part of the assets being purchased. For example, assume the seller has \$200,000 in accounts receivable at close of escrow. Further assume the purchase price for the business is \$200,000 *excluding* the accounts receivable and \$400,000

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including that asset. Further assume the seller is willing to carry back 50% of the purchase price in a long term Promissory Note. You give the seller \$200,000 down and agree to pay the remaining balance of \$200,000 over six years at 10% interest.

Assuming the due dates on the accounts receivable are between 30 and 90 days, then over that time period the accounts receivable you bought will be turned into cash. Thus, within a very short time period, you will have recovered your entire down payment and essentially bought the business for nothing down.

Of course, this example is a bit of an exaggeration over what a reasonable seller is likely to find acceptable. This example was used to make the concept clear. The point is; to the degree you can buy a near-cash asset that will be converted into cash in a short time period with a long-term repayment obligation, the less cash you will end up investing in the acquisition and the higher will be your return on investment. There may be some concern for your ability to collect the accounts receivable you have purchased. This matter can be easily resolved and will be addressed a little later.

Additionally, keep in mind that all of the current assets appearing on the seller's balance sheet probably reflect approximately the amounts necessary to be maintained for that particular type of business. Thus for any current asset, such as accounts receivable which you do not intend to purchase from the seller, you will need to have that much more cash available to invest in the business *immediately* after you buy it (less the average level of accounts payable and other current liabilities).

Suggested contract wording:

| |
|---|
| [] includes; [] does not include the seller's lease deposit of \$ _____ |
|---|

Comment:

In those cases where there will be a straight forward assignment of an existing lease and all other aspects of that contract will remain the same, then, as a matter of convenience, it is probably best to include the lease deposit as part of the bundle of assets being acquired.

However, as with the purchase of any other current asset, it is important that you develop your valuation opinion of the business and make your purchase offer based on the presumption that it includes this asset.

Suggested contract wording:

| |
|---|
| [] The aggregate cost to transfer/assign any and all Franchise Agreements, Dealership Agreements, Distributorship Agreements, or other contracts or agreements in the amount of \$ _____ is: |
| [] included in the purchase price and shall be paid by SELLER. |
| [] not included in the purchase price and shall be paid by PURCHASER as an additional expense of PURCHASER above and beyond the purchase price |

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Comment:

In any business that includes a franchise, dealership, distributorship or similar type of agreement, you need to know all there is about the conditions of transfer or assignment associated with them. Virtually every franchise agreement requires that either the business seller or buyer pay a transfer fee as a condition of the franchisor's approval of that action—this cost can be quite high.

Once again, as with the purchase of any other current asset, you should develop your valuation opinion of the business based on the presumption that your purchase offer includes or does not include this cost.

When it comes to paying a franchise transfer fee, it is not uncommon to encounter sellers who insist that it be paid by the buyer and further insist that the buyer *not* consider this expense as part of his or her cost to acquire the business. This is nonsense. Of course the transfer fee is part of your acquisition cost and should be considered in any valuation opinion and return on investment calculations developed for your purchase offer.

In the final analysis, it is really academic whether it is the seller or purchaser who pays any transfer or assignment fees. The matter should be addressed by making a dollar-for-dollar adjustment in the purchase price up or down depending upon which party actually makes the payment. From an economic impact point of view, it will generally be the seller who bears the true burden of this cost without regard to which party makes the payment.

Suggested contract wording:

| |
|--|
| [] includes; [] does not include other current assets valued and described as: |
|--|

Comment:

Most businesses have one or more pre-paid expenses on their balance sheet as well as deposits paid to vendors for such things as vendor owned product transport and storage containers maintained on the seller's premises. As with the lease deposit, it is most convenient to simply include these assets as part of the bundle of assets being acquired whenever possible.

In some cases, it will not be possible to sell a pre-paid expense or deposit. It is a good idea to obtain a clear understanding which of these assets can and cannot be transferred from seller to buyer before developing and tendering a purchase offer.

Once that determination has been made, then the purchase offer should directly address which of these assets will be and will not be included in the purchase price.

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Suggested contract wording:

SELLER shall; shall not deliver to PURCHASER the operating cash on premises in SELLER'S cash register(s) and/or office safe at close of escrow in the amount of \$_____. The purchase price shall; shall not be increased by said amount of operating cash. If SELLER is to deliver said operating cash to PURCHASER, then a physical count of the cash on hand shall be made by buyer and seller together designee of seller; designee of buyer; designee of buyer and seller; Other:

Describe _____
immediately prior to close of escrow. The cost of counting the operating cash shall be paid by Seller; Buyer; Buyer and Seller and apportioned _____% to Seller and _____% to Buyer.

Comment:

As a matter of logistical convenience, a business's operating cash should be acquired by the buyer. It makes little sense that on the day escrow closes and physical possession of the business changes hands that seller and buyer stand in separate lines at the bank, one converting coins and small bills into a deposit and the other buying an equal amount of the exact same thing.

Here again, you should develop your valuation opinion of the business based on the presumption that your purchase price includes or does not include this asset.

Suggested contract wording:

This purchase price shall not include seller's cash held in any bank accounts nor shall it include any seller near-cash assets such as (but not limited to) marketable securities, Certificates of Deposit, bonds, notes receivable, etc., with the exception of the following which shall be included for the purchase price stated herein:

Comment:

This wording is for the seller's protection. A buyer would be hard pressed to lay claim to such assets as part of the purchase price if not specifically identified in the offer—especially one where the price did not reasonably reflect the value of those assets. Nevertheless, for everyone's peace of mind, it is probably best to include this clause so that there are no misunderstandings later on.

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Suggested contract wording:

The above stated purchase price shall be paid:

100% in cash at close of escrow As modified by Section 20-B below

\$_____ Down payment (which shall include all sums deposited in escrow prior to closing

plus all amounts to be paid subject to Section 20-B below, plus:

PURCHASER shall execute a Promissory Note to the benefit of the SELLER in the amount of \$_____ to be paid in monthly; quarterly

other _____ installments bearing interest of _____% per year for _____ years plus _____[months _____quarters _____

Said payments, including principal and interest shall be \$_____. Additional terms and conditions of this Promissory Note shall be:

Commencement of the note payments shall be _____ and all subsequent payments shall be due on the _____ day each month; quarter;

other (describe) _____ thereafter.

all assets purchased shall be pledged as security for payment of the note

Purchaser shall personally guarantee payments in addition to pledging the assets to be purchased.

Said note shall carry a late charge of \$_____ if payment is not received within _____ days of the due date.

Said note shall; shall not be due on sale of business by PURCHASER.

A default on payment of the premises lease shall constitute a default on the Promissory Note

SELLER herewith agrees to allow PURCHASER to assign the note to a subsequent purchaser under the following terms and conditions:

Other (describe)

Comment:

There is a saying among business brokers that “the seller sets the price and the buyer sets the terms.” The fact is, approximately 75% of all privately owned business sold include seller financing.

This is so for five reasons.

1. As is the case with the purchase of any high-ticket item, few buyers have the wherewithal to pay the full price up-front.
2. One of a buyer’s principal objectives is to obtain the highest possible return on his or her down payment (return on investment)—i.e., the business’s cash flow divided by the down payment. Thus, the more a seller is willing to carry-back in a note, the more attractive that investment will appear to a buyer compared to alternatives.

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3. Most buyers want to “leverage” their existing cash with seller financing and will seek those opportunities where this is possible. If a buyer has, say, \$100,000 in cash and has the option of paying all cash for one business worth \$100,000 or buying a larger business worth \$200,000 by putting \$100,000 down and financing \$100,000, 99.9% of all buyers will buy the larger business.
4. Buyers want some assurance that the seller is not dumping a loser. Generally, the seller’s willingness to carry back a significant portion of the purchase price is taken as an indication that the seller believes the business is viable.
5. Seller carry-back financing is the principal tactic employed to close the gap between a seller’s “ask” and a buyer’s “bid” price.

This last attribute of seller financing is based on a principal of finance which holds that the “face value” of a sum of money to be paid in the future has a lower “intrinsic value”—known as “present value” today.

For example, if you and I agree that your wrist watch is worth \$100 and I agree to buy it, would it make any difference to you if I take the watch now and agree to give you the \$100 now or one year from now? Of course, you want the \$100 now. But how much *more* than \$100 would you want for your watch if I take it now but will not pay until next year? In theory, there is some price at which you will opt to wait a year to collect. How much more is a question of your perceived risk that I will be available, willing and able to pay you at that time. Would you agree on a price of \$150? How about \$1,000? Generally speaking, there should be some amount greater than \$100 you will accept next year that will be equivalent to, i.e., have a “present value,” of \$100—and we will make a deal and I will get your watch today.

Likewise, in the sale of a business, the gap between the seller’s asking price and the most a buyer is willing to pay may be closed if the seller agrees to “carry back” some portion of the purchase price. This does not mean that every gap can be closed. There are some very sticky issues regarding the seller’s perceived risk that the buyer will be available, willing and able to make the future payments and there is the buyer’s concern that the business’s future cash flow will be sufficient to make those payments. However, in theory, *any* gap can be rendered rational from a buyer’s perspective by appropriately adjusting the seller’s carry-back terms of down payment, the number of years over which the balance due will be paid and the interest rate the seller charges for “carrying the paper.”

As a practical matter, a gap between ask and bid for a business of more than around 25% probably cannot be closed with seller financing. For example, consider a business who’s fair market value in an all-cash-at-close-of-escrow deal is \$197,000. Suppose, instead, the seller would not take less than \$240,000 but would “carry paper.” What terms would render a buyer indifferent between \$197,000 all-cash-at-closing and \$240,000? After making some assumptions about the business, my calculations reveal a “rational” buyer would effectively be giving the seller equal value for his business by paying \$240,000 with seller carry-back terms of 50% down and the balance of \$120,000 payable over five years with 10% interest. What if the seller would not take less than \$1,000,000? For this price, my calculations reveal *in theory* a buyer would effectively be giving the seller equal value with terms of 2% down and the balance of \$980,000 payable over 30 years at 5% interest.

Since each business is unique, so must be the terms of sale. But unlike any other transaction, there are literally an infinite number of cash-and-terms solutions buyers and sellers can explore in the quest to find a solution suitable to each.

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The method by which alternative cash-versus-terms purchase solutions can be developed which will yield an all-cash-at-close-of-escrow equivalent is the mathematics of finance. Although mathematics is a precise science, the assumptions which must be made about the business, the business's future prospects and the buyer included in the analysis makes the whole project one of roughly estimating a cash-and-terms combination equal to an all-cash value. Nevertheless, it is possible to quite accurately calculate these equivalencies for one schooled in finance. Just as a buyer is wise to seek professional counsel in determining what a business is worth, so too should the buyer seek help in properly developing a cash-and-terms combination purchase offer.

In addition to the economic issues relating to the tradeoff between cash and terms in a purchase transaction, there are some sticky "administrative" matters concerning the terms of the Promissory Note that must be addressed as well. The first is the nearly universal demand by the seller that the buyer personally guarantee the note. Some buyers are reluctant to make a personal guarantee and in many instances, a refusal to do so will be a deal killer.

As a practical matter, few buyers would object to making a personal guarantee for a home loan, a car loan or for that matter, even a loan to buy a business when it is made by a bank. Yet, because the lender is not a bank, this seems somehow to make a difference. Well, it should and it should not. To the degree that a seller's carry-back loan reflects the financing of hard assets, it is difficult to justify not guaranteeing the loan. However, to the extent the carry-back note is for the purchase of goodwill, a plausible argument can be made by a buyer that a portion of the purchase price should not be personally guaranteed.

Assuming a seller will concede that point, (which quite often they will not) then it is a simple matter of creating two separate notes; one for the tangible assets which is personally guaranteed and one for the goodwill which is not. Additionally, there may be other areas of disagreement about the terms and conditions of a seller carry-back loan where the best form of compromise is to develop separate notes for portions of the total carry back amount with each reflecting different terms.

One other term that can be a sticking point is the buyer's ability to later assign the seller's carry-back loan to a subsequent buyer. This is an important concession for a buyer to try to obtain. If a seller's carry-back note is due on sale, and the buyer decides to later sell the business, the buyer *must* obtain at least the balance due on that note in cash up-front by the new buyer. If the remaining balance is more than the down payment a subsequent buyer is willing to offer, the business is essentially unmarketable. But here again, a compromise solution may be to draft two separate notes; one assignable and one not assignable.

One final comment on seller carry back notes. The buyer should resist the inclusion of a balloon payment in a carry-back note at all costs. In most cases, a seller's insistence on this provision should be a deal killer. The fact of the matter is that in most cases it will be impossible to find a third party who will refinance the remaining balance on a seller carry-back note when the balloon payment comes due. The only source of refinancing will be the seller—and it is *highly* problematic whether or not the seller will be inclined to do that.

As a case in point, I am aware of a transaction where the buyers agreed to a seller carry-back note with just such a balloon payment. After buying the distressed business, reinvesting thousands of dollars to repair broken-down equipment and reinvigorating the business, the seller realized the buyers had created substantially more value in the business than the price the buyers paid. When the balloon payment came due, the seller reneged on an original verbal promise to refinance and instead initiated foreclosure proceedings on the buyers who could not raise the money for the balloon payment. As it happened, the seller

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found another buyer who was ready, willing and able to purchase the business from the seller for a higher price than the current owners paid as soon as he got it back.

Suggested contract wording:

PURCHASER shall assume debts and other liabilities of the SELLER with an aggregate value of \$_____ and shall pay same when due unless otherwise indicated herein. Said liabilities are herewith itemized below as:

the following liabilities, accounts payable, debts, customer deposits, prepaid accounts, wages payable, vacation pay payable, commissions payable and subscriptions and promissory notes payable which represent unsecured SELLER liabilities:

Promissory Notes Payable secured by assets subject to liens as reflected on form UCC1 on file with the Secretary of State provided the lien holders shall agree to such action. In the event the lien holders shall not agree to such action or will do so only upon terms or conditions unacceptable to either PURCHASER or SELLER then all rights and obligations herein may, at the election of the SELLER or the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER. Said Promissory Notes to be assumed by buyer are herewith described as:

Comment:

Generally, all the business's debts are excluded from most small business transactions and are paid off by the seller at the close of escrow. However, occasionally there are business liabilities that, by their nature, cannot be paid off by the seller and therefore *must* be assumed by the buyer. Additionally, it may be to a buyer's advantage to assume responsibility to pay off certain seller debts as a condition of sale.

For example, a seller may have collected advance payments for work in progress contracted by a customer. It would be extremely awkward for the seller to give that customer his money back for the as yet uncompleted portion of the work and simultaneously be approached by the buyer to collect an equal amount from him on the day escrow closes so that the job can be completed. It would be best in this instance for the buyer to simply assume this liability. Or, perhaps the business being sold is a periodical publication where it's subscribers have paid in advance for a year or more of future issues. In this case it would be totally impractical for the seller to send all subscribers a refund for pre-paid but yet undelivered future issues and at the same time the buyer request all subscribers to simultaneously re-subscribe and send the refunded money back. Clearly in this case, the best solution is for the buyer to assume the financial responsibility to deliver all future issues of paid up subscriptions and make an appropriate adjustment in the purchase price for doing so.

Another debt which may be owed by a company that often will not appear on the balance sheet are obligations to pay employees some amount beyond current wages. Topping this list is Vacation-Pay Payable. A buyer needs to find out what kind of commitment a company has made to its employees for paid vacations and determine how much accrued vacation pay, if any, is owed at the time the offer is made and at close of escrow. Armed with this information a buyer can either require the seller to pay that money to the company's employees as a condition of closing or assume that debt.

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How the purchase price will be affected by these various situations will be addressed a little later. A more immediate concern is a buyer's ability to identify exactly how much of such seller liabilities exist. This is so because it is fairly common for owners of small businesses not to record customer pre-paid expenses, vacation pay and commissions payable on their books. It is up to the buyer to ask the right questions to determine if such liabilities exist and if so, then reconstruct the seller's balance sheet and income statement so that they are properly accounted for.

Another instance where it may be advantageous for the buyer to assume certain seller debts is when the business being purchased is distressed. For example, a seller may be months behind in paying various vendors for goods and services purchased by the business. There can be no question but that these vendors are very concerned that the business is about to go bankrupt and they will not get paid. In this case a buyer can approach the vendors directly and offer to pay them some amount less than the seller owes as payment in full as a condition of buying the business. The buyer then applies the entire debt owed by the seller as a credit against the total purchase price but assumes some amount less than that as additional debt. The difference is a reduction in the actual purchase price and the vendors in many cases will be elated that there is now hope they are going to get some money after all.

Assuming seller debt which has been secured by some or all of the tangible assets of the business is more difficult to accomplish. Typically such debts will be for large pieces of machinery or company owned vehicles which were purchased with funds loaned by a bank. In all such cases the lender will have filed a UCC-1² security lien against the equipment purchased with the Secretary of State. And just as certainly, the loan agreement will have a "due on sale" requirement, meaning the loan must be paid off in full if the owner sells the business. Seldom will banks agree to let a buyer assume these debts. This means that if the amount of up-front cash the buyer is willing to give the seller is insufficient to pay off the business's secured loans and thus allow the buyer to acquire a clear and marketable title to those assets, the transaction probably cannot be consummated. That is unless the buyer is willing to accept the risk of acquiring assets in which a third party holds a security interest and a note with a "due on sale" clause. To do so means that if the seller fails to pay off the loan after the buyer has acquired the business, or if the lender finds out the business was sold, the lender can seize and sell the secured assets without regard to how much the buyer paid the seller for them.

As a word of caution, not every seller will be altogether forthcoming about the existence of liens on the business's tangible assets. It is important for a buyer to make an independent determination of whether such liens exist or not. Fortunately, this is a fairly straight forward proposition. By filing a form UCC-3³ with the Secretary of State and paying a small fee—generally around \$20—the existence of any liens can be discovered. It is advisable to conduct a title search in the "official" name of the business such as "Johnson Enterprises, Incorporated" plus any trade name the company goes by such as Joe's Bar and Grill plus the name of the owner—in this example, Joe Johnson. A separate UCC-3 will need to be filed for each name along with the required fee. You will also need to know the business's Federal ID number and the owner's Social Security number to properly complete the UCC-3 title search request form.

² Uniform Commercial Code Form #1

³ Uniform Commercial Code Form #3

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Suggested contract wording:

Not less than 10 days prior to close of escrow:

Escrow Officer

Purchaser

shall notify all creditors by certified mail of the intended sale of the business and advise said creditors of SELLER'S intention to pay off all secured and unsecured liabilities, accounts payable, debts, customer deposits, prepaid accounts and subscriptions and promissory notes payable not assumed by PURCHASER and invite said creditors to submit claims for payment in full into escrow. The escrow officer is herewith instructed to hold back an amount of money sufficient to pay all such debts and to make said payment to said creditors for all undisputed debts of the seller from the escrow account. The escrow officer is herewith instructed to hold back an amount of money necessary to pay off all disputed liabilities of the seller until said dispute is resolved and only upon resolution of said dispute in accordance with applicable law shall the escrow officer pay off said liabilities and turn over any remaining cash to seller.

Comment:

Every state except Nevada has enacted a bulk sales law with a provision which is intended to protect the interests of a business's creditors when a business is sold. The specific wording of this law varies from state to state but the general intent is fairly consistent. That being to ensure that a business's creditors will be paid what they are owed by the seller once the business changes hands. The bulk sales law makes it the responsibility of the business *buyer* to notify the seller's creditors of the impending change of ownership and to advise those creditors to submit a claim for payment into escrow. By operation of the bulk sales law, a failure of the buyer to make this notification to the seller's creditors legally shifts the responsibility to pay those debts onto the buyer after escrow closes. Generally, this notification process is completed by the escrow officer as part of the service provided. However, it is a good idea for the buyer to ensure the escrow officer is going to do this.

For example, in Nevada, there is no requirement that a seller's creditors be notified of an impending sale. Neither is there a "flow through" law which shifts creditor liabilities to the buyer (with a couple of exceptions to be discussed next). However, a buyer should be sensitive to a seller's intention to pay his or her creditors off upon sale of the business because those creditors, most of the time, will be the same vendors the buyer intends to use also. Should these vendors not be paid in full by the seller, there is every possibility some vendor hostility from this failure will be projected onto the buyer which is not something a buyer needs at any time but especially right after taking over the business.

Therefore, it is necessary for a business buyer to be aware of how much money the seller owes to all of the business's creditors and what that seller's intentions are insofar as paying off his or her creditors at close of escrow. As part of this process, it is also important for the buyer to ensure that enough cash will be available at close of escrow to enable the seller to pay off all the company's debts.

In some transactions there will not be enough cash available to the seller at close of escrow to pay off all the debts of the business. If the buyer is not willing to assume those debts as part of the transaction, then the buyer should only proceed under advice of legal counsel.

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If an individual buying a business in Nevada wishes to make Section 10 a condition of sale, that is the buyer's prerogative. However, since it is not a legal requirement, the seller may find it objectionable. Also, making this section a condition of sale will almost certainly generate an additional escrow service fee. If a buyer does not wish to make this action a part of the business transaction, then Section 10 should be lined out.

The foregoing notwithstanding, in every state, including Nevada, there *is* legally mandated "flow through" liability from seller to buyer for any employment wage tax and/or sales tax liability the seller fails to pay. A buyer's ability to ensure the seller will bring the business current with these government agencies is accomplished by requiring the seller to submit into escrow a "Clearance Letter" from the State Department of Taxation and State Department of Labor. Provision for this requirement is included later in this contract.

Suggested contract wording:

The above defined liabilities and debts to be assumed by Purchaser shall be:

Calculated as a deduction from the actual cash and promissory notes and the earn-out agreement to be deposited into escrow by Purchaser for benefit of Seller such that said cash, notes and earn-outs *plus* all liabilities and debts to be assumed by PURCHASER described herein shall equal the purchase price.

or

An addition to the purchase price such that the Actual Deemed Sale Price shall be the sum of the purchase price *plus* all assumed liabilities and debts described herein.

Comment:

It is really academic whether the top-line purchase price includes or excludes the value of debts the buyer intends to assume. The amount the buyer pays for the business will be the same either way. The purpose of this portion of the Purchase Offer is for clarification so that there will be no misunderstanding on the seller's part regarding the buyer's intention.

As a practical matter, it's probably best to make a purchase offer on the basis of the first option listed above. This is so because most business owners think of the value of their business in terms of the asset side of the balance sheet and not their net equity in the business. For example, suppose you intend to purchase a business where all of the assets such as inventory, operating equipment and seller's goodwill are altogether worth, say, \$300,000. This is more than likely how the seller views the value of his business and how it is being marketed. But further suppose that the seller has debts against the business of \$299,999 which you, as the buyer, propose to assume as a condition of the sale. Under the first option, your purchase offer would be \$300,000 whereas under the second option, it would be \$1.00.

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Suggested contract wording:

In the event the debts and other liabilities PURCHASER agrees to assume as a condition of this sale differ at Close of Escrow from the amounts stated above, then the down payment and/or the amount of the promissory note shall be adjusted to reflect said difference(s) as follows:

The down payment shall be increased or decreased as the case may be by an amount not to exceed \$_____.

The promissory note shall be increased or decreased as the case may be by an amount not to exceed \$_____.

In the event any required adjustment in the amount of the down payment and/or face value of the promissory note must exceed the limits specified herein in order to offset changes in the levels of debt PURCHASER has agreed to assume in order to equate the sum of said cash, face value of promissory notes and assumed debt to the purchase price, then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

Comment:

The amounts of the seller's various liabilities at close of escrow will almost certainly be different from the amounts which exist at the time the purchase offer is made. This section of the purchase offer is intended to provide the mechanism by which to make the appropriate adjustment at close of escrow.

In most cases, the differences will not be substantial, however, there is always the possibility that they will be. For this reason, the "not to exceed" provision is included to protect the buyer from the danger of suddenly having to come up with significantly more cash at close of escrow than was intended or perhaps is even possible.

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Suggested contract wording:

[] This purchase offer is contingent upon PURCHASER obtaining third party financing in the amount of \$_____. PURCHASER shall provide SELLER with a copy of a commitment letter or other substantive proof of a third party financing commitment within _____ days. In the event PURCHASER is unable to obtain a financing commitment including terms and conditions acceptable to PURCHASER within said time period and advises SELLER of same, then all rights and obligations herein may, at the election of the SELLER or the PURCHASER, terminate and the deposit shall be returned to the PURCHASER **or** SELLER may extend said deadline for any time period acceptable to SELLER provided PURCHASER increases the security deposit by \$_____ and further provided that said amount plus all amounts previously deposited in escrow shall be retained by the SELLER subject to the terms and conditions defined herein.

[] This purchase offer is contingent upon PURCHASER assuming SELLER'S existing loan(s) with _____ (name of lender) _____ in the aggregate amount of \$_____. In the event PURCHASER is unable to demonstrate an ability to assume said loan(s) by way of a commitment letter or other substantive proof of such ability provided by said lender within _____ days of this offer then all rights and obligations herein may, at the election of the SELLER or the PURCHASER, terminate and the deposit shall be returned to the PURCHASER **or** SELLER may extend said deadline for any time period acceptable to SELLER provided PURCHASER increases the security deposit by \$_____ and further provided that said amount plus all amounts previously deposited in escrow shall be retained by the SELLER subject to the terms and conditions defined herein.

Comment:

Probably the only source of bank financing for the purchase of a small business are Small Business Administration guaranteed loans (or taking out a second mortgage on your home). The loan will be either an SBA 7(a) loan or an SBA 504 loan. Obtaining an SBA loan to buy a business or assuming a seller's existing SBA loan can often be a tedious, cumbersome and time consuming process. Having said that, this obstacle is as much attributable to the lack of adequate preparation on the buyer's part when first seeking such a loan as it is to the bureaucracy of the bank and the SBA.

Therefore, if you are considering this financing avenue, it is wise to anticipate these obstacles. The first thing to do, if you are seeking a new loan, is to establish a rapport with an SBA loan officer at a local bank—and do this well in advance of making a formal purchase offer. If you propose to assume the seller's existing loan, one of the first things you should do is meet with a representative from the seller's bank to begin the loan assumption process.

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The information a bank will probably require in order to assess the merits of making a business acquisition loan or agreeing to allow you to assume an existing loan will be three to five years of federal income tax returns for the subject business, your personal income tax returns, an appraisal of your home and the current balance due on the mortgage. If your contemplated business acquisition will also include the real estate, you will need an appraisal of that property as well.

In addition to this information, it will be helpful to provide the lender with three to five years of professionally “recast” or adjusted year-end financial statements of the business along with a brief description of the business including its history, its customers, and all factors that impart a “going concern” value to it. If the business is being marketed by a professional business broker, these recast financial statements (which are intended to reflect the “real” financial performance of the business) along with all this additional information should have already been prepared and available to you.

In short, it is wise to be well along the way in negotiating a SBA loan for an acquisition and be fairly confident of being able to get the loan before making a formal purchase offer contingent on getting the financing.

A final word of caution is in order regarding SBA business acquisition loans. A buyer should *never* presume that loan approval means the agreed upon purchase price for the business is reasonable! It is a curious convention of the banking industry that they always require an appraisal of real estate as a condition of making a real estate purchase loan but never require an appraisal of a business as a condition of making an SBA guaranteed small business acquisition loan. The primary concern, and with some SBA lenders the *only* concern, is whether the buyer will have sufficient cash flow to service the debt and whether the buyer’s acquired assets and other personal assets such as equity in a home are sufficient to make the lender whole if they must take them in the event of a default.

Deal Structure Summary

The point of departure in structuring a purchase offer is a determination of the business's value. If the business owner had the business appraised by a professional business appraiser, the value conclusion would likely be the business's "fair market value." That would be the most likely price, or the highest price a willing *hypothetical* buyer (one who represents a consensus of opinion of all potential buyers) would pay and a willing, reasonable seller would accept *in cash* at close of escrow in an arm's length transaction where both buyer and seller are knowledgeable of all relevant facts and circumstances of the business, neither buyer or seller are under a compulsion to act and the business has been actively marketed in a freely and widely accessible market place for a reasonable period of time. That's a mouth full, but it is necessary to adequately qualify the term "fair market value."

For any professionally developed business appraisal, it is essential that the analysis be done on the basis of a precise definition of "value." In the case of a specific buyer, in this case, you, the type of value conclusion a professional appraiser would develop on your behalf would be "investment value." That may be more or less than the business's "fair market value." Having made this distinction, it is unlikely a knowledgeable business seller would agree to sell the business to you for less than its fair market value. On the other hand, it is highly unlikely the value of the business from your unique perspective will be substantially greater than its fair market value. There are exceptions to this statement but for the most part apply to a "strategic buyer" who, for some reason unique to that buyer can see a way to extract significantly more earnings from the business than could a buyer who would conduct the business in its historical fashion and may therefore be willing to pay the seller more for that opportunity.

Thus, without regard to the "investment value" of the business from your perspective, it is a good idea to determine the business's "fair market value" first and then tweak that value conclusion to reflect your unique needs and perceptions to arrive at what the business is worth to you. By using this approach you are less likely to arrive at a value conclusion that is way out of line—which does happen. As indicated previously, stories abound of buyers who have paid more than twice a business's most likely fair market value. These buyers did not pay these exorbitant prices because of a unique strategic opportunity; they paid them out of ignorance.

Assuming that a professional appraiser has developed an objective opinion of the business's value, that opinion will be expressed in one of two ways. It will either be a value opinion of *all* the business's assets including cash in the bank, marketable securities, if any, owned by the business, lease deposit, inventory, accounts receivable, machinery and equipment, goodwill and so forth or it will be the business's net equity value. The first form of opinion is known as the Market Value of Invested Capital and the second is referred to as the Owner's Net Equity Value.

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It is very straight forward to convert one value opinion into the other. Net Equity Value is simply the Market Value of Invested Capital minus all the company's debts. Or, Market Value of Invested Capital is Net Equity Value plus all the company's debts.

The purpose of this summary up to this point has been preparatory for its principal purpose. That is to enable you to properly conceptualize how to structure a purchase offer. At this point we will assume you now have a properly developed statement of the business's "investment value." However, let's assume you do not intend to buy all of the business's assets, nor do you intend to assume all of the company's debts. If this were the case, your purchase offer would be the Owner's Net Equity Value.

Instead, you intend to purchase some of the company's assets and assume some of its debts. To illustrate how to formulate your purchase offer, we will use the following example of Superior Metal Products.

In this example, we can see that the Owner's Net Equity Value is \$200,000. This represents how much the owner will take to the bank at close of escrow (excluding transaction fees, if any). This will be seller's net cash-in-his-pocket upon sale. Assume for this exercise that this has been agreed between seller and buyer and is no longer open for negotiation. At this point, the objective is to develop a deal structure suitable to the buyer and seller which will net the seller \$200,000. Amazingly, in the rather simple illustration below there are 144 different possible deal structure combinations that will net the seller the same \$200,000. Many would be illogical, but there are perhaps two dozen plausible possibilities.

The first step in this process is to develop an "economic balance sheet" for the company.

All the nuances of how to do this are beyond the scope of this book but a simple illustration is offered below. Briefly, it is a matter of transforming the financial balance sheet which is a "historical cost" based financial record into what one could call a "true value" record. Generally, the line items most affected by this transformation are the fixed assets of the company. That is to say, without regard to what all the furniture, fixtures, machinery and other operating equipment originally cost the business seller and without regard to their current depreciated "book" value, they all have a current fair market value and that is the value that should appear on the "economic balance sheet." Additionally, the "goodwill" value of a company will not appear at all on the historical cost balance sheet, but will appear on the economic balance sheet.

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The following is an illustration of this transformation process for Superior Metal Products:

| Superior Metal Products | | |
|--|-----------------------|------------------|
| Historical Cost Balance Sheet Recast Into an Economic Balance Sheet as of 12/31/XX | | |
| Assets | Historical Cost Basis | True Value Basis |
| <u>Current Assets</u> | | |
| Petty Cash Fund | \$100 | \$100 |
| Cash In Banks | \$35,000 | \$35,000 |
| Accounts Receivable | \$75,000 | \$75,000 |
| Inventory | \$13,000 | \$13,000 |
| Work In Progress | \$7,000 | \$7,000 |
| Lease Deposit | \$3,000 | \$3,000 |
| <u>Total Current Assets</u> | <u>\$133,100</u> | <u>\$133,100</u> |
| <u>Fixed Assets</u> | | |
| Office Equipment | \$28,000 | \$9,000 |
| Machinery | \$237,000 | \$125,000 |
| Accumulated Depreciation | <\$175,000> | \$0 |
| Goodwill | \$0 | \$32,900 |
| <u>Total Fixed Assets</u> | <u>\$90,000</u> | <u>\$166,900</u> |
| Total Assets | \$223,100 | \$300,000 |
| | | |
| <u>Liabilities</u> | | |
| <u>Current Liabilities</u> | | |
| Accounts Payable | \$15,000 | \$15,000 |
| Wages Payable | \$7,000 | \$7,000 |
| Current Portion LT Debt | \$10,000 | \$10,000 |
| <u>Total Current Liabilities</u> | <u>\$32,000</u> | <u>\$32,000</u> |
| <u>Long Term Liabilities</u> | | |
| LT Debt (less current portion) | \$68,000 | \$68,000 |
| <u>Total Long Term Liabilities</u> | <u>\$68,000</u> | <u>\$68,000</u> |
| Total Liabilities | \$100,000 | \$100,000 |
| Owner's Net Equity | \$123,100 | \$200,000 |

Once the assets and liabilities have been recast into an “economic balance sheet,” the process of determining the purchase offer is simply one of the buyer adding up all the assets that will be purchased and from that total, subtracting all the liabilities which will be assumed. The following examples illustrate how this is done.

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Superior Metal Products Reconstructed (“True Value”) Economic Balance Sheet as of 12/31/XX

| Assets | True Value Pre-Sale | Deal Structure | |
|---|-------------------------|----------------------|------------------------|
| | | Buyer Buys | Seller Keeps |
| <u>Current Assets</u> | | | |
| Petty Cash Fund | \$100 | \$100 | |
| Cash In Banks | \$35,000 | | \$35,000 |
| Accounts Receivable | \$75,000 | | \$75,000 |
| Inventory | \$13,000 | \$13,000 | |
| Work In Progress | \$7,000 | \$7,000 | |
| Lease Deposit | \$3,000 | \$3,000 | |
| Total Current Assets | \$133,100 | \$23,100 | \$110,000 |
| <u>Fixed Assets</u> | | | |
| Office Equipment | \$9,000 | \$9,000 | |
| Machinery | \$125,000 | \$125,000 | |
| Goodwill | \$32,900 | \$32,900 | |
| Total Fixed Assets | \$166,900 | \$166,900 | \$0 |
| <small>All fixed assets are restated at Fair Market Value instead of Book Value</small> | | | |
| Total Assets | \$300,000 | \$190,000 | \$110,000 |
| | | | |
| <u>Liabilities</u> | | <u>Buyer Assumes</u> | <u>Seller Pays Off</u> |
| <u>Current Liabilities</u> | | | |
| Accounts Payable | \$15,000 | | \$15,000 |
| Wages Payable | \$7,000 | \$7,000 | |
| Current Portion LT Debt | \$10,000 | | \$10,000 |
| Total Current Liabilities | \$32,000 | | |
| | | | |
| <u>Long Term Liabilities</u> | | | |
| LT Debt (less current portion) | \$68,000 | | \$68,000 |
| Total Long Term Liabilities | \$68,000 | | |
| Total Liabilities | \$100,000 | \$7,000 | \$93,000 |
| Owner’s Net Equity | <u>\$200,000</u> | | |

In the foregoing illustration, the buyer proposes to buy \$190,000 of the company’s assets and assume \$7,000 of it’s debts. Thus the purchase offer will be either \$190,000 or \$183,000 depending on whether the tendered top-line purchase price includes or excludes assumed debt. To double check the accuracy of this analysis, just add up what the seller will net to see if it is \$200,000. In this case, the seller will get \$183,000 from the buyer, plus the seller will keep the company’s \$35,000 cash in the bank as well as the accounts receivable of \$75,000. That adds up to \$293,000. Out of that sum, the seller must pay off the company’s accounts payable of \$15,000 and it’s long term debt of \$78,000. This

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leaves the seller \$200,000. Just to make sure this process will work every time, let's look at a different deal structure:

| Superior Metal Products Reconstructed ("True Value") Economic Balance Sheet as of 12/31/XX | | | |
|---|------------------------|------------------|------------------|
| Assets | True Value Pre-Sale | Deal Structure | |
| | | Buyer Buys | Seller Keeps |
| <u>Current Assets</u> | | | |
| Petty Cash Fund | \$100 | \$100 | |
| Cash In Banks | \$35,000 | | \$35,000 |
| Accounts Receivable | \$75,000 | \$75,000 | |
| Inventory | \$13,000 | \$13,000 | |
| Work In Progress | \$7,000 | \$7,000 | |
| Lease Deposit | \$3,000 | | \$3,000 |
| <u>Total Current Assets</u> | <u>\$133,100</u> | <u>\$95,100</u> | <u>\$38,000</u> |
| <u>Fixed Assets</u> | | | |
| Office Equipment | \$9,000 | \$9,000 | |
| Machinery | \$125,000 | \$125,000 | |
| Goodwill | \$32,900 | \$32,900 | |
| <u>Total Fixed Assets</u> | <u>\$166,900</u> | <u>\$166,900</u> | <u>\$0</u> |
| All fixed assets are restated at Fair Market Value instead of Book Value | | | |
| <u>Total Assets</u> | <u>\$300,000</u> | <u>\$262,000</u> | <u>\$38,000</u> |
| <u>Liabilities</u> | | | |
| | | Buyer Assumes | Seller Pays Off |
| <u>Current Liabilities</u> | | | |
| Accounts Payable | \$15,000 | | \$15,000 |
| Wages Payable | \$7,000 | | \$7,000 |
| Current Portion LT Debt | \$10,000 | | \$10,000 |
| <u>Total Current Liabilities</u> | <u>\$32,000</u> | | |
| <u>Long Term Liabilities</u> | | | |
| LT Debt (less current portion) | \$68,000 | | \$68,000 |
| <u>Total Long Term Liabilities</u> | <u>\$68,000</u> | | |
| <u>Total Liabilities</u> | <u>\$100,000</u> | <u>\$0</u> | <u>\$100,000</u> |
| <u>Owner's Net Equity</u> | <u>\$200,000</u> | | |

In this case, the buyer purchases \$95,100 in current assets and \$166,900 in fixed assets for a total of \$262,000. Since the buyer is not proposing to assume any of the seller's debt, the purchase offer is \$262,000. In this case, the seller gets \$262,000 from the buyer and keeps \$38,000 in current assets for a total of \$300,000. From this the seller must pay off all of the company's liabilities of \$100,000 leaving him with a net of \$200,000.

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As should now be evident, once the fair market value of the business's assets (not book value!) and its liabilities are laid out in this format, it becomes a fairly straight forward exercise to put together different deal structure scenarios in a way that will hold the originally negotiated seller's net constant.

Another thing that can now be made clear is that despite price negotiations in terms of all or most of the seller's assets, the only thing that is really being negotiated, in the final analysis, is the *goodwill value* of the business. If you think about it, that is the only "wild card" in the deck when you stack things up as has been done above. All other components of the purchase price are more or less established facts going into negotiations and really don't need to be negotiated at all!

Having made this point, it is critically important to understand that the "goodwill" portion of value in a business is determined by that business's earnings. To reiterate a point made early on, an ability to make this determination is the principal skill of business appraisers and requires a substantial amount of specialized education and appraisal experience. Additionally, when a business's value is separated into its component parts as has been done above, it is *very* common to encounter businesses where the goodwill component is *negative*! This is to say the "going-concern" value of a business is *less* than the value of its tangible assets—and in many cases less than the liquidation value.

Of course, this raises the question of why a seller would sell his or her business for less than the liquidation value of its tangible assets. The answer is the seller probably wouldn't do that except in special situations such as an inability to get out from under a lease. From the seller's point of view, the wiser way to go would be to shut the business down and sell off the assets. The fact of the matter is such a business is worth more dead than alive. And, a business need not be losing money before it falls into this predicament. This change of circumstance will always occur before earnings turn negative.

The earlier statement that the only "wild card" in the deck when assets and liabilities are stacked up according to the examples above is ever so slightly off the mark. Another card in the deck that has a little bit of "wildness" in it is the estimated fair market value of the fixed assets (e.g., office equipment, furniture, fixtures, machinery and other equipment). The fair market value of these assets is generally defined for business appraisal purposes as the "cost to replace those assets with identical assets of the same age and in the same condition, including delivery and installation." This value can be determined with fair precision by an equipment appraiser but in most business transactions (and many appraisals as well) this is not done.

The reason it is not essential to make a precise determination of the fair market value of the fixed assets is that there is a trade-off between their value and the goodwill value of the company. That is to say, as one goes up, the other goes down and vice versa. This is because the "going concern" value of a company is a function of its *earnings*, not its assets. Thus, if a company's going-concern value is, say, \$200,000 and the value of the assets are estimated at \$150,000 then the company's goodwill value is \$50,000. However, if the estimated value of that company's assets is \$250,000 then the computed goodwill value would be a *negative \$50,000*.

Again, a discussion of business valuation is beyond the scope of this book. The point here is to emphasize that there is little to be gained in purchase price negotiations by arguing over the "real" fair market value of the equipment. Indeed, it is common to encounter business sellers who tend to unrealistically inflate the estimated fair market value of their equipment and buyers who chip away at the seller's representation while neither realizes that the income tax implications of a business transaction are most favorable for the buyer

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when the value of the fixed assets are established at a high level and favor the seller when set at a low level. If buyer and seller really understood how business values are determined and the income tax implications of purchase price allocation, the buyer would strive to *increase* the estimated value of the equipment and the seller would argue for a *lower* value!

Given this fact, it is a wise seller who makes a *conservative* estimate of the fixed assets' fair market value. This will tend to steer the buyer away from contentious arguments for a lower price by pecking away, line by line, at each piece of equipment's estimated value with the expectation that in so doing, the purchase price should be reduced. Likewise, for the buyer, it will be largely a waste of time and effort to direct more than modest attention to the estimated value of the equipment if it is even close to being in the ball park.

The best advice I can offer business buyer's is to not become embroiled in discussions about the value of the fixed assets the seller has presented. In most cases it is wise to just accept them. However, it is vitally important to focus on the "going concern" value of the business. If the seller has outrageously over estimated the value of the fixed assets, then there will be, with absolute mathematical certitude, a significantly lower and quite possibly negative "goodwill" value that will fall out of a valuation analysis when presented in the format of the preceding illustrations.

One last issue that tends to create conceptual complexity in the foregoing analysis is the proper treatment of a business seller's investment in "leasehold improvements." This is a reflection of the money the business seller has invested to fix up a premises which is leased. Typically, this investment will be for the construction of interior partitions, decorative wall coverings, modifications to the building's electrical, plumbing, heating and ventilating systems and so forth. The business seller's balance sheet will reflect the full cost of this investment as well as the total amount of depreciation taken to date.

The question becomes, "what is the 'true value' of those leasehold improvements?" A very compelling argument can be made that they are always *zero*. By operation of law, all tenant improvements to a leased premises become the property of the building owner immediately upon completion. Thus, without regard to how much a business seller has invested in those improvements and without regard to how that investment is reflected on the seller's Historical Cost balance sheet, the fact of the matter is that those improvements do not belong to the seller and therefore they are not something that can be included in the sale.

This concept is difficult for many sellers to grasp and during price negotiations such individuals can become very insistent that they be compensated in part for that investment. Fortunately, this is an easy accommodation for a buyer to make. In every case, *any* allowance for the seller's leasehold improvements a buyer agrees to accede to the seller should be reflected in total as a reduction in the portion of the purchase price allocated to goodwill. The underlying logic of this tactic is identical to the logic applied in the discussion concerning the "real" value of the business's machinery and equipment. That being that it is more or less nothing but an academic exercise to try to estimate the exact value of those assets because the higher they go, the lower becomes the goodwill value which does not stop going down at zero.

From a seller's point of view it is actually best to mentally "write off" the investment in leasehold improvements and construct a "true value" balance sheet with no value allocated to them. This is so because it then becomes much easier for the seller to make an informed determination of whether the business is worth more dead than alive and therefore whether he or she should accept the purchase offer or have a going-out-of-business liquidation sale.

ADDITIONAL TERMS AND CONDITIONS

Suggested contract wording:

1. DEPOSIT INCREASE.

If this offer is accepted, the deposit shall be increased to \$ _____ no later than _____ in the form of _____

Comment:

This is more or less a customary procedure in the purchase of a business but there is no law that says a buyer must increase the deposit. This may be a requirement of the seller if the initial deposit was only a token amount. However, as will be evident later, a seller may not be overly enthusiastic about making the buyer's deposit inordinately high.

Suggested contract wording:

2. WITHHOLD FROM MARKET

SELLER herewith represents and warrants that SELLER is not in possession of any other Purchase Offer from any other party at this time and additionally agrees that if this Purchase Offer is accepted SELLER will not solicit or encourage directly or indirectly in any manner any discussion with, or furnish or cause to be furnished any information to any person or company other than PURCHASER in connection with, or negotiate for or otherwise pursue the sale of the business described herein:

[] for the term of this agreement and any extensions hereto.

[] other: _____

Comment:

The most effective way to negotiate the sale and purchase of a business is to begin informally, with no binding commitments on the part of either party. The most practical and effective way to move a deal forward is to come to an *informal, non-binding, verbal* meeting of the minds on all of the key issues involved. Then, only after this hurdle has been crossed should any binding contract be entered into.

However, once the point is reached where the parties believe they are in agreement, or at least where the purchaser believes the seller is agreeable to his or her proposal, then, it is in the purchaser's best interest to lock the deal up and not allow the seller to "shop the offer." That is, to allow the seller to approach other interested buyers and use your offer to try to

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leverage a better deal. Such action on the seller's part is tantamount to conducting a "silent auction" using your purchase offer as the opening bid. Protecting yourself from this situation is the purpose of this part of the contract.

Suggested contract wording:

3. CLEAR AND MARKETABLE TITLE

SELLER herewith warrants that the business described herein currently possesses clear and marketable title to all assets to be included in this sale with the following exceptions:

Comment:

It is best to try and force the issue of whether or not liens against the seller's assets exist at the contract signing stage of the agreement. As has been indicated previously, it is a fairly straight forward process to search for title liens by submitting a UCC-3 title lien search form with the Secretary of State. It can take over a week and sometimes longer to obtain the results of the search request. Therefore, whenever possible, the lien search should be initiated well before it comes time to present the purchase offer.

Typically, the title search is a service provided by the escrow officer with the cost added to the escrow service fee. When this is the route taken, then no title search will occur until after this agreement has been signed. Additionally, it is recommended that there actually be *two* title searches conducted. The first one being early in the acquisition process, either before this agreement is signed or immediately thereafter. Then, there should be another search just before closing to make sure that the seller has had the liens removed if this was to be accomplished prior to closing and/or to find out if the seller has had *additional* liens placed on the business's assets after the first search was conducted.

Suggested contract wording:

4. INVENTORY VALUATION.

All salable inventory on hand at the time of physical possession shall delivered to PURCHASER. The value of said inventory shall be [] seller's cost; [] replacement cost; [] retail selling price; [] other: _____ to be calculated and/or determined as follows:

Comment:

Since inventory levels change minute by minute in a company, usually an average value is agreed upon in purchase price negotiations and the final value is determined based on a physical count just prior to close of escrow. In some deals, a purchase price is established excluding the value of inventory whereupon the total value determined through the physical count is added on.

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In either case, the resulting calculation of the inventory's actual value on hand just prior to close of escrow will be used to adjust the final purchase price. There is danger for both the seller and the buyer suffering financial harm from either the seller receiving less than a fair price for the business or the buyer over-paying based on miscalculation and/or deception relative to how the value of the inventory is determined. This is especially true in retail and manufacturing businesses.

For example, consider a hypothetical retail business that sells "widgets." Let's assume that the purchase agreement calls for the total value of the inventory to be added to the agreed upon purchase price. As is typical in the sale of retail businesses, the inventory is counted and the retail selling price of each item is recorded. Assuming there are 10,000 widgets on the store's shelves and each one cost the seller \$10, then the value of the inventory—at seller's cost—would be \$100,000. This is the amount to which the seller is entitled based on the purchase agreement.

However, assuming the seller marks his goods up 30% above his cost, then each widget's retail price would be \$13. This makes the retail value of all the inventory \$130,000. If buyer and seller agree that the value of the inventory at seller's cost is 70% of the value calculated at retail, then the seller will be under compensated for his business by \$9,000. 70% of \$130,000 is \$91,000 and that's what the seller will get. But we know the seller's actual cost was \$100,000. The mistake was assuming that if the seller marks his goods up 30% over cost, then cost must be 70% of the retail price. Actually, the seller's cost, in this example, is 10/13 of his retail price. (i.e., \$10 cost divided by \$13 retail price is 76.923% of retail). Thus the correct calculation to determine a product's cost based on its retail value is to multiply that retail value by Seller Cost divided by Retail Price which in this case is 10/13 or .76923. $\$130,000 \times .76923 = \$100,000$.

In the real world, a typical store will have hundreds of products on the shelves and not all are marked up over seller's cost uniformly. The correct approach then is to multiply the value of the inventory calculated at retail value by the ratio of cost of goods sold on the seller's financial statement (or categories of products by that category's average cost of goods sold). The ideal solution—which is not always practical—is to match each item of inventory for sale with the seller's purchase invoice and calculate the seller's exact cost to the penny.

One danger for the buyer lies in the seller deceptively marking up the retail price of all the goods in the store the night before the physical inventory is taken. This is not a miscalculation; its fraud pure and simple, but it has been known to happen.

On occasion, a seller may require the buyer to add the value of the store's inventory based on its retail value to the purchase price. In this case, the buyer will be paying twice for the difference between seller's cost of inventory and retail value. This is so because that difference represents future earnings, the value for which presumably has already been incorporated into the goodwill portion of value.

In some cases, the correct way to value the inventory is to do so based on its replacement cost. This would be appropriate for example when the inventory is comprised of precious metals or other commodities whose wholesale price fluctuates. If a seller has \$100,000 in gold in inventory purchased at \$300 an ounce and the day escrow closes, the market price of gold is \$325 an ounce, then it would be reasonable for the buyer to pay \$108,333 and not the seller's actual cost.

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Suggested contract wording:

5. PURCHASE PRICE ADJUSTMENT FOR INVENTORY ON HAND.

Immediately preceding close of escrow (or such other time as stated herein as:

_____)
a physical count of the inventory on hand shall be made by buyer and seller together
 designee of seller; designee of buyer; designee of buyer and seller; other:
Describe _____

The value of said inventory to be determined as stipulated in item 4. Upon determination of the value of the inventory on hand, the purchase price indicated above shall be adjusted up or down as the case may be to reflect the difference between the value of the inventory included in said purchase price and the actual value as determined by the physical count. Said adjustment either up or down shall not exceed \$ _____.

Or

The purchase price shall be increased by the full value of the inventory as determined by the physical count. Said inventory value shall not exceed \$ _____.

Or

Other: _____

Said physical inventory shall be taken by _____

The cost of taking the physical inventory, if any, shall be paid by seller; buyer; buyer and seller and apportioned _____% to seller and _____% to buyer.

Comment:

This section of the contract dovetails with the immediately preceding section and the section appearing earlier:

includes; does not include an allowance for salable inventory valued at \$ _____; said value to be determined as stipulated in item number 4 below.

If an indication was made in the earlier section that the tendered purchase price *includes* the inventory, then the first option should be selected here.

As a matter of transaction logistics, taking a physical count of all the merchandise and raw materials on hand and appending a seller's cost or replacement cost value on each item can be a major project. Moreover, it is not a project that can be put off for the convenience of either party; it *must* be done immediately preceding close of escrow. This may require working through the night before the day escrow is to close.

If it is evident this will be the case, adequate plans for accomplishing this task should be made well before it comes time to do the counting. There are firms in all major metropolitan areas that offer an inventory counting service. Considering the impending stress that is

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likely to be the lot of the buyer when physical possession of the business is assumed upon close of escrow, it is generally prudent to put the burden of counting the inventory onto someone else.

Whether it is the buyer and/or seller or both or a counting service who actually counts the inventory, there must be agreement among the parties as to how a dollar value will be applied to the physical count. This requirement was addressed previously, and whatever method has been agreed upon must be communicated to whomever physically does the counting and valuation.

Additionally, it is a good idea for the seller and buyer to obtain a clear idea of each other's assumptions about how the physical count should proceed and try to agree in advance on any "counting rules" if such seem necessary. For example, if a restaurant is changing hands, how should the value of prepared foods be determined or should such items be included at all? I have seen instances where only packaged raw materials were included in the count and all prepared foods were excluded altogether and other instances where *everything* was considered including the value of a bowl of Jell-O and a batch of potato salad which had to be negotiated on the run.

Of course, there will be a cost associated with engaging the services of an outside counting firm and who is to pay that cost needs to be agreed upon in advance.

Suggested contract wording:

6. PURCHASE PRICE ADJUSTMENT FOR WORK IN PROGRESS & FINISHED GOODS.

Immediately preceding close of escrow (or such other time as stated herein as:

_____)
a determination of value for any work in progress and finished goods shall be made by
[] buyer and seller together [] designee of seller; [] designee of buyer; [] designee
of buyer and seller; [] other: _____

The value of said work in progress shall be determined as follows:

Comment:

In any kind of manufacturing company or other business where manufacturing-like processes take place such as automobile or other repair and maintenance services, there are going to be unfinished projects on the premises when ownership changes hands. Therefore it is necessary to agree in advance how to place a value on them.

Work in Progress value can be determined by either adding up the cost of raw materials, labor and overhead embodied to date in it or by subtracting from it's finished state, all the costs still necessary to complete it. A value for finished goods available for sale can be valued based on all the production costs embodied in it or by subtracting from it's retail price, the total costs of labor, materials and the overhead required to sell, handle and ship the product.

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Suggested contract wording:

Upon determination of the value of the work in progress

the purchase price indicated above shall be adjusted up or down as the case may be to reflect the difference between the value of the work in progress included in said purchase price and the actual value as determined by the analysis. Said adjustment either up or down shall not exceed \$_____.

Or

The purchase price shall be increased by the full value of the work in progress as determined by the analysis. Said work in progress value shall not exceed \$_____.

Or

Other: _____

Said work in progress analysis shall be made by_____

The cost of determining the value of the work in progress, if any, shall be paid by
 seller; buyer; buyer and seller and apportioned _____% to seller and
_____% to buyer.

Comment:

This section of the contract dovetails with the immediately preceding section and the section appearing earlier:

includes; does not include an allowance for work in progress and finished goods valued at \$_____ ; said value to be determined as stipulated in item number 6 below.

If an indication was made in the earlier section that the purchase price *includes* the work in progress and finished goods, then the first option should be selected here.

Just as with inventory, determining the value of work in progress and finished goods can be a major project. Neither is this a project that can be put off for the convenience of either party; it *must* be done immediately preceding close of escrow. This too may require working through the night preceding the day escrow is to close.

If it is evident this will be the case, adequate plans for accomplishing this task should be made well before it must be accomplished.

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Suggested contract wording:

7. ACCOUNTS RECEIVABLE VALUATION.

Immediately preceding close of escrow (or such other time as stated herein as:

_____)
an analysis of seller's Accounts Receivable shall be made by buyer and seller together
 designee of seller; designee of buyer; designee of buyer and seller; other:
Describe _____

The value of said Accounts Receivable shall be their face value; discounted by _____%
for collection and administrative fees, other (describe). Upon determination of the
value of the Accounts Receivable,

the purchase price indicated above shall be adjusted up or down as the case may be to
reflect the difference between the value of the Accounts Receivable stipulated herein and the
actual value as determined by the analysis (less discount for collection).

Said adjustment either up or down shall not exceed \$_____.

Or

The purchase price shall be increased by the full value of the Accounts Receivable as
determined by the analysis.

Or

Other: _____

The cost of analyzing the Accounts Receivable shall be paid by seller; buyer;
 buyer and seller and apportioned _____% to seller and _____% to buyer.

Comment:

Assuming the seller has an efficient manual or automated accounts receivable accounting system, making a determination of the exact amount of such receivables at close of escrow should not be a problem. If this is not the case, the buyer should be well aware of this fact before any purchase offer is made and include clear language in the purchase offer as to how a determination will be made if there is an intent to purchase them.

The most problematic aspect relating to an acquisition of the seller's accounts receivable is agreeing on a collection fee for benefit of the buyer. As one can imagine, the seller is not likely to be very accommodating in this regard. Thus, unless for the strategic reasons previously discussed, the buyer should opt not to buy them or be prepared to accept something less than full payment for assuming this responsibility. Having said that, it is still important for the buyer to get as clear a picture as possible of what will be entailed in collecting the seller's accounts receivable if they are to be included in the purchase.

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In some cases, the seller will keep the accounts receivable but look to the buyer to collect them on his or her behalf. If this is the case, the buyer should seek adequate compensation for providing this service.

As with the inventory and work in progress, the following provision was made earlier for the buyer to indicate whether or not there is an intention to purchase the receivables.

includes; does not include an allowance for accounts receivable valued at \$_____.

If the first choice was selected, then in the section under discussion here, so should the first option be selected.

Suggested contract wording:

8. HOLD-BACK FOR ACCOUNTS RECEIVABLE

In the event the purchase price includes seller's Accounts Receivable, then a portion of the purchase price paid to seller at close of escrow in the amount of \$ _____ shall be held back in escrow for _____ days at which time PURCHASER, at PURCHASER'S option, may exchange any uncollected accounts receivable for an equal amount of cash in the hold-back account and said uncollected accounts receivable will be returned to SELLER along with any remaining cash in said hold-back account.

Other (describe)

Comment:

This section is self explanatory.

Suggested contract wording:

9. HOLD-BACK FOR REFUNDS, RETURNS, ALLOWANCES & REWORK

A portion of the purchase price paid to seller at close of escrow in the amount of \$_____ shall be held back in escrow for _____ days against which PURCHASER may submit claims in excess of [] \$_____ or [] _____% of gross sales revenue for uninsured refunds to customers which exceed the resale value of merchandise returned plus any post-sale allowances for products sold or the uninsured or otherwise non-reimbursable cost of redoing or repairing work or services rendered by seller prior to close of escrow. Any expenses incurred by PURCHASER for refunds, returns, allowances and/or rework for merchandise sold or services rendered by SELLER after the time period specified herein shall become a burden of the PURCHASER and the SELLER shall be held harmless therefrom and all funds remaining in said Hold Back Account shall be immediately turned over to SELLER. The method by which PURCHASER and SELLER shall calculate or determine the dollar amount of said claims shall be as follows:

Upon submission of said claims by Purchaser, the Escrow Officer shall immediately notify the Seller of same and Seller shall have _____ days following such action to contest same. Notification shall be made to Seller's agent for service who is _____ located at _____ by certified mail. The Escrow Officer shall immediately reimburse Purchaser for any claim not contested by Seller within said time period. For purposes of this paragraph, the Escrow Officer shall only consider claims contested by Seller submitted in writing and either hand delivered or sent by certified mail. The Escrow Officer shall not reimburse Purchaser for claims properly contested within the specified time period until authorized to do so by Seller or the court. An amount of money equal to contested claims shall be retained by the Escrow Officer after the proscribed time period for releasing funds remaining in said Hold Back Account and shall only be released to Seller or Purchaser as the case may be upon resolution of the dispute as provided herein.

Nothing in this paragraph shall serve to negate Purchaser's remedies at law for post-transaction customer requests for refunds, returns, allowances or costs of redoing or repairing work or services rendered beyond the time limit specified herein in cases of fraud in which the Seller is directly or indirectly implicated and/or in cases of willful neglect and/or gross negligence and/or when the Seller knew or should have known a request for a refund, return, allowance or cost of redoing or repairing work or services rendered would probably occur.

Nothing in this paragraph shall apply to discount coupons, free merchandise or services or other promotional price discount purchase or service rights conferred on prospective customers by Seller prior to close of escrow and submitted for redemption after close of escrow.

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Comment:

Merchandise returns and allowance and the need to repair or redo previously performed work and/or service is a normal cost of doing business. To some degree, every business owner must incur such costs from time to time. If properly developed, the purchase price for the business will either have directly or indirectly reflected the historical amount of such costs for the subject business. Assuming this to be the case, the buyer needs to be fully prepared to face the prospect of incurring some of these costs and, if maintaining the good name and reputation of the business acquired is important, absorbing them gracefully.

Therefore, it is unreasonable for the buyer to look to the seller after ownership changes hands to be compensated for any of these costs that are within the normal range of the seller's historical experience. The purpose of this section of the contract is to protect the buyer from any extraordinary costs along these lines. It is a wise buyer who assumes a conservative posture toward this issue and accedes to the seller a little more than reasonable benefit of the doubt.

Suggested contract wording:

10. DISCOUNT COUPONS, FREE MERCHANDISE OFFERS & OTHER DISCOUNTS

Seller herewith stipulates that the following discount coupons, free merchandise or service offers and other similar promotional price discounts and/or service rights discounts may be, to the best of Seller's knowledge, valid rights redeemable by customers after the expected close of escrow date:

Purchaser herewith acknowledges advice of same and herewith waives any and all rights of recovery from Seller for said claims with the following exception(s):

Comment:

Offering various promotional and advertising discounts is as American as apple pie. As often as not, most business owners—especially retailers—have no earthly idea what the potential redemption is likely to be from past promotional offers. As with returns and allowances, a properly developed purchase offer will have taken into account the subject business's historical price discount activities and the seller should honor redemption requests proffered by the seller without comment.

Probably the most appropriate use of the "exceptions" clause is for the buyer to obtain protection from or maintain control over the seller's promotional activities after acceptance of the offer up to the close of escrow.

Suggested contract wording:

11. TERM OF THIS AGREEMENT AND CLOSING

This Exclusive Option to Purchase shall terminate and coincide with Close of Escrow which shall be on _____. Said term of this agreement and closing date may be extended or shortened by mutual written agreement of SELLER and PURCHASER. On or before said closing date, both parties shall deposit with an authorized escrow holder, selected by the undersigned PURCHASER, all funds and instruments necessary to complete the contemplated sale in accordance with the terms hereof including the balance of the purchase price or down payment and promissory note(s) as the case may be for the benefit of the SELLER, a valid Bill of Sale for such business and property together with any lease or lease assignment of the premises on which the business is located. Thereafter, any party, including Agent, may disclose the terms of sale.

Comment:

Some transactions will take longer to complete than others. As a practical matter, a buyer should probably allow a minimum of eight weeks to complete the process once this contract has been signed in all but the simplest of transactions. However, there may be circumstances surrounding a transaction that may require significantly more time to deal with. In every case though, by the time it is appropriate for the parties to enter into this contract, the buyer should have a good idea of how long it will likely take to address all of the possible contingencies.

Suggested contract wording:

12. PHYSICAL POSSESSION.

Physical possession shall be delivered to PURCHASER at [] close of escrow;
[] other: _____

Comment:

In most cases, physical possession of the business occurs immediately upon close of escrow. However this is not always the case. There are occasions, for all kinds of reasons, where the buyer assumes physical possession prior to close of escrow. (There may be occasions where physical possession is to occur after escrow closes although I have never heard of any). In any case, all parties to the transaction must be aware that this is a very high risk proposition and should be avoided whenever possible. However, in those instances where it cannot be avoided, it is *highly* advisable that the parties enter into an "Interim Management Agreement." The issues which such a contract should address are beyond the scope of this book. However, in every instance where this will occur, the parties should consult legal counsel for assistance.

Suggested contract wording:

13. PRORATIONS.

Rents, property tax, franchise or other taxes, if any, premiums on insurance acceptable to PURCHASER, franchise fees, interest, utility expenses and other expenses of the business and/or property are to be prorated as of the date of transfer of the business. Security deposits, advance rentals or considerations involving future lease credits shall be credited to SELLER unless specifically stated otherwise herein.

Comment:

Ideally, escrow will close on the first day of the month and there will be little in the way of mid-month adjustments that must be made for such expenses. Of course, in most cases this will not happen. Thus, these expenses must be allocated to buyer and seller at close of escrow. Making this allocation is the job of the escrow officer. However, this can only be done accurately when the escrow officer is provided with a list of all the kinds of ongoing expenses which will need to be so allocated.

Suggested contract wording:

14. SALES TAX

Any sales tax due for the sale of the personal property shall be paid by PURCHASER unless otherwise agreed to in writing by SELLER and PURCHASER.

Comment:

The sales tax due on the sale of personal property and vehicles included in the sale of a business is often not considered until late in the game—and this tax can be substantial. In some states, such as Nevada, no sales tax must be paid when all the personal property of the business is being sold while in California, no such exemption exists. Be sure to determine the specific requirements in your state.

However, in some states, there are caveats to the sales tax exemption. For example, in Nevada, if the business seller has sold off more than one piece of operating equipment in the twelve months preceding the sale of the business, then there will be sales tax due on all the personal property included in the transaction. It is important for the business buyer to find out if there will be a sales tax liability. Also, a sales tax will have to be paid on the purchase of any vehicles included in the transaction.

Even though it is customary for the buyer to pay this tax, it is negotiable. Moreover, if the tendered purchase price is properly anticipated and reflects the buyer's need to incur this cost as part of the transaction, then without regard to the fact that the buyer writes the check, it will be the seller who bears the true economic burden.

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Suggested contract wording:

15. RISK OF LOSS

Any risk of loss to the business or property shall be born by the SELLER until title has been conveyed to the PURCHASER.

Comment:

This means that the seller must maintain all insurance policies in effect until close of escrow. It also means that the buyer should have made complete insurance provisions prior to close of escrow such that they automatically go into effect the moment possession takes place.

In those cases where buyer and seller have entered into an interim management agreement, the insurers for both parties need to be fully apprised of this fact so that adequate precautions can be taken.

Suggested contract wording:

16. MAINTENANCE OF GOODWILL

Until possession is delivered, SELLER agrees to continue to operate the business in the manner in which it is being operated at the date of this offer and to maintain the goodwill of the business and all personal property in normal working order subject to the exceptions and/or exclusions listed below. The SELLER shall not disclose or in any way let it be known to the business's employees, customers, vendors or other parties who have no need to know, that a transfer of ownership is pending. This also specifically means SELLER shall not raise or lower selling and/or service prices, raise or lower employee wages, fire, lay off or make other substantive changes in company personnel, modify existing credit terms or make any other substantive changes to standard operating procedures or the assemblage of fixtures, machinery or other operating equipment in affect at the time of this offer without first notifying PURCHASER in writing of such need or intention to do so *and* obtaining PURCHASER'S written approval for such actions. If SELLER fails to comply with this condition, then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

Exceptions and/or Exclusions:

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PURCHASER shall respond to such requests for changes upon receipt within ____ hours in writing. PURCHASER'S failure to respond to any specific request from SELLER to make changes within ____ hours shall be deemed as PURCHASER'S approval. PURCHASER'S failure to respond to a specific request from SELLER to make said changes shall not negate this clause nor serve as a waiver of PURCHASER'S right to approve future changes requested by SELLER. Upon refusal of PURCHASER to approve reasonable changes necessitated by the normal and customary course of business and consistent with SELLER'S established standard operating procedures requested by SELLER, SELLER may at SELLER'S option cancel this agreement not sooner than ____ hours subsequent to notifying PURCHASER of such intention in writing and therewith all rights and obligations herein may, at the election of the SELLER, terminate and end and the deposit shall be returned to the PURCHASER. If PURCHASER approves the requested change in writing previously denied within ____ hours of being advised by SELLER of an intention to cancel this agreement, said approval shall invalidate SELLER'S notice of cancellation. For purposes of this clause, Facsimile transmissions and/or e-mail messages shall be deemed as "notice or advice in writing."

Comment:

There can be no question but that the time period between the signing of this agreement and close of escrow is extremely precarious. There is enormous potential for the seller to back off from giving 100% to the business during this period. There is also potential for instability and uncertainty among the employees as well. The buyer should be aware that great damage to the business's good name and reputation and its continued ability to conduct business in the normal and customary fashion can occur in a very short time period. Therefore, the buyer needs to take the greatest precautions possible to insure this will not occur.

There is also the risk of the seller being tempted to milk the company for cash in anticipation of a change of ownership by doing such things as raising prices, lowering quality, selling off equipment and so forth. The buyer should take every precaution possible to keep this from happening.

For these reasons alone, it is best not to sign this contract until there appears to be substantial agreement among the parties as to terms of sale. In the buyer's best interest the transaction process should be moved along as quickly as humanly possible once this contract has been signed.

Suggested contract wording:

17. LEASE

PURCHASER to assume the existing lease. This sale is conditioned upon landlord's consent to assignment of said lease concurrent with close of escrow.

This sale is conditioned upon PURCHASER'S ability to negotiate a new lease with landlord to become effective concurrently with close of escrow.

This sale is conditioned upon PURCHASER'S ability to negotiate a lease with the SELLER who also owns the real property in/on which this business operates to become effective concurrently with close of escrow. The cost of developing the lease shall be paid by seller; purchaser; seller and purchaser and apportioned ____% to seller and ____% to purchaser.

other terms and conditions:

If PURCHASER is unable to:

Obtain an assignment of said lease within _____ days of the date of this agreement:

Negotiate a new lease or extension to the existing lease acceptable to PURCHASER within _____ days of the date of this agreement:

Other:

then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

PURCHASER herewith stipulates that the purchase price contained herein is predicated on the assumption that the future rent that the business will be required to pay will not be materially different from the current rent (and rent escalators) and that the future term of a new lease if such is required, will be acceptable. Therefore, all parties to this agreement herein acknowledge that any deviation between PURCHASER'S existing assumptions regarding the terms of the lease and the terms ultimately determined to be acceptable to the premises owner shall render the purchase price null and void and in the event the parties to this agreement cannot renegotiate the purchase price prior to the date specified in Section 11 or any extension thereto, then all rights and obligations herein may, at the election of the PURCHASER or the SELLER, terminate and end and the deposit shall be returned to the PURCHASER.

NOTE: If an assignment of an existing lease or the execution of a new lease shall be made a condition of this agreement and if a fully executed lease assignment or new lease is not placed in escrow by the date specified in Section 11 or any extension thereto, then, in the absence of a waiver of this condition signed by PURCHASER and SELLER, this agreement shall become null and void and all rights and obligations of both parties shall automatically terminate and end and the deposit shall be returned to the PURCHASER.

Comment:

Unless you plan to buy the real property in which the business is situated or the business rents space on a month-to-month basis, you will also have to become party to a commercial lease as a condition of buying the business. Addressing this matter during the acquisition process is almost never a minor detail. Indeed, the collateral task of acquiring an assignment of an existing lease or negotiating a new lease can often take more time and effort than the business purchase negotiations.

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In almost every business, the rent paid to the premises owner represents a significant cost of doing business. As such, the rent paid and terms of the lease have a significant bearing on the value of the business. Additionally, in those cases where there is little time left on the existing lease, it becomes vital that the business buyer negotiate a new lease with the property owner concurrent with the purchase of the business.

Unfortunately, the need to do this creates a fair degree of complexity in the acquisition process. This is so because the value of the business becomes something of a moving target. That is to say, it is impossible to determine the value of a business when there is little time remaining on a lease until after the rent the premises owner intends to charge the buyer on a new lease becomes known. It is rare that a property owner will lower the rent upon commencement of a new lease. This means, all else remaining the same, the value of the business will decline if the rent goes up.

On occasion, the business seller will own the real property in which the business is situated but intends to hold on to the real estate and only sell the business. This situation can create a couple of problems. The first is that the task of determining the value of the business becomes much more complex when the only “occupancy costs” appearing on the seller’s financial statements are the interest paid on a real estate loan, plus the real estate property taxes, insurance and maintenance. This is especially true when those interest, taxes, insurance and maintenance expenses have been commingled with similar non-real estate related costs on the business’s financial statements. It requires the trained eye of an experienced business appraiser to “separate the apples from the oranges” so to speak in order to determine the value of a business under these circumstances.

Additionally, any initial determination of the appropriate allocation of total value to business and real estate will generally be made under the assumption the “income from real estate” is based on the business paying “fair market value” rent. It may be that the building owner plans to charge the buyer of the business something other than fair market value rent—and it is usually more. Under this circumstance, the originally calculated value of the business will go down.

Therefore, in situations where the buyer must negotiate a new lease as a condition of purchasing the business, it can only be after the lease negotiations have been finalized either by signing a new lease or letter of intent that the value of the business can be determined.

Besides the issue of the rent the buyer must pay, and the term of the lease, another word of caution is in order. *There is no such thing as a ‘standard commercial lease’!* Virtually every commercial lease is different in some way. Some commercial leases are contained in just a couple of typewritten pages while others can be forty pages long or more. These contracts should be viewed by a business buyer as an economic and legal minefield and should never be accepted and/or renegotiated without expert assistance. And even assuming you get such assistance, it is still important that *you* read and understand the significance of each sentence and how each condition and requirement may affect you in the future.

Another thing to be aware of is that commercial leases are negotiable just like any other contract. It is a common ploy of property owners to maintain that their lease is non-negotiable and that you must “take it or leave it.” Sometimes this is true and sometimes it is not. In situations where you are buying the business and the seller still has a long time left to go on the lease who, moreover, is financially solid and pays the rent on time, then the property owner is not likely to be in much of a negotiating mood. On the other hand, when the end of the lease term is near at hand and/or the ability of the tenant to continue to pay the rent is somewhat doubtful, there is likely to be more room for negotiations.

Suggested contract wording:

18. DEFECTS AND INSPECTIONS

Seller represents that he/she knows of no defects, deficiencies or violations of local, state or federal law and/or codes affecting the business, the business's operating equipment or the premises in which the business is situated and agrees that he/she will advise PURCHASER in writing of same which come to his or her attention prior to the completion of the sale with the exception of those defects, deficiencies and legal and/or code violations itemized below which PURCHASER and Seller acknowledge exist and which PURCHASER herewith excludes from this agreement under the terms and conditions as follows:

SELLER may, at SELLER'S option, correct any identified defects within _____ days of the stipulated date for close of escrow, or other date agreed to by SELLER and PURCHASER in writing in which case, such corrective action shall herewith be deemed a non-defect for purposes of this agreement provided said corrective action meets the standards necessary for lawful operation of the business or if some other higher or lower standard has been agreed to by PURCHASER and SELLER, then said higher or lower standard.

Upon notice to PURCHASER by SELLER of any such defects or upon discovery of any such defects by PURCHASER by any other means including, but not limited to the list of inspections identified below then PURCHASER may, at PURCHASER'S option, cancel this agreement provided PURCHASER advises SELLER of said discovery of previously unknown or undisclosed defect(s) in writing within ____ hours of said discovery and further provided PURCHASER advises SELLER in writing of an intention to cancel this agreement due to said previously unknown or undisclosed defects within the same time period and further provided the cost to correct any defect or the aggregate cost to correct multiple defects is expected to exceed \$_____ or provided SELLER does not correct said defects within _____ days of the stipulated date for close of escrow, or other date agreed to by SELLER and PURCHASER in writing or negotiate a purchase price adjustment to offset PURCHASER'S expected cost to correct said defects after close of escrow.

PURCHASER herein specifically requires that the following inspections be made at PURCHASER'S expense:

- A due diligence investigation of the business to be performed by PURCHASER and/or PURCHASER'S designee(s). PURCHASER herein stipulates that said investigation may involve several hours of SELLER'S and/or SELLER'S employees' time and SELLER herewith agrees to make a good faith effort to assist PURCHASER in said investigation provided however, said good faith effort specifically shall exclude SELLER incurring any costs of money or time to develop additional records or reports that do not presently exist such as (but not limited to) audited financial statements, customer surveys, employee surveys, market forecasts, sales and/or earnings forecasts or projections, etc.
- An independent audit of SELLER'S Financial Statements
- Phase I Environmental Assessment
- Phase II Environmental Assessment if recommended by the Phase I analysis
- Structural inspection of the premises

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-] Pest inspection of the premises
-] Well production/water quality
-] Fuel or other storage tanks
-] Inspection of all or selected operating equipment
-] Appraisal/Valuation Analysis of the business
-] Appraisal/Valuation Analysis of all or selected operating equipment
-] Appraisal of the real property on/in which the business operates.
-] Other: _____

Said inspections/ appraisals /valuations shall be completed within _____ days. For purposes of this agreement, an appraisal of the business's "going concern" value or an appraisal of any real property to be included in this purchase indicating the purchase price offer tendered herein exceeds the value of same as indicated on said appraisal shall be defined as a defect.

If PURCHASER fails to complete said inspections within the specified time limit, then PURCHASER shall therewith forfeit the right to complete said inspections, provided SELLER made a good faith effort to accommodate PURCHASER'S inspection efforts. If SELLER, SELLER'S employees or SELLER'S agents, shall obstruct or not reasonably cooperate or not reasonably assist (when such cooperation and/or assistance is necessary) with PURCHASER'S inspection efforts then, upon ____ hour notice to SELLER of such obstruction, failure to cooperate with and/or failure to assist PURCHASER in said due diligence activities then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER under the terms and conditions specified in Paragraph 31 below.

Comment:

The variety of continuing challenges any company faces and must overcome to remain profitable are substantial; there are literally hundreds of problems, threats, regulations and opportunities requiring the constant attention of business owners. Some of these issues are relatively minor while some are potentially life threatening. However, they all to some degree combine to shape a company's future and how management addresses them will determine what that future will be.

For anyone considering buying a business, it is important to gain some insight into the nature of these problems, threats, regulations and opportunities and how the current owners are dealing with them. Moreover, to the greatest degree possible this insight should be acquired *before* the business is purchased.

This research effort is known as the buyer's "due diligence" investigation. The more thorough the effort devoted to this task by the buyer, the less risk there will be of encountering unexpected problems after ownership changes hands. There are four primary areas which a buyer's due diligence investigation should address: Financial, Legal, Operational and Market.

On an informal basis, this investigative process should begin the moment a buyer first encounters a potential acquisition and should address all four areas. However, the logical place to initiate a formal study is the financial performance of a business. Unless a business's earnings history support the asking price—or nearly so—there is no point in

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going any further. By now it should be clear that how to relate a business's reported earnings to its value is a very involved project.

The legal investigation principally focuses on the business's compliance with all the local, state and federal regulations which affect it. At the local level, a buyer should ascertain whether a business is in compliance with codes enforced by the Health Department, Building Department, Planning and Zoning agencies, Alcoholic Beverage Control and the Fire Marshall. At the state level the investigation should focus on compliance with regulations established by an assortment of State Boards which may regulate a business depending on its nature in addition to a search of the Secretary of State's UCC-1 files to see what liens may have been placed on the company's assets. At the federal level a buyer should determine if a company is in compliance with federal (and state equivalents of) Occupational Safety and Health Administration, Americans with Disabilities Act, Equal Employment Opportunity Commission, Immigration and Naturalization Service, the Employee Retirement Income Security Act and the Comprehensive Environmental Response, Compensation and Liability Act—known as "CERCLA."

In addition to the foregoing, a determination must be made regarding the assignability and under what conditions of such things as the business's lease, franchise agreement, supplier agreements and other contracts.

An investigation of the company's operations is essentially an examination of the company's operating equipment, physical facilities, suppliers, employees and standard operating procedures to ascertain the adequacy of each to sustain the company's current earnings and achieve any anticipated increases.

Finally, a buyer should look at a business's product line, product development, trade marks, patents, pricing strategy, market niche, location, customer base, advertising and competition to insure as best as possible that those factors are adequate and/or are not undergoing some change that is likely to have a negative affect on the company's expected future earnings.

As should be evident, the due diligence investigation is no small task and is best approached using a well thought out check list. Additionally, it is unlikely a buyer will be adequately knowledgeable in all areas that need to be examined. Thus it is advisable to engage the assistance of experts whenever a buyer doubts his or her own ability to adequately assess any of the above described attributes.

Another prominent feature of this section is the very last sentence which is the inclusion of the buyer's right to terminate the contract "according to section 31 below." From the seller's point of view, this is a condition with some very sharp teeth because it places a *monetary* penalty on the *seller* for failure to cooperate.

The buyer should anticipate a very stern objection from the seller for this condition. This is probably something the typical seller will never have anticipated in any purchase offer. Traditionally, the risk of losing some money for failure to complete a transaction has always been a one-sided proposition: it has only been a risk for the buyer. Paragraph 31 is intended to create a level playing field in this regard and necessarily so.

Many business sellers tend to take a rather cavalier attitude toward the buyer's due diligence investigation. Sometimes due to laziness, sometimes disorganization and on occasion due to an intentional effort to defraud the buyer, seller's are often slow or non performing

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when it comes to assisting the buyer in the process or providing the buyer with requested documents and disclosures. Buyers need to be aware of this propensity among sellers and create a situation where they cannot get away with it. In situations where the seller refuses to agree to this condition, the buyer should become considerably more wary of the honesty of the seller and the wisdom of continuing the acquisition process.

Suggested contract wording:

19. ADDITIONAL DOCUMENTS

Seller shall deliver to PURCHASER for approval the following documents within _____ days of acceptance. If SELLER does not deliver all documents requested by PURCHASER within said time period then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER under the terms and conditions specified in Paragraph 31 below.

PURCHASER shall be deemed to have approved said documents unless written notice to the contrary is delivered to SELLER or SELLER'S Agent within _____ days of receipt of said documents by PURCHASER. In the event PURCHASER finds any facts, circumstances, conditions or other attributes of the business or business records and/or documents unacceptable to PURCHASER for any reason whatsoever then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

SELLER herewith warrants that all such documents will be true and complete to the best of SELLER'S knowledge.

PURCHASER may extend the deadline by which SELLER must provide the requested documents by so advising the SELLER in writing of such extension however, if SELLER fails to provide all the documents requested by said extended deadline then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER under the terms and conditions identified in Paragraph 31 below.

List of all furniture, fixtures, equipment and machinery plus a general description of all small tools, office equipment and other miscellaneous and/or incidental assets to be included in the purchase price and exclusions thereto, if any.

Inventory of all supplies (e.g., cleaning supplies, office supplies, repair parts, etc.) to be included in the purchase price. PURCHASER herein acknowledges said inventory changes daily and herewith agrees that no adjustment in the purchase price shall be made if, at the date of closing, the value of said inventory differs from that indicated on said report by less than _____%

Profit & Loss Statements and Balance Sheets for the years ending:

Federal Income Tax returns for the years ending:

Accounts Payable and Accounts Receivable Aging Report

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- Name, address & phone number for all vendors, suppliers & creditors
- Sales Tax returns for:
- Copy of all insurance policies currently in effect for the business
- Copy of all contracts to which the business is a party. (e.g., Premises Lease, Equipment Lease(s), Franchise Agreements, Dealership Agreements, advertising contracts, Bill Board contracts, Yellow Pages contracts, etc.)
- Resume, job descriptions, pay rates and general information on the following employees:
- Samples and/or copies of company advertising and/or other marketing material
- Secretary of State title lien search
- Articles of Incorporation and Bylaws
- Other:

Comment:

This section of the contract is essentially a continuation of the buyer's "due diligence" investigation and also allows the buyer to terminate the contract according to section 31.

Suggested contract wording:

20-A. SALE OF VEHICLES

Ownership transfer of

All vehicles to be included in the purchase of this business

Only those vehicles for which the seller has possession of the title shall be accomplished through escrow. Within _____ days from the date of this agreement, seller shall deposit into escrow the titles to all vehicles to be acquired by buyer provided seller has physical possession of said titles together with a detailed description of all vehicles to be acquired by buyer including the make, model, year and VIN Number (Vehicle Identification Number).

Within _____ days from the date of this agreement Seller shall make a determination of all costs associated with ownership transfer of each vehicle subject to this agreement including (but not limited to) sales tax, registration, title fee, license plate fee, supplemental county tax, privilege tax, etc. and advise the Purchaser and the escrow officer of such findings.

For all vehicles subject to this agreement which have unpaid loan balances and for this reason, title to said vehicles are in the possession of a third party lender, seller shall, within _____ days from the date of this agreement also deposit into escrow a Letter of Authorization instructing the escrow officer to pay off said loans using funds held back from the sale proceeds due seller together with a *Limited Power of Attorney for a vehicle title transfer* empowering the escrow officer to complete same in the name of the seller. Simultaneous with the submission of said Letter of Authorization, Seller shall also submit a notarized Letter of Request addressed to said third party lender, requesting that the titles for said vehicles be sent to the escrow officer upon payment of the remaining loan balance.

At close of escrow, seller shall provide the escrow officer with the odometer reading on all vehicles subject to this agreement, and any required documentation indicating each vehicle is in compliance with applicable emission laws and a statement indicating the amount of the unpaid balance and accrued interest and other fees, if any, required to be paid a third party lender (under the presumption payment will be received by the bank within 5 business days) as a condition of obtaining free and clear title to said vehicles.

At close of escrow Purchaser shall provide the escrow officer with a *Limited Power of Attorney for a vehicle title transfer* empowering the escrow officer to complete same in the name of the Purchaser for all vehicles subject to this agreement for which the vehicle titles are held by a third part at close of escrow together with proof of insurance on all vehicles subject to this agreement.

At close of escrow, Purchaser shall deposit into escrow an additional sum equal to all fees required to be paid as a condition of ownership transfer for all vehicles subject to this agreement.

Purchaser's payment of said fees as a requirement of ownership transfer

shall not shall be applied to the total purchase price of the subject business.

Or

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At close of escrow, the funds necessary to pay the fees required as a condition of ownership transfer on all vehicles subject to this agreement shall be placed into escrow and allocated to the purchase price as follows:

At close of escrow, the seller shall sign off as the legal owner on the vehicle title document and the purchaser shall sign on as the legal owner on the vehicle title document for each vehicle subject to this agreement on all vehicle title documents available at said time.

At close of escrow, the escrow officer shall preside over the execution of a Bill of Sale for each vehicle subject to this agreement and provide a copy of said document to Purchaser and Seller and retain additional copies as needed.

At close of escrow, the escrow officer shall submit to the Department of Motor Vehicles said completed vehicle title documents together with payment of all fees required as a condition of ownership transfer for said vehicles, a copy of the Bill of Sale, Purchaser's proof of insurance and any other required documentation.

Escrow officer shall additionally submit to the Department of Motor Vehicles a notarized Letter of Request signed by the Purchaser directing said Department to send the new vehicle title to Purchaser's Lender.

At close of escrow, the escrow officer shall pay off all outstanding vehicle loans from the sale proceeds held back for this purpose. Upon receipt of the vehicle titles from said third party lenders, the escrow officer shall complete the appropriate sections on said titles in the name of the Seller and in the name of the Purchaser and submit same to the Department of Motor Vehicles together with two attached *Limited Powers of Attorney for a vehicle title transfer* empowering the escrow officer to complete same in the name of the Seller and Purchaser, payment of all fees required as a condition of ownership transfer for said vehicles, a Bill of Sale for each vehicle, Purchaser's proof of insurance and any other required documentation.

Escrow officer shall additionally submit to the Department of Motor Vehicles a notarized Letter of Request signed by the Purchaser directing said Department to send the new vehicle title to Purchaser's Lender.

Immediately following close of escrow PURCHASER shall take those actions required to obtain a temporary registration and/or operating permit from the Department of Motor Vehicles in Purchaser's name pending receipt of a new title document, permanent registration and vehicle license plates such as (but not limited to) proceeding directly to the Department of Motor Vehicles with the Bill of Sale and proof of insurance and other documents as may be required to obtain said temporary registration and/or operating permit and, upon obtaining said documents, placing same in said vehicles. Additionally, SELLER shall remove the license plates from all vehicles subject to this agreement and submit same to the Department of Motor Vehicles for cancellation.

If either Seller or Purchaser do not comply with all conditions of this section within or at the times specified herein then all rights and obligations may, at the election of the other party to this agreement, terminate and end and the deposit shall be returned to the PURCHASER and all vehicle titles shall be returned to the Seller.

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Comment:

The transaction logistics involving any company owned vehicles which are to be included as part of a business acquisition and over which the escrow officer is to maintain control require special handling. For this part of the transaction there will be a need to comply with the procedures of the state's Department of Motor Vehicles and possibly a third party lender

Section 20-A has been designed to accomplish this task. The transaction method provided in Section 20-A has been developed with the intent to comply with the State of Nevada's Department of Motor Vehicles policies and procedures. This format may not work in every case due to the possible unique circumstances of a particular transaction and, of course, varying state laws. Therefore, *it is highly recommended that buyers and sellers ascertain in advance of the date escrow is to close how to complete the contemplated transaction which will included vehicles and remain in compliance with applicable state law and plan the transaction accordingly!*

For example, to the best of my knowledge based on discussions with the State of Nevada's Department of Motor Vehicles, it is *impossible* to make an exact determination of the sales tax, registration fee and other costs of ownership transfer for a vehicle (not being purchased from a dealer) except by presenting them with copy of the vehicle title and registration and, for vehicles more than four years old, an *appraisal!* In the case where the vehicle title is in the possession of a lender, this will necessitate getting a photo copy of the title from that lender. If the lender is unwilling to accommodate this request, then it is absolutely impossible to know at close of escrow exactly what the transfer fees will be.

If an exact determination of the vehicle transfer fees cannot be made at close of escrow, then the method of ownership transfer provided in Section 20-A will not work. If this is the circumstances of the transaction, then the escrow officer cannot maintain control of the process. In this situation, Section 20-A will need to be replaced with the alternative Section 20-B provided below.

There may be an occasion where some of the Purchaser's funds are to be provided by a third party lender which, additionally requires to hold title to all vehicles included in the transaction and additionally requires that those titles pass directly from the current title holder to them. If this is the case and if the vehicle titles are in the possession of the seller's lender and if, additionally, the transaction cannot be completed in accordance with Section 20-A, then the transaction is technically deadlocked and cannot be consummated. There are two possible solutions for this situation. The first is for the seller to pay off the vehicle loans prior to close of escrow, get the titles and proceed according to Section 20-A with an additional requirement that the escrow officer send the titles to the buyer's lender. The second is for the buyer to additionally provide the Department of Motor Vehicles with a notarized letter of instruction to send the new titles to his or her lender. This may require that the lender accompany the buyer to the DMV to insure that the buyer hands over that letter of instruction.

The method by which the titles are to change hands recommended in 20-A serve the interests of both parties. This method ensures that the buyer will get all the vehicle titles of course, but it also protects the seller. Should the buyer obtain possession of the vehicle titles directly, there is the possibility that he or she will not then register the vehicles with the Department of Motor Vehicles in an effort to avoid having to pay the sales tax on them. Should this happen and should the buyer become involved in an accident, the seller may, in some instances, still be liable as the registered legal owner and could possibly be sued by an injured party.

Suggested contract wording:

20-B. SALE OF VEHICLES

Ownership transfer of

Those vehicles to be included in the purchase of this business for which the titles to said vehicles are in the possession of a third party lender

All vehicles to be included in the purchase price of this business

shall NOT be accomplished through escrow.

The purchase price for the business allocated to the purchase of vehicles indicated above and the fees required for ownership transfer such as (but not limited to) sales tax, registration, title fee, license plate fee, supplemental county tax, privilege tax, etc. shall not be deposited into escrow.

Seller and Purchaser herein agree to consummate this portion of the total acquisition in the following manner:

Not more than 60 days preceding close of escrow, seller shall obtain a certified emissions analysis indicating each vehicle is in compliance with applicable emission laws and, for vehicles more than four years old, obtain an appraisal.

Immediately preceding close of escrow, seller shall obtain a statement indicating the amount of the unpaid balance and accrued interest and other fees, if any, required to be paid a third party lender as a condition of obtaining free and clear title to said vehicles and provide said statement to Purchaser and the odometer reading from each vehicle.

Prior to close of escrow, Purchaser shall obtain proof of insurance on each vehicle subject to this transaction.

Immediately following close of escrow, Purchaser shall pay Seller the agreed portion of the total purchase price allocated for each vehicle included in the transaction (less any amount due a third party lender). At this time, seller shall sign off as the legal owner on each vehicle title document and the purchaser shall sign on as the legal owner on each vehicle title document available and the parties shall execute a Bill of Sale for said vehicles. Then, Seller and Purchaser shall, together, personally appear at the office of each lender whereupon Purchaser shall pay off the loans on said vehicles, obtain title to same whereupon seller shall sign off as the legal owner on the vehicle title document and the purchaser shall sign on as the legal owner on the vehicle title document and the parties shall execute a Bill of Sale for said vehicles.

Immediately subsequent to obtaining the titles to all the vehicles subject to this transaction and completing same indicating a transfer of ownership,
 Seller and Purchaser Purchaser shall proceed directly to the Department of Motor Vehicles, turn in said titles whereupon Purchaser shall, present proof of insurance for said vehicles, a duly executed Bill of Sale, a certified emissions analysis indicating each vehicle is in compliance with applicable emission laws and, for vehicles more than four years old, an appraisal and pay _____% and Seller shall pay _____% of all fees required to transfer ownership of said vehicles to Purchaser.

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Purchaser's payment of fees to the Department of Motor Vehicles as a requirement of ownership transfer [] shall not [] shall be applied to the total purchase price of the subject business.

Immediately subsequent to completion of the Department of Motor Vehicles vehicle ownership transfer requirements, Purchaser shall place each temporary vehicle operating permit in the subject vehicles and Seller shall remove the license plates from said vehicles and submit same to the Department of Motor Vehicles for cancellation.

Suggested contract wording:

21. LICENSES AND PERMITS

Seller herein warrants, after due inquiry, that the following licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) to conduct business constitute all such sanctions legally required to conduct business in its ordinary and customary fashion:

Seller herein stipulates that Seller personally possesses the following legally required licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) necessary to conduct business in its ordinary and customary fashion and represents that Purchaser will be legally required to possess or acquire same prior to close of escrow in order to similarly conduct business in its ordinary and customary fashion:

Seller herein stipulates that some or all of seller's employee(s) are required to possess the following licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) and meet or exceed minimum age requirements which are legally required to continue to conduct business in its ordinary and customary fashion:

Seller herein warrants that seller's employee(s) possess all the licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) and meet or exceed minimum age requirements as defined above to continue to conduct business in its ordinary and customary fashion with the following exceptions:

This sale is contingent upon approval of transfer of any licenses by federal, state or local agencies or franchisor or other vendor or upon issuance of any new licenses, permits, professional credentials, college degrees, certificates and/or other similar consent(s) to conduct business required by Purchaser prior to close of escrow with the exception of the following:

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In the event Seller's employees do not possess those licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) legally required to conduct business in its ordinary and customary fashion identified above or meet a minimum age requirement to carry out their job responsibilities as provided by applicable law then all rights and obligations herein may, at the election of the Purchaser, terminate and end and the deposit shall be returned to the Purchaser.

Nothing in this paragraph shall serve to negate Purchaser's legal remedies to collect damages from Seller incurred by Purchaser due to failure of Seller to disclose herein all licenses, permits, professional credentials, college degrees, certificates and/or other similar consent(s) legally required to be held by Seller or Seller's employees or other legal requirements regarding minimum age, citizenship or other legally required right to work conditions in order to conduct business in its ordinary and customary fashion or Seller's failure to disclose employees currently working without possessing said legally required licenses, permits, professional credentials, college degrees, certificates and/or other similar consent(s) or meeting minimum age requirements, citizenship or other legally required right to work conditions.

Comment:

No business should ever be purchased "as is." It is necessary and appropriate that the buyer require the seller to make certain "representations and warranties" regarding the business as a condition of buying it. This section of the contract serves as just such a seller "representation and warranty" obligation. There are more seller representation and warranty sections to follow which are sufficiently generic to be included in every purchase contract. However, since many businesses are unique in certain ways, the buyer should provide for additional seller representations and warranties that will be appropriate given the business's unique attributes but which have not been included here.

Suggested contract wording:

22. CONTRACT ASSIGNABILITY

Seller herein represents that the following Franchise Agreements, Dealership Agreements, Distributorship Agreements or similar contracts and agreements constitute all such agreements necessary for the conduct of business and, to the best of Seller's knowledge, can and will be transferred or assigned to Purchaser: _____

In the event, Purchaser is unable to have the above described contracts and/or agreements transferred, assigned or otherwise made to have the same affect prior to or at close of escrow, then all obligations herein may, at the election of the Purchaser, terminate and end and the deposit shall be returned to the Purchaser.

The preceding paragraph shall specifically prohibit Purchaser from invalidating a consummated purchase transaction should Purchaser fail to obtain an assignment of any Franchise Agreement, Dealership Agreement, Distributorship Agreement after close of escrow if Purchaser voluntarily postponed attempting to obtain said transfers and/or assignments until after such time. This condition shall not apply, however, to any such required transfers and/or assignments material to the operation of the business which Seller failed to disclose to Purchaser herein.

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Comment:

Making a determination of exactly what sort of arrangements or agreements a seller may have with various vendors and how those elements of the business will carry over to a new owner can sometimes be more of a challenge than meets the eye. Sometimes what a seller may represent as an “exclusive” dealership right or territorial right may be only an informal understanding which that vendor can withdraw at any time. Even though the seller may *believe* he or she enjoys certain privileges granted by a vendor, it is up to the buyer to make sure those same circumstances will continue once the business is sold.

As a case in point, I am aware of a transaction where a franchised restaurant operator had obtained an “Area Development Agreement” from the franchisor. This Area Development Agreement extended to the franchisee a rather large portion of a major metropolitan area as his exclusive territory to further develop. So long as the franchisee opened new units at a pace acceptable to the franchisor, none of that territory would be assigned to any other new franchisee. This Area Development Agreement did not cost the franchisee anything. It was the custom of the franchisor to extend such agreements to franchisees in good standing pretty much upon request.

However, when this franchisee sold the one and only restaurant within the geographical area allocated to him by the Area Development Agreement, he also sold his area development rights to the buyer for an additional \$100,000. The problem was that the Area Development Agreement automatically expired when the original franchisee (the seller) sold out. To add insult to injury, the new franchisee (the buyer) could have obtained the very same Area Development Agreement from the franchisor for the same price paid by his predecessor—i.e., nothing.

Suggested contract wording:

23. EQUIPMENT SATISFACTORY

SELLER herewith warrants that the assemblage of furniture, fixtures, equipment, machinery, small tools, employee uniforms and operating supplies are sufficient and in adequate condition to conduct business in the normal and customary manner as of the date of this agreement with the following exception(s):

SELLER further agrees that he/she will advise PURCHASER in writing of any change(s) in the status of said assemblages prior to the completion of the sale. Upon such advice, if said changes diminish the value of said assemblages by more than \$_____ then all obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

Comment:

Seller representation and warranty.

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Suggested contract wording:

24. INVENTORY GOOD AND SALABLE

SELLER herewith warrants that all the inventory to be included in this transaction is good and salable with the following exception(s): _____

Comment:

Seller representation and warranty.

Suggested contract wording:

25. PURCHASER INSURABILITY

PURCHASER herein represents that to the best of PURCHASER'S knowledge, PURCHASER can obtain insurance and surety bonds both in types and limits approximately the same as SELLER currently has in place and can obtain minimum limits as required by any landlord, franchisor or other entity which has the authority to require the business or business owner to obtain specified insurance coverage.

In the event PURCHASER is unable to obtain said insurance or demonstrate said ability by way of an insurance binder or letter of intent from a bona fide insurance company prior to or at close of escrow, then all obligations herein may, at the election of the PURCHASER or SELLER, terminate and end and the deposit shall be returned to the PURCHASER.

Comment:

Although they are not as frequently encountered in a business purchase offer as seller representations and warranties, there is also a need for some buyer representations and warranties as well. This one is intended to protect the buyer as much as the seller. It forces the buyer to be aware of the requirement to obtain insurance and requires that such action be taken prior to close of escrow.

The best approach for the buyer to complete this requirement is to make contact with a commercial insurance agent early in the acquisition process. In order for this agent to properly assist the buyer, that agent will need copies of the seller's current insurance policies. Additionally, the insurance agent will need a copy of the existing lease or, if a new lease is to be negotiated, the tenant insurance requirements to be included in that lease as well as a copy of the franchise agreement and any other business related contracts which require the business and/or the business owner to carry some specific type of insurance.

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Suggested contract wording:

26. GOVERNMENT APPROVAL—LEGAL NOTICES

SELLER shall obtain any governmental approvals and give any notices required by law or necessary to avoid liens upon the business and/or property sold or legally required as a condition of ownership transfer.

Prior to close of escrow the SELLER shall pay all amounts owed for employment wage taxes and sales taxes and/or make appropriate arrangements to pay said taxes by submitting into escrow proof of obtaining taxing authority clearance in the form a *Clearance Letter* issued by said authorities. In the event SELLER is unable to obtain said clearances prior to or at close of escrow, then all obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

Comment:

This is a “house keeping” section for protection of the buyer. This doesn’t make it unimportant however. It may be that local custom or state law requires that the seller notify his or her creditors of an impending sale in accordance with the bulk sale law. Keep in mind that any unsecured debts of the seller will legally become the debts of the buyer if proper notice is not given to the seller’s creditors (except in Nevada).

Also, in some states, the law requires that notice be posted on the premises if a liquor license is to be transferred from seller to buyer. And, there may be other legal requirements unique to certain industries where some sort of notice must be made. It is always best to consult legal counsel regarding the types of notices that may be required as a condition of ownership transfer.

Suggested contract wording:

27. NONCOMPETITION

SELLER herewith agrees not to compete directly or indirectly with PURCHASER or utilized SELLER’S knowledge, skills or reputation in a way that could negatively impact the profitability of this business subsequent to ownership transfer for a period of _____ years within a radius of _____ miles with the following exception(s) and/or other conditions:

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Comment:

This condition is very prevalent in purchase agreements and depending on the circumstances, a very important aspect of the deal. It is impossible to anticipate all the unique circumstances that may affect any particular transaction. Therefore, it is up to the buyer to “see through” the stated motives of the seller for selling out and identify the real motives if they differ in an attempt to identify any potential threat to the continued profitability of the company the seller may pose.

As a word of caution, it is best for the buyer to not become overly aggressive in structuring the terms and conditions of the not-to-compete agreement. The reason for caution is that should this agreement later be challenged by the seller in court, and should the court find that the limits placed on the seller were too severe, then it has become the custom of some courts to negate the not-to-compete portion of the contract altogether.

Suggested contract wording:

28. SELLER ORIENTATION AND TRAINING

As a condition of PURCHASER acquiring the business described herein and as part of the purchase price, SELLER herewith agrees to assist PURCHASER in affecting as smooth a transition of ownership as possible by making a good faith effort to provide PURCHASER with orientation and training. Said SELLER provided orientation and training shall specifically include and/or exclude the following:

Comment:

It is customary in the vast majority of small business sales that the owner stay on for a period of time after the sale to orient and train the buyer in the operation of the business. Typically this orientation and training period ranges between a couple of weeks and a couple of months, depending upon the complexity of the business and the buyer’s needs. It is also customary that the seller provide this assistance at no additional cost to the buyer. However, it is a matter of judgment on a case by case basis what would constitute an appropriate length of time for the seller to assist the buyer.

Custom however is not law. Nowhere is it stated that the seller has to do this. As a practical matter, the buyer is apt to find a more accommodating seller when that individual has agreed to carry back some portion of the purchase price in a promissory note because, obviously, the seller wants to get paid and is therefore motivated to do everything necessary to ensure that will happen.

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In those cases where the seller receives the entire purchase price in cash at close of escrow, that individual is clearly going to be less motivated to assist the buyer afterwards. If the sale is an all-cash transaction, the buyer should seriously consider including a monetary “hold-back” condition in this section which the escrow officer will release to the seller only after the agreed upon training has been provided. For that matter, even when the seller has accepted a portion of the purchase price in the form of a promissory note, it is not a bad idea to provide similar protection. In every case however, it is wise to define the nature of the training to be provided as clearly as possible. This would include some description of who, how, when, for how long and where.

If the seller requires to be paid for this training, then this cost needs to be considered in the initial valuation analysis of the company and properly reflected in the purchase price because such a fee is essentially a requirement for an additional investment of working capital on the buyer’s part.

On occasion, the buyer may wish to begin the training process before escrow closes. If the ultimate consummation of the transaction is to be predicated on the buyer’s ability to satisfactorily learn how to manage the business during this period or perhaps determine if this is really what he or she wants to do, then the wording of this section must be crafted with extreme care. Such a condition of sale is very dangerous territory. Many sellers will not agree to this arrangement either out of common sense or advice of counsel. Do not be surprised if the seller will not go along with this condition—in most cases it is not a reasonable request.

Suggested contract wording:

29. PURCHASE PRICE OFFSET

All parties to this agreement herein acknowledge that all businesses, including the business subject to this agreement have problems in various stages of development, often unknown or unknowable at any particular moment in time. Therefore, it is the intention of the parties to this agreement that actual losses that would not have been insured under the insurance coverage carried by the SELLER at close of escrow or covered by PURCHASER'S insurance policy resulting from such problems presently unknown to the SELLER which become manifest after transfer of ownership, despite SELLER'S best effort to fully disclose all circumstances of the business, be allocated in a fair and equitable manner.

Therefore, any formerly or currently uninsured losses or expenses of the following nature: [] equipment or facility breakdowns [] other (description attached) sustained by the business within _____ days of ownership transfer which, in the aggregate, are less than [] _____% of the purchase price or [] \$_____ or [] _____% of gross sales revenue shall be borne by the PURCHASER and the SELLER shall be held harmless therefrom. However, any of the above defined losses or expenses which exceed said threshold amount sustained by the business within said time period herein specified shall be borne by the SELLER up to a maximum of [] _____% of the purchase price or [] \$_____ or [] _____% of gross sales revenue to the extent said losses or expenses were not insured at close of escrow or insured by PURCHASER subsequent to close of escrow provided PURCHASER can clearly document such losses or expenses and further provided such losses or expenses occurred through no fault of the PURCHASER, or as a result of vandalism, sabotage, natural disasters or acts of war. Any unexpected losses or expenses sustained after said time period shall be borne entirely by the PURCHASER. Any losses or expenses sustained by the PURCHASER not identified above shall be borne by the PURCHASER upon close of escrow or taking possession of the business, which ever occurs first if not simultaneous, with no right of purchase price offset.

SELLER'S repayment of said losses shall be accomplished by way of an offset to the payments of principal and interest PURCHASER makes to seller which amount shall not exceed _____% of each periodic payment. This repayment plan notwithstanding, said plan shall not serve to negate SELLER'S legal rights to receive payments in accordance with the terms and conditions of the promissory note. Therefore, any amounts held back by PURCHASER shall be deposited into an escrow account maintained by _____ until written instructions for the dispensation of the funds is received by the escrow officer and signed by both SELLER and PURCHASER or by the court.

In the event PURCHASER pays 100% of the purchase price in cash at close of escrow, then the escrow officer is herewith instructed to establish an "offset account" into which _____% of the purchase price shall be held for the purpose contemplated herein. Said offset account shall be maintained until said time period has expired at which time, if no claims are made, the funds in said account shall be turned over to the SELLER. In the event PURCHASER submits a claim against said offset account, an amount sufficient to discharge said claim shall be maintained by the escrow officer until written instructions for the dispensation of the funds is received and signed by both SELLER and PURCHASER or received from the court.

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This paragraph shall in no way negate PURCHASER'S other rights and remedies at law pursuant to any fraudulent misrepresentation or willful withholding of material facts and circumstances of the business by the SELLER.

Comment:

As certainly as the sun will rise in the east and set in the west, soon after escrow closes, one or more pieces of operating equipment in the business just purchased are going to break down. Count on it. Do not be surprised if a key employee quits, the company loses an important account or a new competitor opens up down the street. Murphy's Law seems to operate with a vengeance on nearly every business buyer starting the day escrow closes. Simply put, business is risky—always has been and always will be. This is why the rate of return that investors require from a business investment are so much higher than most other investments—especially income property.

If you have properly researched the industry in which the business you are buying operates and properly researched the unique aspects of this particular business and therewith applied the appropriate capitalization rate to a realistic expected income stream, then you have adequately anticipated these events in the purchase price and will be able to ride them out.

On the other hand, presuming you have conducted a thorough due diligence investigation of the business and further presuming the seller has not disclosed any impending major catastrophe, then in all likelihood the price you pay for the business will reflect the logical additional presumption that the business will perform pretty much into the near future as it has been performing in the recent past. When this turns out not to be the case and a major catastrophe beyond what could normally be expected befalls the business soon after ownership changes hands, then the price paid for the business will have been too much. It does not matter whether or not the seller was aware that this catastrophe, whatever it may be, was about to happen. The fact is it happened and you did not get what you thought you were paying for.

The purpose of this section is to provide for this situation. The colloquial term used to describe this feature of a purchase offer is a "basket" and it serves two purposes. First, it forces the buyer and seller to proactively address the issue of unexpected losses which may be suffered by the business after escrow closes. To a fair degree this helps create a post-transaction environment less prone for acrimony on the buyer's part by forcing the buyer to consciously acknowledge the likelihood that some things are going to go wrong after ownership changes hands and to calmly and objectively anticipate that fact before hand.

Secondly, this provision essentially shifts some of the risk of the unknown back on to the seller. Sellers will not like this provision and can be expected to argue for its exclusion from the contract. Probably the best way to deal with the issue is to try to keep it from being perceived by the seller as an attack on his or her integrity. This is, after all, simply a process of risk allocation, nothing more. Say, "look Mr. Seller, we cannot possibly know as much about this business as you do, even with a thorough due diligence investigation. To a large degree the price we are offering is a reflection of your representations and expectations for this business. If what we get turns out to be something less than what we paid for, we do not believe we should have to suffer all the consequences alone. It is a business risk that should be shared and that is all we are asking of you."

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Of course, it is helpful to have some objective way of establishing the dollar amount above which the seller must begin to “share the pain.” Insofar as equipment failures are concerned, basing the hurdle on two standard deviations above the average monthly cost of repairs and maintenance over the last year times the number of months allowed as the seller’s participation period would probably be a reasonable buyer proposal. (Or, to keep the math a little simpler perhaps X times the monthly average cost might work).

Another very useful purpose for this provision is to provide the buyer protection for post-transaction costs to correct pre-existing violations of all the various governmental regulations under which the business must operate. However, addressing that issue through this section of the contract has some very strong pros and cons.

On the positive side, it sends a wake-up call to the seller to take your due diligence investigation seriously and actively cooperate in attempting to identify any and all regulatory violations that may exist. Usually, when the question is put to the seller about the existence of any violations the response is typically a casual “none.” The fact of the matter, however, is that probably every business is in violation of something. Equally true is the fact that there is probably no business owner in the country who is aware of all the governmental regulations with which he must comply. (For example, the Americans With Disabilities Act specifies the maximum allowable foot-pounds of pressure necessary to open any public access door and also specifies the minimum allowable closure rate for any door with a self-closer mechanism. Who knows this stuff?) Thus, by shifting some of the risk of correcting pre-existing code violations back to the seller, there is apt to be a more careful effort on the seller’s part to uncover and disclose what those violations may be. At that point, the buyer has the option of waiving a requirement to correct them, requiring the violations be corrected, adjusting the purchase price or walking away from the deal.

On the negative side, the act of putting the risk of absorbing the cost to correct pre-existing violations back on the seller is tantamount to requiring the seller to assume a potentially enormous unknown liability. Without some protective maximum cost absorption limits afforded the seller, or some other protective device it is doubtful a seller would ever agree to this provision. For example, a seller may envision a buyer inviting every regulatory body in existence to drop by for a little “look see” after close of escrow.

For this reason, this section provides for a maximum limit to the seller’s potential liability exposure thus shifting the risk of loss beyond the maximum back to the buyer. In all probability the crafting of this section of the agreement may require addressing the exposure to corrective action liability by categories.

As a practical matter, the greatest risk of exposure to requirements to correct violations in small businesses will lie at the local level in most cases. This would be the county health department, fire marshal, building inspection and zoning. Also, some industries are more apt to be in violation of certain regulations than others. For example, it is doubtful a retail dress shop in the local mall would have much exposure to environmental contamination violations whereas a metal plating company that has been in the same location for forty years would likely have substantial exposure to this risk.

Ultimately It is up to the buyer to become as knowledgeable as possible regarding the regulatory environment in which the business operates and conduct the due diligence investigation with benefit of that knowledge. It is also advisable in many cases that the buyer obtain the assistance of experts (for a fee of course) for various portions of the due diligence investigation. There will be little comfort for the buyer who believes this section of the purchase agreement is sufficient protection if the seller is financially unable (or unavailable) to pay any costs which this contract would make the seller’s responsibility.

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For example, I am aware of the sale of a small restaurant with a transaction price of \$25,000. The buyer purchased the restaurant for cash and after close of escrow the health department made the buyer close the restaurant until several code violations were corrected at an estimated cost in excess of \$30,000. The seller disavowed any responsibility for this situation and maintained it was entirely the buyer's problem.

Suggest contract wording

30. PURCHASER DEFAULT

In the event that PURCHASER fails to pay the balance of the purchase price, or to complete the purchase as herein provided, SELLER may, subject to any rights of the Agent herein, retain all amounts paid hereunder as damages for the breach of this agreement by PURCHASER; provided however, that SELLER may take such action as he deems appropriate to recover such portion of the amounts paid hereunder as may be allowed by law. In the event that PURCHASER shall so default, PURCHASER agrees to pay Agent, the commission which Agent is entitled to receive as hereinafter provided. The obligation of PURCHASER to Agent shall be in addition to any rights which Agent may have against SELLER in the event of default. In the event legal action is instituted by any party to this agreement to enforce the terms of this agreement, or arising out of the execution of this agreement or the sale, the prevailing party shall be entitled to receive from the other party a reasonable attorney fee to be determined by the court in which such action is brought.

Comment:

The buyer needs to be fully aware of the fact that, subject to the various contingencies provided in this agreement, by signing this contract he or she has bought the business. Of course, this agreement provides for numerous escape clauses and it's fairly inconceivable that a buyer could not walk away from the deal based on any number of opportunities to do so during the due diligence process. However, as the contingencies are either met or waived, the "noose becomes tighter" so to speak, and eventually, all opportunities to walk away will be gone. At that point, the ability for the buyer to walk away will only be possible with a concomitant forfeiture of the earnest money deposit and quite possibly an obligation to pay any broker involved in the transaction the fee that would have been earned had the deal closed.

It may occur to the buyer to simply omit this section of the contract altogether. Such a tactic may be worth a try but in all likelihood this "oversight" will not be missed by the seller's attorney.

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Perhaps one of the most common reasons a buyer may fail to perform is due to the realization at the last minute that he or she doesn't have enough cash to close the deal and/or invest as working capital. Such a situation is not adequate justification for the buyer to seek mercy from the seller and try to turn back the clock. It is the buyer's responsibility to insure that sufficient cash is available to make the deal work and it is one of the very first considerations a buyer should make when contemplating a transaction. Indeed, this reason for failure to perform is probably the one most apt to raise the ire of the seller and as such, no mercy should be expected.

As part of the analysis of a business acquisition, a buyer should consider not only the cash required for the down payment on the business but all the other demands which will be placed on his or her cash reserves as well. The buyer should anticipate a need to pay for an assortment of licenses and permits depending upon the type of business being purchased such as a business license, health department permit, gaming license and so forth. In addition to this there will be registration fees to be paid on any vehicles purchased as well as a sales tax plus a requirement to make deposits to the Department of Labor for State Disability Insurance, a Sales Tax Deposit (usually accomplished by purchasing a Surety Bond in lieu of an actual cash deposit), lease deposit and utility company deposits. Cash will also be required to pay the buyer's share of escrow fees and attorney fees.

Additionally, a buyer would be well advised to seek some legal and tax accounting advice during the course of the acquisition process as well as some business valuation consultation. If the buyer is buying a franchised business there is likely to be some costs associated with the transfer of the franchise plus travel and lodging expenses connected with the formal training program the buyer may have to attend.

In addition to all the foregoing, the buyer needs to plan for the amount of working capital that will need to be invested in the business. A quick estimate of how much this will be can be made by subtracting the Current Liabilities from the Current Assets on the seller's most recent Balance Sheet. A better method is to develop a weekly cash flow and cash-on-hand forecast for the first six months of operations. From this analysis one should be able to see how much of a cash reserve will be needed at the outset because the amount of cash-on-hand can never drop below zero. That is to say, owning a business is like playing poker: you're profitability can ebb and flow, but when you run out of cash, you're out of the game.

Suggest contract wording

31. WILLFUL FAILURE OF SELLER TO PERFORM

In the event SELLER shall refuse to consummate the transaction contemplated herein or if SELLER, SELLER'S employees and/or agents make any material disclosures or representations to PURCHASER discovered to be false or misleading and/or if SELLER withholds knowledge about facts or circumstances of the business and/or real estate which could reasonably have the affect of diminishing the value of said property of sufficient severity that PURCHASER therewith elects not to consummate the transaction contemplated herein or if SELLER, and/or SELLER'S employees or agents willfully obstruct, fail to reasonably cooperate with and/or reasonably assist PURCHASER when such cooperation and/or assistance is necessary or otherwise interfere with PURCHASER'S good faith efforts to consummate the contemplated transaction according to the terms, conditions and spirit of this agreement or if SELLER solicits other purchase offers for the business after signing this agreement and/or negotiates with the parties making a purchase offer, or if SELLER sells, leases, otherwise disposes of the business and/or real property to another party during the Hold-Off-Market time period specified in Paragraph 2 above or if the SELLER misrepresents his or her authority and/or authorization to enter into and/or consummate this agreement or takes other actions which makes the contemplated transaction impossible to consummate during the term of this agreement or if SELLER is unable to deliver all assets and real property to the PURCHASER free of any liens or encumbrances (with the exception of those liens and encumbrances identified above which PURCHASER has agreed to accept) then SELLER shall pay PURCHASER [] an amount equal to the amount PURCHASER has deposited in escrow or [] \$_____ at the time PURCHASER shall demand same in writing. Additionally, upon such demand, all obligations herein will terminate and end and the deposit shall be returned to the PURCHASER.

Said payment to PURCHASER for SELLER'S failure to perform provided herein shall have no affect on any other agreement SELLER may have with SELLER'S and/or PURCHASER'S Agents to pay said Agents a fee or commission for duties performed and/or services rendered despite SELLER and PURCHASER'S failure to consummate the contemplated transaction.

Comment:

Provision of this condition in very large business transactions is common. It is known as a seller "bust up" fee. Generally, however, it is not commonly encountered in small business transactions. But there is ample reason why it should be. Unlike the sale of almost anything else, the attempted sale of businesses are occasionally ended in mid-course by the seller. Considering the time, effort and money a buyer will expend pursuing an acquisition, it is not unreasonable for the buyer to seek compensation when the seller suddenly calls the deal off.

Additionally, this section of the contract provides a rather strong incentive for the seller to cooperate and appropriately assist the buyer in his or her due diligence investigation and, not lie or intentionally withhold material facts about the business. It also puts the seller on notice regarding the need to be able to provide clear title to the operating equipment. In

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many cases, at the time this agreement is signed the seller will not have clear title. This sets the clock ticking on the seller accomplishing this task or if there will not be sufficient money passing from buyer to seller to clear any liens, then to stop the process at this point and not waste any more of the buyer's time.

This section is an attempt to create a more level playing field inasmuch as the buyer has placed an earnest money deposit at risk which will be lost should the buyer fail to perform. Why shouldn't the seller be held to the same standard? Moreover, given the fact the purchaser has taken him or herself "out of play" so to speak regarding an ability to purchase another, perhaps more attractive business, once this contract has been signed, why shouldn't the seller be equally tied up? Again, the buyer's due diligence investigation is going to require a great deal of the buyer's time, effort and money and therefore it is not unreasonable for the buyer to feel assured the rug will not be pulled out from under his feet at the last minute.

Having said all this, the fact remains that the seller has not really put any money at risk to the same extent as has the buyer. No money has been required to be placed in escrow although such a condition could be added but it is unlikely a seller will agree to this request.

Additionally, the notion of making the seller's penalty for failure to perform an amount equal to the buyer's earnest money deposit is based on the theory of fairness. One could make this amount anything, but there is the risk that asking too much could be considered excessive by the court if challenged and possibly struck down.

Suggested contract wording:

32. SALE PRICE ALLOCATION

For purposes of compliance with Internal Revenue Code Section 1060 and completion of IRS Form 8594 the purchase price shall be allocated as follows:

| | | |
|-------------------------------|-----------------|--------------------------------------|
| Accounts Receivable | \$ _____ | (plus or minus adjustment at C.O.E.) |
| Inventory | \$ _____ | (plus or minus adjustment at C.O.E.) |
| Work in Progress | \$ _____ | (plus or minus adjustment at C.O.E.) |
| Finished Goods | \$ _____ | (plus or minus adjustment at C.O.E.) |
| Operating Supplies | \$ _____ | |
| Land | \$ _____ | |
| Building | \$ _____ | |
| Equipment & Machinery | \$ _____ | |
| Vehicles (total) | \$ _____ |list each vehicle separately |
| Customer List | \$ _____ | \$ _____ |
| Secret Manufacturing Process | \$ _____ | \$ _____ |
| Proprietary Software | \$ _____ | \$ _____ |
| Trade Name/Trade Mark | \$ _____ | \$ _____ |
| Covenant Not to Compete | \$ _____ | \$ _____ |
| Seller's Consulting Agreement | \$ _____ | \$ _____ |
| Franchise Agreement | \$ _____ | \$ _____ |
| Other | \$ _____ | \$ _____ |
| Goodwill (Balance of Price) | \$ _____ | \$ _____ |
| TOTAL | \$ _____ | |

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Comment:

There is a legal requirement that both the seller and the buyer file IRS form 8594 with their next tax return subsequent to the sale or purchase of a business. In many cases determining how to allocate the purchase price for this purpose is more than a small detail.

The allocation of the purchase price has everything to do with the taxes the seller will have to pay out of the sale proceeds as well as establish the tax shelter limits the buyer can obtain from depreciable assets. Generally the seller will want to minimize the amount of the purchase price allocated to the machinery and equipment and maximize the amount allocated to goodwill. The buyer on the other hand will want to do the exact opposite. This aspect of the transaction is one most in need of review by a CPA because it is highly complex and needs the careful attention of an expert.

As a practical matter, it would appear the “fairest” point of departure is to allocate an amount of the purchase price to the fixed assets equal to their estimated fair market value—defined as the cost to replace each piece of equipment with an identical piece the same age and in the same condition, delivered and installed. But, this is only a suggested point of departure. Generally, the tax savings available to the seller from allocating a lower value to the fixed assets will be greater than that available to the buyer from a high allocation. Thus, it would not be unreasonable for the parties to “split the difference” by making a low allocation accompanied by an appropriate purchase price reduction.

One of the seller’s assets for which no price allocation provision has been included above is leasehold improvements. Recall the discussion earlier about the fact that a seller does not legally own those improvements. Given this fact, then without regard to the consideration given them in the valuation analysis, it doesn’t make sense to allocate any of the purchase price to them because the seller doesn’t own them. This may seem like a trivial detail because, from the Internal Revenue Service’s viewpoint, it doesn’t matter one way or the other if any allocation is made to this asset. The reason this should be avoided is because it may leave the door open later for the buyer to attempt to recover the portion of the purchase price allocated to the leasehold improvements under the legal theory that the seller sold something he or she didn’t own. Thus, from the seller’s point of view, why leave this door open when there is no need to?

Because the allocation of the purchase price is such a complex area of federal tax law, it has created much confusion among buyers and sellers. Getting into any more detail about this issue is beyond the scope of this book. However, there are two matters that probably warrant some discussion.

The first has to do with the actual purchase price to be allocated when the buyer assumes some of the seller’s debts. The Internal Revenue Service considers the price paid in cash and notes *plus* all seller debts assumed by the buyer as the “Actual Deemed Sale Price.” Thus, when completing IRS form 8594, amount to be allocated will be the actual deemed sale price. [See IRS Reg. 1.338-3(d)(1)]

The second has to do with misapprehending the allocation process as a *valuation* process. How the value of the assets are allocated on form 8594 has absolutely *nothing* to do with how the value of the business was determined in the first place. Determining the value of the business must, of necessity, come first. In that process, as demonstrated earlier, various values were appended to the assets including goodwill. In that process, there was no consideration of the Covenant Not To Compete or a Seller Consulting Fee for example. These are purchase price *allocation tactics* necessary for tax and legal considerations. Thus

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the amount allocated to goodwill on form 8594 may be something altogether different from what that actual value was originally determined to be. Likewise, even though it has been previously stated that it is customary for the seller to provide the buyer with some training and orientation for no charge subsequent to ownership transfer, the allocation of the purchase price may include an allowance for this activity nonetheless. Again, this is simply a *price allocation* tactic for tax purposes. By assigning some portion of the purchase price to this allocation category does not somehow mean that the buyer must now pay the seller additional money. This would only be true *if* post-purchase seller compensation was included as part of the purchase offer and specifically identified as such in the agreement.

Business valuation and business purchase price allocation are separate specialties each requiring specialized training and experience and practitioners in one field may not be qualified to delve into the other.

Suggested contract wording:

33. ESCROW OFFICER

Purchaser herewith directs that the escrow company/escrow officer who shall manage the escrow function for this transaction shall be _____.
All fees payable for escrow services shall be paid _____% by buyer and _____% by seller.

Comment:

Selection of the escrow officer in the transaction is always the prerogative of the buyer. There are two areas of concern here. First, it is wise to select an escrow officer who is familiar with business transactions. This is a complex task and often beyond the ability of someone who's experience has largely been limited to residential and commercial real estate. It is wise for the buyer to either seek recommendations or interview several such individuals before making a decision.

Second, when submitting the seller or seller's agent with an earnest money deposit, it is probably not a good idea to make an earnest money deposit payable to the seller or seller's agent (or seller's agent's trust account). It is highly advisable to make the earnest money deposit out to the title company wherein resides the escrow officer who is to handle the escrow responsibilities.

Suggested contract wording:

34. PURCHASE AGREEMENT AND BILL OF SALE

Ownership transfer of this business shall be accomplished by way of a definitive Purchase Agreement and Bill of Sale. The requirement to execute said definitive Purchase Agreement notwithstanding, the parties to this Agreement herewith agree that in the event any term or condition or the interpretation of any term or condition or the intent of any term or condition in said Purchase Agreement may be in conflict with this Agreement, then in such case, this Agreement shall control in any disputes arising therefrom. Selection of the attorney who shall draw up the Purchase Agreement and Bill of Sale shall be made by Seller; Purchaser; Seller and Purchaser together; Escrow Officer. The cost to develop the Purchase Agreement and Bill of Sale shall be paid by Seller; Purchaser; Seller and Purchaser and apportioned ____% to Seller and ____% to Purchaser.

Comment:

The intent of the Purchase Offer form presented here is to serve as Phase Two of a three-step process. Phase One being informal, non-binding discussions with the seller, Phase Two being the bilateral execution of this agreement and Phase Three the execution of the Purchase and Sale Agreement.

Not everyone agrees this is the best course of action. There is one opposing school of thought holding that the process should take place in two phases: informal discussions and execution of the Purchase and Sale Agreement.

There is yet another school of thought that believes the process should be single phased; that is, execution of the Purchase and Sale Agreement not preceded by informal negotiations. This second alternative is the approach used in the sale of residential real estate. Typically, submission of the Purchase Offer and Acceptance form is the first time a seller finds out how much a buyer is willing to pay for a home and what other terms and conditions a buyer requires. If the seller finds the offer acceptable and signs it, the transaction is therewith fully consummated because the “purchase offer” *is* the Purchase and Sale Agreement. If the initial offer or other terms are unacceptable to the seller, the seller submits a counter offer which becomes appended to the original offer. If the buyer accepts by signing the counter offer, the transaction is legally consummated and the two contracts combined become the Purchase and Sale Agreement. If the buyer objects to something in the counter offer then a counter-to-the-counter-offer is tendered and all three documents combined become the Purchase and Sale Agreement. This process can, in theory, go on indefinitely with the legally binding Purchase and Sale Agreement being the sum of the combined terms and conditions of all the counter offers appended to the original Purchase Offer and Acceptance Agreement. Although this is standard operating procedure in residential real estate sales and seems to work fine, it has no place in business transactions.

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The only two viable options will be either the two phased approach or the three phased approach recommended here. The principal objection to the three phased approach is that the third phase becomes an opportunity to reopen negotiations after all the issues were believed to have been put to bed in phase two. This is a legitimate objection.

On the other hand, the principal objection to the two phased approach is that it requires the active involvement of both parties' attorneys once the informal negotiations have been completed which can become very expensive. Therefore, the intent of the approach presented here is an attempt to create sort of a hybrid cross between a two phased and three phased approach combining the advantages and eliminating the disadvantages of both.

This is to say, this Purchase Offer form can be completed in large part, if not entirely by the buyer without the involvement of an attorney or CPA if one so desires. This is why the form has been developed in a "check the box/fill in the blanks/line out the non-applicable" format. However, such a form once completed would be quite awkward and pretty much unacceptable as the official Purchase and Sale Agreement. Thus, once fully executed, this form is intended to serve as the basis for the development of a "clean" definitive Purchase and Sale Agreement not littered with lined out paragraphs and discarded contract options. At the same time however, the wording of section 34 includes the following statement:

The requirement to execute said definitive Purchase Agreement notwithstanding, the parties to this Agreement herewith agree that in the event any term or condition or the interpretation of any term or condition or the intent of any term or condition in said Purchase Agreement may be in conflict with this Agreement, then in such case, this Agreement shall control in any disputes arising therefrom.

By including the preceding sentence, the door is closed to making changes or deletions to the agreement as it exists but leaves the door open for either party's attorney to make additions which should be anticipated—but not necessarily agreed to. Keep in mind that your attorney's principal objective will be to protect your interests. This is as it should be but there are two dangers here. First is that attempts to further insulate you from possible harm may give rise to your attorney suggesting additions which the seller finds unacceptable and kill the deal—especially in this case where there is likely to be a strong perception in the minds of both parties that the deal *has been made*. It is important for you to make clear to your attorney that your ultimate objective is to *make a deal* and therefore, not put what has been accomplished to date at risk unnecessarily. Additionally, the process of making marginally necessary additions as "trial balloons" and further allowing your attorney and the seller's attorney to pass these drafts back and forth can get extremely expensive. Thus, by using the Purchase Offer form presented here with the principals to the transaction working things out before bringing in an attorney, hopefully the legal costs associated with the transaction can be kept to a minimum.

Granted, this is not a perfect solution. But at least the approach presented here has been done so with an attempt to minimize or at least maintaining some control over legal costs in mind. However in no case should the preceding be interpreted to mean that this process should be attempted without obtaining legal advice altogether. No purchase offer form or any other contract or agreement connected with the purchase or sale of a business should be signed without advice of counsel.

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Suggested contract wording:

35. OTHER TERMS AND CONDITIONS

Comment:

Undoubtedly there will be unique circumstances in most transactions that will require special treatment. No printed form can anticipate every situation. Neither is it practical to use a “check box” approach to address situations that occur only occasionally. The purpose of this section is to provide for these special needs.

Suggested contract wording:

36. TIME IS OF THE ESSENCE

Time is of the essence of this agreement. The term “days” as used herein means calendar days unless otherwise specified.

Comment:

This is a “house keeping” clause necessary to avoid any ambiguity regarding the many instances in this contract where time deadlines have been expressed in terms of days.

Suggested contract wording:

37. EXPIRATION

This offer shall expire unless a copy hereof with SELLER’S written acceptance is delivered to the PURCHASER or to his agent on or before _____o’clock []AM; []PM on _____.

SELLER warrants the accuracy of the information after due inquiry by dating and signing the attached documents and statements.

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Comment:

The amount of time the buyer affords the seller to consider the purchase offer has some tactical implications. If you do not allow reasonable time for the seller to consider the offer it will almost certainly not be signed and returned. This is a stressful time for the seller and any perception of being forced to move too fast will likely cause the seller to suspect the buyer is being deceptive in some fashion and therewith back away—perhaps permanently.

On the other hand, the time period allotted for a response is the time the seller has to “shop the offer.” Thus, it’s a judgment call how much time to give the seller to respond. Keep in mind that the seller has probably been obtaining some professional advice throughout the informal negotiation period. If all the terms and conditions included in the offer have been discussed informally, then the time necessary for the seller to respond at this point should not be great. If, however, many of the terms and conditions in the offer have not been previously discussed then the seller will need more time.

Ideally, by the time this purchase offer is presented to the seller, there will be *no surprises*. Everything appearing on the document will have been discussed in advance and the parties will have come to an agreement before hand.

If it is not accepted, but the reasons are known and can be worked out, don’t try to append amendments to this agreement—start over. Remember, this form was not developed to be used in the offer/counter-offer/counter-to-the-counter-offer format.

Appearing perhaps as something as an after thought, is the sentence wherein the seller warrants the accuracy of all documents attached to the signed and accepted purchase offer as accurate “after due inquiry.” This is a subtle but important aspect of the entire agreement. In places here and there in this contract the seller has been required to make representations and warranties based either on “the best of seller’s knowledge,” or “after due inquiry.” Legally, “after due inquiry” is a much higher standard to which the seller is being held. Where ever possible, it will be to the buyer’s advantage to obtain “after due inquiry” language in the contract.

Suggest contract wording

38. ACKNOWLEDGMENTS

PURCHASER acknowledges receipt of a copy of all pages of this agreement. Purchaser acknowledges that he/she has not received or relied upon statements or representations made by the agent which are not herein expressed, including any statements or representations regarding the effect of this transaction upon PURCHASER’S Tax Liability.

Comment:

This is a business broker protection clause.

Suggested contract wording:

39. AGREEMENT SUBJECT TO REVIEW

This agreement is subject to the review of PURCHASER'S and SELLER'S advisors including but not limited to their respective attorneys, CPA's, insurance agents and lenders. Upon said review, any of said advisors objections to any terms or conditions of this agreement shall be presented to the opposite party in writing and submitted into escrow whereupon, all obligations herein may, at the election of the party who's advisor has submitted said objection(s) terminate and end and the deposit shall be returned to the PURCHASER.

Additionally

PURCHASER makes this agreement subject to the review of the following parties whose approval shall be limited to the identified specific issues:

Upon review, any objections to any terms or conditions of this agreement identified by said party shall be presented to the opposite party in writing and submitted into escrow whereupon all obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

SELLER makes this agreement subject to the review of the following parties whose approval shall be limited to the identified specific issues:

Upon review any objections to any terms or conditions of this agreement identified by said party shall be presented to the opposite party in writing and submitted into escrow whereupon all obligations herein may, at the election of the SELLER terminate and end and the deposit shall be returned to the PURCHASER.

If no written objection by either party's advisor(s) is received and presented to the other party to this transaction and entered into escrow within _____ days of the date of this agreement, then said failure to object shall be deemed as an approval of said advisors for purposes of this section of this agreement.

Comment:

This is the ultimate escape clause for both seller and buyer. However, it is not a "get out of jail free" card. It requires that any objections be put in writing. Because of the liability that will be incurred by any advisor who enters a written objection, it is unlikely an advisor will so object for anything except clearly substantive reasons. Therefore, it is highly advisable to allow all your advisors to review this agreement *before* you sign and submit it.

If either party identifies additional individuals whose approval is required as a condition of consummating this agreement, be careful not to be frivolous with the reasons for withholding that approval; they may not withstand court testing.

Making a Small Business Purchase Offer

Suggested contract wording:

OFFER

The undersigned PURCHASER hereby submits this offer and agrees to purchase the business described herein for the price and terms subject to the additional conditions and contingencies specified.

FEES AND COMMISSION

PURCHASER

hereby acknowledges that (name of brokerage company) and (name of agent) is his/her/their Agent of Record for this transaction, represents their interests exclusively and agrees to pay Agent as provided in the [] Buyer's Broker Employment Agreement [] Other: _____

for services rendered. In the event that PURCHASER defaults and fails to complete the sale, Agent shall be entitled to receive one-half of PURCHASER'S deposit, but not more than the commission earned, without prejudice to Agent's rights to recover the balance of the commission from PURCHASER. In the event that SELLER has been deemed to have willfully failed to perform or is found to have engaged in any of the actions defined within Section 31 herein, then SELLER shall be liable to pay Agent one-half of SELLER'S "bust-up" fee as provided in Section 31 but not more than commission earned, without prejudice to Agent's rights to recover the balance of the commission and fees from SELLER. The mutual rescission of this agreement by PURCHASER and SELLER shall not relieve said parties of their obligations to Agent hereunder. In the event legal action is instituted by Agent against SELLER or PURCHASER or both to collect the commission and other fees due, or any portion thereof, then said defendant(s) agree to pay the Agent such additional sum as the court may adjudge. This agreement shall not limit the rights of Agent provided for in any other agreement which may be in effect between SELLER or PURCHASER and Agent.

Agent _____
Signature Date Time

Broker _____

PURCHASER _____
Signature Date Time

PURCHASER _____
Signature Date Time

Comment:

Once this agreement has been completed, the buyer and if represented by an agent, the buyer's agent additionally, will then sign it and deliver it to the seller. This is the point of

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no return for the buyer. Once it has been signed, only the seller has the power to terminate the transaction at this point by refusing to sign. If the seller signs, you have bought the business, subject to all of the preceding contingencies of course.

Suggested contract wording:

ACCEPTANCE

The undersigned SELLER accepts the foregoing offer and agrees to sell the business described herein for the price and on the terms and conditions herein specified. The undersigned SELLER hereby covenants that he is the owner and/or President of the above mentioned business and has the legal right to sell same as evidenced by a Corporate Resolution to Sell, attached hereto and made a part hereof if this business is a corporation.

FEES AND COMMISSION

SELLER

hereby acknowledges that (name of brokerage company) and (name of agent) is his/her/their Agent of Record for this transaction, represents their interests exclusively and agrees to pay Agent as provided in [] SELLER'S Listing Agreement

[] Other: _____
for services rendered. In the event that PURCHASER defaults and fails to complete the sale, Agent shall be entitled to receive one-half of PURCHASER'S deposit, but not more than the commission earned, without prejudice to Agent's rights to recover the balance of the commission from PURCHASER. In the event that SELLER has been deemed to have willfully failed to perform or is found to have engaged in any of the actions defined within Section 31 herein, then SELLER shall be liable to pay Agent one-half of SELLER'S "bust-up" fee as provided in Section 31 but not more than commission earned, without prejudice to Agent's rights to recover the balance of the commission and fees from SELLER. The mutual rescission of this agreement by PURCHASER and SELLER shall not relieve said parties of their obligations to Agent hereunder. In the event legal action is instituted by Agent against SELLER or PURCHASER or both to collect the commission and other fees due, or any portion thereof, then said defendant(s) agree to pay the Agent such additional sum as the court may adjudge. This agreement shall not limit the rights of Agent provided for in any listing or other agreement which may be in effect between SELLER or PURCHASER and Agent.

SELLER _____
Signature Date Time

SELLER _____
Signature Date Time

Comment:

Assuming the seller finds that all is well with the purchase offer, by signing this agreement, the transaction, save for one technicality, has been consummated.

Fees and Commissions

A very conspicuous portion of this and the preceding section deals with the issue of the broker's fee or commission which must be paid at close of escrow. In some contracts,

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whatever that fee or commission may be is spelled out in this section. This custom has not been carried forward here. Instead, reference is made to the fee or commission payable as spelled out in the pre-existing seller's Listing Agreement or Buyer's Broker Employment Agreement which should be submitted into escrow by the broker along with this agreement. This has been done in order to prevent any inclination by the buyer or the seller (or their respective attorneys) to try to renegotiate that fee at this point.

Unfortunately, just this sort of event has been known to happen in more than a few transactions. This is not the time for the parties, in particular the party who must pay the fee, to try to change it. The time to negotiate the broker's fee is prior to the time that employment agreement is signed. An attempt to reduce the fee at this point by suggesting the deal will not close otherwise is likely, in the vast majority of instances, to result in the deal not closing. This is dangerous territory and if the principals truly want the transaction to be consummated, the broker's fee should not be made an issue other than, perhaps, the buyer and seller exploring some way to share this cost if need be.

Various business brokerage books go into some detail on this problem. Based on that literature it would appear the proclivity to tamper with the broker's fee resides often with one or the other principal's attorneys. The principals to the transaction should be sensitive to this tendency and be aware that consummation of the transaction is being put at great risk should this occur. In addition to the danger of "cratering" a deal over an objection to the size of the fee due a broker, the business brokerage literature points out that principals along with their attorneys who have engaged in this tactic have been successfully prosecuted under the RICCO (Racketeering Influence & Corrupt Organizations Act) and suffered *triple damages* for an attempt to defraud the broker of a legitimately earned fee. Also, a broker may be able to obtain *punitive damages* in addition to the previously awarded triple damages previously awarded under RICCO.

Suggest contract wording

| | | | |
|--|-------|-------|-------|
| The undersigned PURCHASER hereby acknowledges receipt of the accepted agreement | | | |
| PURCHASER _____ | _____ | _____ | _____ |
| Signature | Date | Time | |
| PURCHASER _____ | _____ | _____ | _____ |
| Signature | Date | Time | |
| PURCHASER _____ | _____ | _____ | _____ |
| Signature | Date | Time | |

Comment:

The one remaining technicality necessary to have a fully executed contract is the requirement that the buyer acknowledge receipt of a copy which the seller has signed. Upon obtaining this additional signature of the buyer, the contract is in full force and effect.

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Corporate Resolution to Sell

whereas, _____ President of _____ Corporation doing business as _____ does hereby certify that at a combined meeting of the stockholders and directors of the Corporation duly called and held at the office of the Corporation on _____ 19____ wherein a quorum of the stockholders and directors were present and voting throughout, it was upon motion duly made and seconded, that the corporation would endeavor forthwith to find a buyer for the Corporation's Assets.

Upon finding such buyer, the Corporation will make every reasonable effort to negotiate a price in cash and other valuable consideration in exchange for all or the majority of the Corporation's tangible assets, intangible assets and goodwill acceptable to the stockholders and directors and upon a meeting of the minds of said buyer and the Corporation, the Corporation will therewith affect a transfer of the Corporation's Assets to the buyer for said cash and other valuable consideration as soon as practicable.

Upon finding such buyer, the Corporation will make an assignment of any leases on Real Estate and/or Chattel owned by the Corporation for cash and other valuable consideration and upon terms acceptable to the stockholders and directors further provided, however, that the owners of such Real Estate or Chattel agree to such assignment of said lease(s) and further provided that if said owners of Real Estate and/or Chattel leased to the Corporation require the Corporation to remain on as guarantors of said contracts as a condition of assignment to said buyer that the Corporation will make such guarantee.

If the terms of the buyer *exclude* the purchase of all or any portion of Real Estate owned by the Corporation that, notwithstanding such exclusion, the Corporation will sell all or the majority of the Corporation's tangible assets, intangible assets and goodwill excluding any Real Estate owned by the Corporation and furthermore will, if so desired by the buyer, lease the Real Estate owned by the Corporation to the buyer of the Corporation's Assets for cash and other valuable consideration upon terms acceptable to the stockholders and directors.

If the terms of the buyer *include* the assumption of any debts or other liabilities of the Corporation, that the Corporation will transfer such debts or other liabilities to the buyer for a reduction in the cash and other valuable consideration the buyer would otherwise pay for the Corporation's Assets at an exchange rate acceptable to the stockholders and directors further provided, however, that such debt holders affected by said transfer agree to such assumption by the buyer of the Corporation's debts and other liabilities.

It is anticipated that the sale of the Corporation's Assets or Liabilities will be as a Bulk Sale of Assets and therewith will not involve the sale or exchange of the Corporation's stock. However, should a buyer wish to purchase all or a controlling percentage of the corporation's outstanding stock as opposed to the corporation's assets, or merge the corporation into another corporation, the approval for such action is herewith stipulated in this resolution _____, in their capacity as _____ of the Corporation be empowered, authorized and directed to execute, deliver and accept any and all documents and undertake all acts reasonably required or incidental to accomplish the foregoing resolution, all on such terms and conditions as they in their discretion deem to be in the best interest of the Corporation.

Upon the motion duly made and seconded the forgoing resolutions were passed unanimously by a vote of all stockholders present, such stockholders representing a quorum as defined in the By Laws of the Corporation.

I further certify that said resolutions are in full force and effect without rescission, modification or amendment.

By the Board of Directors, this resolution is adopted this _____ day of _____ 19____

President of the Corporation

Comment:

This is the Corporate Resolution to Sell which must be submitted to the buyer along with the Purchase Offer form if the subject company is a corporation.

The Purchase Offer Form Completion Instructions

The Purchase Offer form presented here has been designed as a “check the box/fill in the blank/line out the inapplicable” format. Thus, to avoid any misunderstanding, one should check the appropriate box *and* line out the unused alternative selections. For example if it is intended the Seller should take some action or be responsible for some condition, the form should be completed as follows:

Purchaser, Seller, Purchaser and Seller together, Other _____
Shall take the following action...

If there is a section of the contract which does not apply, strike out that section and inscribe your initials in the margin adjacent to it. For example, if there will be no earn out made a part of this agreement then do the following:

~~Plus and additional contingency payment or “Earn Out” payment in an amount and/or payment method to be determined as follows:~~

~~Minus an adjustment to future payments in an amount and/or to be determined as follows:~~

In those cases where the contract calls for a description of specific exceptions or exclusions to a preceding statement of agreement and there are none, then write in “none.”
For example:

The foregoing terms and conditions shall apply in all cases subject to the following specific exclusions: **None**

In those instances where there is not enough space to write in the terms or conditions to which the parties have agreed, make reference to an attached exhibit instead. For example:

This purchase price shall include all the seller’s furniture, fixtures, equipment and operating supplies currently used in the business but specifically excluding the following:

See Exhibit 2 attached hereto and made a part hereof

BUSINESS PURCHASE OFFER AND DEPOSIT RECEIPT

Notice: This is a binding legal contract and all parties to this agreement are herewith advised to have it reviewed by their attorney, CPA, insurance agent and lender before signing. Real estate agents are not allowed to give legal, tax or insurance advice. By signing this contract the parties herewith agree to indemnify and hold agent harmless from disputes or damages that may be created hereby.

Whereas _____
hereinafter known as PURCHASER wishes to purchase the business and/or real property known as _____

and

Whereas _____
who is/are
 the owners
 the Corporation President acting on behalf of the stockholders

hereinafter known as SELLER wishes to sell this business and/or real property

Now Therefore, PURCHASER herewith tenders an offer to purchase said business and/or real estate under the following terms and conditions. PURCHASER further stipulates and the parties herein agree that this Purchase Offer and Deposit Receipt is intended to represent an Exclusive Option To Purchase said business and/or real estate, for the time period specified hereunder and shall not be construed as a Purchase and/or Sale Agreement.

Received from _____ hereinafter designated as PURCHASER
the sum of \$ _____ (_____ Dollars)
evidenced by Personal Company Cashier's Other check payable to _____

as an earnest money deposit to be applied toward the purchase of the business described herein.

The purchase price for the business business and real property described herein shall be \$ _____ (_____ dollars)

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Plus any additional contingency payment or "Earn Out" payment in an amount and/or payment method to be determined as follows:

Minus an adjustment to future payments in an amount and/or to be determined as follows:

for the business known as _____

situated in the State of _____ City of _____, County of _____

located at _____

This transaction shall be a purchase of the seller's assets; corporate stock

This purchase price shall include all the seller's furniture, fixtures and operating equipment currently used in the business but specifically excluding the following:

The purchase price shall include all the seller's goodwill comprised of everything customarily included in such definition such as (but not limited to) Company d/b/a name, trademarks, all phone numbers, fax numbers, e-mail address, customer lists, customer accounts, computer data bases, current files, current operating records, contacts, proprietary software, secret processes/recipes, patents, distributorship rights and agreements and all other such assets with the exception of the following specific exclusions:

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This purchase price also:

includes; does not include the real property in/on which the business operates which is also owned by the seller (if applicable)

includes; does not include an allowance for salable inventory valued at \$ _____; said value to be determined as stipulated in item number 4 below.

includes; does not include an allowance for work in progress and finished goods valued at \$ _____; said value to be determined as stipulated in item number 6 below.

includes; does not include an allowance for accounts receivable valued at \$ _____

includes; does not include the seller's lease deposit of \$ _____

The aggregate cost to transfer/assign any and all Franchise Agreements, Dealership Agreements, Distributorship Agreements, or other contracts or agreements in the amount of \$ _____ is:

included in the purchase price and shall be paid by SELLER.

not included in the purchase price and shall be paid by PURCHASER as an additional expense of PURCHASER above and beyond the purchase price

includes; does not include other current assets valued and described as:

SELLER shall; shall not deliver to PURCHASER the operating cash on premises in SELLER'S cash register(s) and/or office safe at close of escrow in the amount of \$ _____. The purchase price shall; shall not be increased by said amount of operating cash. If SELLER is to deliver said operating cash to PURCHASER, then a physical count of the cash on hand shall be made by buyer and seller together designee of seller; designee of buyer; designee of buyer and seller; other: Describe _____ immediately prior to close of escrow. The cost of counting the operating cash shall be paid by Seller; Buyer; Buyer and Seller and apportioned _____% to Seller and _____% to Buyer.

This purchase price shall not include SELLER'S cash held in any bank accounts nor shall it include any seller near-cash assets such as (but not limited to) marketable securities, Certificates of Deposit, bonds, notes receivable, etc., with the exception of the following which shall be included for the purchase price stated herein:

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The above stated purchase price shall be paid:

100% in cash at close of escrow As modified by Section 20-B below

\$_____ down payment (which shall include all sums deposited in escrow prior to closing

plus all amounts to be paid subject to Section 20-B below, plus:

PURCHASER shall execute a Promissory Note to the benefit of the SELLER in the amount of \$_____ to be paid in monthly; quarterly

other _____ installments bearing interest of _____% per year for _____ years plus _____ months _____ quarters _____

Said payments, including principal and interest shall be \$_____. Additional terms and conditions of this Promissory Note shall be:

Commencement of the note payments shall be _____ and all subsequent payments shall be due on the _____ day each month; quarter;

other (describe) _____ thereafter.

all assets purchased shall be pledged as security for payment of the note.

Purchaser shall personally guarantee payments in addition to pledging the assets to be purchased.

Said note shall carry a late charge of \$_____ if payment is not received within _____ days of the due date.

Said note shall; shall not be due on sale of business by PURCHASER.

A default on payment of the premises lease shall constitute a default on the Promissory Note

SELLER herewith agrees to allow PURCHASER to assign the note to a subsequent purchaser under the following terms and conditions:

Other (describe)

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PURCHASER shall assume debts and other liabilities of the SELLER with an aggregate value of \$_____ and shall pay same when due unless otherwise indicated herein. Said liabilities are herewith itemized below as:

the following liabilities, accounts payable, debts, customer deposits, prepaid accounts, wages payable, vacation pay payable, commissions payable and subscriptions and promissory notes payable which represent unsecured SELLER liabilities:

Promissory Notes Payable secured by assets subject to liens as reflected on form UCC1 on file with the Secretary of State provided the lien holders shall agree to such action. In the event the lien holders shall not agree to such action or will do so only upon terms or conditions unacceptable to either PURCHASER or SELLER then all rights and obligations herein may, at the election of the SELLER or the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER. Said Promissory Notes to be assumed by buyer are herewith described as:

Not less than 10 days prior to close of escrow:

Escrow Officer

Purchaser

shall notify all creditors by certified mail of the intended sale of the business and advise said creditors of SELLER'S intention to pay off all secured and unsecured liabilities, accounts payable, debts, customer deposits, prepaid accounts and subscriptions and promissory notes payable not assumed by PURCHASER and invite said creditors to submit claims for payment in full into escrow. The escrow officer is herewith instructed to hold back an amount of money sufficient to pay all such debts and to make said payment to said creditors for all undisputed debts of the seller from the escrow account. The escrow officer is herewith instructed to hold back an amount of money necessary to pay off all disputed liabilities of the seller until said dispute is resolved and only upon resolution of said dispute in accordance with applicable law shall the escrow officer pay off said liabilities and turn over any remaining cash to seller.

The above defined liabilities and debts to be assumed by Purchaser shall be:

Calculated as a deduction from the actual cash and promissory notes and the earn-out agreement to be deposited into escrow by Purchaser for benefit of Seller such that said cash, notes and earn-outs *plus* all liabilities and debts to be assumed by PURCHASER described herein shall equal the purchase price.

or

An addition to the purchase price such that the Actual Deemed Sale Price shall be the sum of the purchase price *plus* all assumed liabilities and debts described herein.

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In the event the debts and other liabilities PURCHASER agrees to assume as a condition of this sale differ at Close of Escrow from the amounts stated above, then the down payment and/or the amount of the promissory note shall be adjusted to reflect said difference(s) as follows:

The down payment shall be increased or decreased as the case may be by an amount not to exceed \$_____

The promissory note shall be increased or decreased as the case may be by an amount not to exceed \$_____

In the event any required adjustment in the amount of the down payment and/or face value of the promissory note must exceed the limits specified herein in order to offset changes in the levels of debt PURCHASER has agreed to assume in order to equate the sum of said cash, face value of promissory notes and assumed debt to the purchase price, then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

This purchase offer is contingent upon PURCHASER obtaining third party financing in the amount of \$_____. PURCHASER shall provide SELLER with a copy of a commitment letter or other substantive proof of a third party financing commitment within _____ days. In the event PURCHASER is unable to obtain a financing commitment including terms and conditions acceptable to PURCHASER within said time period and advises SELLER of same, then all rights and obligations herein may, at the election of the SELLER or the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER **or** SELLER may extend said deadline for any time period acceptable to SELLER provided PURCHASER increases the security deposit by \$_____ and further provided that said amount plus all amounts previously deposited in escrow shall be retained by the SELLER subject to the terms and conditions defined herein.

This purchase offer is contingent upon PURCHASER assuming SELLER'S existing loan(s) with _____ in the aggregate amount of \$_____. In the event PURCHASER is unable to demonstrate an ability to assume said loan(s) by way of a commitment letter or other substantive proof of such ability provided by said lender within _____ days of this offer then all rights and obligations herein may, at the election of the SELLER or the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER **or** SELLER may extend said deadline for any time period acceptable to SELLER provided PURCHASER increases the security deposit by \$_____ and further provided that said amount plus all amounts previously deposited in escrow shall be retained by the SELLER subject to the terms and conditions defined herein.

Additional Terms and Conditions

1. DEPOSIT INCREASE.

If this offer is accepted, the deposit shall be increased to \$ _____ no later than _____ in the form of _____

2. WITHHOLD FROM MARKET

SELLER herewith represents and warrants that SELLER is not in possession of any other Purchase Offer from any other party at this time and additionally agrees that if this Purchase Offer is accepted SELLER will not to solicit or encourage directly or indirectly in any manner any discussion with, or furnish or cause to be furnished any information to any person or company other than PURCHASER in connection with, or negotiate for or otherwise pursue the sale of the business described herein:

for the term of this agreement and any extensions hereto.

other: _____

3. CLEAR AND MARKETABLE TITLE

SELLER herewith warrants that the business described herein currently possesses clear and marketable title to all assets to be included in this sale with the following exceptions:

4. INVENTORY VALUATION.

All salable inventory on hand at the time of physical possession shall delivered to PURCHASER. The value of said inventory shall be seller's cost; replacement cost; retail selling price; other: _____ to be calculated and/or determined as follows:

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5. PURCHASE PRICE ADJUSTMENT FOR INVENTORY ON HAND.

Immediately preceding close of escrow (or such other time as stated herein as: _____),

a physical count of the inventory on hand shall be made by buyer and seller together designee of seller; designee of buyer; designee of buyer and seller; other:

Description:

The value of said inventory to be determined as stipulated in item 4. Upon determination of the value of the inventory on hand, the purchase price indicated above shall be adjusted up or down as the case may be to reflect the difference between the value of the inventory included in said purchase price and the actual value as determined by the physical count. Said adjustment either up or down shall not exceed \$ _____.

Or

The purchase price shall be increased by the full value of the inventory as determined by the physical count. Said inventory value shall not exceed \$ _____.

Or

Other: _____

Said physical inventory shall be taken by _____

The cost of taking the physical inventory, if any, shall be paid by Seller; Buyer; Buyer and Seller and apportioned _____% to Seller and _____% to Buyer.

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6. PURCHASE PRICE ADJUSTMENT FOR WORK IN PROGRESS & FINISHED GOODS.

Immediately preceding close of escrow (or such other time as stated herein as:

_____)
a determination of value for any work in progress and finished goods shall be made by
[] buyer and seller together [] designee of seller; [] designee of buyer; [] designee
of buyer and seller; [] other: _____

The value of said work in progress shall be determined as follows:

Upon determination of the value of the work in progress

[] the purchase price indicated above shall be adjusted up or down as the case may be to
reflect the difference between the value of the work in progress included in said purchase
price and the actual value as determined by the analysis. Said adjustment either up or down
shall not exceed \$_____.

Or

[] The purchase price shall be increased by the full value of the work in progress as
determined by the analysis. Said work in progress value shall not exceed \$_____.

Or

[] Other: _____

Said work in progress analysis shall be made by_____

The cost of determining the value of the work in progress, if any, shall be paid by
[] Seller; [] Buyer; [] Buyer and Seller and apportioned _____% to Seller and
_____% to Buyer.

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7. ACCOUNTS RECEIVABLE VALUATION.

Immediately preceding close of escrow (or such other time as stated herein as:

_____)
an analysis of seller's Accounts Receivable shall be made by buyer and seller together
 designee of seller; designee of buyer; designee of buyer and seller; other:
Describe _____

The value of said Accounts Receivable shall be their face value; discounted by _____%
for collection and administrative fees, other (describe). Upon determination of the
value of the Accounts Receivable, the purchase price indicated above shall be adjusted
up or down as the case may be to reflect the difference between the value of the Accounts
Receivable stipulated herein and the actual value as determined by the analysis (less
discount for collection).

Said adjustment either up or down shall not exceed \$_____.

Or

The purchase price shall be increased by the full value of the Accounts Receivable as
determined by the analysis.

Or

Other: _____

The cost of analyzing the Accounts Receivable shall be paid by Seller; Buyer;
 Buyer and Seller and apportioned _____% to Seller and _____% to Buyer.

8. HOLD-BACK FOR ACCOUNTS RECEIVABLE

In the event the purchase price includes seller's Accounts Receivable, then a portion of the
purchase price paid to seller at close of escrow in the amount of \$ _____ shall
be held back in escrow for _____ days at which time PURCHASER, at
PURCHASER'S option, may exchange any uncollected accounts receivable for an equal
amount of cash in the hold-back account and said uncollected accounts receivable will be
returned to seller along with any remaining cash in said hold-back account.

other (describe)

9. HOLD-BACK FOR REFUNDS, RETURNS, ALLOWANCES & REWORK

A portion of the purchase price paid to SELLER at close of escrow in the amount of \$_____ shall be held back in escrow for _____ days against which PURCHASER may submit claims in excess of [] \$_____ or [] _____% of gross sales revenue for uninsured refunds to customers which exceed the resale value of merchandise returned plus any post-sale allowances for products sold or the uninsured or otherwise non-reimbursable cost of redoing or repairing services rendered by SELLER prior to close of escrow. Any expenses incurred by PURCHASER for refunds, returns, allowances and/or rework for merchandise sold or services rendered by SELLER after the time period specified herein shall become a burden of the PURCHASER and the SELLER shall be held harmless therefrom and all funds remaining in said Hold Back Account shall be immediately turned over to SELLER. The method by which PURCHASER and SELLER shall calculate or determine the dollar amount of said claims shall be as follows:

Upon submission of said claims by Purchaser, the Escrow Officer shall immediately notify the Seller of same and Seller shall have _____ days following such action to contest same. Notification shall be made to Seller's agent for service who is _____ located at _____ by certified mail.

The Escrow Officer shall immediately reimburse Purchaser for any claim not contested by SELLER within said time period. For purposes of this paragraph, the Escrow Officer shall only consider claims contested by SELLER submitted in writing and either hand delivered or sent by certified mail. The Escrow Officer shall not reimburse Purchaser for claims properly contested within the specified time period until authorized to do so by SELLER or the court. An amount of money equal to contested claims shall be retained by the Escrow Officer after the proscribed time period for releasing funds remaining in said Hold Back Account and shall only be released to SELLER or Purchaser as the case may be upon resolution of the dispute as provided herein.

Nothing in this paragraph shall serve to negate Purchaser's remedies at law for post-transaction customer requests for refunds, returns, allowances or costs of redoing or repairing work or services rendered beyond the time limit specified herein in cases of fraud in which the SELLER is directly or indirectly implicated and/or in cases of willful neglect and/or gross negligence and/or when the SELLER knew or should have known a request for a refund, return, allowance or cost of redoing or repairing work or services rendered would probably occur.

Nothing in this paragraph shall apply to discount coupons, free merchandise or services or other promotional price discount purchase or service rights conferred on prospective customers by SELLER prior to close of escrow and submitted for redemption after close of escrow.

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10. DISCOUNT COUPONS, FREE MERCHANDISE OFFERS & OTHER DISCOUNTS

SELLER herewith stipulates that the following discount coupons, free merchandise or service offers and other similar promotional price discounts and/or service rights discounts may be, to the best of SELLER's knowledge, valid rights redeemable by customers after the expected close of escrow date:

Purchaser herewith acknowledges advice of same and herewith waives any and all rights of recovery from SELLER for said claims with the following exception(s):

11. TERM OF THIS AGREEMENT AND CLOSING

This Exclusive Option to Purchase shall terminate and coincide with Close of Escrow which shall be on _____. Said term of this agreement and closing date may be extended or shortened by mutual written agreement of SELLER and PURCHASER. On or before said closing date, both parties shall deposit with an authorized escrow holder, selected by the undersigned PURCHASER, all funds and instruments necessary to complete the contemplated sale in accordance with the terms hereof including the balance of the purchase price or down payment and promissory note(s) as the case may be for the benefit of the SELLER, a valid Bill of Sale for such business and property together with any lease or lease assignment of the premises on which the business is located. Thereafter, any party, including Agent, may disclose the terms of sale.

12. PHYSICAL POSSESSION.

Physical possession shall be delivered to PURCHASER at [] close of escrow;
[] Other: _____

13. PRORATIONS.

Rents, property tax, franchise or other taxes, if any, premiums on insurance acceptable to PURCHASER, franchise fees, interest, utility expenses and other expenses of the business and/or property are to be prorated as of the date of transfer of the business. Security deposits, advance rentals or considerations involving future lease credits shall be credited to SELLER unless specifically stated otherwise herein.

14. SALES TAX

Any sales tax due for the sale of the personal property shall be paid by PURCHASER unless otherwise agreed to in writing by SELLER and PURCHASER.

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15. RISK OF LOSS

Any risk of loss to the business or property shall be born by the SELLER until title has been conveyed to the PURCHASER.

16. MAINTENANCE OF GOODWILL

Until possession is delivered SELLER agrees to continue to operate the business in the manner in which it is being operated at the date of this offer and to maintain the goodwill of the business and all personal property in normal working order subject to the exceptions and/or exclusions listed below. The SELLER shall not disclose or in any way let it be known to the business's employees, customers, vendors or other parties who have no need to know, that a transfer of ownership is pending. This also specifically means SELLER shall not raise or lower selling and/or service prices, raise or lower employee wages, fire, lay off or make other substantive changes in company personnel, modify existing credit terms or make any other substantive changes to standard operating procedures or the assemblage of fixtures, machinery or other operating equipment in affect at the time of this offer without first notifying PURCHASER in writing of such need or intention to do so *and* obtaining PURCHASER'S written approval for such actions. If SELLER fails to comply with this condition, then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER

Exceptions and/or Exclusions:

PURCHASER shall respond to such requests for changes upon receipt within ____ hours in writing. PURCHASER'S failure to respond to any specific request from SELLER to make changes within ____ hours shall be deemed as PURCHASER'S approval. PURCHASER'S failure to respond to a specific request from SELLER to make said changes shall not negate this clause nor serve as a waiver of PURCHASER'S right to approve future changes requested by SELLER. Upon refusal of PURCHASER to approve reasonable changes necessitated by the normal and customary course of business and consistent with SELLER'S established standard operating procedures requested by SELLER, SELLER may at SELLER'S option cancel this agreement not sooner than ____ hours subsequent to notifying PURCHASER of such intention in writing and therewith all rights and obligations herein may, at the election of the SELLER, terminate and end and the deposit shall be returned to the PURCHASER. If PURCHASER approves the requested change in writing previously denied within ____ hours of being advised by SELLER of an intention to cancel this agreement, said approval shall invalidate SELLER'S notice of cancellation. For purposes of this clause, Facsimile transmissions and/or e-mail messages shall be deemed as "notice or advice in writing."

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17. LEASE

PURCHASER to assume the existing lease. This sale is conditioned upon landlord's consent to assignment of said lease concurrent with close of escrow.

This sale is conditioned upon PURCHASER'S ability to negotiate a new lease with landlord to become effective concurrently with close of escrow.

This sale is conditioned upon PURCHASER'S ability to negotiate a lease with the SELLER who also owns the real property in/on which this business operates to become effective concurrently with close of escrow. The cost of developing the lease shall be paid by SELLER; Purchaser; SELLER and Purchaser and apportioned ____% to SELLER and ____% to Purchaser.

Other terms and conditions:

If PURCHASER is unable to

Obtain an assignment of said lease within _____ days of the date of this agreement:

Negotiate a new lease or extension to the existing lease acceptable to PURCHASER within _____ days of the date of this agreement:

Other:

then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

PURCHASER herewith stipulates that the purchase price contained herein is predicated on the assumption that the future rent the business will be required to pay will not be materially different from the current rent (and rent escalators) and that future term of a new lease if such is required, will be acceptable. Therefore, all parties to this agreement herein acknowledge that any deviation between PURCHASER'S existing assumptions regarding the terms of the lease and the terms ultimately determined to be acceptable to the premises owner shall render the purchase price null and void and in the event the parties to this agreement cannot renegotiate the purchase price prior to the date specified in Section 11 or any extension thereto, then all rights and obligations herein may, at the election of the PURCHASER or the SELLER, terminate and end and the deposit shall be returned to the PURCHASER.

If an assignment of an existing lease or the execution of a new lease shall be made a condition of this agreement and if a fully executed lease assignment or new lease is not placed into escrow by the date specified in Section 11 or any extension thereto, then, in the absence of a waiver of this condition signed by PURCHASER and SELLER, this agreement shall automatically become null and void and all rights and obligations of both parties shall terminate and end and the deposit shall be returned to the PURCHASER.

18. DEFECTS AND INSPECTIONS

SELLER represents that he/she knows of no defects, deficiencies or violations of local, state or federal law and/or codes affecting the business, the business's operating equipment or the premises in which the business is situated and agrees that he/she will advise PURCHASER in writing of same which come to his or her attention prior to the completion of the sale with the exception of those defects, deficiencies and legal and/or code violations itemized below which PURCHASER and SELLER acknowledge exist and which PURCHASER herewith excludes from this agreement under the terms and conditions as follows:

SELLER may, at SELLER'S option, correct any identified defects within _____ days of the stipulated date for close of escrow, or other date agreed to by SELLER and PURCHASER in writing in which case, such corrective action shall herewith be deemed a non-defect for purposes of this agreement provided said corrective action meets the standards necessary for lawful operation of the business or if some other higher or lower standard has been agreed to by PURCHASER and SELLER, then said higher or lower standard.

Upon notice to PURCHASER by SELLER of any such defects or upon discovery of any such defects by PURCHASER by any other means including, but not limited to the list of inspections identified below then PURCHASER may, at PURCHASER'S option, cancel this agreement provided PURCHASER advises SELLER of said discovery of previously unknown or undisclosed defect(s) in writing within ____ hours of said discovery and further provided PURCHASER advises SELLER in writing of an intention to cancel this agreement due to said previously unknown or undisclosed defects within the same time period and further provided the cost to correct any defect or the aggregate cost to correct multiple defects is expected to exceed \$_____ or provided SELLER does not correct said defects within _____ days of the stipulated date for close of escrow, or other date agreed to by SELLER and PURCHASER in writing or negotiate a purchase price adjustment to offset PURCHASER'S expected cost to correct said defects after close of escrow.

PURCHASER herein specifically requires that the following inspections be made at PURCHASER'S expense:

[] A Due Diligence investigation of the business to be performed by PURCHASER and/or PURCHASER'S designee(s). PURCHASER herein stipulates that said investigation may involve several hours of SELLER'S and/or SELLER'S employees' time and SELLER herewith agrees to make a good faith effort to assist PURCHASER in said investigation provided however, said good faith effort specifically shall exclude SELLER incurring any costs of money or time to develop additional records or reports that do not presently exist such as (but not limited to) audited financial statements, customer surveys, employee surveys, market forecasts, sales and/or earnings forecasts or projections, etc.

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19. ADDITIONAL DOCUMENTS

SELLER shall deliver to PURCHASER for approval the following documents within _____ days of acceptance. If SELLER does not deliver all documents requested by PURCHASER within said time period then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER under the terms and conditions specified in Paragraph 31 below.

PURCHASER shall be deemed to have approved said documents unless written notice to the contrary is delivered to SELLER or SELLER'S Agent within _____ days of receipt of said documents by PURCHASER. In the event PURCHASER finds any facts, circumstances, conditions or other attributes of the business or business records and/or documents unacceptable to PURCHASER for any reason whatsoever then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

SELLER herewith warrants that all such documents will be true and complete to the best of SELLER'S knowledge.

PURCHASER may extend the deadline by which SELLER must provide the requested documents by so advising the SELLER in writing of such extension however, if SELLER fails to provide all the documents requested by said extended deadline then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER under the terms and conditions identified in Paragraph 31 below.

List of all furniture, fixtures, equipment and machinery plus a general description of all small tools, office equipment and other miscellaneous and/or incidental assets to be included in the purchase price and exclusions thereto, if any.

Inventory of all supplies (e.g., cleaning supplies, office supplies, repair parts, etc.) to be included in the purchase price. PURCHASER herein acknowledges said inventory changes daily and herewith agrees that no adjustment in the purchase price shall be made if, at the date of closing, the value of said inventory differs from that indicated on said report by less than _____%

Profit & Loss Statements and Balance Sheets for the years ending:

Federal Income Tax returns for the years ending:

Accounts Payable and Accounts Receivable Aging Report

Name, address & phone number for all vendors, suppliers & creditors

Making a Small Business Purchase Offer

20-A. SALE OF VEHICLES

Ownership transfer of

all vehicles to be included in the purchase of this business

Only those vehicles for which the SELLER has possession of the title shall be accomplished through escrow. Within ____ days from the date of this agreement, SELLER shall deposit into escrow the titles to all vehicles to be acquired by buyer provided SELLER has physical possession of said titles together with a detailed description of all vehicles to be acquired by buyer including the make, model, year and VIN Number (Vehicle Identification Number).

Within ____ days from the date of this agreement SELLER shall make a determination of all costs associated with ownership transfer of each vehicle subject to this agreement including (but not limited to) sales tax, registration, title fee, license plate fee, supplemental county tax, privilege tax, etc. and advise the Purchaser and the escrow officer of such findings.

For all vehicles subject to this agreement which have unpaid loan balances and for this reason, title to said vehicles are in the possession of a third party lender, SELLER shall, within ____ days from the date of this agreement also deposit into escrow a Letter of Authorization instructing the escrow officer to pay off said loans using funds held back from the sale proceeds due SELLER together with a *Limited Power of Attorney for a vehicle title transfer* empowering the escrow officer to complete same in the name of the SELLER. Simultaneous with the submission of said Letter of Authorization, SELLER shall also submit a notarized Letter of Request addressed to said third party lender, requesting that the titles for said vehicles be sent to the escrow officer upon payment of the remaining loan balance.

At close of escrow, SELLER shall provide escrow officer with the odometer reading on all vehicles subject to this agreement, a certified emissions analysis (in the state of Nevada), indicating each vehicle is in compliance with applicable emission laws and a statement indicating the amount of the unpaid balance and accrued interest and other fees, if any, required to be paid a third party lender (under the presumption payment will be received by the bank within 5 business days) as a condition of obtaining free and clear title to said vehicles.

At close of escrow Purchaser shall provide the escrow officer with a *Limited Power of Attorney for a vehicle title transfer* empowering the escrow officer to complete same in the name of the Purchaser for all vehicles subject to this agreement for which the vehicle titles are held by a third part at close of escrow together with proof of insurance on all vehicles subject to this agreement.

At close of escrow, Purchaser shall deposit into escrow an additional sum equal to all fees required to be paid as a condition of ownership transfer for all vehicles subject to this agreement.

Purchaser's payment of said fees as a requirement of ownership transfer

shall not shall be applied to the total purchase price of the subject business.

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Or

At close of escrow, the funds necessary to pay the fees required as a condition of ownership transfer on all vehicles subject to this agreement shall be placed into escrow and allocated to the purchase price as follows:

At close of escrow, the SELLER shall sign off as the legal owner on the vehicle title document and the purchaser shall sign on as the legal owner on the vehicle title document for each vehicle subject to this agreement on all vehicle title documents available at said time.

At close of escrow, the escrow officer shall preside over the execution of a Bill of Sale for each vehicle subject to this agreement and provide a copy of said document to Purchaser and SELLER and retain additional copies as needed.

At close of escrow, the escrow officer shall submit to the Department of Motor Vehicles said completed vehicle title documents together with payment of all fees required as a condition of ownership transfer for said vehicles, a copy of the Bill of Sale, Purchaser's proof of insurance.

Escrow officer shall additionally submit to the Department of Motor Vehicles a notarized Letter of Request signed by the Purchaser directing said Department to send the new vehicle title to Purchaser's Lender.

At close of escrow, the escrow officer shall pay off all outstanding vehicle loans from the sale proceeds held back for this purpose. Upon receipt of the vehicle titles from said third party lenders, the escrow officer shall complete the appropriate sections on said titles in the name of the SELLER and in the name of the Purchaser and submit same to the Department of Motor Vehicles together with two attached *Limited Powers of Attorney for a vehicle title transfer* empowering the escrow officer to complete same in the name of the SELLER and Purchaser, payment of all fees required as a condition of ownership transfer for said vehicles, a Bill of Sale for each vehicle, Purchaser's proof of insurance.

Escrow officer shall additionally submit to the Department of Motor Vehicles a notarized Letter of Request signed by the Purchaser directing said Department to send the new vehicle title to Purchaser's Lender.

Immediately following close of escrow PURCHASER shall take those actions required to obtain a temporary registration and/or operating permit from the Department of Motor Vehicles in Purchaser's name pending receipt of a new title document, permanent registration and vehicle license plates such as (but not limited to) proceeding directly to the Department of Motor Vehicles with the Bill of Sale and proof of insurance and other documents as may be required to obtain said temporary registration and/or operating permit and, upon obtaining said documents, placing same in said vehicles. Additionally, SELLER shall remove the license plates from all vehicles subject to this agreement and submit same to the Department of Motor Vehicles for cancellation.

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If either SELLER or Purchaser do not comply with all conditions of this section within or at the times specified herein then all rights and obligations may, at the election of the other party to this agreement, terminate and end and the deposit shall be returned to the PURCHASER and all vehicle titles shall be returned to the SELLER.

20-B. SALE OF VEHICLES

Ownership transfer of

Those vehicles to be included in the purchase of this business for which the titles to said vehicles are in the possession of a third party lender

All vehicles to be included in the purchase price of this business

shall NOT be accomplished through escrow.

The purchase price for the business allocated to the purchase of vehicles indicated above and the fees required for ownership transfer such as (but not limited to) sales tax, registration, title fee, license plate fee, supplemental county tax, privilege tax, etc. shall not be deposited into escrow.

SELLER and Purchaser herein agree to consummate this portion of the total acquisition in the following manner:

Not more than 60 days preceding close of escrow, in the state of Nevada, SELLER shall obtain a certified emissions analysis indicating each vehicle is in compliance with applicable emission laws and, for vehicles more than four years old, obtain an appraisal.

Immediately preceding close of escrow, SELLER shall obtain a statement indicating the amount of the unpaid balance and accrued interest and other fees, if any, required to be paid a third party lender as a condition of obtaining free and clear title to said vehicles and provide said statement to Purchaser and the odometer reading from each vehicle.

Prior to close of escrow, Purchaser shall obtain proof of insurance on each vehicle subject to this transaction.

Immediately following close of escrow, Purchaser shall pay SELLER the agreed portion of the total purchase price allocated for each vehicle included in the transaction (less any amount due a third party lender. At this time, SELLER shall sign off as the legal owner on each vehicle title document and the purchaser shall sign on as the legal owner on each vehicle title document available and the parties shall execute a Bill of Sale for said vehicles. Then, SELLER and Purchaser shall, together, personally appear at the office of each lender whereupon Purchaser shall pay off the loans on said vehicles, obtain title to same whereupon SELLER shall sign off as the legal owner on the vehicle title document and the purchaser shall sign on as the legal owner on the vehicle title document and the parties shall execute a Bill of Sale for said vehicles.

Immediately subsequent to obtaining the titles to all the vehicles subject to this transaction and completing same indicating a transfer of ownership,

Seller and Purchaser Purchaser

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shall proceed directly to the Department of Motor Vehicles, turn in said titles whereupon Purchaser shall, present proof of insurance for said vehicles, a duly executed Bill of Sale, a certified emissions analysis indicating each vehicle is in compliance with applicable emission laws and, for vehicles more than four years old, an appraisal and pay _____% and SELLER shall pay _____% of all fees required to transfer ownership of said vehicles to Purchaser.

Purchaser's payment of fees to the Department of Motor Vehicles as a requirement of ownership transfer [] shall not [] shall be applied to the total purchase price of the subject business.

Immediately subsequent to completion of the Department of Motor Vehicles vehicle ownership transfer requirements, Purchaser shall place each temporary vehicle operating permit in the subject vehicles and SELLER shall remove the license plates from said vehicles and submit same to the Department of Motor Vehicles for cancellation.

21. LICENSES AND PERMITS

SELLER herein warrants, after due inquiry, that the following licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) to conduct business constitute all such sanctions legally required to conduct business in it's ordinary and customary fashion:

SELLER herein stipulates that SELLER personally possesses the following legally required licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) necessary to conduct business in its ordinary and customary fashion and represents that Purchaser will be legally required to possess or acquire same prior to close of escrow in order to similarly conduct business in it's ordinary and customary fashion:

SELLER herein stipulates that some or all of SELLER's employee(s) are required to possess the following licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) and meet or exceed minimum age requirements which are legally required to continue to conduct business in it's ordinary and customary fashion: (see attachment)

SELLER herein warrants that SELLER's employee(s) possess all the licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) and meet or exceed minimum age requirements as defined above to continue to conduct business in it's ordinary and customary fashion with the following exceptions: (see attachment)

This sale is contingent upon approval of transfer of any licenses by federal, state or local agencies or franchisor or other vendor or upon issuance of any new licenses, permits, professional credentials, college degrees, certificates and/or other similar consent(s) to conduct business required by PURCHASER prior to close of escrow with the exception of the following: (see attachment)

In the event SELLER'S employees do not possess those licenses, permits, professional credentials, college degrees, certificates and other similar consent(s) legally required to conduct business in it's ordinary and customary fashion identified above or meet a minimum age requirement to carry out their job responsibilities as provided by applicable law then all rights and obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

Nothing in this paragraph shall serve to negate PURCHASER'S legal remedies to collect damages from SELLER incurred by PURCHASER due to failure of SELLER to disclose herein all licenses, permits, professional credentials, college degrees, certificates and/or other similar consent(s) legally required to be held by SELLER or SELLER'S employees or other legal requirements regarding minimum age, citizenship or other legally required right to work conditions in order to conduct business in it's ordinary and customary fashion or SELLER'S failure to disclose employees currently working without possessing said legally required licenses, permits, professional credentials, college degrees, certificates and/or other similar consent(s) or meeting minimum age requirements, citizenship or other legally required right to work conditions.

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22. CONTRACT ASSIGNABILITY

SELLER herein represents that the following Franchise Agreements, Dealership Agreements, Distributorship Agreements or similar contracts and agreements constitute all such agreements necessary for the conduct of business and, to the best of SELLER's knowledge, can and will be transferred or assigned to PURCHASER:

In the event, PURCHASER is unable to have the above described contracts and/or agreements transferred, assigned or otherwise made to have the same affect prior to or at close of escrow, then all obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

The preceding paragraph shall specifically prohibit PURCHASER from invalidating a consummated purchase transaction should PURCHASER fail to obtain an assignment of any Franchise Agreement, Dealership Agreement, Distributorship Agreement after close of escrow if PURCHASER voluntarily postponed attempting to obtain said transfers and/or assignments until after such time. This condition shall not apply, however, to any such required transfers and/or assignments material to the operation of the business which SELLER failed to disclose to PURCHASER herein.

23. EQUIPMENT SATISFACTORY

SELLER herewith warrants that the assemblage of furniture, fixtures, equipment, machinery, small tools, employee uniforms and operating supplies are sufficient and in adequate condition to conduct business in the normal and customary manner as of the date of this agreement with the following exception(s):

SELLER further agrees that he/she will advise PURCHASER in writing of any change(s) in the status of said assemblages prior to the completion of the sale. Upon such advice, if said changes diminish the value of said assemblages by more than \$_____ then all obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

24. INVENTORY GOOD AND SALABLE

SELLER herewith warrants the all the inventory to be included in this transaction is good and salable with the following exception(s):

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25. PURCHASER INSURABILITY

PURCHASER herein represents that to the best of PURCHASER'S knowledge, PURCHASER can obtain insurance and surety bonds both in types and limits approximately the same as SELLER currently has in place and can obtain minimum limits as required by any landlord, franchisor or other entity which has the authority to require the business or business owner to obtain specified insurance coverage.

In the event PURCHASER is unable to obtain said insurance or demonstrate said ability by way of an insurance binder or letter of intent from a bona fide insurance company prior to or at close of escrow, then all obligations herein may, at the election of the PURCHASER or SELLER, terminate and end and the deposit shall be returned to the PURCHASER.

26. GOVERNMENT APPROVAL—LEGAL NOTICES

SELLER shall obtain any governmental approvals and give any notices required by law or necessary to avoid liens upon the business and/or property sold or legally required as a condition of ownership transfer.

Prior to close of escrow the SELLER shall pay all amounts owed for employment wage taxes and sales taxes and/or make appropriate arrangements to pay said taxes by submitting into escrow proof of obtaining taxing authority clearance in the form a *Clearance Letter* issued by said authorities. In the event SELLER is unable to obtain said clearances prior to or at close of escrow, then all obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

27. NONCOMPETITION

SELLER herewith agrees not to compete directly or indirectly with PURCHASER or utilized SELLER'S knowledge, skills or reputation in a way that could negatively impact the profitability of this business subsequent to ownership transfer for a period of _____ years within a radius of _____ miles with the following exception(s) and/or other conditions:

28. SELLER ORIENTATION AND TRAINING

As a condition of PURCHASER acquiring the business described herein and as part of the purchase price, SELLER herewith agrees to assist PURCHASER in affecting as smooth a transition of ownership as possible by making a good faith effort to provide PURCHASER with orientation and training. Said SELLER provided orientation and training shall specifically include and/or exclude the following:

29. PURCHASE PRICE OFFSET

All parties to this agreement herein acknowledge that all businesses, including the business subject to this agreement have problems in various stages of development, often unknown or unknowable at any particular moment in time. Therefore, it is the intention of the parties to this agreement that actual losses that would not have been insured under the insurance coverage carried by the SELLER at close of escrow or covered by PURCHASER'S insurance policy resulting from such problems presently unknown to the SELLER which become manifest after transfer of ownership, despite SELLER'S best effort to fully disclose all circumstances of the business, be allocated in a fair and equitable manner. Therefore, any formerly or currently uninsured losses or expenses of the following nature: [] equipment or facility breakdowns [] other (describe)

sustained by the business within _____ days of ownership transfer which, in the aggregate, are less than [] _____% of the purchase price or [] \$_____ or [] _____% of gross sales revenue shall be borne by the PURCHASER and the SELLER shall be held harmless therefrom. However, any of the above defined losses or expenses which exceed said threshold amount sustained by the business within said time period herein specified shall be born by the SELLER up to a maximum of [] _____% of the purchase price or [] \$_____ or [] _____% of gross sales revenue to the extent said losses or expenses were not insured at close of escrow or insured by PURCHASER subsequent to close of escrow provided PURCHASER can clearly document such losses or expenses and further provided such losses or expenses occurred through no fault of the PURCHASER, or as a result of vandalism, sabotage, natural disasters or acts of war. Any unexpected losses or expenses sustained after said time period shall be born entirely by the PURCHASER. Any losses or expenses sustained by the PURCHASER not identified above shall be born by the PURCHASER upon close of escrow or taking possession of the business, which ever occurs first if not simultaneous, with no right of purchase price offset.

SELLER'S repayment of said losses shall be accomplished by way of an offset to the payments of principal and interest PURCHASER makes to SELLER which amount shall not exceed _____% of each periodic payment. This repayment plan notwithstanding, said plan shall not serve to negate SELLER'S legal rights to receive payments in accordance with the terms and conditions of the promissory note. Therefore, any amounts held back by PURCHASER shall be deposited into an escrow account maintained by _____ until written instructions for the dispensation of the funds is received by the escrow officer and signed by both SELLER and PURCHASER or by the court.

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In the event PURCHASER pays 100% of the purchase price in cash at close of escrow, then the escrow officer is herewith instructed to establish an "offset account" into which _____% of the purchase price shall be held for the purpose contemplated herein. Said offset account shall be maintained until said time period has expired at which time, if no claims are made, the funds in said account shall be turned over to the SELLER. In the event PURCHASER submits a claim against said offset account, an amount sufficient to discharge said claim shall be maintained by the escrow officer until written instructions for the dispensation of the funds is received and signed by both SELLER and PURCHASER or received from the court.

This paragraph shall in no way negate PURCHASER'S other rights and remedies at law pursuant to any fraudulent misrepresentation or willful withholding of material facts and circumstances of the business by the SELLER.

30. PURCHASER DEFAULT

In the event that PURCHASER fails to pay the balance of the purchase price, or to complete the purchase as herein provided, SELLER may, subject to any rights of the Agent herein, retain all amounts paid hereunder as damages for the breach of this agreement by PURCHASER; provided however, that SELLER may take such action as he deems appropriate to recover such portion of the amounts paid hereunder as may be allowed by law. In the event that PURCHASER shall so default, PURCHASER agrees to pay Agent, the commission which Agent is entitled to receive as hereinafter provided. The obligation of PURCHASER to Agent shall be in addition to any rights which Agent may have against SELLER in the event of default. In the event legal action is instituted by any party to this agreement to enforce the terms of this agreement, or arising out of the execution of this agreement or the sale, the prevailing party shall be entitled to receive from the other party a reasonable attorney fee to be determined by the court in which such action is brought.

31. WILLFUL FAILURE OF SELLER TO PERFORM

In the event SELLER shall refuse to consummate the transaction contemplated herein or if SELLER, SELLER'S employees and/or agents make any material disclosures or representations to PURCHASER discovered to be false or misleading and/or if SELLER withholds knowledge about facts or circumstances of the business and/or real estate which could reasonably have the affect of diminishing the value of said property of sufficient severity that PURCHASER therewith elects not to consummate the transaction contemplated herein or if SELLER, and/or SELLER'S employees or agents willfully obstruct, fail to reasonably cooperate with and/or reasonably assist PURCHASER when such cooperation and/or assistance is necessary or otherwise interfere with PURCHASER'S good faith efforts to consummate the contemplated transaction according to the terms, conditions and spirit of this agreement or if SELLER solicits other purchase offers for the business after signing this agreement and/or negotiates with the parties making a purchase offer, or if SELLER sells, leases, otherwise disposes of the business and/or real property to another party during the Hold-Off-Market time period specified in Paragraph 2 above or if the SELLER misrepresents his or her authority and/or authorization to enter into and/or consummate this agreement or takes other actions which makes the contemplated transaction impossible to consummate during the term of this agreement or if SELLER is unable to deliver all assets and real property to the PURCHASER free of any liens or encumbrances (with the exception of those liens and encumbrances identified above which PURCHASER has agreed to accept) then SELLER shall pay PURCHASER [] an amount equal to the amount PURCHASER has deposited in escrow or [] \$_____ at the time PURCHASER shall demand same in writing. Additionally, upon such demand, all obligations herein will terminate and end and the deposit shall be returned to the PURCHASER.

Said payment to PURCHASER for SELLER'S failure to perform provided herein shall have no affect on any other agreement SELLER may have with SELLER'S and/or PURCHASER'S Agents to pay said Agents a fee or commission for duties performed and/or services rendered despite SELLER and PURCHASER'S failure to consummate the contemplated transaction.

Making a Small Business Purchase Offer

32. SALE PRICE ALLOCATION

For purposes of compliance with Internal Revenue Code Section 1060 and completion of IRS Form 8594 the purchase price shall be allocated as follows:

| | | |
|------------------------------|----------|--------------------------------------|
| Accounts Receivable | \$ _____ | (plus or minus adjustment at C.O.E.) |
| Inventory | \$ _____ | (plus or minus adjustment at C.O.E.) |
| Work in Progress | \$ _____ | (plus or minus adjustment at C.O.E.) |
| Finished Goods | \$ _____ | (plus or minus adjustment at C.O.E.) |
| Operating Supplies | \$ _____ | |
| Land | \$ _____ | |
| Building | \$ _____ | |
| Equipment & Machinery | \$ _____ | |
| Vehicles (total) | \$ _____ |list each vehicle separately |
| Customer List | \$ _____ | \$ _____ |
| Secret Manufacturing Process | \$ _____ | \$ _____ |
| Proprietary Software | \$ _____ | \$ _____ |
| Trade Name/Trade Mark | \$ _____ | \$ _____ |
| Covenant Not to Compete | \$ _____ | \$ _____ |
| Seller's Consulting Agree. | \$ _____ | \$ _____ |
| Franchise Agreement | \$ _____ | \$ _____ |
| Other | \$ _____ | \$ _____ |
| Goodwill (Balance of Price) | \$ _____ | \$ _____ |
| TOTAL | \$ _____ | |

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33. ESCROW OFFICER

Purchaser herewith directs that the escrow company/escrow officer who shall manage the escrow function for this transaction shall be _____.
All fees payable for escrow services shall be paid _____% by buyer and _____% by SELLER.

34. PURCHASE AGREEMENT AND BILL OF SALE

Ownership transfer of this business shall be accomplished by way of a definitive Purchase Agreement and Bill of Sale. The requirement to execute said definitive Purchase Agreement notwithstanding, the parties to this Agreement herewith agree that in the event any term or condition or the interpretation of any term or condition or the intent of any term or condition in said Purchase Agreement may be in conflict with this Agreement, then in such case, this Agreement shall control in any disputes arising therefrom. Selection of the attorney who shall draw up the Purchase Agreement and Bill of Sale shall be made by SELLER; Purchaser; SELLER and Purchaser together; Escrow Officer. The cost to develop the Purchase Agreement and Bill of Sale shall be paid by SELLER; Purchaser; SELLER and Purchaser and apportioned _____% to SELLER and _____% to Purchaser.

35. OTHER TERMS AND CONDITIONS

36. TIME IS OF THE ESSENCE

Time is of the essence of this agreement. The term “days” as used herein means calendar days unless otherwise specified.

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37. EXPIRATION

This offer shall expire unless a copy hereof with SELLER'S written acceptance is delivered to the PURCHASER or to his agent on or before _____ o'clock []AM; []PM on _____.

SELLER warrants the accuracy of the information after due inquiry by dating and signing the attached documents and statements.

38. ACKNOWLEDGMENTS

PURCHASER acknowledges receipt of a copy of all pages of this agreement. Purchaser acknowledges that he/she has not received or relied upon statements or representations made by the agent which are not herein expressed, including any statements or representations regarding the effect of this transaction upon PURCHASER'S Tax Liability.

39. AGREEMENT SUBJECT TO REVIEW

This agreement is subject to the review of PURCHASER'S and SELLER'S advisors including but not limited to their respective attorneys, CPA's, insurance agents and lenders. Upon said review, any of said advisors objections to any terms or conditions of this agreement shall be presented to the opposite party in writing and submitted into escrow whereupon, all obligations herein may, at the election of the party who's advisor has submitted said objection(s) terminate and end and the deposit shall be returned to the PURCHASER.

Additionally

[] PURCHASER makes this agreement subject to the review of the following parties whose approval shall be limited to the identified specific issues:

Upon review, any objections to any terms or conditions of this agreement identified by said party shall be presented to the opposite party in writing and submitted into escrow whereupon all obligations herein may, at the election of the PURCHASER, terminate and end and the deposit shall be returned to the PURCHASER.

[] SELLER makes this agreement subject to the review of the following parties whose approval shall be limited to the identified specific issues:

Upon review any objections to any terms or conditions of this agreement identified by said party shall be presented to the opposite party in writing and submitted into escrow whereupon all obligations herein may, at the election of the SELLER terminate and end and the deposit shall be returned to the PURCHASER.

If no written objection by either party's advisor(s) is received and presented to the other party to this transaction and entered into escrow within _____ days of the date of this agreement, then said failure to object shall be deemed as an approval of said advisors for purposes of this section of this agreement.

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OFFER

The undersigned PURCHASER hereby submits this offer and agrees to purchase the business described herein for the price and terms subject to the additional conditions and contingencies specified.

FEES AND COMMISSION

PURCHASER

hereby acknowledges that _____ is
and _____ is
his/her/their Agent of Record for this transaction, represents their interests exclusively and
agrees to pay Agent as provided in the [] Buyer's Broker Employment Agreement
[] other: _____

for services rendered. In the event that PURCHASER defaults and fails to complete the sale, Agent shall be entitled to receive one-half of PURCHASER'S deposit, but not more than the commission earned, without prejudice to Agent's rights to recover the balance of the commission from PURCHASER. In the event that SELLER has been deemed to have willfully failed to perform or is found to have engaged in any of the actions defined within Section 31 herein, then SELLER shall be liable to pay Agent one-half of SELLER'S "bust-up" fee as provided in Section 31 but not more than commission earned, without prejudice to Agent's rights to recover the balance of the commission and fees from SELLER. The mutual rescission of this agreement by PURCHASER and SELLER shall not relieve said parties of their obligations to Agent hereunder. In the event legal action is instituted by Agent against SELLER or PURCHASER or both to collect the commission and other fees due, or any portion thereof, then said defendant(s) agree to pay the Agent such additional sum as the court may adjudge. This agreement shall not limit the rights of Agent provided for in any other agreement which may be in effect between SELLER or PURCHASER and Agent.

Agent _____
Signature Date Time

Broker _____

PURCHASER _____
Signature Date Time

PURCHASER _____
Signature Date Time

Making a Small Business Purchase Offer

ACCEPTANCE

The undersigned SELLER accepts the foregoing offer and agrees to sell the business described herein for the price and on the terms and conditions herein specified. The undersigned SELLER hereby covenants that he is the owner and/or President of the above mentioned business and has the legal right to sell same as evidenced by a Corporate Resolution to Sell, attached hereto and made a part hereof if this business is a corporation.

FEES AND COMMISSION

SELLER

hereby acknowledges that _____ is
and _____ is
his/her/their Agent of Record for this transaction, represents their interests exclusively and agrees to pay Agent as provided in [] SELLER'S Listing Agreement
[] other: _____

for services rendered. In the event that PURCHASER defaults and fails to complete the sale, Agent shall be entitled to receive one-half of PURCHASER'S deposit, but not more than the commission earned, without prejudice to Agent's rights to recover the balance of the commission from PURCHASER. In the event that SELLER has been deemed to have willfully failed to perform or is found to have engaged in any of the actions defined within Section 31 herein, then SELLER shall be liable to pay Agent one-half of SELLER'S "bust-up" fee as provided in Section 31 but not more than commission earned, without prejudice to Agent's rights to recover the balance of the commission and fees from SELLER. The mutual rescission of this agreement by PURCHASER and SELLER shall not relieve said parties of their obligations to Agent hereunder. In the event legal action is instituted by Agent against SELLER or PURCHASER or both to collect the commission and other fees due, or any portion thereof, then said defendant(s) agree to pay the Agent such additional sum as the court may adjudge. This agreement shall not limit the rights of Agent provided for in any listing or other agreement which may be in effect between SELLER or PURCHASER and Agent.

SELLER _____
Signature Date Time

SELLER _____
Signature Date Time

The undersigned PURCHASER hereby acknowledges receipt of the accepted agreement

PURCHASER _____
Signature Date Time

PURCHASER _____
Signature Date Time

Making a Small Business Purchase Offer

Corporate Resolution to Sell

whereas, _____ President of _____ Corporation doing business as _____ does hereby certify that at a combined meeting of the stockholders and directors of the Corporation duly called and held at the office of the Corporation on _____ 19____ wherein a quorum of the stockholders and directors were present and voting throughout, it was upon motion duly made and seconded, that the corporation would endeavor forthwith to find a buyer for the Corporation's Assets.

Upon finding such buyer, the Corporation will make every reasonable effort to negotiate a price in cash and other valuable consideration in exchange for all or the majority of the Corporation's tangible, intangible assets and goodwill acceptable to the stockholders and directors and upon a meeting of the minds of said buyer and the Corporation, the Corporation will therewith affect a transfer of the Corporation's Assets to the buyer for said cash and other valuable consideration as soon as practicable.

Upon finding such buyer, the Corporation will make an assignment of any leases on Real Estate and/or Chattel owned by the Corporation for cash and other valuable consideration and upon terms acceptable to the stockholders and directors further provided, however, that the owners of such Real Estate or Chattel agree to such assignment of said lease(s) and further provided that if said owners of Real Estate and/or Chattel leased to the Corporation require the Corporation to remain on as guarantors of said contracts as a condition of assignment to said buyer that the Corporation will make such guarantee.

If the terms of the buyer *exclude* the purchase of all or any portion of Real Estate owned by the Corporation that, notwithstanding such exclusion, the Corporation will sell all or the majority of the Corporation's tangible assets, intangible assets and goodwill excluding any Real Estate owned by the Corporation and furthermore will, if so desired by the buyer, lease the Real Estate owned by the Corporation to the buyer of the Corporation's Assets for cash and other valuable consideration upon terms acceptable to the stockholders and directors.

If the terms of the buyer *include* the assumption of any debts or other liabilities of the Corporation, that the Corporation will transfer such debts or other liabilities to the buyer for a reduction in the cash and other valuable consideration the buyer would otherwise pay for the Corporation's Assets at an exchange rate acceptable to the stockholders and directors further provided, however, that such debt holders affected by said transfer agree to such assumption by the buyer of the Corporation's debts and other liabilities.

It is anticipated that the sale of the Corporation's Assets or Liabilities will be as a Bulk Sale of Assets and therewith will not involve the sale or exchange of the Corporation's stock. However, should a buyer wish to purchase all or a controlling percentage of the corporation's outstanding stock as opposed to the corporation's assets, or merge the corporation into another corporation, the approval for such action is herewith stipulated in this resolution.

_____, in their capacity as _____ of the Corporation be empowered, authorized and directed to execute, deliver and accept any and all documents and undertake all acts reasonably required or incidental to accomplish the foregoing resolution, all on such terms and conditions as they in their discretion deem to be in the best interest of the Corporation.

Upon the motion duly made and seconded the forgoing resolutions were passed unanimously by a vote of all stockholders present, such stockholders representing a quorum as defined in the By Laws of the Corporation.

I further certify that said resolutions are in full force and effect without rescission, modification or amendment.

By the Board of Directors, this resolution is adopted this _____ day of _____ 19____

President of the Corporation

In Conclusion

The process of purchasing a small business, as perhaps you can tell from this book, can be quite complicated. There is no substitute for basic common sense on your part, a solid understanding of general business principles, and the advice and guidance of qualified professionals in the legal, accounting, and business brokerage fields. You are well advised to read all you can to learn as much as possible about the process and to select highly qualified advisors to assist you. If you would like more information about the business purchase and sale process, and a further discussion of the concepts presented in this book, I recommend each of the following two books:

“Strategies for Successfully Buying or Selling a Business” by Russell L. Brown Copyright 1998, ISBN 0-9657400-0-5 \$29.95 (softcover). This book has been recommended by Kiplinger’s Personal Finance Magazine and has won the North American Bookdealers Exchange (NABE) Best Business Book of the Year Award.

“Preparing Your Business For Sale” by Russell L. Brown, Copyright 1998, ISBN 0-9657400-2-1 \$39.95 (hardcover) or ISBN 0-9657400-1-3 \$29.95 (softcover). This book has been recently published and is recommended by Mr. Tom West, founder and past president of the International Business Brokers Association (IBBA).

Both of these books may be purchased in better bookstores or ordered directly from the publisher:

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ABOUT THE AUTHOR

Toby Tatum is a member of the International Business Brokers Association (from which he has earned the designation Certified Business Intermediary), The M & A Source, the world's largest networking organization of Business Transaction Intermediaries specializing in the sale of midsize private companies, the Institute of Business Appraisers and the Institute of Certified Business Counselors from which he has earned the designation Certified Business Counselor. He was formerly the President, Chief Executive Officer, Chief Financial Officer and majority stock holder of a company with annual sales of nine million dollars employing in excess of two hundred fifty people. In that capacity he has bought, sold and started operating units from scratch with ultimate oversight responsibility for all aspects of company operations and finance. Consequently, his experience in the sale and acquisition of businesses is from an owner's perspective which can be invaluable when working with client business owners and buyers.

Mr. Tatum obtained his Bachelors Degree in Management from Sonoma State University and his Masters Degree in Business Administration from San Francisco State University. Additionally, Mr. Tatum has completed numerous courses on the valuation of privately owned businesses, has passed the Institute of Business Appraisers examination for the Certified Business Appraiser credential and is well founded in both the theory and practical application of this skill.

Mr. Tatum is a former Associate Professor of Management at Sonoma State University, former member of the Board of directors of the California Restaurant Association, former member of the Sonoma National Bank Advisory board, former member of the Board of Trustees for the National Sizzler Franchise Association, and former member of Sizzler Restaurants International's Strategic Planning Committee, Government Affairs Committee and Concept Committee. His biographical sketch has appeared in Marquis Who's Who In Finance and Industry in America, Marquis Who's Who In The West, and the Who's Who Historical Society's Who's Who In California. He is an experienced speaker on topics including Selling and Buying Businesses, Business Management, Strategic Planning and Total Quality Management, has published articles in newspapers and trade journals and is currently a columnist for the Reno Gazette-Journal writing about selling, buying and valuation of small businesses.

Making a Small Business Purchase Offer is Mr. Tatum's first book.

You may contact the author through the publisher at rds@businessbookpress.com