

Chapter 12

In Chapter 12, we'll be getting involved in the actual basically what you call a negotiation of the contract, actually making the offer to purchase, counteroffer and going through the period called escrow or closing, go through a thing called bulk sale, also filing a financing statement, and going through the different areas that basically are at the end of the transaction or for those of you who are brokers, you're basically in the middle. In other words, you've already put the information together. You've got the listing. You're now going to sell it to somebody.

So, we're going through the different purchase areas here, and as you look at the purchase document on page 12-1, I'm not going to take you through every area. What I'd like you to do is use this as a guide when you're drawing up a contract or if you're having an attorney draw up a letter of intent or some short document.

The thing I want to warn you on as you start putting a transaction together, I don't want to put down my attorney friends, but the thing you have to realize is if you bring the attorneys in too soon, your chance of putting a transaction goes down quite a bit. It's not that the attorneys don't do a good job. It's what we try to do is we try to get a basic agreement between buyer and seller in writing, which is three or four pages long or maybe five pages, and then later go to the attorney.

Now, again, the attorney can say, "Well, you should've come to me first." Well, you can go to the attorney. You can check with him, but if you start getting him in there monkeying around with it right in the beginning and the buyer has one and the seller has one, you're going to find your chance of ever putting a transaction becomes very small. So, what we do is we try to take the pressure off the back of the attorney by going

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through the standard things that we normally want agreement on which is the price, the terms, whether they're going to stay or not, the down payment, and these are things basically that is something that the buyer and seller agree to based on how they feel.

The attorneys, basically, should be protecting you in the other areas. The CPAs should be protecting you in the area of taxation. Getting back to the attorneys, they should be protecting you in the area that has to do with legal protection and not getting in the other area of saying, "Gosh it is not a high enough price. That is not enough of a down payment." And, although attorneys may be very bright in a lot of areas, I still have not met very many attorneys that know anything about pricing a business even though they profess and give their clients information in that area. The same thing with CPAs, and the problem is you put them in a position where they have to overprotect you. What you should be considering doing – again, it's up to you to decide – you should be considering using some short form agreement. Again, it could be a one-page letter of intent that your attorney could draw up and then further refine it, or do what we do here which is use a short form purchase agreement. You could either use a state document that is available in your state, or use our example here.

Incidentally, if you do use a state form, you're going to find it really doesn't cover enough, and we've looked at all of them. What we suggest you do then, is go through here and pick out the areas your state form doesn't cover and pull our paragraphs out and use them as addendums to the contract.

Now, you have to realize we're not trying to beat the attorneys out of anything, and also the contracts that we use and any agreements have been drawn up by attorneys.

We pay attorneys for doing this over and over again. So, we're not beating them out of anything.

You're also going to find as we go through this later in this section, we're going to have the attorneys then come in as we have agreement on the short form, and the attorneys then will take the short form and expand it. We've also found if the attorneys find something blatantly wrong with what the agreement is, the agreement can still always be modified between buyer and seller by going back. But, the thing is we try to keep the attorneys and the other people out of the areas that basically is none of their business. Again, protecting the client is their business, but the thing is getting them out of areas that they really have no expertise in, but yet do make comments to their client. I know I'm going to get a lot of nasty letters from attorneys now.

The purchase agreement now – let's start going through it and let's start talking about the deposit. Many of you think that when you're putting up a deposit or earnest money or whatever you want to call it which is money to get the seller to pull the business of the market, you think a lot of money has to be put up. Well, it can be a token amount or what you can do is what we do most of the time. We use a promissory note. Where do you get promissory notes from? You can get them from the stationary store, and a promissory note you buy a pack of them, you'll have enough to buy businesses for your lifetime.

Now, a promissory note, what we normally do is we put up a promissory note as a down payment or earnest money, and on it we write that this money will be substituted by cash on or before the close, or we will then put up cash for this note after the offer is accepted. We don't like to put it up when it's accepted because things can still go wrong.

What we'd rather have you do is put it up at some point in the transaction after everything's been verified, after all the contingencies have been lifted, even maybe after your CPA has checked the business out because if you don't do this, we end up with a problem in a business.

The other thing I want to warn you on, when you do run into a business, and you do have to put up cash, what we normally do is we'll open up two escrows or two neutral accounts. One will be on the business, and the other one will be set-up stating that this money as a down payment or a deposit will not be funded to the regular escrow or closing until the following conditions have been met because what happens, we find in most cases if there is misrepresentation most of it is on the part of the seller, and usually what the seller's trying to do is get money in their hand. They then end up misrepresenting which causes the buyer to back out, and the buyer then has trouble getting the money. Why? Because it's already in the hands of the seller.

So, we are usually trying to figure out some method whether we're representing the buyer or the seller to keep that money in a neutral account as long as possible, and the reason for it is when we do have the problems, it makes it a lot easier to pull the buyer and seller apart and undo the transaction. Now, again, we start talking about this promissory note. For those of you that have fantasies about the fact that sellers are not going to accept these notes. If the seller comes to you and said, if you need a recourse, and say to them, "Look, I don't want a promissory note. I want money." Well, when they come to me and ask for that, what I say to them basically is, "Look, if I have to take money out of accounts that I have that are interesting bearing or something like stock I'm going to have to pay tax on, and put it up on this transaction, how do I know it's going to

go ahead? Now, if you insist I put it up, I will” But, since of most of the misrepresentation is on the part of the seller, I’d like you the seller to put up an equal or greater amount of money in an account, and have that account say that if this transaction does not go ahead because the seller has misrepresented, this money is given to the buyer. In all the years I’ve been doing this, everytime I bring this up as a thought to the seller, the seller then backs out and says the promissory note will be fine.

Incidentally, from a legal standpoint or from the attorney’s standpoint, having a promissory note is not that bad. Why? It gives the seller access to all the assets of the buyer, not just the cash. It’s an easy way to go. We do it all the time especially in the larger businesses.

The next thing and again, we’re talking about the price and terms, assets, liabilities – when you get down to allocation in here, this is allocation based on a couple of things. First of all, there’s a couple of different ways you can buy a company or sell a company, and if you’re looking at the bottom of 12-1 and over to the first part of 12-2, you’re going to find we have allocated. We have broken down the value of the business into it’s basic parts. When you’re talking to your CPA, you’re going to find that maybe the buyer and seller have agreed to a price of \$100,000. You now are going to break the price down into it’s basic components to get tax benefits to buyer or tax benefits to seller.

Now, this is in a sole proprietorship you allocate, or if you’re buying the assets and liabilities of a corporation. If you’re buying the stock in a corporation, you’re not going to be allocating on the offer to purchase. Why? All you’re doing is buying the stock. You’re just buying the stock. So, if you’re buying assets and liabilities – to repeat – or if you’re buying a sole proprietorship, you’re going to find that you are able to do a

thing called allocating, and as you sit down with your CPA he or she will break this down for you tax-wise. Again, you're going to have to have an agreement between buyer and seller in this.

The other thing we mentioned as you go into the paragraph under this allocation, it says, "An actual inventory shall be taken by buyer and seller at the time of closing, and adjustments if any shall be made at the completion of inventory. Any variation in access of a certain percentage between estimated and actual values for either the receivables, which is A, or the inventory, which is B, shall give the buyer the option to terminate the agreement." And, the reason we put that in there is sometimes in the transaction, the amount of inventory, or the accounts receivable, could vary so much that it could kill a transaction, and what we're doing now is giving the buyer the opportunity to spell out what variation they can live with. Again, don't come back and ask me what the amount is, ten percent of \$100,000 is only \$10,000 and you could possibly live with that, but if it were a million dollars and ten percent could you live with \$100,000 variation if you used ten. So, what you're going to have to do is work this backwards and use your common sense, but you're going to find it's going to help you.

You're also going to find as you go through the agreement we have a number of things in here that discuss different areas – buyer's remorse and seller's remorse, and spell it out for you. So, read the different areas.

Now, keep in mind also, this document was developed a long time ago to protect both the buyer and the seller, and you're going to find if you happen to be a buyer you may not want to use all the paragraphs and the same thing from the standpoint if you're working from the seller's standpoint. You may find all the paragraphs may not apply to

what you're trying to use. So, just don't blatantly or in total take the form and sign it and use it because you're going to find there's going to be a paragraph or two in there that are not to your benefit.

If you look at page 12-9, there's a thing called covenant not to compete. It's something that a lot of you asked me about, and this is the agreement not to compete. In this example right here, it's included as part of the original document. As you or your CPA check the law, you're going to find that this has to be a separate written document. So, as you get into the escrow closing period, whoever's handling the paperwork such as the attorney will have to draw up a separate document for the non-competition agreement.

But, basically, all the non-competition agreement says is the fact that the seller will not compete with the buyer for a radius of so many miles, and also for so many years. We find in certain parts of the United States, the non-competition agreement may not be valid. They may have – such as Montana – they may have a rule that states that you can only have non-competition within the county. Or in Honolulu, they don't allow the non-competition law from the standpoint of the legal side. The reason for that is if you set up a 50 mile non-competition in Honolulu, the person would probably have to go to Australia.

The thing you have to remember in the covenant not to compete or the non-competition is you have to keep it fair because you're going to find the courts are not going to allow you to set-up a non-competition agreement that will keep the buyer or the seller from every gaining employment or feeding their family. So, you're going to have to make sure it's fair.

You're also going to find out in the area of years, you're going to be able to write it off based on the number of years. So, if the non-competition agreement happens to be for a value of \$100,000 and it's for a five year period, the buyer can write-off \$20,000 a year. IRS then just tries to keep it inline by saying, "We would like you to have a non-competition agreement not go beyond your normal life." In other words, the insurance companies have put out actual tables based on that if you're at a certain age as a man or woman, you will probably live so many years based on their statistics. The government then uses this to make sure you don't go beyond that period. Again, I'm not trying to give you a complete definition. I just want you to understand that in this program.

As we finish this contract, basically what you're going to have is the buyer and seller are sitting down and they're negotiating. You're going to have things called counteroffers where the buyer's going to make an offer to the seller. The seller's not going to like certain things, and counteroffer back. By the time you're finished even though you're starting with a small document, you may end up with a couple of more pages as buyers or sellers want to make changes in the original document. Eventually, if you've done your homework, you'll get to the point where you do have agreement between buyer and seller.

Now, in the contract we just talked about here, I want you to realize there's one basic thing we've left out, and that's called the contingencies, and if you look at the next page we have here, you're going to find that we have a thing called contingencies. Now, contingencies are also known as weasel clauses, and again, please don't call them weasel clauses in the contract or the negotiation. You'll screw it up because you'll scare the seller. But, again, if you want a full disclosure, that's what they are.

Contingencies mean basically this contract is subject to the following things happening. An example here, the buyer's example – it says the purchase is subject to inspection and approval in writing of the books and records of the buyer, and what you have to realize here from a buyer's standpoint - you have to sign-off on these things.

I also want you to realize as a buyer, you don't have to go back and explain to the seller why you didn't like the books, and you don't have to explain to the seller that you didn't like page seven, eight, and nine in the journal. What you have to do is if you have checked the books and you don't like them, do not sign off and approve them. And, also beware – beware of people that write the contracts in reverse, and what they end up doing is they'll put it down, and again I can't quote it exactly, but it will say that you will have – the buyer will have so many days to verify and check the books let's say ten days. If at the end of the ten day period, they have not notified the escrow in writing that they don't like the books, the contract will then assume that we are going forward.

In other words, if you don't go back as a buyer and tell them in writing that you didn't like it and spell out specifically what it was, that you have to go ahead with the contract. Do not get trapped into that.

Now, in all the years I've been working with people that have it that way, it's usually something that comes from the business broker's community, and again of all the times I've seen it, I have also found if I further check these brokerage firms, they also try to rip off people in other areas. Is that a rip-off? Yes, because what they're trying to do is rip you off in the negotiation.

The next thing is we say the purchase is subject to inspection and approval in writing of the equipment by the buyer. These give basically a buyer the agreement, and

again if you're doing a good job as a buyer, you basically have gotten the seller to take the business of the market. You've gotten the seller to agree to certain things, and you then have a way out.

The thing you have to realize as you get involved in financing, if you have gotten the owner to carry back financing for 75 percent, and you hit the owner with a contingency that said, "This is subject to my borrowing 25 percent down and four million other dollars." What you're going to find is the seller is going to get very upset with you because even though the seller has said to you, "This is what I want. I would like to get 25 percent down and I will finance the other 75 percent over so many years." They get very uptight when they know you don't have the financing because basically what it is when a person comes in to a seller and the seller said to the buyer, "Do you have a financial statement?" and, small businesses like Mom and Pops or little start-ups, they're going to find they want the financial statement because they want to check your cash flow to make sure you can make the debt payments because the business won't have a lot of money or none.

When you get into the larger businesses over \$50,000, most owners are not asking for a financial statement because they want to find out where the secondary source of repayment or how are you going to repay the money because the business you're buying can repay it and do it safely. What they're trying to find out in your financial statement is can they see on your financial statement where you're going to get the down payment from? Again, the basic thing you're looking at here is they want proof that you can come up with the money. Very few sellers really care where the money's coming from, but what they like to do is make sure you're not a tire kicker and they want to make sure that

if you agree to give them 25 percent down, that you can deliver on it, and that's the key thing. I'm not going to say the other never exists, but that's the key thing they're looking for.

Now, what you're going to find is for those of you representing the sellers or if you are a seller listening to this, you have to realize we're teaching this from two sides, and what you should do is counteroffer because what happens is if a person buying the business comes in an offer that tells you that they want this subject to inspecting the books and there's no date on it, that means you can keep this thing open forever. So what you should do is consider counteroffering.

When they put down the purchase is subject to inspection and approval in writing, you should put down that you have to do it within ten days, or if they want to inspect the equipment, within three days. Again, I'm not recommending that this be the period, you should put something down. This enables you to cut them off and you have counteroffered. They then have to make that decision. If they haven't made that decision and signed off in that time, you don't have to go ahead with the contract.

Now, keep in mind, if an offer has been made and there's a counteroffer that said that you have to do it within ten days, and you're the buyer, and say your CPA has not had a chance to get finished in ten days, you still could go back to the seller and get the thing changed. Don't be afraid of that, but do spell out all the details.

Now what I'd like you to do now is we're going to turn to the backside, just flip the page over, and you're going to find now we're going to start talking about the escrow, the closing, the consummation of the transfer from buyer to seller. Now, as we're going

to be taking this to a period now. We've got the buyer and seller to agree to terms. We've gotten the sign-off on it.

Now, before you do this, before you go out and start to open up an escrow or go through the closing period, or bringing attorneys into it, CPAs, I want you to realize I want you to get the financing done first. Now, I don't mean say I don't want you to hire the CPAs or the accountants or the attorneys on an ala carte basis to check contracts and do various things, but we normally do not bring them in to do the major billing and the major checking until after we've had all the basic things done. Why? Because too many things can still go wrong.

So, before you open up the escrow or start incurring a lot of expense, what I'd like you to consider doing is get the contingencies out of the way like number one, do you have a financing problem? Are you still having trouble with the down payment? Have you gotten approval from the bank? Have you worked with your suppliers? If you haven't done that, what I want you to do as soon as the thing is signed off before you commit yourself to spending money as a buyer, I want you to side step down the street and take care of your financing.

As soon as you take care of your financing then, come back and do the thing you called open up the escrow, sit down with the attorney, sit down with the CPA, but don't do it before you have all these things done. Why? Because if you don't do that, you'll end up committing yourself to a lot of money, and the transaction will not go ahead, and you'll have to waste that money, and again, knowing full well that you're going to have spend the same large amount of money on the next one. So, please do it in the right order. Take your time.

Now, once you've arranged whatever you have to arrange – financing or whatever – we then consider going to what we call the escrow or closing period, and if you look at the sheet it says, “The consummation of the transfer from seller to buyer.” Again, the consummation – quite often we're using an attorney and we usually recommend using an attorney because they're also required to handle and expedite the legal work.

Now, again, we have over the years tried to work with banks, title companies and escrow companies, and although in some areas we do have exceptional ones we've worked with, we have found over the years that they don't do a good job in our area. They also tend to make comments about the legal part of the transaction or the tax part of it, or just say, “What kind of a Mickey Mouse deal is this?” And, what happens is we have a hard time keeping people that know nothing more than how to shuffle papers from giving legal advice, giving tax advice, and again we've just had bad experiences with them. If you've happened to have a good one, fantastic. In fact, we'd love it if you could come back and recommend them after you get down using them because having good people in this area to work with would be fantastic. But, we haven't found that over the years.

The next thing I want to talk about here is the actual purchase agreement because what we're talking about here on this page under B is where talking about the long form, and we're saying pages and pages of protection for buyer and seller and brokers. Do not be tempted to use a short form to carry through the full transaction.

Now, in the past have I seen things go through with a short form? Yes, I have. Have I also seen a lot of lawsuits because of that? Yes, I have. What I'd like you suggest you do is take your time and go the right way. It may be a little more expensive, but

you're going to find that once the attorneys take the three words whether we have agreement between buyer and seller, and expand the three words out to 50, 500 whatever it happens to be, add a lot of other boilerplate which is just standard paragraphs, you're going to find that you're going to find fewer lawsuits. You're also going to find fewer buyers and sellers pulling out. Why? It's very easy in your mind to take three words of an agreement between you and the other party and twist them and say, "I can get out of this."

Once they get it up to many, many words, you're going to find that most people don't back out because the reality hits them right in the face when they sit down and read that long paragraph and say, "Oh, it isn't as I thought it was." Why? Because it's been spelled out with a lot of words, and although I don't like having to go to long contracts, I have found over the years you have to do it. You have to spend the money.

For those of you listening that are still thinking about, "Gosh, I'm not go through an attorney. I'm not going to use a CPA." Number one, every person in the transaction needs an attorney. Every person in the transaction needs a CPA that knows what they're doing. In fact, you're going to have to find an attorney and CPA that understand business. You're not looking for a divorce attorney. You want an attorney that has done this before a number of times. You want a CPA that knows how to check books. You're not looking for a CPA that has worked as a controller for a large corporation. You have to have somebody that can help. Just because they have a title, doesn't mean they have the experience or that they should be working in this area.

As we turn the page now, we start to get involved in the area that is very interesting. It's a thing called a bulk sale, and the bulk sale is broken into two divisions.

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The one that we have in the section here in the book is from the California Uniform Commercial Code, but you're going to find that it is very easy and very similar to the national, and let me explain it from a national and a state standpoint.

Many years ago, the Uniform Commercial Code was developed at the national level. What has happened since then as far as I know, all the states we have been in, they have adopted the Uniform Commercial Code. The only one that we have found that has been a little different has been the one in Louisiana, but over the years every state that we have worked in has had the Uniform Commercial Code.

What has happened is the states then have varied the Uniform Commercial Code that was set up at the national level, and set it up for their own level. The reason why we use California is most of the people that we work with are from the California area, and we also find that the Uniform Commercial Code in California is the best one to use in a teaching situation because the California area is the toughest one. California is the one that other one's normally follow, and that doesn't mean that California is the leader. What we find generally is that California leads in the area of fraud, and since I happen to be from the state I'm not criticizing another state.

Now, what we have here is we have Division Six of the California Commercial Code, bulk sale, and basically bulk sale is just posting in the newspaper of general circulation information that the business is being sold. And, what happens is it gives information to the creditors, unsecured creditors. In a few minutes we're going to cover a thing called the financing statement which shows how a creditor can put a lien on a business or remove it, whatever. They're secured. But, the thing is we also have a lot of unsecured creditors out there, and a bulk sale goes out to protect those people.

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Also, for those of you who are buyers in the business, this is the only basic protection that you get when you take over that company. Why? Bulk sale, we don't have the normal protection that you have say in the area of real estate.

First of all, we're saying on a bulk sale used in California, it has to be recorded in the Office of the County Recorder in the county or counties in which the property's to be transferred at least 12 business days prior to the bulk transfer. Most states require that you give the information at the county level. The difference between California which tells you that you have 12 business days to the other areas is some of them will say seven days, some 14, some 20. So, find out from your state what it is.

Also, I want to warn you that as you get the information from your state, you better check it for another state because each state is basically different and also each state basically in December ends up changing various parts of the things. So, you're going to have to find out what it is today, and at the end of every year the first part of the next year, you're going to have to find out what changes have been made, and they do make a lot of changes.

B is one of the most important things and it said, "Published at least once in a newspaper of general circulation", and it also tells you how much ahead of time you have to do it, and again two things vary from state to state. Number one, how many times you have to publish. In California, it's only once. Other states it's two, three or four times. And, the other thing that varies is how many days ahead of time you have to do it, and you better make sure you follow both of those.

"Personally deliver or send by certified mail in this 12 days, a copy of this transfer" to whom? The county tax collector. Why? Over the years, many unscrupulous

business owners have tried to beat the local, state and county people and federal out of taxes they owe. So, what did they do? You have to send notice to these people. Why? Because they'd like to collect the money.

I also put in there what a business day was because in the state of California, with a lot of holidays you might cut the bulk sale short by a couple of days and end up goofing up the buyer.

Okay, I'm not going to talk about the notice contains because you're going to find as you go down to publish this, say you happen to be the buyer, and it's your basic responsibility because it's protecting you. You have to go down and publish this, and when you go down to your local paper, you're going to find they have beautiful NCR snap out forms, and on it each one has a different color and as you sign it and fill it out, it gives the newspaper all the information that they need. It also tells you how much money you pay. You hand it to them. There's usually little arrows on it going to the next copies to tell you which copy goes to the county, which goes to the tax collector, and so on which is your copy. So, they've made it very easy today in the United States.

Also, don't be tempted to put these notices in little Mickey Mouse newspapers because if you do end up with a lawsuit you're going to end up that you may not win the case. So, what I suggest you do is follow the law. It was set up for certain purposes and don't go around it.

Now, in some states, you have to go through the bulk sale is protecting the buyer and the creditors, in other states you have an option or some states only require certain businesses to do it. All I want to tell you is one thing, if you're going into a business and you want to protect yourself and you're a buyer, do not waive the bulk sale, and again, I

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don't happen to be an attorney and I'm not protecting you from a legal standpoint, but I have been in business many, many years now and all I can tell you is everytime I have seen a person violate this or try to take a shortcut and that's what most of you do – you say, “Hey I'm going to take a shortcut. Why go through the bulk sale? I can close sooner. I can take over sooner.” Right, and you're going to get ripped-off sooner. So, what am I telling you? Fine, you're your own person, you can listen to your own attorney, but as a friend, I just want to tell you please use the bulk sale whenever possible because you're going to find it's going to help you out.

Now, what I've done in this section also, I have included all the other information that has to do with the California Code in this area, and the reason for that is some of you do need more detail. So, I have left the information in here for you, and I'm not going to cover it.

Now, what I'd like you to do now is in this section, I'd like to turn to the next important section here, and the section is on page 12-21, and it's called the financing statement. The financing statement, again, you're going to find this in the National Uniform Commercial Code. You're going to find the local one. It's Division Nine of the California Commercial Code, and again it's part of the National Commercial Code, and what we're doing now is we're going to have three different copies that we have available. We have the UCC-1, the UCC-2, and the UCC-3. These are all forms that have to do with placing liens on businesses.

Now, in real estate you have things called deeds of trust and you have mortgages. Again, these things basically are liens on real estate. In business, the only type lien we have is a thing called a financial statement and they are secured at the state level, at the

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Secretary of State. Now, in certain states, you're going to have to check this out because in some states you also have to record these at the county level. California, again, it's just at the state level at this time.

The first thing you have is the UCC-1 which is the financing statement and again it's effective for a period of five years from the date of filing and you better check on this because in the days before we got involved in education, most of the financing on business from banks or from owners was five years and less. As we start to expand it, you'll find most of our financing now is out in the 15-20 year category and beyond and you better worry about it from the seller's standpoint. Why? You're going to find at the end of the five year period this will be removed from the record which means there is no longer this lien on the business. Again, from a buyer's standpoint, you're not going to worry about it, but if you happen to be the seller, you better remind yourself every five years to go back and renew this or you're going to find the lien's removed and the buyer can then go out and rehawk whatever you have put the lien on because it doesn't have to be a lien on the business. It might be the lien on the equipment, the receivables or any other item in there. It might just be a lien that the plumber put on the business because you didn't pay your plumbing bill. It could be anything.

Now, if you want to see what the financing statement looks like, look at page 12-25 in this section. Again, for those of you from other states other than California, you're going to find that you can get them in your state or in California, any state, by going to a stationary store and you're going to find they have four or five copies, snap out NCR. You don't even need carbon paper, and they sell them very inexpensively in little

packets, and you then can go out and file your financing statement. You can then put the lien on the business.

The next thing that we have is the UCC-2. It's on page 12-26 for those of you who want to see a copy of it, and we're doing a number of things here. The first thing we're using it for is continuation. A continuation statement may be filed by the secured party of record within six months prior to the expiration. Why? You want to continue it on for other five year periods. For release from the collateral described – so, it's releasing the collateral.

The next one is assignment. A secured party certifies that the secured party has assigned to the assignee all the secured party's rights under the financing statements. So, you're assigning it to somebody else.

The next one is a termination. A secured party certifies that the security party no longer claims a security interest. Great. The last one is an amendment. The financing statement is amended as set forth. You're going to make a change in it. So, it's used for all these things.

The thing that is quite often forgotten is the fact that when the thing is paid off, a lot of people forget to have this thing removed, and what happens is you come up to buy the business and you find there's still a lien on the business. What I want to warn you also in this area – if there's a lien on the business, and even though the seller is telling you it's been removed, we find quite often that what we should do whether we're listing it or buying it is back-off, let the seller have it removed, and then tell them to call us as soon as it's removed. Why? Because quite often that little \$50,000 lien on there is clouding a five million lawsuit that's about to be filed. So, let's clean the thing up as

much as possible. Do not take a “Subject To” – we just back off – no “Subject to” and we also don’t say the sellers going to indemnify it guaranteed there’s no problem because although they may be very wealthy and be worth hundreds of thousands, the lawsuit behind it may be for millions. So, let’s take it safe. Take your time.

The next thing is a UCC-3, and that’s the information copy and you’re going to find it’s mailed to the Secretary of State with X number of dollars depending on what state you’re in, and you’ll send back the financial information on that state. The only bad news is sometimes depending on how busy they are, it takes a week, week and a half, or two weeks to get it back. If you’ll check with your local escrow company or your local title company or attorney that works on business opportunity escrows or closings, you’re going to find by going to them, they will tell you the different companies in your city that actually provide service, and will give you this information on liens within a couple of hours.

By calling these people on the phone, they will get information on your company, and they will then call their service that’s in your state capitol. They’ll walk across the street. They’ll research it and call you back in two, three or four hours. You then have a verbal response.

If you then in writing in a couple of days, you’ll get the written copy of it in the mail. It’s not very expensive, and for those of you in a hurry, go that way. Incidentally, I don’t care how clean you think a company is, always do this. I don’t care if you’re the broker, the seller or the buyer, just run one of these prior to the time you’re about to sell it or mention it to somebody so you can find out ahead of time if you’re about to have any

problems because a lot of times you may have a lien on it that you forgot about it or it just may be something that's come up that's a mistake. So, let's get it taken care of.

The one thing I want to tell you also about the three different UCC copies is you go to different states, and all the states I've been in they do have three different copies, but what they've done to be a little creative, what we call here the UCC-1, they may call it two. They may call it three. They may call it one. So, you're going to find a variation in that area.

But, as you go out to look at the basic form, the basic form is the same. A few lines may be different, but the concept is the same and the information required or the things that the forms do provide is the same in every category. But, again, I'm sure it would be nice to have standard statements, but we don't have that.

As you turn the page, we're going to start talking about a thing called inventory because as you start to think about the closing period, when you think about the other, you're probably going to say, "Why don't you provide a complete checklist in this area you can use?" Well, we've looked at that over the years, and we certainly would like to provide a checklist, but the problem is we can not provide a checklist other than what we're about to go through that would apply in enough areas because in most categories you're going to find that as you go to the escrow company, the title company that you're working with, or if you're going to the attorney or whoever's handling the escrow – it could be a CPA – you're going to find that they already have checklists. They will give you a checklist, and the good thing about the checklist they're going to give you, it will apply in the area that you're buying this business in or you're selling the business. I'd rather have you do that then us give you something that's going to mislead you. So, what

we'd like to do is just take you through the areas that are general and the other areas you're going to have to get the specific information from your professionals.

Inventory – taken by independent appraisers. We talked about this before, but the thing you have to realize is we're talking about taking the inventory and usually you can have the buyer and seller take the inventory a day or so or a couple of hours before the thing closes and the buyer takes over. But, the thing you have to realize is buyers and sellers normally fight when they get down to the inventory point, and there's a good chance of blowing the transaction. Also, if you happen to be a broker, it's not too good to have them take the inventory because everytime there's a discussion between buyer and seller, and they can't reach a decision, they will usually call you the broker agent over and have you subtract it from your fee, which is a nice way for them to settle an argument. Most of the time, the broker will go along with this which is not fair to the broker.

What we say is the independent appraisers – they're listed in the yellow pages of the phone book – and again, these people come in for a very small fee based on how many hours it's going to take. They'll take the inventory. You'll also find in most cases they are bonded which means if there's a mistake made, you'll find that they're insured for the mistake and they'll make it good. And, you're also going to find one other thing you're going to find is they specialize in certain areas. Again, they will have specialists within the specialty areas which means they know more about the inventory than usually the seller does. In most cases, the buyer of a business is not as knowledgeable as the seller. It's a good protection for the buyer to use an outside company. We recommend it highly, but again it's up to you.

We start to get involved with sales tax. We have two different sales taxes. Number one sales tax you're going to run into is a sales tax that is collected from customers or clients of the business. This is collected by the seller normally, and the seller has collected this over the past month, the past two months whatever the collection period is, and this money is owed to the state in the transaction.

Now if you happen to be in a state where you collect sales tax, you're going to have to realize that the state sales tax organization has to be notified. If you do not notify the state sales tax organization that the business is selling and they are entitled to a sales tax, you're going to find that we have a thing called "Successor's Liability". The law of Successor's Liability basically states that in this case if the seller has collected the sales tax and either the buyer or the seller or somebody has not notified the state sales tax organization of the sale, then what happens is the state has recourse against not only the seller who's collected sales tax, but if you happen to be the buyer, you also are going to become responsible for the sales tax that was collected by the seller before you even bought the business. So, you better make sure that the state is notified. They don't like to be ripped-off.

Why do we have these laws? Because in the past, they've been ripped-off a number of times.

The next thing has to do with sales tax that you collect on the sale of equipment, and again, we talk about California. There's a couple of other states in the United States that collect sales tax on equipment, and when you have a collection on sales tax on equipment in a transaction, the state has to be notified. Now, normally the buyer is responsible for paying the sales tax on equipment either during a transaction or after the

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transaction, and the buyer's responsible for the sales tax. Now, because the state has a hard time collecting the sales tax from time to time, we again have the law of Successor's Liability which states that number one the buyer is liable for paying the sales tax, but if the buyer does not notify the state organization, the seller also becomes responsible.

Where we have this most often is after you take over the business and you decide you have some excess equipment, the buyer's going to say to you, "Gosh why do we have to contact the state? I'll just pay you the \$10,000 for the equipment, and we'll save whatever the percentage is." What happens when the state catches you, you're going to find they have a hard time finding the buyer of the equipment, but they always have access to you the owner. So, what I'd suggest you do is play it by the book. Do notify the state. It's only there to protect you.

Utilities – please remember to transfer the utilities to the new owner before the closing or you may become a new account with a large deposit, and you have to realize many times we're going to be doing a thing called dissolving a corporation. If you're dissolving a corporation during the transaction and you're changing the names, you may have to go back to the utilities and change. In fact, in most cases you do. If you're going in as a sole proprietorship, and again, you're taking over on a Monday, the normal owner of that business is going to go in on Friday. The owner of that business is going to change and take the utilities out of his or her name. The problem is if you don't get in there also before the weekend, the utilities will consider you a cancelled account and on Monday about six a.m. they'll cut off all the utilities. When you then take over the business in the morning, you're going to find all your employees outside because there's nothing working. As you then go down to the utilities to have it turned back on, they're going to

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consider you a new account and they're going to want beaucoup dollars for deposits. So, I suggest you do it a head of time. This is one of the goofs that a lot of people get themselves involved in.

Special permits and licenses, next page – a license or a permit may be required for new application. Again, a lot of you think about liquor licenses or beer and wine licenses in different states, but the other thing you better keep in mind how about having to take over the franchise agreement. I mean, you're going to have to have approval on that. Suppose you want to take over a Ford or a Chevy agency. Either Ford or General Motors is going to have to approve you or you can't go ahead, and for those of you that don't want to get approval, and want to take over the business subject to, I can tell you a number of horror stories on this from people that took over auto agencies and couldn't get approval. When they don't approve you, guess what you can't get. They won't sell you any of their cars. It might be motorcycles. It might be a Kawasaki dealership. It might be a tractor dealership. On these, you're going to need approval on a distributorship or the franchise. So, you better make sure you get this. In fact, when you write the offer, the offer should be subject to you getting approval on you taking over as a buyer.

Franchise status – we mentioned this many times. If you happen to be a state that does have franchises or does have a franchise law, I suggest you check with the corporation commissioner right at the end of your attorney check to make sure there's no cease and desist order that's been issued.

Now, keep in mind, that we've talked to a number of people from the Department of Corporations from different states, and they tell us that they do not give out

information on their investigation until after they've finalized because of problems with lawsuits.

Department of Employment – you need a Certificate of Release from the State Department of Employment or the buyer may be liable for unpaid unemployment taxes and employee benefits such as unemployment and disability insurance. So, please contact them.

Local taxes – local tax releases should be obtained. Again, I'd love to give you a list on this, but this keeps going on and on, and as the tax burden keeps shifting and the government wants to collect more taxes at different levels, it's impossible for us to keep up or even put it on a checklist. So, what you're going to have to do is check as you get involved and then be prepared for more of them on a year to year basis.

We'd like to remind you to assume the phone number. Take it over. Please assume the post office box, and the last thing, please remember to refile the fictitious business name if you're in a state that requires it. In some states, it's not required anymore. What you're doing here is if your name is Art Hamel, and you're operating as Johnny Jones, they want you to publish that in the newspaper so the creditors will be aware of the fact that you're working under a name, or operating under a name other than your own. So, it's operating under another name other than yourself.

One last thing I want to mention, and it's a thing we have a hard time figuring out where to put it. It probably should be in the section by bulk sale, but a short while ago in this tape, we covered a thing called bulk sale and in covering bulk sale there's a little warning that we have to give you now, and the warning has to do with the fact of what happens if you are going through and buying a corporation.

Now, if you buy the assets and liabilities of a corporation, there's not much of a problem, but suppose in buying a corporation you decide to buy the stock. Now, if you buy the stock, one of the things that we have recommended over the year not because I'm smart but because the attorneys I work with all over the United States have recommended it – not recommended it – forced me to do it. We usually do not keep the corporation that we take over, and what we normally do, and I don't know the steps – you're going to have to check with your attorney on this, your tax attorney – you're going to find out what happens during the escrow or closing period. We will take the corporation that we have purchased, and the attorneys then will form a new corporation for us. The purpose of the new corporation is at that exact moment that the thing closes – the escrow or the closing – and the lightning strikes and all the money shifts from person to person, and the buyer ends up taking over the business, you're going to find that basically what we have here is a situation where we have a problem, and when you take over a corporation, you buy the stock, you're going to find that you take over all the assets known and unknown, all the liabilities known and unknown.

Now, you can't get protection under the bulk sale because the bulk sale basically puts a notice in the newspaper and allows you as an individual to come in and pick-up the known assets and liabilities which is fine with a sole proprietorship if you buy assets and liabilities of a corporation. But, if you're buying a stock whether you run bulk sale or not, it doesn't make any difference, as soon as you take over that stock, you take over the lawsuits that haven't been filed yet. And, even though there are no lawsuits on the books, you're going to find about an hour after you takeover 15 people are going to sue you for 40 million dollars. Why? Because the old owner was a flake, and you now are the new

person which is very honorable, reputable and probably has a lot of money. So, they're going to go after you.

You're going to find also, how about the unpaid payroll taxes? How about the unpaid matching payroll? How about the fraud the former owner committed? You then become the new stockholder, and also known as what? I think it's called stuckee. No, that has nothing to do with the stock. It's another term. We'll cover it in the next section of our tapes.

What I'm trying to tell you, what you should do is sit down with your attorney and decide whether you want to keep that corporation. What we do in most cases is we will have our attorneys again dissolve a corporation and will then have our corporation move in at that last moment when the lightning strikes and take over the known assets and liabilities. The ones that we don't know about then remain with the former owners of the corporation, and they get stuck with the problems they caused for themselves.

There's one other way you can consider going and you can have them do a thing called indemnify. In other words, have the former owners guarantee that there are no other problems or no other debts, but the problem is even though the owners are going out of this business and may be very wealthy, do they have enough money to really protect you against what you could get hit with? Again, I'm suggesting that you talk to your attorney and decide which way to go. Again, in most cases we find we go with a dissolution of the corporation because it keeps us out of trouble.