

(5th Ed)

NOTICE: Keep these questions, but mark your answers on the accompanying quiz answer form and return to:
REAL ESTATE LICENSE SERVICES; 5059 NEWPORT AVENUE #209, San Diego, California 92107

Selling Business Opportunities in CA-part I Quiz

In accordance with CalBRE regulations, the student must do mandatory quizzes prior to taking the final exam(s). Please note that your score on the mandatory quizzes will not determine in any way if you pass or fail your course. Only the final will determine if you pass or fail the course.

After you answer your quizzes, please mail your answers to us. After we receive them, you may take your final exam. If you want the answers to the quizzes, you must send a self-addressed stamped envelope.

The quiz answers will not be sent to you unless you send a self-addressed stamped envelope with one ounce First-Class postage attached.

To expedite the completion of your final exams and courses, you may complete your quizzes online by logging in with your email address and password to www.RELSTONEexams.com

Review for Section #1

Quiz Section #1 is to be taken after reading pages 7-13

- P.10 1. Good will is the most valuable item a business owner has to sell.
a. True b. False
- P.11 2. A capable business broker is not responsible for dealing with the expectations of buyers.
a. True b. False
- P.11 3. In a business opportunity transaction, a real estate broker typically acts as agent for the seller.
a. True b. False
- P.12 4. Knowledge, training, and experiences are commodities offered by business opportunities brokers.
a. True b. False
- P.13 5. It is not appropriate for a business opportunities broker to offer business advice to clients.
a. True b. False

Review for Section #2

Quiz Section #2 is to be taken after reading pages 14-29

- P.17 1. A franchise offering prospectus may be delivered to a prospective buyer any time before the closing of the sale.
a. True b. False
- P.18 2. California real estate license is required to sell franchise opportunities.
a. True b. False
- P.22 3. Successful business opportunities brokers can expect to work at their jobs only from 9 to 5.
a. True b. False
- P.27 4. In some cases, a principal will waive his broker's fiduciary duties.
a. True b. False

- 5. A business opportunities broker should show a willingness to listen.
a. True b. False P.29

Review for Section #3

Quiz Section #3 is to be taken after reading pages 30-34

- P.30 1. At the introductory meeting, it is appropriate for a broker to talk about the sales price of a business with a prospective buyer.
a. True b. False
- P.31 2. California brokers and agents cannot offer real property for sale until obtaining an agreement as authorization to sell.
a. True b. False
- P.31 3. Because the sale of every business opportunity is different, brokers should draft their own listing agreements.
a. True b. False
- P.32 4. When completing a business listing agreement, any spaces where information is not applicable or unknown should be left blank.
a. True b. False
- P.33 5. When completing a business listing agreement, any confusing legal language that the owner doesn't understand should be carefully explained.
a. True b. False

Review for Section #4

Quiz Section #4 is to be taken after reading pages 35-48

- P.35 1. If a business owner has previously engaged in negotiations to sell her business and doesn't inform her new broker, a commission dispute is likely.
a. True b. False
- P.40 2. Stock in trade is represented by wholesale cost of inventory.
a. True b. False

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- 3. OWC means that a business owner will finance the sale of his business.
 - a. True
 - b. False
- 4. Distress factors can motivate a business owner to sell her business.
 - a. True
 - b. False
- 5. A rule of thumb for business broker commission is 10 percent.
 - a. True
 - b. False

Review for Section #5

- Quiz Section #5 is to be taken after reading pages 49-60
- 1. An owner's emotional attachment to his business will influence its selling price.
 - a. True
 - b. False
 - 2. The consideration of customers arising from an established and well conducted business is known as good will.
 - a. True
 - b. False
 - 3. Gross sales minus the cost of sales and operating expenses is gross profit.
 - a. True
 - b. False
 - 4. An assignable and favorable lease is a positive desirability factor.
 - a. True
 - b. False
 - 5. Labor issues often contribute to a business's negative desirability factor.
 - a. True
 - b. False

Review for Section #6

- Quiz Section #6 is to be taken after reading pages 61-75
- 1. When a business is formed as a corporation, it is more valuable.
 - a. True
 - b. False
 - 2. A profit and loss statement should encompass the most recent two-year period in order to accurately assess a business's overall profitability.
 - a. True
 - b. False
 - 3. A business's financial information is the property of its owner.
 - a. True
 - b. False
 - 4. A profit and loss statement shows the assets and liability of a business.
 - a. True
 - b. False
 - 5. A business's liabilities are categorized as current and long term.
 - a. True
 - b. False

Review for Section #7

Quiz Section #7 is to be taken after reading pages 75-100, as well as page 204 (Glossary)

- 1. A recorded lien against business assets constitutes a secured liability.
 - a. True
 - b. False
- 2. An owner's equity is represented by the difference between the total liabilities and assets of her business.
 - a. True
 - b. False
- 3. The name of the business for sale should be disclosed to a potential buyer during the first interview.
 - a. True
 - b. False
- 4. All sales of business assets must be carried out with a written contract.
 - a. True
 - b. False
- 5. An alienation clause allows a party holding a promissory to demand full payment in case of default.
 - a. True
 - b. False

Review for Section #8

Quiz Section #8 is to be taken after reading pages 208 through page 220 in Glossary

- 1. Original cost plus capital improvements less depreciation equals book value.
 - a. True
 - b. False
- 2. The loss of property value brought about by age, physical deterioration, or obsolescence is called "depreciation."
 - a. True
 - b. False
- 3. When an agent acts for two principals in the same transaction, he or she is commingling.
 - a. True
 - b. False
- 4. The procedure whereby legal instruments and/or funds are deposited with a neutral third party and subject to the provisions of a written contract is called "escrow."
 - a. True
 - b. False
- 5. California's Franchise Investment Law is found within the Business and Professions Code.
 - a. True
 - b. False

NOTICE

When you complete these quizzes, transfer your answers to the quiz answer form and return to:

Real Estate License Services
 5055 Newport Avenue #209
 San Diego, CA 92107

Please keep the quiz questions. Return only the completed answer form. You may not take your final exam until we receive your completed answer form.

If you have any questions, please telephone (619) 222-2421.

Transfer your answers to your quiz answer form.

NOTICE: These questions must be returned with your answer sheet.
 REAL ESTATE LICENSE SERVICES, 5059 NEWPORT AVENUE #209, San Diego, California 92107

SELLING BUSINESS OPPORTUNITIES IN CALIFORNIA-PART I FINAL EXAMINATION#1

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FINAL EXAM ANSWER FORM INSTRUCTIONS

The Final Exam Answer Form is the blue answer card marked "SCANTRON Score Form No. SC881-E" Before beginning your final exam, fill in the Student Information on the Answer Form COMPLETELY. Make sure that you PRINT your name, student record number, etc. If you are also taking the course SELLING BUSINESS OPPORTUNITIES IN CALIFORNIA PART II, your answers to the PART II final exam should be filled out on the reverse side of the answer form.

Answer the 40 final exam multiple-choice questions on the Final Exam Answer Form on the side marked SELLING BUSINESS OPPORTUNITIES IN CALIFORNIA PART I. Completely fill in the square of the appropriate letter (A, B, C or D).

USE A NO. 2 PENCIL ONLY. Using a pencil other than a No. 2 may cause the computer to incorrectly score your final exam. For each answer, choose the best answer and fill in the appropriate box (A, B, C or D) on the Answer Form. Fill in the box completely and dark. For example, if your answer on question 37 was "B" you would do the following:

37. [A] [C] [D]

If you need to change an answer, make sure that you erase the old answer completely.

THIS IS AN "OPEN BOOK" EXAMINATION. THE TEXTBOOK MAY BE USED DURING THE EXAM.

- | | |
|---|--|
| <p><i>P.10</i> 1. Which of the following is the most valuable single item of most business owners when selling their businesses?
 a. the commercial lease c. the trade fixtures
 b. the accounts receivable d. the good will</p> <p><i>P.13</i> 2. Is it appropriate for a business opportunities broker to offer business advice to clients?
 a. yes and it is even expected
 b. yes if the broker has the expertise of a business consultant
 c. only if the broker and client are also friends.
 d. no, a business opportunities broker should never offer business advice to clients</p> <p><i>P.11</i> 3. In a business opportunity transaction, a real estate broker typically acts as agent for:
 a. the business itself
 b. the buyer
 c. the seller
 d. all parties who have a relevant interest in the transaction</p> <p><i>P.17</i> 4. Under California's Franchise Investment Law, when must the franchise offering prospectus be delivered to a prospective purchaser?
 a. 10 days before the franchise agreement is effective
 b. with the first receipt by the seller of any monies
 c. 10 days before the franchise agreement is effective or 14 days before the seller receives consideration
 d. anytime before the closing of the sale</p> <p><i>P.11</i> 5. A capable business broker performs which of the following in a business opportunity transaction?
 a. managing the expectations of the buyer
 b. dealing with the expectations of the seller
 c. recognizing the rights and interests of relevant third parties
 d. all of the above</p> <p><i>P.29</i> 6. Which of the following are commodities offered by business opportunities brokers?
 a. knowledge b. training c. experience d. all of the above</p> | <p>7. Bill is not a real estate licensee. May he participate in the sale of a franchise interest? <i>P.18</i>
 a. no because he is not licensed by the California BRE (CalBRE)
 b. only if he works under the direct supervision of a real estate licensee
 c. yes as long as he has the consent of the parties to the transaction
 d. yes if he is identified in the registration</p> <p>8. Which of the following is a correct statement about successful business opportunities brokers? <i>P.22</i>
 a. They generally work their jobs from 9 to 5.
 b. Nights and weekends are not necessary when serving clients.
 c. They may be called upon to respond quickly to buyers and sellers.
 d. Work hours are consistent</p> <p>9. When may a broker assume his principal has waived the broker's fiduciary duties? <i>P.11</i>
 a. when the principal does not return the broker's telephone calls
 b. never
 c. when the broker has failed to perform his fiduciary duties and the principal does not notice
 d. when a business opportunity remains unsold for one year or more</p> <p>10. Which of the following is the most important quality a business opportunities broker can convey at the first meeting with a prospective client? <i>P.30</i>
 a. a hard-nosed demeanor to suggest strength
 b. a willingness to listen
 c. conceit to suggest knowledge and experience
 d. cordiality in order to make a friend of the seller when the transaction has been completed</p> <p>11. All of the following should be covered in the initial meeting with potential business owner EXCEPT: <i>P.30</i>
 a. pricing the business.
 b. the length of time the owner has been in business.
 c. the nature of the business.
 d. if the business is profitable.</p> |
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- P.31 12. California brokers and agents cannot offer real property for sale until:
 - a. they have been shown proof of ownership.
 - b. the property or business has been formally appraised.
 - c. the broker or agent inspects the property or business.
 - d. obtaining an agreement as authorization to sell.
- P.31 13. Which of the following forms is most often used with selling business opportunities?
 - a. Open Listing Agreement.
 - b. Agency Listing Agreement.
 - c. Business Listing Agreement
 - d. Listing Agreement Exclusive
- P.32 14. When completing any contract connected with the sale of a business, what should a broker do when a space is not applicable to the transaction?
 - a. leave the space blank.
 - b. fill in the space with xxxxx.
 - c. fill in the space with ///// or xxxxx and initial it.
 - d. fill in the space with any answer that is obviously not applicable.
- P.33 15. Which of the following is the most appropriate response when a business owner has questions about the legal verbiage in a listing agreement?
 - a. "Don't worry about it; it's just standard contract language."
 - b. "I will explain it to you."
 - c. "Let's just sign the contract now, and you can look it up later."
 - d. "You should ask your attorney for interpretation if there is anything you don't understand."
- P.35 16. If a business owner has previously engaged in negotiations to sell her business and doesn't inform her new broker, which of the following is likely?
 - a. a flawless transaction as long as the buyer is happy with the terms.
 - b. a commission dispute.
 - c. The new broker will be cut out of any commission.
 - d. The previous broker will not see any commission.
- P.30 17. Which of the following best describes "stock in trade"?
 - a. the good will associated with a business.
 - b. a business owner's wholesale cost of inventory.
 - c. the business owner's personal expertise.
 - d. the listing price for the business.
- P.41 18. What does the acronym "OWC" mean?
 - a. The Owner Will Carry the note.
 - b. The company's Officer's Wives have formed a Club.
 - c. The business bank account has sufficient Operating Working Capital.
 - d. The business requires an Operational Watch Commander for security during nighttime hours.
- P.42 19. All of the following would be considered distress factor EXCEPT:
 - a. insolvency proceedings.
 - b. building decay.
 - c. lack of suitable personnel.
 - d. retirement age.
- P.44 20. What is the customary commission for a business broker?
 - a. 2 percent
 - b. 10 percent
 - c. 6 percent
 - d. 4 percent
- P.50 21. All of the following should influence a business's selling price EXCEPT:
 - a. the financial history of the enterprise.
 - b. the owner's emotional attachment.
 - c. the desirability of the business's good will.
 - d. the value of fixtures and equipment.
- P.51 22. The consideration of customers arising from an established and well conducted business is called:
 - a. patronage
 - b. good will
 - c. clientele
 - d. sponsorship
- P.52 23. Gross sales minus the cost of sales and operating expenses equals:
 - a. net profit
 - b. profit
 - c. gross profit
 - d. depreciated profit.
- P.57 24. Which of the following is a positive desirability factor?
 - a. an assignable and favorable lease.
 - b. an unassignable lease.
 - c. the absence of a written lease.
 - d. an oppressive lease.
- P.59 25. Which of the following is a negative desirability factor?
 - a. protection from competition.
 - b. recently upgraded equipment and facilities.
 - c. challenging labor issues.
 - d. well lighted and marked parking.

- P.65 26. Which of the following is a correct statement about corporate stock transactions as a means of selling a business?
 - a. Corporate stock transactions are simple to execute.
 - b. Being held as a corporation makes the business more valuable.
 - c. A business's worth is its worth regardless of how the assets are held.
 - d. Being held as a corporation makes the business less valuable.
- P.69 27. A profit and loss statement should encompass which of the following in order to accurately assess overall profitability?
 - a. 1 year
 - b. 2 years
 - c. 18 months
 - d. 5 years
- P.68 28. When a business is up for sale, profit and loss statements, balance sheets, sales tax reports, and similar financial information is the property of:
 - a. the buyer, once he or she makes a down payment on the business.
 - b. the business owner and his or her immediate family.
 - c. the business owner.
 - d. the broker.
- P.73 29. Which of the following shows a business's assets and liabilities?
 - a. profit and loss statement.
 - b. accounts payable and accounts receivable reports.
 - c. transaction reports.
 - d. balance sheet.
- P.75 30. Liabilities are categorized as:
 - a. short and long term.
 - b. open and aging.
 - c. detailed and summarized.
 - d. current and long term.
- P.75 31. All of the following are secured liabilities EXCEPT:
 - a. a recorded lien against business assets.
 - b. a pink slip on a company vehicle.
 - c. a recorded judgment against assets.
 - d. a credit card balance.
- P.75 32. The difference between assets and liabilities is:
 - a. debt
 - b. reserves
 - c. equity
 - d. liquidity
- P.80 33. Which of the following should not be disclosed by a broker on the first interview with a buyer or buyer's broker?
 - a. the name of the business for sale.
 - b. the type of business.
 - c. the general location of the business.
 - d. the asking price for the business.
- P.95 34. Which of the following sales does not have to be consummated with a written contract?
 - a. one that is less than \$1,000.
 - b. one that is less than \$500.
 - c. one that is less than \$10,000.
 - d. one that takes place between family members.
- P.204 35. What type of clause allows a party holding a promissory to demand full payment in case of default?
 - a. alienation clause
 - b. subordination clause
 - c. prepayment clause
 - d. acceleration clause
- P.208 36. Original cost plus capital improvements less depreciation equals:
 - a. actual cash value
 - b. fair market value
 - c. replacement value
 - d. book value
- P.160 37. The loss of value of property brought about by age, physical deterioration or obsolesce is:
 - a. deterioration
 - b. wear and tear
 - c. depreciation
 - d. attrition
- P.215 38. When an agent acts for two principals in the same transaction, which of the following is taking place?
 - a. escrow
 - b. dual agency
 - c. commingling
 - d. double dipping
- P.216 39. The procedure whereby legal instruments and/or funds are deposited with a neutral third party and subject to the provisions of a written contract is called:
 - a. collateral
 - b. estoppel
 - c. escrow
 - d. bond
- P.117 40. California's Franchise Investment Law is found within the:
 - a. Government Code
 - b. Real Estate Code
 - c. Business and Professions Code
 - d. Corporations Code

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CHAPTER 2

BUSINESS OPPORTUNITIES AND THE REAL ESTATE LICENSEE

WHAT CONSTITUTES A *BUSINESS OPPORTUNITY*?

The Real Estate Law of California defines “business opportunity” as meaning and including the sale or lease of the business and good will of an existing business enterprise or opportunity. (Business and Professions Code §§10030.)

THE SALE OF A BUSINESS OPPORTUNITY

Business opportunities transactions always involve the transfer of business assets of one description or another, such as inventory, equipment, trade fixtures, trade name, customer lists, accounts receivable, leasehold interest, and what lawyers and accountants refer to as “goodwill”. Simply stated, a business opportunity offers its owner the chance to succeed or fail in a closely defined commercial environment.

Some business opportunities have well established value, sometimes reckoned in millions of dollars. Those falling within this category generally bear nationally or internationally known names or logos, or have well-documented histories of profitable earnings from sales or other operations. Most businesses that find themselves on the market do not. One of the challenges that business brokers face on a daily basis is sorting out the “good” business opportunities from the rest, a chore closely akin to locating the proverbial needle in the haystack and only then, investing time and resources toward promotion of a sale or otherwise generating interest on the part of prospective buyers.

The conveyance of a business opportunity generally involves the bargain and sale of personal property — to which the rules and laws governing transfer of chattels apply. This type of commercial transaction also typically involves the transfer of a leasehold interest in commercial real estate, this aspect being governed by real property legal principles. In fact, the most valuable single item of value among the assets of most business owners is the commercial lease that the proprietor enjoys, for better or worse.

Business opportunities transactions come in all shapes and sizes, ranging from the mega-dollar transfer of an NYSE listed multinational corporation to the sale of grandmom's dog grooming shop on Main Street. Neither buyers nor sellers fit any particular type of profile, and there is no such thing as conventional financing. The actual legal constraints and requirements are few, and governmental regulation of such deals is virtually non-existent.

Historically in this country, the vast bulk of business assets transfers have been transacted informally without benefit of assistance by brokers or escrows. Most of these have resulted in passing from generation to generation, or otherwise within a family or group of close associates. Sometimes these have been informally arranged by bankers, lawyers, neighbors, fellow parishioners, lodge brothers, surviving spouses, or simply local gadflies, often without even the formality of written contracts. And the overwhelming majority of these transactions were accomplished uneventfully. Few were fraught with litigation or issues of controversy. "That," as they say, "was then...this is now."

Suffice it to say that every time business assets are transferred from one party to another, a whole series of issues arises. Many of these are fairly obvious — such as the continuing rights of commercial creditors, landlords, tax collectors and the like. Some are not so apparent, especially in cases where the parties

themselves are of limited education, or where their overwhelming interest is limited to matters of day-to-day commerce or, sometimes even the challenge of making a deal.

This is where the assistance of a capable business broker (or accountant or lawyer) can be essential in order to finesse and adjust the reasonable expectations of a seller with those of his buyer, while at the same time recognizing the rights and interests of relevant third parties such the landlord, trade creditors, and tax collectors.

Q-1
#2-b

P-1
F-5

In business opportunity transactions, the real estate broker acts as an agent for someone else — the principal, who seeks to sell, lease, exchange, or acquire certain business assets for the purpose of generating profits. The laws of agency require the real estate licensee to exercise utmost good faith, loyalty, and honesty in all relationships with the principal while being under the corresponding duty of dealing fairly and honestly with the other party or parties to the transaction and their representative(s).

Q-1
#3-a

P-1
F-3

ETHICAL CONSIDERATIONS FOR THE BROKER HANDLING BUSINESS OPPORTUNITY TRANSACTIONS

A broker must recognize that, although it is usually the seller who actually employs the licensee to sell or lease a business, the broker also has a great legal and ethical responsibility to the purchaser. Often the buyer is investing substantial cash assets, sometimes even his life savings, and should be given every opportunity to properly evaluate all material aspects of the seller's business.

P-1
F-8

Fiduciary
Duty

In the field of business opportunities sales, such games as "hide the ball," "bait and switch," and other quick-sale devices sometimes practiced in less honored professions are thoroughly disproved as unethical and illegal. And, doubtless prove equally unprofitable, since in the real world, resorting to such tricks only

rarely produces a completed sale or a paid commission to its perpetrator.

The fact is, contemporary biz-ops practice is founded on the concept of full disclosure and more or less regulates itself on such principles as the implied covenant of good faith and fair dealing.

Of course, sellers of business assets are like sellers of every other commodity. They demand results: defined as bona fide offers from qualified buyers at prices meeting, if not exceeding, their listing prices. And the concept of sellers' withholding of critical information affecting the value and desirability of that which they seek to sell is, regrettably, not an unknown phenomenon.

Even though it is true that sellers owe their actual and prospective buyers a duty of good faith and fair dealing, it is their agent(s) who owe corresponding ethical responsibility to principals and third parties alike. A seller who is shown to have breached this duty stands to lose the benefits of a sale, within or without litigation. But the sales agent who breaches this duty may find himself forfeiting a valuable license and the right to participate in an honored profession.

**BUYERS AND SELLERS RELY ON BROKER'S EXPERTISE,
BUT BIZ-OPPS AGENTS ARE NOT BUSINESS
CONSULTANTS**

Q-1
#4-a The primary commodity that business opportunity brokers have to sell in their knowledge, training, and experience in the field of business assets transactions. All brokers, especially those with novice clients, should anticipate questions about all phases of acquiring, managing and maintaining the subject business, and the well meaning broker will be sorely tempted to double as his client's business consultant. This is especially true where, as is generally the case, a commission may be on the line.

A fine line exists between the business opportunities broker's responsibilities as his seller's (or buyer's) agent and that of a general business consultant. Many business brokers enjoy a superior level of expertise in the operation and management of businesses. Most do not. The skills required of real estate licensees acting as business brokers are quite different from those of business consultants who often hold specialized degrees from universities or have achieved their knowledge from years in the trenches of commerce.

Q-1
#5-b

There is no provision of law that precludes a licensee from offering business advice to his or her clients. However, most of the time, it is just not a very good idea. That is except in limited cases — where the broker or agent can demonstrate special skills in this area, equivalent to those enjoyed by established consultants, and where the relationship between agent and principal expressly calls for the rendering of such advice.

P-1
F-2

At least once during the course of every business buy/sell transaction an issue will arise on which the buyer (or seller) will require consultation. Usually, the question is framed: "Well, what would you do?" With a potential commission riding on the answer, it is certainly tempting for the business broker to supply answers to this type of query.

Many agents have come to grief at some future time when it appeared that they had insufficient expertise to provide a credible answer, or that the answer actually provided was intended to promote a pending transaction (thus resulting in payment of compensation to the agent). The best response to the type of inquiry cited above is: "Well, if it were me, I would hire an accountant (or lawyer or consultant) to advise me further."

ADVISING PROSPECTIVE BUYERS

In order to capably advise or represent the interests of an owner desiring to market his assets as a business opportunity, the

FRANCHISE INVESTMENT LAW

P-1
F-40

Before California's Franchise Investment Law was enacted in 1970, the sale of franchises was subject to only limited regulation. Only insofar as a franchise could be classified as a security would the Corporate Securities Law apply to such transactions. The widespread growth of the franchising industry created numerous problems not covered by that law. So in the interests of protecting investors and promoting the expansion of franchising, legislation was enacted, the rough outlines of which business brokers should be aware. This legislation is entitled the Franchise Investment Law. (Corporations Code §§31000-31516)

Essentially, the Franchise Investment Law is a modified disclosure law designed to provide the prospective purchaser with full advance disclosure of the franchise agreement and other matters directly relevant to the franchise relationship.

P-1
F-4

These disclosures must be contained in an offering prospectus which, together with all proposed sale agreements, must be delivered to the prospective purchaser at least 14 business days before any franchise agreement takes effect, or at least 14 business days before the receipt of any consideration is payable, whichever occurs first. (Corporations Code §§31119).

Q-2
#1-b

FRANCHISERS MUST REGISTER SALES UNLESS EXEMPT

The law provides that, unless specifically exempted, every franchiser who proposes to offer or sell a franchise must register each such sale with the California Department of Business Oversight (DBO). Certain limited exemptions are available, but even where an exemption is given, the franchiser must make specific disclosures to the prospective franchisee. (Corporations Code §§31101)

INTENT OF THE LAW

The intent of the law is to provide a prospective franchisee with sufficient information to enable him to make an intelligent

decision to invest or not, to protect the franchisee against fraud or unfulfilled promises, and to provide a better understanding of the business relationship between the franchiser and franchisee. There are specific categories of franchises that are regulated under their own subsections of the law (such as gas stations), and even the most knowledgeable of business opportunities brokers should be sure to consult legal counsel to determine whether any special regulatory law applies to a particular transaction at issue.

CATEGORIES OF PERSONS AUTHORIZED TO SELL FRANCHISES

There are three categories of persons authorized to sell non-exempt franchises under §§31210 of the Corporations Code.

They are:

1. A person identified in an application filed with the DBO for an offering of a franchise in California;
2. A person licensed as a real estate broker or a real estate salesperson; and
3. A person licensed by the DBO as a broker-dealer or agent under the California Corporate Securities Law.

Thus, a real estate broker, real estate salesperson, or a broker-dealer or agent can sell franchise interests without being identified in the registration. And a person identified in the registration application can participate in the sale of a franchise interest even though not licensed as a real estate broker, salesperson, broker-dealer, or agent.

BECOMING FAMILIAR WITH FRANCHISE INVESTMENT LAW

Franchising is a relatively new form of business enterprise as it was relatively unknown before the advent of Golden Arches back in the 1950s. The conscientious real estate professional who wishes to handle a franchise sale should become familiar with

stepsister, the facsimile machine. The phone should be used primarily to enhance relationships between the agent and potential clients and to generate appointments, if possible. It should not be used for the purpose of closing deals or actually securing listings, but rather to schedule appointments wherever and whenever possible. Telephone calls should be short and to the point. For instance, when a buyer calls in response to an ad in the paper and asks for information on a particular business, your immediate response should be. "Fine, when can we get together to discuss that business?"

EXUDE PROFESSIONALISM

Every contact made by the agent provides a meaningful opportunity for the agent to enhance the confidence of the prospective client as to his knowledge and professionalism. Get to the point without delay. Never engage in gossip or diatribe, and do not waste time by promoting businesses irrelevant to your prospective client's interests or objectives. Show that you know what you are doing, but never brag or indulge in "war stories".

You do not need to know everything there is to know, but you do need to demonstrate that you are a good listener and respectful of others' privacy. Be forthright and assertive in getting the information you need and in working with your clients. Your efforts in this regard will tend to earn the client's confidence.

TIME CAN BE THE AGENT'S ENEMY

Being a successful business broker is not a ⁹⁻⁵ nine-to-five job. The successful agent is one who is not reluctant to work nights or weekends where necessary to serve the interests of his clients.

The decision of a business owner to sell his assets is generally reached only after days and weeks of soul-searching. But once the decision is reached, he typically wants out as soon as possible, without games, or any undue delay. The same is true of a buyer who has finally decided to roll the proverbial dice and

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The moral to this story is not hard to ascertain, from the standpoint of each of the parties. As far as the business broker is concerned, NEVER, EVER undertake representation of one or more parties without taking the role seriously. There is no such thing as a principal's waiver of the broker's fiduciary duties. And unless the broker fully understands the nature and extent of his fiduciary responsibilities in each and every transaction, and is fully prepared to discharge these in a capable manner, he should decline to become involved. Otherwise it will appear that his ONLY interest in a given client or transaction was simply to cash a commission check.

CHAPTER 3

THE BUSINESS LISTING TRANSACTION

MAKING CONTACT

Once a business owner expresses an interest in the concept of selling his or her business assets, the agent should make arrangements for an appointment as an immediate priority. Good listings are not easy to come by and opportunities deferred are generally opportunities lost. The initial appointment should take place at the agent's office. Assuming this is the initial meeting between the parties, the appointment serves two useful purposes: First, it provides the owner with an opportunity to receive answers to relevant questions, and second, it provides the broker with an opportunity to display his knowledge, training, experience, motivation, and personality.

(Listen too)

The general appearance of the broker and his surroundings can be an important determining factor in whether the owner ultimately elects to entrust the marketing of his business to this particular broker. Perhaps subliminally, the owner will ask himself the following, "Is this broker someone I want to have representing me? What kind of an impression will he make on prospective buyers? Does he seem capable and motivated to perform an adequate marketing program? Can I count on him to return my calls and to be there when I need him? Can I work with this guy over the next few months?"

As a matter of introduction, the broker might present the prospective seller with a promotional brochure, including a brief resume, description of the range of services the broker offers,

and containing answers to frequently asked questions regarding the subject of business opportunities transactions. The discussion between the parties should begin informally with an introduction and general discussion of the owner's objectives. The broker should not appear aggressive. He should demonstrate his willingness to listen.

Although the agent will eventually compile a complete file of information relevant to the owner's assets, it is generally not a good idea to take notes during the informal introductory session. You will have time enough for this later when preparing your checklist. And besides, it may well be that, after the introductory interview, you will decide not to accept the role of seller's agent. Or the seller may elect not to offer it.

In directing the discussion, the agent should generally inquire as to the nature of the relevant enterprise, the length of time the proprietor's been in business, the number of employees, whether or not the business is deriving a profit, and other issues which then seem relevant. It is never helpful to discuss pricing issues at this early stage since the agent requires a lot more information before he can make an assessment as to probable market value and provide a sound recommendation as to asking price.

Only if, after the introductory discussion, the owner expresses a serious interest to market his assets and to do so under the agent's auspices, does the agent reach for a pencil and checklist. And, only then, proceed with a detailed fact finding interview. Bear in mind that information regarding relevant business assets is what constitutes the agent's stock in trade.

For this reason, it is important to learn as much about the owner and his assets as possible, so the agent should take great care, and devote whatever time is necessary, to obtain a complete and accurate inventory of exactly what his principal intends to sell. Most established business opportunities offices use checklists for this purpose. Some are better and more complete than

others. Any broker intending to solicit business assets listings as part of his or her practice should develop their own checklist of relevant information, and use it whenever the opportunity arises.

THE LISTING AGREEMENT

The transaction between an owner and an agent authorizing the latter to promote the sale of business assets is itself a serious and complex transaction that requires a great deal of care and a high level of skill.

As indicated above, California brokers and agents are legally precluded from offering real property for sale without having first obtained the owner's consent in the form of an Authorization to Sell in one form or another. This rule applies to the sale of business opportunities as well as the marketing of real property. Not only is the agent's observance of the law critical to those who would maintain their real estate licenses free of adverse enforcement action, but the presence of a signed listing is a prerequisite to the agent's entitlement to a commission.

When real estate or business assets are marketed to the general public, the marketing broker or agent impliedly warrants that he indeed has an enforceable listing. This warranty is of particular relevance to potential buyers' agents who ordinarily seek compensation for their services by virtue of commission cooperation with the listing agent.

While there is no such thing as a mandatory Listing or Authorization to Sell agreement in California, the California Association of Realtors (CAR) has developed a Business Listing Agreement, the use of which is highly recommended for all business opportunities brokers. This form is especially helpful in that it sets forth the essential duties of the agent while providing an unambiguous basis for compensation.

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Use of this CAR version — with each of the blanks capably filled in and duly executed — greatly minimizes the chances of a dispute arising between the principal and his/her agent. A copy of this most recent edition may be found in the Appendix.

As with any similar form, it is important that all spaces on the form be completed. Where, for some reason, a given space is inapplicable, the space should be slashed (////) or ex-ed out (xxxx) and initialed.

Always reserve sufficient time to secure all the requisite information from the owner so that the listing form can be completed with accuracy. The contract between broker and principal should be transacted in person and under circumstances where the parties are able to freely converse, discuss their objectives and ask any questions pertaining to the relationship.

After all, once the listing agreement is signed the owner effectively entrusts his business assets to his agent for the purpose of marketing these. And the agent binds himself and impliedly promises his best efforts to locate a buyer, using all the of the knowledge, training, experience and resources at his disposal. This form should never be executed in blank.

Now let's refer to the Business Listing Agreement itself:

Paragraph 1 (Exclusive Authorization) is a concise statement of the contractual relationship between the "Owner" and the "Broker." The listing agreement referred to, while styled as simply a Business Listing Agreement, is, in reality, an Exclusive Business Listing Agreement which grants to the agent the sole and exclusive right to market the owner's assets. As in the general practice of real estate sales, there are other types of agency agreements (such as the open listing, or agency listing) which may be deployed by the parties. In the field of business opportunities practice, these are rarely used.

The agent should take care to correctly identify the true owner of the assets to be sold. This is particularly true when the business has been incorporated at some point in the past and the person with whom the listing is transacted is simply a shareholder of the corporation, most typically the shareholder. The same reasoning applies with partnerships, limited liability companies, and other entities such as family trusts and the like.

It is not uncommon for persons holding the entirety of corporate stock to identify themselves as "owners" of the relevant business when, technically, they are simply shareholders of a corporation which, in turn, owns the relevant assets.

Paragraph 2 (Business Disclosure Statement) provides an important, mostly self-explanatory caveat with respect to the parties' relationship. The agent should not attempt to explain the legalese that appears in Paragraph 2 and should instead refer the owner to his own attorney in the highly unlikely event that questions were to arise during the parties' interview.

Paragraph 3 (Documentation) provides a checklist as to documentation that the owner agrees to provide to the agent within ten days of execution of the listing. Of course, not every item applies in every instance, but it is important that this checklist be completed carefully and accurately since potential buyers and their agents can be expected to rely on any such information provided.

Where copies of documents are called for (such as a franchise agreement, a fictitious name statement, an inventory of fixtures and equipment, or sales tax returns), the agent should make certain that his seller actually makes these available and that legible copies are entered into the seller's file.

Paragraph 4 (Real Property). In the unlikely event that the business assets owner also owns, and has elected to sell, the

In light of the fact that business brokers rely to a great extent on the practice of cooperation and commission sharing with their fellow brokers, the absence of a minimum commission (or otherwise unattractive percentage) may act as a deterrent to potential cooperating brokers referring their buyers.

Paragraphs 6 G. (1) and (2) merit special mention. Stranger things have happened than a seller's omitting to disclose prior marketing activities with regard to his business. Often a prior brokerage relationship may have been selectively forgotten, a fact which could place the prior and successor agents at loggerheads when it comes time to claim a commission.

The listing agent should specially direct his client's attention to Paragraph 6 G, and after eliciting a negative response should enter a slash (////) on the line following G. (1) while requesting that the client enter his initials thereafter. If, upon inquiry, the client's response is anything other than negative, the broker should question the prospective client thoroughly and perhaps make direct inquiry of the relevant predecessor to ascertain whether or not he retains any exclusive marketing rights.

If the owner has previously offered his assets to, or engaged in negotiations with, one or more third parties, it may be unfair for the agent to claim a commission in the event one of these identified parties ultimately became the purchaser. Where this is indeed the case, the would be seller should be encouraged to disclose this fact and to identify any relevant party or parties. Based on the owner's disclosure, the agent may (or may not) elect to take the listing. Otherwise, the potential exists for a nasty commission dispute.

If after discussing the issue, it appears that the seller has not exposed his business to any identifiable third party, or if, having done so, he is nevertheless prepared designate the agent as exclusive, paragraph 6 G. (2) should be similarly slashed and initialed.

3. **OWNER.** Identify owner(s) along with business and home residence addresses and phone numbers and email addresses.
4. **ADDRESS AND PHONE NUMBERS.** Enter phone numbers, email and street addresses of business and its owner(s), as well as any Web site address.
5. **MAP CODE.** Use Thomas Brothers Map Code; put in nearest cross street.
6. **PRICE.** Owner's suggested listing price or expectations.
7. **PLUS STOCK IN TRADE?** This amount should be the wholesale cost of the inventory. In most cases this will be a rough estimate since the owner will rarely know the exact value of his inventory. The value of the inventory will be adjusted during escrow after the buyer takes possession and a physical inventory is taken. This figure should also include the value of any floored merchandise since the buyer will have to qualify for the flooring.
8. **ENCUMBRANCES WHICH MAY BE ASSUMED.** This is a total figure of all notes, Small Business Association or flooring loans, and other encumbrances that a buyer may be able to assume, thus potentially reducing his down payment requirement. If there is a note, which cannot be assumed by a buyer, do not include it in this figure. List the total of each individual encumbrance in the following lines, showing the monthly payment of each and the applicable interest rate(s).
9. **CASH DOWN.** This is the amount the owner indicates he is willing to accept as a down payment on his business. Be sure to point out that the commission comes out of this figure. If the owner indicates that he wants all cash for his business, point out the realities of life in that it is very difficult to get "all cash" for any business because a buyer will use his funds to purchase as large a business as possible. Avoid increasing owners' expectations in this regard.

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10. **OWC.** "OWC" means "Owner will carry." Normally this will be the total price minus the total of the cash down and encumbrances that can be assumed. If the owner has a particular monthly payment in mind, indicate this amount and the interest rate on the note the owner will carry. There are many creative means available to adjust the differences between sellers who typically desire as much cash as possible as soon as possible, and those typical buyers, who invariably prefer to fund their deferred payment obligations through revenues derived from the assets themselves.
11. **GROSS SALES.** Can be estimated based on most recent monthly, quarterly, or annual figures, subject, of course, to potential verification by any future business purchaser.
12. **NET PROFITS.** Can also be estimated based on most recent monthly, quarterly, or annual figures, subject, of course, to potential verification by any future business purchaser. If the owner has included personal expenses in his business accounts, these amounts may be added back in as profit. If the owner took a salary, indicate the total salary for the period reported. If the husband and wife or partners took a salary, indicate all of these also.
13. **ACCOUNTANT.** Identify the name and phone number of the accountant or bookkeeping service who can be contacted for accounting verification. If the owner maintains his own books, indicate this fact.
14. **EMPLOYEES.** Indicate the total number of employees along with a breakdown as to the different jobs performed by these. Also disclose estimates as to wages paid to different categories of employees, indicating which are full- and part-time workers.
15. **OWNER WORKS.** If the owner contributes his own personal service, show the amount of time he/she, or other non-compensated family members work and the type and extent of services performed by each.

16. **TALK TO HELP.** Inquire as to the measure of confidentiality the owner expects from his agent. For example, may the owner's manager or employees be consulted? Do they know of the impending marketing of the business?
17. **BUSINESS HOURS.** Record the hours of business operations.
18. **ESTABLISHED.** How many years has the business been in operation? How long has the business been operated by the present owner?
19. **REASON FOR SELLING.** This item of information is of particular relevance to potential buyers — for obvious reasons. Just as obviously, many sellers are reluctant to disclose their "real" motivation (as opposed to a concocted one). Brokers should avoid certifying the accuracy of this information to potential buyers, although it is not improper to disclose "Owner indicates he wants to sell because. . ."
20. **SHOW ONLY BY APPOINTMENT?** Where the owner has indicated a desire to be present when the business is shown, be sure to record this fact.
21. **COVENANT-NOT-TO-COMPETE WITHIN...** This type of agreement that sellers typically make is relevant to, and demanded by, many knowledgeable buyers. What, if anything, will this business owner agree to in this regard? Two-mile radius of three years? Five-mile radius for ten years? The entire county, forever? Or whatever?
22. **ACCOUNTS RECEIVABLE/ ACCOUNTS PAYABLE.** Will the presence of an overwhelming number of these become a factor in the pricing and sales promotion of the owner's assets? Inquire, and list any unusual circumstances in this regard.
23. **DISTRESS FACTORS, IF ANY.** Has the owner/business proprietor been involved in any adverse-creditor or insolvency proceeding within the last five years, or filed for protection

BF. Build & Decay

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27. **LISTING STATUS.** An agent who is sufficiently committed to invest time and resources in the marketing of an owner's business assets should strive to obtain an exclusive listing. In the event an owner balks at providing an exclusive listing, this fact should be noted, and if the agent is willing to act in a non-exclusive capacity, an open listing agreement should be specially prepared for execution by the parties.
28. **EXPIRATION DATE.** Any agreement to list real or personal property should bear an expiration date. With this in mind, the agent should request the maximum amount of time that the owner is inclined to offer.
29. **COMMISSION.** Business brokers, as a rule, employ a commission structure in excess of that used by real estate brokers. Commissions, while always a matter of negotiation between the owner and his prospective agent, are generally reckoned in the ten percent range. These days the normal custom and practice in biz-ops is to specify a minimum commission ranging anywhere from \$6,000 to as much as \$25,000, depending upon the apparent value of the relevant assets and any foreseeable complicating factors.

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DETAILED INFORMATION REQUIREMENTS ON SPECIAL LISTINGS

The following is a partial list of information a licensee should acquire with respect to certain types of listings for dissemination to prospective buyers:

AUTO RELATED

A person buying any auto related business should have some degree of familiarity with the field in which they are buying. For example, a person buying an auto body shop should be familiar with that type of business. An auto repair buyer or an auto wrecking business buyer should be knowledgeable in the mechanical field. A buyer for an auto parts store should have some knowledge or experience pertaining to that field, or a

BASIC COMPONENTS OF AN EVALUATION

The basic components, which together influence the evaluation of a business, include in order of relative importance:

1. recent financial history of the enterprise;
2. perceived desirability of such intangible assets as the business premises lease, trade name, logo, customer list(s) collectively referred to as "goodwill";
3. value of fixtures and equipment;
4. everything else, including prepaid franchise fees (if any), the often overlooked seller's covenant not to compete, required special licenses, if any (such as a liquor, or beer and wine license), and the wholesale cost of inventory or merchandise for resale.

Often, particularly when assets of a food and beverage retailer are at issue, the listing price does not include any figure for inventory. In those instances, the price will be stated as \$xxx plus food and beverage inventory at wholesale existing prior to close of escrow. Most buyers prefer not to inherit large amounts of unsold inventory at wholesale— or any other price— for obvious reasons, but this is an issue upon which the parties themselves typically reach agreements during the course of a transaction, most often without the assistance, or even the knowledge, of their broker(s).

The covenant not to compete, or promise, is one commonly given by sellers to buyers of their business assets. Simply stated, the seller promises not to develop or operate a similar business within a specified geographical radius for a specific length of time.

Fixtures and equipment can be based on market, actual replacement, or cost value, or any other value that the seller wishes to assign to these so long as the seller is prepared to disclose his basis for determining the figure.

Again, brokers should never purport to act as appraisers and ought to accept the seller's value of his equipment unless there is some apparent and compelling reason not to accept this figure. As for example, where the value given seems fraudulent or completely beyond the bounds of reason.

Most of the time the only major element in the pricing of a given business upon which reasonable minds can widely differ is that of goodwill. And that figure represents the major portion of the price of most businesses which are sold.

GOODWILL

The term "goodwill" is defined in Black's Law Dictionary as "the favor which the management of a business wins from the public" or as "the fixed and favorable consideration of customers arising from an established and well conducted business". Admittedly, these definitions only state what the term goodwill consists of according to legal authority. They contain no hint as to what goodwill is worth.

One way to look at the problem of valuation of goodwill is this: A party acquiring business assets does so for the purpose of generating revenues from sales or other business operations. Those revenues, as a practical matter, are valueless except insofar as these yield profits to the proprietor.

Like any other type of investment, the acquisition of business assets is accomplished for a price. At some point during the expected life span of the business investment, the acquiring party fully expects to have recaptured (or paid off) his initial investment (the price) and to start earning a clear profit for his

own exclusive benefit. Is it reasonable to expect a hypothetical investor to own and operate business assets for ten years before he starts generating net profits? Or five years? Three? Two?

There is no one formula that applies in every instance, since experience shows that it is the intuitive desirability factor which ultimately influences an interested party to become a "highly motivated buyer" willing to defer his net profits for as much as two years or more.

Most of the time, persons acquiring business assets expect to recapture the entirety of their investments within a three-year period of acquiring them. Where the desirability factor or latent profit potential appears overwhelming, experience has shown that buyers are willing to pay more. Therefore, in the vast majority of cases, goodwill can be reasonably estimated in an amount equal to about three times annual net income. Or at least somewhere within a range of between 2-½ times and 3-½ times net.

The agent's deployment of such net income based criteria is not intended to imply that no breakeven or losing business has marketable goodwill. While it is true that most fitting in this category do not enjoy marketable goodwill, there are a multitude of related facts that might lead a prospective buyer to conclude that an otherwise marginal enterprise is worth acquiring.

NET PROFIT

The term "net profits" can best be defined as the amount that remains from gross sales after deducting the amount of cost of sales (such as the wholesale cost of inventory) and operating expenses (such as rent, utilities, advertising, payroll, and insurance). It is what is left over from operating revenues at the end of the proverbial day.

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And the seller of business assets who cannot deliver a written lease has little to sell. The lack of a long-term written lease, or a business existing under the terms of an oppressive lease, rates as highly negative in the desirability factor column. The often used phrase, "Buyer to negotiate new lease with landlord," generally implies that the relevant assets are to be sold at their replacement value without allocation for goodwill.

Conversely, the owner/seller who enjoys a freely assignable commercial lease on favorable terms and is in a good location has a valuable asset to convey to his buyer — a highly positive desirability factor.

POTENTIAL FOR PRODUCT/SERVICE EXPANSION OR OBSOLESCENCE

As buyers of video rental stores with large inventories of VHS format tapes will attest, the advent of DVD players rendered these products obsolete. And with it, those who would rent these to consumers. On the other hand, some businesses stand on the threshold of ground breaking technologies or, for one reason or another, offer promise of expanding revenues well beyond those experienced by their present proprietors.

Ventures of a visionary nature can produce a highly positive desirability factor but should be approached with great caution by both prospective buyers and business brokers. After all, if this type of business offers such a rosy future, why indeed has the owner decided to turn his back on it and sell?

NEED TO UPGRADE EQUIPMENT OR FACILITIES

Some businesses require periodic reshaping and cosmetic upgrading, just to maintain their shares in a competitive marketplace. Retailers of consumer items as well as purveyors of food and beverages find that their sales decline as their facilities become tired. Manufacturers often experience downturns in productivity when equipment or machinery begin to

various competitors tends to decrease, resulting in the reduction of profitability.

When suggesting a price for a given business, the agent should take cognizance of this competitive environment and adjust accordingly. This adjustment should take into account not only current conditions, but also reasonably anticipated changes on the horizon. For instance, the desirability of the Bongo's Burgers business assets mentioned above took a steep downward turn the day it first became known that McDonald's and Burger King planned to locate next door.

EXCLUSIVITY RIGHTS

In some instances, it may be important for the business proprietor to achieve protection from competition in his immediate vicinity. This is especially true where the enterprise is based in a shopping mall and where the goods and/or services it offers are unique or of a highly specialized nature. Where this is the case, the owner should seek to obtain an exclusivity clause in his lease whereby the premises lessor promises not to lease nearby premises to others engaging in the owner's trade.

Negotiation and enforcement of such clauses generally requires the assistance of an attorney, but once an effective exclusivity provision is granted, this would certainly qualify as a positive desirability factor.

LABOR ISSUES

One principal reason why owners of businesses elect to sell is their continuing inability to attract quality employees at wages they deem appropriate or economically feasible. To the extent this is an issue with respect to a given business, this fact constitutes an often overlooked negative desirability factor.

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GEOGRAPHICAL DETERIORATION

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Since most businesses operate from an established location, if the surrounding neighborhood is such that customers would prefer to conduct their business elsewhere (due to safety concerns or just for aesthetic reasons), this fact is a clear negative desirability factor.

Where a given business cannot effectively be moved from a venue showing indications of continued serious deterioration, this fact should be regarded as a highly negative (perhaps even a completely disqualifying) desirability factor.

PARKING

For most businesses, safe and convenient parking is absolutely essential. Where parking exists, preferably in a well lighted, marked, off street lot, this should be deemed a positive desirability factor. Where it does not exist, a negative desirability factor is present.

OVERALL ECONOMY

The presence of a severe economic local or national recession or depression, the threat of war, or other calamity constitutes a major negative clouding the desirability factors horizon.

SAMPLE EVALUATION #1

Let's use an example to perform a thumbnail evaluation: An owner of a retail sporting goods business has indicated a desire to sell.

The store nets about \$60,000 a year before any owner's salary is deducted, and the owner works full time. Were the owner to retire or become disabled, his services could be replaced by an employee for about \$25,000 annually, including benefits. The inventory fluctuates, averaging about \$75,000.

CORPORATE STOCK TRANSACTIONS

One of the advantages enjoyed by business proprietors who incorporate is that when it comes time to sell, they may elect to simply transfer the entirety of their corporate shares to their buyer instead of participating in a business assets transaction.

The concept is simple. The assets remain in place just as they were. The corporation, or other legally constituted business entity remains the owner. In a stock transfer, each of the assets and each of the liabilities (cash, accounts receivable, inventory, equipment, buildings, real estate, accounts payable, notes payable, tax losses, etc.) remains a corporate asset. Only the corporate stock changes hands.

Corporate stock transactions, although theoretically simple, are usually prompted by tax considerations, which are never simple. Stock transactions rarely consist of over-the-counter tenders of share certificates. Usually these are achieved through the machinations of accountants, attorneys, and sometimes even bankers or creditors.

The role of a business broker in such transactions is typically limited due to the legal and accounting complexities involved. As well it should be. Whenever a seller or buyer indicates a preference that a given transaction be completed as a corporate stock sale, the agent should insist that each party retain legal counsel before proceeding further.

As to the issue of valuation, the actual worth of business assets is not materially affected by the format of their ownership, corporate or otherwise. While such concepts as book value and accelerated depreciation tend to drive such transactions forward, what the business broker needs to know is that a business is worth whatever it is worth, regardless of the format by which the relevant assets are held.

buyer, while providing the latter with a reasonable opportunity to rescind the ongoing transaction if he so elects based on the content of the disclosed accounting irregularities.

Just as the biz-ops broker is not either a business consultant or an accountant, neither is he supposed to function as a business records cop. Whether or not his clients observe standard accepted accounting procedure is a matter for their own discretion. Subject, of course, to the duty of full disclosure to potential buyers.

FINANCIAL RECORDS SHOWN TO BUYER AS A CONTINGENCY OF SALE

Financial records of a given business are certainly relevant to any potential buyer. However, proprietors of businesses have legitimate reason to demand that these records be shared only with those having a "need to know", such as bona fide buyers. For his part, however, the person interested in acquiring assets has a legitimate need to know as much as possible about the owner's business assets and their profitability. How does the business opportunities broker balance the rights of the seller to maintain confidentiality of his financials with those of an inquiring prospective purchaser?

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First of all, such items as P&L statements, balance sheets, sales tax reports, and other information of a financial nature are the property of the proprietor. These are shared with the biz-ops broker for the sole and limited purpose of assisting the agent in his assets marketing efforts. These are not intended for the general dissemination to the general public, and the broker who violates this fiduciary duty will inevitably and quickly lose his or her client's trust and confidence.

Books, P&L statements, and other accounting records of a business should NEVER be provided to the buyer, or to anyone else, without the prior written permission of the owner.

Prospective buyers will appreciate the broker's discretion in this matter and will invariably be willing to consider making offers based on the owner's general representations of profitability, so long as these appear credible and reasonable. (It is for this reason that the biz-ops agent should take great care in the preparation of his original listing and disclosure agreement.)

Once the prospective buyer becomes an actual buyer with his submission of a formal offer that has been accepted by the seller, his "need to know" becomes more immediate and relevant. Most offers contain contingencies, or prerequisites to the purchaser's obligation to perform the terms of the buy/sell agreement. The capable business opportunities broker will have learned to draft offers in such a way so as to protect their buyer/clients by including various contingencies.

These are typically phrased such as, "Buyer's review and approval of Seller's financial records, the same to include all ledgers, bank statements, sales tax returns and books of account, profit and loss statements, and balance sheets for the past three years."

One of the more important contingencies included on the typical business-assets offer to purchase is the requirement that the seller furnish all his financial records (usually within a specified period of time), and that buyer be given the right to review and approve the same (also within a specified and limited time frame). Many such contingencies also include language by which the buyer agrees to maintain the confidentiality of any/all financial records supplied by the seller.

BALANCE SHEETS

Another type of financial statement that the biz-ops broker is likely to encounter is a balance sheet, showing the financial condition of the business, the assets and liabilities as of a certain date.

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P-1
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CURRENT AND LONG-TERM LIABILITIES

Liabilities are listed as current liabilities and long-term liabilities.

Examples of current liabilities are trade payables to purveyors, rent and sales taxes owed, and such other normal recurring obligations as insurance premium and utilities payments, advertising and equipment-lease accounts, employment development and state disability taxes and the like.

Long-term liabilities include bank loans extending for more than one year, deferred obligations in favor of business sellers, judgment creditors, limited partners as so forth.

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Liabilities may be secured or unsecured. Secured liabilities are those for which the creditor or obligee enjoys some protection in the form of collateral (such as a recorded lien against the business assets, pink slip(s) on vehicle(s), or recorded abstract of judgment against the assets owner).

Except credit card.

OWNER'S EQUITY

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The difference between the total liabilities and the assets is the owner's equity. Assuming a business owner has \$100,000 in assets and \$50,000 in liabilities, his owner's equity is \$50,000. Often, a business assets owner will have a negative equity value, connoting a situation where the gross amount of the liabilities exceeds the aggregate sum of the assets.

A business of this sort is generally difficult to market successfully unless the overall circumstances are such that eventual profitability appears reasonably foreseeable. Or where the owner is willing to take a loss at least in the short term.

INTERPRETED BY OWNER

One of the most important things for the business opportunities agent to remember about financial statements is that these

The initial contact represents the agent's first — and more often than not, his last, and only — opportunity to establish rapport with the caller. Many, if not most, first-time callers (and virtually all callers who refuse to identify themselves) will prove to be time wasters. This fact should not discourage the agent from taking calls, since it is through this medium that the skillful agent can establish himself as competent, knowledgeable, and downright essential to anyone seriously interested in acquiring, or selling, business assets in the relevant time zone.

INQUIRIES RELATED TO A PARTICULAR BUSINESS OFFERING

When a customer relates that he's calling about a particular advertised business offering and requests information, the biz-ops broker should inquire as to when and where they might meet in person to discuss the specifics. The only information that should be shared on the phone is generic, such as the general nature of the relevant business, the general location, and the asking price.

If the caller is not satisfied, the broker should explain that the seller has a right to expect a degree of confidentiality in the dissemination of proprietary information and that he (the broker) is scrupulous about maintaining his relationship with the seller. (If the caller cannot appreciate the broker's scruples in this regard, he will not be a good candidate with whom to conduct business anyway.)

The business opportunities broker should never, under any circumstances, disclose the identity of any listed business or seller over the phone. Nor should he engage in guessing games with callers. Where and when the potential customer asks for information about a given business beyond the generic, he should be informed that such will be provided during the course of the personal interview. If the caller refuses to agree to an

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Name

AGENTS SHOULD NOT SHARE PROPRIETARY INFORMATION

These days, the "listing book" once so prevalent in the biz-ops business is rarely used, so most of the agent's research is conducted online. In those locales where the listing book or business opportunities brochures are still in use, these constitute proprietary materials of the trade and generally should not be shared with clients. By conducting a reasonably thorough telephone screening, the agent should have gained a good idea as to the type of business the prospective client seeks as well as the level of his intended financial investment.

With these parameters in mind, the agent will have had an ample opportunity to research the local market for available business assets, or for potential buyers.

Having done the research beforehand, chances are that the knowledgeable broker will be able to present the potential buyer with a short list of, preferably, not more than three possible acquisition targets. Again, the broker should not identify these by name, but rather generically (by describing the type of business, approximate location, approximate amount of disclosed sales, and asking price).

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If one or more of the acquisition candidates seems attractive to the buyer, the agent should present his broker/buyer representation contract for review, and possible execution. This accomplished, it's time to take the new client shopping for a business. After calling the listing owner(s) or broker(s) in the clients order of preference for appointment(s), the agent may be well-positioned to make a deal.

INTERVIEWING PROSPECTIVE SELLERS

The protocol between broker and owner/prospective seller is similar to that discussed above, although the parties discussion

CHAPTER 7

BUSINESS PURCHASE AGREEMENT AND JOINT ESCROW INSTRUCTIONS

AGREEMENTS IN WRITING

Although numerous business assets transactions have been memorialized by notes scrawled in pencil on the back of used envelopes, and others have been sealed with a mere handshake, many others have erupted in misunderstanding, frustration and even litigation. Suffice it to say that today no competent biz-ops broker would attempt to ply his or her trade under conditions of such informality.

Although, technically, a transaction involving the sale of personal property valued at less than \$500 is legally enforceable without the necessity of any writing at all, it would be difficult to contemplate the transfer of business assets from an owner to a buyer without the terms and covenants being reduced to writing.

The Statute of Frauds of historical derivation renders any contract for the sale of goods in excess of \$500, as well as any lease of real property in excess of one year unenforceable unless the same be in writing signed by "the party to be charged."

LETTER OF INTENT

Buyers sometimes choose to reduce the terms of their offers to writing in the form of a letter of intent, which is really an offer by another name. A letter of intent can be drafted informally, with or without the assistance of a broker, and is most often deployed in lieu of an unsolicited offer for unlisted properties. In order to be effective, a letter of intent should state all of the cogent terms of

GLOSSARY

ADA, or Americans With Disabilities Act. federal legislation intended to provide equal access to, and enjoyment of, public commercial facilities by the disabled

abatement. process by which a nuisance is controlled or terminated; or, a legal pleading seeking dismissal of a cause of action on some legally recognized grounds, such as the expiration of the statute of limitations

ABC. Alcoholic Beverage Control, a state regulatory agency

abstract of judgment. a document issued by the court which may be recorded in order to create a judgment lien against those assets of the judgment debtor located within the county

acceleration clause. provision in a contract or other legal document, such as a promissory note, that upon a certain event, such as the default in payment of an installment note, the time for performance of specified obligations shall be advanced

acceptance. unqualified assent to the act or proposal of another

accord and satisfaction. an agreement between two or more persons for the delivery and acceptance of a sum of money or other valuable consideration in lieu some other obligation in full settlement thereof

accounts payable. amounts owed by a proprietor of a commercial enterprise arising from normal business operations

accounts receivable. amounts owed to a proprietor of a commercial enterprise arising from normal business operations

blue sky. phrase commonly used to describe intangible assets, such as goodwill, which collectively augment the value or desirability of a given business

board of directors. collective group of persons, or body, duly authorized to act on behalf of a corporation

bona fide. good faith; often used to describe a motivated party possessing the ability and willingness to acquire property

book value. the value specified in the accounting records of the owner representing the original cost plus capital improvements less depreciation

broker. a person employed by another, the principal, usually for the purpose of assisting in the acquisition, sale, financing or management of property, such as a real estate broker

bulk sale law. the Bulk Transfers Law codified as Article 6 of the Uniform Commercial Code and enacted in California as Division Six of the state Commercial Code, applicable to the transaction of bulk sales

bulk sale. any transfer of a major part of the materials, supplies, merchandise or inventory of an enterprise not in the ordinary course of business

bulk sales law. legislative enactment found in Division 6 of the Uniform Commercial Code for the protection of buyers and the seller's creditors which applies to transactions involving all, or substantially all, of the sellers assets, except in the normal course of business

business license. authority granted by a governmental jurisdiction to enabling a party to legally conduct business

business assets. items of personal property customarily deployed in a commercial enterprise

demised premises. specified parcel of real estate to which the lessee is entitled to possession under the terms of a lease

Department of Business Oversight. agency of the state government under whose auspices corporations are chartered and their activities regulated

deposit. a partial payment of money made by a prospective purchaser as evidence of good faith; in some jurisdictions, earnest money

depreciation. loss of value of property brought about by age, physical deterioration or functional or economic obsolescence; a term used in accounting to compute or substantiate loss of value for tax purposes

discount points, or points. a commission paid to a lender at the time a loan is made, one point being equal to 1 percent of the principal amount lent

disorderly house. business premises commonly known as, or alleged to be, a venue for prostitution activities

double escrow. the process by which a purchaser of real or personal property transfers his interest in a pending transaction to a third party prior to the closing of escrow

dual agency. an agency relationship in which an agent acts concurrently for both principals in the same transaction

due diligence. process by which a party engaged in a transaction to acquire property assures himself of the value and/or desirability of that which he seeks to acquire, usually by means of inspection(s), review of documents, and consultation with professionals

earnest money. a deposit made by a prospective purchaser as evidence of good faith.

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easement. a right, privilege or interest in the real property of another, limited to a specific purpose, such as ingress and egress

economic obsolescence. type of depreciation characterized by loss in value due to reduced desirability and usefulness of a structure due to extraneous causes such as zoning restrictions, deterioration of the neighborhood, or changes in the law

employee. one who provides services to, and subject to the supervision of another, the employer

encumbrance. any legal right to, or interest in, property owned by another which tends to diminish its value, such as a lien against, or easement on, the subject property

encumbrancer. one who has given value in exchange for a legal right to, or interest in, property owned by another

environmental impact report. certification by an environmental expert or other qualified individual as to the probable results of a proposed project, especially with respect to the potential for environmental degradation

equipment. items of tangible personal property which enable one, such as a business proprietor, to engage in commercial operations

equity. body of common law principles application to certain types of legal actions, such as claims for injunctive relief, where the award of monetary damages would provide insufficient relief; the value of real or personal property over and above the aggregate of liens encumbering it

escrow. procedure whereby legal instruments and/or funds are deposited with a neutral third party subject to the provisions of a written contract, called escrow instructions

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#4-a

48 license, or Type 48 License. a type of ABC-issued license which permits the retail onsite distribution of distilled liquor either in conjunction with or without the sale of food

franchise. permission granted by an individual or a legal entity to market its product(s) or service(s) under conditions set forth in a written contract

Franchise Tax Board. state agency which administers and collects franchise and income taxes from individuals and business entities

Franchise Investment Law. state legislative enactment found within the Corporations Code which regulates the offering for sale of franchises and which is intended to protect the rights of franchisees

fraud. the making of a false statement of a past or existing fact with knowledge of its falsity, or with reckless indifference as to its truth, with the intent to cause another to rely thereon, and which is reasonably relied upon by an innocent party to their detriment

free look. colloquial phrase to describe a prospective buyer's interim possession of property or operation of a business without a corresponding obligation to complete a purchase, solely in order to test the market, a disfavored practice among sellers

freehold estate. an estate, or mode of property ownership of indeterminable duration, such as a fee simple or life estate

functional obsolescence. a type of depreciation which is characterized by loss in value due to out-of-date, old fashioned, or poorly designed equipment

general partner. participant in a limited partnership who enjoys the exclusive right and duty to manage its business operations and who bears personal liability for the liabilities of the venture

goodwill. an intangible business asset of value implying the expectation of continuing and profitable public patronage