STEPS INVOLVED IN THE PURCHASE OF A FRANCHISED BUSINESS – FROM THE PURCHASER'S POINT OF VIEW

Clients often ask us what steps are involved in the purchase of a Franchised Business. The steps listed may not be all of the steps and of course each contract is different. This is meant as a guide only.

STEP	COMMENT
Work out what you can afford	This might sound obvious but there are a lot of costs involved in buying a business particularly a franchised business. The type of costs you will be looking at are: • Training fees payable to the franchisor; • Legal costs payable for the franchisor; • Your legal costs for checking the franchise agreement, the lease if it is a retail premises and the actual transfer of the business costs; • Search fees, for checking the business to make sure it is unencumbered and various other searches like food hygiene for food premises, town planning etc; • Stamp duty, payable to the state government; • Bank application fees; • Accountant's fees for checking the business records and advising on viability. All these need to be added to the cost of the business and included in the budget.
Find the business	Once you know how much you have to spend then you find the business. This is not an easy task and may take some time.
Agree on the price	Sometimes it is difficult to work out what you want to pay for the business if the vendor will not give you all of the financial information. Vendors can be reluctant to give out too much information until the contract is signed. Purchasers are reluctant to sign the contract without the information. So the contracts are always subject to due diligence and checking the financials.
Negotiate the contract	Usually the broker (if there is one) will prepare the contract and send it to either the vendor's solicitors or the purchaser's solicitors. The contract will be amended until the parties are happy with it. There will be numerous conditions to be included such as: • Subject to Franchisor's consent, completion of training and satisfactory franchise documents; • Subject to satisfactory lease; • Subject to due diligence; • Subject to searches; • What happens with the staff? • Is there any leased equipment? • Who pays out the lease? • Is there any equipment on loan such as drink fridges or ice cream freezers? • What licenses need to be transferred? There are a lot of things to be considered before the contract is signed and it is strongly recommended that legal advice be obtained before signing the contract.

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Warning—this article is only meant to give you general information and should not be relied on as legal advice. If you want more information then talk to one of our lawyers.

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STEP	COMMENT
The Purchaser signs first	Because the purchaser is making an offer to purchase the business, they sign the contract first. The contract is then presented by the broker to the vendor or if there is no broker then the contract is sent from the purchaser's solicitors to the vendor's solicitors for signature by the vendor. Assuming that the vendor accepts the offer then the vendor signs the contract and a copy of the signed contract is sent back to the purchaser's solicitors.
Payment of deposit	As soon as the contract is signed the deposit must be paid. The deposit is held in the trust account of either the broker or one of the solicitors. There are various clauses in the contract that deal with the deposit. Generally if a condition in the contract is not met, the deposit is refunded. If the purchaser breaches the contract then the deposit can be forfeited.
Notice to Franchisor	Once the contract is signed the vendor will need to give a copy of the signed contract to the Franchisor. The existing franchise agreement may contain a right of first refusal which means that the Franchisor must advise if they want to buy the business for the price set out in the signed contract. The existing franchise agreement will set a time usually fourteen to twenty one days for the Franchisor to make that decision and to give notice as to whether they wish to buy.
Finance Application	The purchaser needs to make their application for finance as soon as they can. This may not be able to be completed until the purchaser has all the financial information for the business. The banks will take usually at least three weeks to give finance approval. The banks should be given plenty of time and any information required by the bank should be provided as soon as possible.
Due Diligence	The standard Business Sale Agreement in QLD has a clause for verification of books and records for the business within ten business days of the contract. The vendor is to give accounts to the business within three business days after execution of the contract. That leaves the purchaser only seven business days to get the information to their accountant and verify the records. In addition to the financial records, the purchaser should also have a due diligence clause in the contract so they can check out the business assets and the plant and equipment and make sure that they are all appropriate for the business and in good condition. Otherwise, the purchaser does take the assets as is. The contract contains a warranty that the assets are all that are needed to operate the business and are working however there are no guarantees as to how long they will work. That is something for the purchaser to check into during due diligence. Once Due Diligence is completed a notice needs to be given to the vendor in writing whether or not the person is satisfied with due diligence. If that notice is not given then the buyer is deemed to be satisfied. Notice must be given by 5pm on the due date. Time is of the essence of contracts in Queensland and therefore if notice is not given the purchaser is taken to have accepted due diligence. Be very careful about the dates if you do not think you can complete due diligence by the due date then leave plenty of time to request an extension. The vendor is not compelled to grant an extension and may refuse. That leaves the purchaser with a choice to either accept the due diligence or advise that it is not satisfactory as it is not completed.
Franchisor's Consent	Assuming the Franchisor does not exercise its right of first refusal, the purchaser will then need to lodge an application with the franchisor to be approved as the franchisee. The application process will depend on the franchisor's requirements and may involve one or more interviews and various other processes.

STEP	COMMENT
Franchisor's consent (continued)	The Franchisor has 42 days from the date of the application to advise whether or not consent is granted. If the Franchisor gives no answer within 42 days then they are deemed to have given consent. This time is set by the *Franchising Code of Conduct* and cannot be changed. The purchaser should make sure that they give the Franchisor all the information required in a timely manner. This will include such things as the purchaser's asset and liability statements, qualifications, work history, references and why the purchaser wants to be a Franchisee in that particular system.
Lease	If the vendor leases the premises direct from the landlord then the vendor is to provide a copy of the lease within five business days from the date of the contract. The buyer then has five days to peruse the lease and advise the purchaser if it is accepted. If no notice is given then again the purchaser is deemed to have accepted the lease. Generally the lease is provided by the vendor's solicitor direct to the purchaser's solicitor.
Purchaser's trial period	This is the time during which the purchaser can attend at the business each day for the purposes of verifying the trading performance. In other words check the takings. In a franchised business, generally the purchasers can check the takings with the Franchisor. However, if the business is not franchised then this is a way the purchaser can check the takings to ensure the accuracy of the profit and loss statements.
Searches	At the appropriate time, the purchaser's solicitors will conduct searches. If it is a food business that will include an application for transfer of the food hygiene license which will involve an inspection by the council of the premises to determine that the premises comply with the council's health requirements. There are many other searches that will be done such as; • a search on the vendor to see that they are properly incorporated if they are a company or not bankrupt if they are individuals; • Personal Properties Security Register Searches to check encumbrances on the assets; • Town plan search to check that the business can be carried on in accordance with town plan; • Business name search; • Search on the Franchisor; • Trade Mark Search. The exact searches to be done will depend on the type of business being purchased.
Disclosure documents from the Franchisor	Once the purchaser has been approved as a franchisee, the franchisor will provide disclosure documents. These will include the disclosure document prepared in accordance with the *Franchising Code of Conduct,* a copy of the Franchise agreement in the form in which it is to be signed, copies of any documents the franchisor will require to be signed and a copy of the Franchising Code of Conduct. The purchaser cannot sign the final franchise documents until at least 14 days after they have received the disclosure documents. That 14 days is the time in which the purchaser needs to read the document and obtain legal and accounting advice on the terms of the proposed franchise agreement. Generally the contract will be subject to the purchaser confirming they are happy with the terms of the franchise agreement within 14 days of having received the documents.
Signing the Franchise Agreement	Once the purchaser has accepted the terms of the agreement, the final franchise documents can then be signed. Different Franchisors have different systems for when the final documents get signed.

STEP	COMMENT
Signing the Franchise Agreement (continued)	Many systems require that the Franchise Agreement is signed before the purchaser starts training. For a retail business, training can be many thousands of dollars. Therefore the purchaser should be sure that they are going to complete the purchase of the business and have satisfied themselves in all other respects before they start training. Since the Franchise Agreement contains clauses regarding completion of training protection of the Franchisor's confidential information and intellectual property, generally the franchise agreement is signed before training commences. However, some systems do not require the document to be signed then and leave it to be signed until after training. In that case the Franchisor would require the purchaser to sign undertakings regarding confidentiality and intellectual property. Generally the purchaser pays the cost of the training.
Transfer of the Lease	If the property is leased direct to the vendor, the lease needs to be transferred. This cannot be done without the landlord's consent. The vendor needs to notify the landlord as soon as the contract is signed that the business has been sold. The landlord will probably require a copy of the signed contract. In addition the landlord will require an application form to be completed by the purchaser which again will ask for statements of assets and liabilities, trading history , both personal and business references etc. Landlords can take some weeks to grant consent and may grant consent subject to conditions such as a guarantee from the directors of the purchaser if the purchaser is a company.
Documents to Transfer the Lease	The purchaser's solicitors will compare the transfer of the lease and generally a Deed of Assignment for the lease. That document contains an indemnity from the vendor in regard to outstanding money up to the date of assignment. The landlord will also want a Deed of Covenant which is a document that binds the purchaser to the terms of the lease. If there is a mortgage on the property then the mortgagee's consent to the transfer of the lease also needs to be obtained. The landlord's solicitors costs and the costs for the mortgagee's consent are payable by the vendor.
What if the lease is held by the Franchisor?	If the lease is held by the franchisor then the franchisor will give the purchaser a copy of the lease with the disclosure documents. The contract will set out whether or not the lease is held by the Franchisor or by the vendor. Many leases signed by franchisors contain a right for the franchisee to change without the landlord's consent, however, generally the landlord does wish to know that the franchisee is changing and will want to consent to the transfer of the business. The landlord in that case may have documents that need to be signed including a guarantee by the directors of the purchaser to guarantee performance under the lease.
Retail Shop Leases Act	If the premises to be transferred are a shop governed by the shop leases act then there are various disclosure documents that need to be given. These are; • An assignees disclosure document which is prepared by the purchaser that is delivered to the vendor and the landlord. • An assignors disclosure document which is delivered by the vendor to the purchaser and the landlord.

STEP	COMMENT
Retail Shop Leases Act requirements (continued	• A disclosure document which is delivered by the land lord to the purchaser generally with a copy of the lease. There are strict time limits in the *Retail Shop Leases Act* about when the notices need to be given and the parties should make sure they comply with those time limits.
Finance Approval	The contract will set a time for finance approval. Again time is of the essence and notice must be given to the vendor on or before the due date as to whether or not finance is approved. Again extensions may be requested but there is no obligation on the part of the vendor to grant an extension. When the finance approval letter is received from the bank the purchaser should give a copy of that letter to their solicitor. The solicitor cannot confirm that finance is approved until the formal letter of approval setting out all of the conditions of consent and all of the terms of the loan have been received by the purchaser. The solicitor will generally want to check that to make sure there are no conditions that cannot be complied with. Once the buyer and the solicitor have confirmed that the conditions are acceptable, notice should be given to the vendor in writing that finance is approved. That notice should be given by the due date.
Signing documents with the bank	Generally the documents are sent out with the loan approval letter so these need to be signed and given back to the bank. Banks have procedures that need to be complied with. They get the documents back, they check the documents, they certify the loan ready for settlement . It then needs to go to someone else to be checked and recertified and then they will give a booking reference. Without that booking reference settlement cannot be booked with the bank. When time comes to book settlement, the bank will generally want three to four days notice. Banks are very strict with their time requirements.
Training	Training is usually carried out before settlement. The purchaser needs to go to training with the franchisor and this can take some weeks or even months. So what happens is that all documents are signed and everything is ready to settle and the parties just wait until the purchaser has completed training and the franchisor certifies that training is satisfactorily completed.
Franchisor's requirements for settlement	The franchisor's consent will be granted subject to any transfer fee under the existing franchise agreement being paid by the vendor and any money outstanding to the franchisor being paid and any suppliers being paid. There will be other conditions unique to each system. So when it comes to settlement, both the vendor's and purchaser's solicitors need to check with the franchisor to see how much money is to be paid to them on settlement. Settlement cannot proceed without the franchisor giving the final go ahead for settlement.
Settlement Figures	The solicitors will work out the settlement figures which will include adjustments for things such as; • Rent and Outgoings; • Electricity; • Stock; • Money payable to the franchisor; • Leases to be paid out. Once the figures are confirmed, the vendor's solicitors will provide the purchaser's

STEP	COMMENT
Settlement figures (continued)	solicitors with cheque details. Cheques to be drawn at settlement cover such things as; • Any amount needed to pay out the vendor's bank • Any amount needed to pay the landlord any rent or outgoings outstanding • The amount to pay the franchisor what they require on settlement • The amount to pay the landlord's costs • And the mortgagees costs (if any) The money at settlement must be paid by a bank cheque.
Stock take	The stocktake is usually carried out at close of business on the day before settlement. The parties meet at the premises and carry out the stocktake. If there is a lot of stock then a stock taker firm might be called in to assist in the stocktake. Sometimes the franchisor will attend the stocktake to make sure that the stock is there for the purchaser to open the business the next day. The obligation under the contract is to buy good and saleable stock and there is no obligation on the purchaser to buy any stock that does not fit that description. The stock take amount is confirmed by the parties at the end of the stock take and told to the solicitors on the morning of settlement and included in the settlement figures. If that cannot be done then the purchaser needs to pay the vendor for the stock at the same time as settlement.
Settlement	Settlement is the exchange of money for documents at a time agreed that suits the solicitors and the banks. Generally it is not until 2pm on the settlement date. There is no need for the parties to attend at settlement, they can leave that to their solicitors.
Hand over of the shop	If the stocktake is done on the night before settlement then the purchaser opens the shop on the settlement morning. The vendor usually remains at the premises on that day until settlement occurs. If for some reason the stocktake cannot be done until the night of the day of settlement, then the vendor will operate the business on the settlement day and the purchaser will take over the business at the end of the stocktake.
Electricity, telephone and other services	The solicitors do not get involved in the transfer of electricity and telephone. This is done by the parties direct. The purchaser should make sure that they lodge their applications with the telephone company and the electricity company well before settlement.
Eftpos Machine	Make sure you give the bank plenty of time regarding the eftpos machine whether it is to take it away or is to get a new one. The vendor will want to make sure that all money due to them is paid through their eftpos machine up until handover and the purchaser will want to make sure they get all their money from handover. Discuss this with the bank early to make sure the eftpos machine will be available.
Equipment on Lease	Sometimes the equipment at the premises is leased. If that is the case then the company from whom the equipment is leased is to be notified by the vendor and the purchaser needs to apply to have the lease transferred to them. This needs to be arranged to coincide with settlement. This is generally arranged by the parties direct with the leasing company and the lawyers are not involved. The parties must make sure this is complied with before settlement. The buyer of course should have their documents checked by their lawyer before signing.
GST	If the vendor is giving the purchaser everything necessary to operate the business then it will generally be the sale of a going concern and GST will not be payable on the purchase price or the stock. If for some reason it is not the sale of a going concern then GST will be payable in addition to the purchase price and the vendor will need to provide a tax invoice on settlement. The purchaser should make sure they are registered for GST.

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Employees	The purchaser has an obligation to take over the employees of the business listed in the contract. The employees have no obligation to accept the offer of employment. For all employees except casual employees, adjustments are to be made at settlement for wages, holiday pay, sick pay etc. The purchaser will need to check carefully to make sure all these payments have been made and that the adjustments given are correct. The casual employees do not have any entitlement to those type of payments and therefore no adjustment is made. The purchaser does take on any employees with the rights that they had before settlement. So for example if the employee has been there for a number of years and would be entitled to pro rata long service leave then the purchaser takes over that obligation. The purchaser cannot offer the employees less compensation than they were receiving with the vendor. Adjustments for employees are very technical and need to be looked at by the accountant to ensure that they are correct.
Seller's Tuition	If the business is a franchise business then many franchisors do not require the vendor to stay and give tuition to the purchaser. The contract generally provides that the purchaser can get tuition for a week before and after settlement. This may be of assistance in business where the buyer is to be introduced to the customers. That assistance is given at no cost to the buyer.
Interest on late payment	If for any reason the purchaser is late in settling, the vendor can charge interest at a rate which is set in Queensland by the Queensland Law Society. There can be a different rate put in the contract. Of course, this depends on if the vendor agrees to an extension again there is no obligation on the vendor to agree to an extension.
Default	Failure by the purchaser to comply with the terms of the contract can mean that the purchaser is in default. There are many clauses in the contract dealing with default and the consequences of default. These include: • The right of the vendor to terminate the contract; • Forfeiture of the deposit; • A claim for damages by the vendor; • Possible claim for specific performance; • Right to loss on resale. There are also clauses dealing with default by the vendor giving the purchaser various rights. Default is not recommended as the consequences can be very serious to the parties.
Conclusion	As stated above, this is not meant to set out every possible step in the process or cover every eventuality. This is meant to give parties an idea of the steps involved in the sale of the purchase of a franchise business. Parties should not rely on this as containing a full and complete record and should make sure they obtain proper legal and accounting advice before entering into any documents in regard to purchasing the business or franchise.