Why Buy A Business?

By Donald L. Beezley, Business Intermediary

It's long been understood that small businesses are the engine of economic growth in the United States. Perhaps most importantly at the personal level is that business ownership is potentially one of the best avenues to financial and life independence.

There are two sets of questions you must ask yourself—first, is business ownership for me; and, if you are going to go down the business ownership path, the next question you must ask yourself is: *should I start a business from scratch, or buy an existing one?*

Is Business Ownership for You?

Only you can answer that question. Below are some brief thoughts on exploring the answer to that question.

Reality Check

One of the most important aspects of owning a business has to do with your personality. Are you willing to work 6 or 7 days a week for long periods of time? Can you handle the significant stress that comes with the financial ups and downs that almost always accompany owning a business—especially in the early years? Are you honest enough about your strengths and weaknesses to either work on your weaknesses, or outsource those in some way? For example, if you're a great salesman but hate the numbers, or don't like to pay attention to operations, be sure a dependable accountant will keep you straight on the financial stuff and a good employee is on your team to help you ensure quality operations. Besides the personal aspects you need to consider, you must also assess your financial strength. Don't assume you will instantly make money when you start a business—you won't. In fact, depending on the type of business, you'll probably lose money for at least six months, and possibly for several years. Remember that no one owes you success. Making money requires creating value. And creating value takes time. As you work hard and service your market, the money will come if your business idea is sound, you execute a good plan, and run a good business. If possible, it's very beneficial to have a spouse who is working a "regular" job to help ensure steady income while you get the business off the ground. This can help relieve the financial stress that can come with starting a business and allow you to focus more on building a great business than on how you're gong to make the mortgage payment. Also consider talking with friends or family members who own businesses to understand what their experience has been. Last but not least, and you've heard it a million times, do something you love. If you hate dealing with the public, a restaurant may not be the way to go!

Should you start up a business from scratch, or buy an existing one?

All things being equal, I'm going to suggest that you primarily consider buying an existing business. The primary conditions in which it may make sense to start a new business are: you have significant and superior expertise in an area that will allow you to out-compete and gain market share from existing competitors; you have a unique idea that creates a new market.

The Benefits of Buying an Existing Business

An existing business has eliminated a number of unknown variables for you:

1. You already know the number of customers/clients the business has.
2. Operating systems are in place.
3. Experienced employees are in place.
4. The company brand already has a presence in the marketplace
5. A bank can make a more informed lending decision—possible getting you better terms
6. You may be able to get the seller to finance some or most of the purchase price
7. You have immediate cash flow—a known return on your investment.

Other possible benefits:

1. An existing owner who can train you.
2. Retaining existing customers or clients is cheaper than getting new ones.
3. Employees may be energized by change and new opportunities.
4. No distraction from the myriad of start-up activities that have nothing to with the ongoing process of building sales and profits—setting up payroll, designing systems and processes, etc.
5. Established supplier relationships.

Some of the possible issues with buying an existing business:

1. Your due diligence didn't uncover problems.
2. Older equipment.
3. Loss of clients or customers loyal to the previous owner.
4. Resistance to change by employees and customers.
5. Operating systems may be outdated or inadequate because the previous owner didn't "change with the times."

Employees

One of the most important and delicate situations that you—and the seller—will handle is dealing with employees, particularly key employees. A buyer will typically not be allowed (and generally should not be allowed) to talk with key employees until a purchase contract and earnest money are in place. Handling conversations with employees poorly can cause serious harm to a business, including unplanned resignations, defection to competitors, loss of critical information, or just general unrest and negativity. Clearly, handling employee interviews—both before and after you take over, will be one of the most important things you do.

Franchises

Starting a new business that is a franchise is not the same as buying an existing business. Just because other units of the franchise are up and running doesn't mean they are successful, that it's a good franchise or that you will be successful as a franchisee. Investigate all aspects of a franchise carefully including the franchisor, talk to other franchisees, investigate the development agent or master franchise for your territory if there is one, talk to customers, etc. Most franchises take a significant chunk of your business right of the top in the form of royalties—whether you're making money or not. Be sure that what they have to offer is worth it. For additional information, read the BizByOwner article ***Is Franchising for Me?*** And search the Internet for additional sources of information about franchising.

Planning

Even when buying an existing business, it is critical that you put together a succinct plan for how you are going to achieve your objectives with the business. At a minimum, consider the following areas:

- Put down on paper why you believe you will be successful with the business.
- Identify your sales and profitability goals for the business by creating a pro forma financial plan with an income statement including monthly projections for at least one year (monthly for one year, quarterly for a second year, and an annual third year is typical).
- Objectively identify the investment required in facilities upgrades, employees and marketing that will allow you to achieve your goals.
- Identify your customers as it relates to your marketing plan.
- Do a comprehensive Cash Requirements analysis to ensure that you are not undercapitalized—a cash requirements sheet is part of the BizByOwner Buyer's Tool Kit. Be sure it reflects all of the plans required to generate the results in your pro forma plan (marketing, equipment, employees, facilities…).
- After you get started in the business, keep yourself accountable to your pro forma plan by aligning your monthly financial statements in the same format and comparing your actual results to the plan each and every month, and identify what changes need to be made to stay on plan for both sales and profitability.

In Conclusion

If you do your homework you will have significantly reduced risk when you purchase an existing business versus starting one from scratch. The due diligence phase is critical; be thorough, and objective and rely on your partners in the process like your CPA or attorney. Even if there are aspects of the business that need improvement, as long as you have properly identified them during due diligence and adjusted your offer and plans accordingly, you have a much lower probability of failure.

So search your soul, and then start your search for the business that will let you live your dreams of financial success and independence!