

Buying a Business in Florida: Due Diligence Issues

by Gary Kauffman, Esq.

Buying a business can be complex. Whether you're purchasing a small restaurant or a large manufacturing facility, it is crucial to conduct the proper due diligence activities that will help you to evaluate your business. This article will highlight just some of the key due diligence inquiries (often occurring after you've already gone to contract with your Seller) for a buyer purchasing a business in Florida.

1. Financial Records. Ask your Seller to provide you with copies of all financial records, including a balance sheet, profit and loss statement, tax records, check registers, QuickBooks files, and cash flow records. Find out where funds are going to, and coming from. Is Seller infusing cash into the business, with little income showing? Are there spikes in income or costs? If profits are low, are Seller's principals receiving other benefits (e.g., a car) through the company? Consider an accountant review (see #5 below)

2. Real Estate. The most important due diligence is often evaluating the real estate used by the business. If your Seller owns the property, do a full property inspection and title search. And if your Seller is renting, have your attorney review the lease. Confirm that the lease term (with renewal options) is sufficient; that the rent and pass-through costs are affordable; that you have adequate parking; and confirm who pays for utilities and equipment maintenance. If the tenant is responsible to maintain its own air-conditioning system, get it inspected. This is Florida. If the a/c system is old, find that out now, to avoid a major surprise cost after completion of the sale (the "closing"). Finally, confirm that the lease is assignable. Your attorney may have to negotiate with the landlord, whose consent is generally required for any lease assignment.

3. Key Contracts. It is vital to review all major contracts that you may wish (or be required) to assume. Examples include employment contracts; union

agreements (if debt is being assumed); equipment leases; supplier contracts; etc. Make sure that essential contracts are assignable!

4. Seller Liabilities. Most buyers will want to purchase the Seller's *assets*, rather than its *stock*. By doing an asset sale, a Buyer avoids acquiring the *liabilities* of the business being sold. That said, even in an *asset* sale, a Buyer runs the risk of acquiring certain Seller liabilities if the Buyer doesn't do his or her homework. Below are some examples (by the way, always try to have a portion of the purchase price be a 5-year term loan from Seller, with *offset* rights; so if you have to pay any Seller liabilities, you can offset such costs against installments under the Seller Loan):

a. Liens & Charges. If the Seller borrowed money for the business, the Seller may have granted a mortgage, security interest, or other lien or charge on its assets. Unless a lien is satisfied (paid off) at closing, the Seller's debt to its lender will become your debt – or the lender may foreclose or repossess the assets you've just purchased. If your business includes real estate, have your attorney order a title search to discover mortgages; and if the business includes equipment, have your attorney order a UCC-1 search with the Florida Secured Transaction Registry to discover liens. And liens are not just about lenders. Your Seller's assets may have a tax lien in favor of the Internal Revenue Service; or a judgment lien in favor of a creditor. Ask your attorney to search the public records for all of these.

b. Lawsuits. Your attorney should also search the public records to find out if the Seller is involved in any lawsuits. You don't want to acquire your Seller's mess. Even if a suit does not create a *judgment lien* on any assets, you do not want nuisance litigation from an unpaid vendor or disgruntled employee.

c. Sales Taxes. Is the business required to collect Florida sales tax? If so, Florida Statutes §212.10 imposes

potential liability on the Buyer for the Seller's sales taxes. To avoid acquiring the Seller's debts, get copies of its filed tax returns and canceled checks, and have your accountant review them. Also consider requesting a clearance letter from the Florida Department of Revenue, for assurance that your Seller is not in default. But some Sellers won't cooperate with this, for fear that a request might prompt an audit. In this case, require the Seller (and its principals) to indemnify you for any tax liabilities. And how do you *enforce* an indemnity? Again, it helps to have a Seller Loan, with offset rights.

5. Accountant Review. Finally, consider having an accountant help review the Seller's books and records as part of your due diligence process. An accountant can help to determine if past revenues justify your purchase price; if certain taxes are being paid; and a proper purchase price *tax allocation*.

Conducting proper due diligence on your business will help you avoid any surprises, and ensure that your business achieves your goals. While purchasing a business is complex, it can also be rewarding. It can offer you new challenges, and to realize a new dream. Whatever your reasons, enjoy the ride!



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