Defining Assets When Purchasing An Existing Business

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Thousands of businesses are purchased every year. The motivations for purchasing a business are as varied as the number of buyers: to expand the buyer's existing business with a similar operation or to create new opportunities through a complimentary business. Perhaps the buyer seeks to change careers or add income to an existing one. And there is always the notion that buying an existing business avoids some of the risk associated with opening a new business. Business purchases are typically structured in one of two ways: a stock transfer or an asset purchase. A stock purchase involves buying the stock (or membership interest) of the company that owns the business. Typically, liabilities are assumed as well. An asset purchase involves just the assets of a company. In either format, determining what is being acquired is critical. This article focuses on some of the important categories of assets to consider in a business purchase: real estate, personal property, and intellectual property.

Real Estate

For many businesses (especially retail and restaurants) the real estate may be the most substantial asset. The seller either owns or leases the property, and there are different considerations for each alternative. If real estate is part of the sale, it will likely represent the bulk of the purchase price. If the business operates in leased premises, the seller would assign the lease to the buyer, and it is very likely that the landlord will need to consent to the assignment. The lease may also impose other assignment requirements, such as providing a personal guaranty. Also, it is important to determine how much time is remaining on the lease and whether there are any extension periods. Therefore, the purchaser should evaluate any leases early to determine what impact they might have on the future viability of the business.

Personal Property

The assets of the business will likely include a variety of personal property, such as cash, accounts receivable, contracts, warranties, inventory, supplies, furniture, equipment, and vehicles. Developing a list of assets at the outset is a critical element of the due diligence the buyer will undertake with the seller's assistance. Some items, such as furniture, equipment, and vehicles may also be leased rather than owned, and consequently might involve leasing issues similar to those involved with real estate leases. Cash and accounts receivable can vary significantly between the time the purchase contract is signed and the date of the closing and, thus, should be monitored closely to avoid a diminution in the value of the business.

Intellectual Property

Additionally, the assets of an existing business will likely include at least some form of intellectual property. Intellectual property is a category of intangible rights that protect commercially valuable products created by the human intellect. These include *trademarks* (a word, phrase, or logo that the seller uses to identify the source or origin of its goods or services); *trade secrets* (any information or technique not known to the public which provides an advantage over competitors); *copyrights* (which protect original works of authorship and include the exclusive right to reproduce the material and to prepare derivative works of the material); and *patents* (the exclusive right to make, use, or sell an invention for a specified period).

Almost all businesses have intellectual property. Trademark rights flow from use of the mark in commerce and do not require registration with the government, so it is possible that even a small one-person business could have trademark rights worth investigating. Domain names and trade names, for example, may include trademark rights. Similarly, copyrights are created the instant the work is fixed in physical form, and are not required to be registered with the government. Copyrights in website content may be a concern for a particular business. Finally, trade secrets are not immediately obvious by their very nature, but can include valuable information for the buyer of an existing business such as customer lists, financial information, new product ideas, vendor information, methods, techniques, data, or anything that gives a business a competitive advantage by virtue of the fact that it is not known to competitors.

It is important to identify any intellectual property and to investigate whether the seller exclusively owns the intellectual property rights or whether another person or entity owns any portion of the intellectual property rights by virtue of a license, assignment, or similar grant. It is also important to investigate whether there is any dispute regarding ownership of the intellectual property and whether there are any pending infringement claims.

Brokers, Accountants and yes, Lawyers

The seller and buyer who complete their transaction without the assistance of professionals are increasingly rare. Business brokers are an indispensable resource not only in marketing the business and trying to get the highest price for it, but in assisting the seller in addressing the issues outlined above; so that when a ready, willing and able buyer comes along, the buyer can undertake due diligence in an efficient manner. An accountant can assist on either side of the deal: for the seller by preparing a current profit and loss statement or financial statements and for the buyer to review the seller's books and depreciation schedules. An attorney experienced in business transactions can assist either side in documenting the deal as well as assisting in the due diligence process. Each of these professionals play an important role in identifying the assets to be sold, how the deal is structured, and carrying out the wishes of the seller and the buyer.