

PURCHASE OF BUSINESS

MEMO TO CLIENT

General

Purchase of Business and being self-employed is an important step in your career. Statistics show that proper advice from the professionals such as Lawyers and Accountants can make a significant difference in the success of your business.

Discussion & Video tape

The following will provide you with some guidelines on purchase of business. This is not an exhaustive memorandum. Specific details should be discussed with us personally.

We also have videotape you can watch on VHS format which can give you general information on the purchase of a business.

Preliminary General Inquiries

Before any formal agreement is prepared to purchase a business, you should be sure that you could technically handle the business and make sure that you have sufficient funds not only for the purchase but also for the cash flow required in the initial period to meet the business expenses and your expenses.

Examine the business to be purchased

You should check out the business location, the equipment and the assets of the business. You should study the financial statements of the business carefully to be sure that it can generate business for you and there is sufficient profit margin for you. If the business is not presently profitable you should be sure that you would be able to make it profitable by rectifying the problems of the seller.

If you are purchasing the building as well you should check out the building. If the company has any patents, trade marks etc. you should look at them as well.

You should decide if you will manage the business or if you will need the expertise of the existing management.

Franchise

For franchise organizations you should examine the franchiser by asking for their credit rating, which can be obtained from their banks. You should find how long they have been in the business in the type of business you are going to do and who the key people are and their business experience in the franchise organization.

Projected financial statements

It is a good practice to prepare your projected statement and the cash flow statement for the next two or three years. You may need the assistance from your accountant.

Customer list

You should obtain a list of the customers, and if there is an opportunity you should even acquaint yourself with your important customers.

Competition

Do not ignore your competition and ascertain that the business can compete effectively. If you are a manufacturer you should determine that the raw materials are available, and that your suppliers will give you the usual credit for payment.

Licenses

The local municipalities licence some kinds of businesses, such as restaurants, bowling alleys, auto body shops, etc. In some cases, provincial licenses are applicable and you should make inquiries with the vendor to ascertain that these licenses will be available to you when you acquire the business. Examples of such provincial license are liquor license and auto dealership license.

Offer to Purchase

Business offers are very different than house purchase offers. It is helpful if an agent can put the information together. The final draft should be prepared by us or checked by us.

We will bill separately for the preparation of the offer. We do not act as agents who charge fees only if the deal goes through.

Asset Purchaser or Share Purchase

There are basically two ways of purchasing a business; purchasing assets or shares. If the vendor organization is incorporated, you could purchase the shares and acquire the ownership of the company by purchasing and owning the shares.

In the alternative, only assets could be purchased such as furniture, inventory, goodwill, and even the name. This is called Bulk Sales purchase. The two transactions are legally quite different from each other, and have entirely different implications in the number of ways to the Purchaser.

We normally recommend an asset purchase because there is less risk of undisclosed liabilities affecting the purchaser. This question should be discussed with your accountant and us.

Bulk Sales Act

Where assets are purchased, the Ontario Bulk Sales Act must be complied with. This act is designed to provide protection to creditors of the vendor, and this protection is achieved by putting the onus on the purchaser to obtain an affidavit of vendor's creditors and they have to be paid off. If the Act is not complied with, the purchaser becomes liable for the purchase price to the creditors of the vendor.

Searches

We will conduct a number of searches, such as the Personal Property Security Act, Bankruptcy, Executions, Bank Act, municipal zoning, health and fire regulation compliance, Retail Sales Tax etc. These searches are needed to make sure that the assets being purchased are free and clear of any liens. For each type of purchase we will determine the searches to be conducted and advise you regarding the same.

Financing

A common way to finance the business is to give a lien on the assets of the company under the Personal Property Security Act (Chattel Mortgage). If you are a corporation, you could sell some portion of your equity shares to a partner and raise capital. The banks are another source of capital. They usually want very good security and unless the business is well established they will ask for a mortgage on your house.

Your purchase agreement should be made conditional if you are not sure of getting the loan from the bank or other source.

There are a number of grants and loans available from the government.

Allocation of Values

You should let us know the way the purchase price is broken down between goodwill, chattels and inventory. Retail Sales tax of 8% is payable on the chattels you purchase. Where land and buildings are purchased there will be land transfer tax on the value of the real property. Depreciation can be claimed on the chattels. For these reasons your allocation of price between the various assets being purchased is important. You should discuss this with you accountant.

Closing

Closing date is when you get the ownership of the business. It is usually about a month or more after the agreement is signed.

Inventory

Inventory should be taken the day prior to closing. Usually the cost of inventory is paid on top of the purchase price. If the amount is large arrangement should be made to pay for it over a time period. You should either agree to have an independent appraiser to evaluate the inventory or you should do it together with the vendor.

Goods and Services Tax

On the purchase of the business you should file the form for the exemption from GST. Please call 954-9875 for the information.

FEES

Our fees for the purchase agreement and the completion of the purchase transaction will be based on time spent and complexity of the transaction in relation to the size of the business.

We will be pleased to give you some estimate of the fees but new problems can arise which were not anticipated and in such cases additional fees will be charged.

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