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The Basics of Buying a Business

DISCLAIMER: This outline is a general guide. Be sure to contact an attorney if you have questions or specific issues that need to be addressed.

No matter if you're purchasing a thriving shop with a valuable list of clients or a hometown favorite that's about to close its doors, businesses aren't something you can just buy off the rack and pay for at the register. The process takes time and diligence. From your first offer through the closing of the sale, you'll see many legal documents and sign many contracts along the way. Below is a short walkthrough of the basic business buying process. Remember, business sales are incredibly nuanced and may differ from these steps depending on the company and industry. This is an area it's really important to make sure you work with an attorney!

Step 1: Buyer's Initial Research and Goal Setting

Set goals, budget, and do research. Buyers should [meet with an attorney](#) early on to help outline a specific process and what is needed in each step, including potential industry rules and regulations, and to make a plan to make sure they are protected and legally compliant.

Step 2: Make an offer, negotiate a purchase price, and get the ball rolling!

This step really depends on the facts, but when a buyer has found the business they want to purchase, this typically involves the buyer making an offer, potential back and forth of negotiation, and finally settling on a purchase price (and how that purchase price may be modified down the road in the process).

- **Is this an asset purchase or an equity purchase?** In an asset purchase, buyers are only buying the assets of the business, including any property, the business name, maybe a client list, trademarks or copyrights, etc. In an equity purchase, they're purchasing the entire business itself, including any existing debts and liabilities. Typically, sellers favor an equity purchase because they are passing on the whole business and outstanding liabilities to the buyer, but buyers prefer an asset sale because they are just getting the assets and not taking on any previous potential actions of the seller.

Step 3: Entering the Sales Process with LOI or purchase agreement, hand money, and other agreements

The offer to purchase is typically memorialized with an LOI presented by the buyer to the seller. This stage also often includes the signing of a confidentiality agreement or NDA (download our [NDA resource](#) here) because, in order to enter the next due diligence process, the seller will likely turn over information they want to keep private before the sale is final.

- **What is an LOI?** Simply put, an LOI is an agreement to enter into an agreement. Although it is not binding, it will typically include the major expected terms of the sale, including the agreed-upon purchase price, a timeline for due diligence and closing/purchase, and detail terms of earnest money.

- **So then, what is earnest money?** Sometimes, called “hand money,” earnest money is put down from the buyer to show the seller that they are serious about moving forward and entering into a good-faith buying process. A common example of terms related to this is one where the seller can keep this money if the buyer backs out for no fault of the seller, and on the other side, often the agreement will allow for the return of hand money to the buyer if due diligence (in the next step) reveals an issue on the part of the seller.

☐ **Step 4: Due Diligence**

Due diligence in a business purchase is very important because it’s important to know WHAT the buyer is all buying or taking on. Due diligence gives buyers the ability to make sure everything is as the seller says it is and that there aren’t any major liabilities the buyer isn’t willing to take on or wasn’t aware of. After due diligence, the buyer will need to determine if the business is one they indeed want to move forward with purchasing now that they have a more complete picture of the business’ legal, financial, and organizational health.

Due diligence may include the review of:

- Seller’s business structure and corporate documents, such as partnership agreements, operating agreements or bylaws, certificates of organization or articles of incorporation;
- Employee information, such as wages, benefits, roles and responsibilities;
- Contractual obligations;
- License statuses (such as liquor licenses);
- Any real property being transferred;
- Financial due diligence such as tax returns, balance sheets, and any liens;
- Any transferring leases;
- Liabilities or liens on business assets;
- Buyer’s proof of funds, if they haven’t already;
- Among others

Purchase Agreement: Sometimes, this step is precluded by the actual signing of the purchase agreement. Unlike an LOI, this *is* a legally binding contract that details the purchase price, list of assets, timeline, and earnest money terms. It may include allowing time for due diligence and what due diligence, or other contingencies that can terminate the buyer’s obligation to buy if certain issues arise upon due diligence and further inspection. For example, if the business actually turns out to be insolvent or has any liens on its assets, the buyer may be able to cancel the sale and walk away without violating this contract (depending on the contract). It is typically to sign a purchase agreement with a due diligence provision for purchase of a real estate asset of a business or if the buyer is quite familiar with the business already and just set out specific due diligence provisions.

☐ **Step 5: Negotiations and any changes to sale following due diligence**

Following due diligence, the buyer may have the opportunity to clarify and change any details that may have been unknown during initial negotiations. The buyer may come back after learning one thing or another with a desired change in the purchase price or an ask for certain fixes of an outstanding issue before sale.

☐ **Step 6: Finalize purchase agreement**

Next, parties finalize the purchase agreement (introduced above). This agreement will include: a list of assets and/or equity involved in the purchase; the purchase price; any warranties and representations; a closing date; allocation of closing costs; and any conditions to closing the parties agree upon, and what is to occur at closing.

☐ **Step 7: Prepare for closing**

Both parties will have time to prepare whatever they need by the closing date. This may include: the creation of additional business entities for purchase, if needed; governance compliance like bulk sales clearance; getting payment ready; any required filings prior to closing; the preparation of any title transfer documents if real property (or other property, like vehicles, trademarks, etc.) is involved; assigning contracts, and detailing inventory exchanges.

Step 8: Closing

Finally, both parties will deliver and sign all of their closing documents and make payment. The business is transferred!

Step 9: Post-closing information

After closing, either party may be required to submit change of ownership notifications and specific compliance filings related to the transfer of a business. Work with an attorney to make sure everything is in the right place and help address any additional business needs.