

“Tips and Tricks for Buying an Accounting Business”

Presented by:

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Tom has over 25 years' legal and business experience including:

- Being an owner and director of his former firm, Murfett Legal;
- Previously working for local law and major national firms;
- Being the national operations manager for a financial advisory IT platform provider;
- Previously being the WA Legal Technology Group Manager for a National Law Firm
- Owning and managing an IT consultancy business; and
- Being a director and in-house counsel for a public company.



He is also a regular publisher of articles and is one of Australia's leading presenters of legal seminars to and for various professional bodies, associations and government authorities on a wide range of business law and professional development-training topics including:

WA Department of Commerce • Chartered Accountants Australia and New Zealand • Law Society of WA • Innovation Centre of WA • LegalWise CLE • The Tax Institute • Institute of Public Accountants • Governance Institute of Australia • National Electrical & Communications Association (WA) • Australian Hotels Association (WA) • Small Business Development Corporation • Australian Institute of Conveyancers (WA) • CPA Australia • Mortgage & Finance Association of Australia • City Insolvency Discussion Group • Forum for Directors of Indigenous Organisations (FDIO) • Stirling Business Centre • Institute of Certified Bookkeepers • Western Suburbs Business Association • Business Foundations Inc. • WA Business Assist • WA Reckon Partners • WA Indian Docs Inc.



Disclaimer

This seminar is not legal advice and must not be relied on as such.

The information presented in this seminar is intended only as a guide, as to the topic and the matters discussed.

If you have a matter which relates to this seminar or you require legal advice, careful review and analysis of your matter's particular facts, information and documents are required before proper legal advice can be given or applied to your matter.



What Sort of Accounting Business Is It?

- Financial accounting (including bookkeeping)
- Tax and Compliance (have all Tax Agent requirements been satisfied all as required by the *Tax Agent Services Act 2009*?)
- Audit (Auditing Competency Standard for Registered Company Auditors and ASIC requirements (RG 180))
- Management/ Business Advisory
- Does it provide licensed financial services e.g. Superannuation advice via an AFSL authorisation?

What's the Structure the Accounting Business Operates from?

- Sole-practitioner (home-based?)
- Part-time or full-time practice?
- Company or partnership?
- Is it a part of a franchise system? e.g. tax franchises



Business vs. Asset Sales

- May only need certain assets e.g. goodwill, IP, key staff and/or certain P&E, as already have everything else.
- If Seller in a financially distressed position, may be wait until voluntary administration or even liquidation, and the negotiate with those (external administrator) parties...
 - of course the purchase of the Business then will not be as going concern/GST-free.

Selling agents and 'known , possible buyers' (e.g. management buy-outs, open trade sale, merger, competitor etc)

- Note: Business Brokers are only licensed, and insured!, to sell businesses and assets , not equity (e.g shares sales). See definition of s.4(d) "business transaction" in *Real Estate and Business Agents Act 1978 (WA)*.
 - Conversely, for an unlicensed broker, "management consultant" or "corporate advisor", they will have no claim for commission or fee even if they successfully 'sell' such.
 - Secondly, the consequences for trading without a license are severe, with penalties ranging from **fines ranging upwards of \$10,000 to prison sentences of up to 2 years in some States.**
- Same therefore also goes for accountants - who neither hold a Business Brokers licence or an appropriate AFS license under the *Financial Services Reform Act 2001 (Cth)* and the *Corporations Act 2001(Cth)*.



Pre-Contracting matters to address

- *for Seller –*
 - Confidentiality Deed/NDAs!
 - ASIC, ABN, PPSR www.ppsr.gov.au and IP Australia www.ipaustralia.gov.au searches plus review Seller's current 'website.
 - As to any PPSR registrations - must promptly identify what they are which encumbrances need be removed and/or paid-out (and how, if shortfall?) at settlement
 - Key documents' compilation and review.
 - Can informal commercial matters tidied-up/ratified?
 - Be very careful as to exactly what Seller representations have or will be made e.g. "Sales brochure" or information memorandum from the Business Broker, "Business Reports", Vendor Warranties & Due Diligence disclosures, Financial Statements etc
 - Also at least notify/ speak to your Seller's commercial lawyer asap!

continued...



Pre-Contracting matters to address (cont.)

- *for Buyer –*
 - Buyer entit(y)ies (e.g. goodwill/IP in one and assets in another) and GST registration
 - General due diligence as per above for seller i.e. ASIC, ABN, PPSR and IP Australia searches plus ‘website’ review and Credit search
 - Also, highly recommend using the Australian Business Licence and Information Service” (ABLIS) www.ablis.business.gov.au
 - Also try and get as much possible information (e.g. financials, premises & equipment leases, key contracts’ details etc) from Seller with having to pay or sign for such! Helps negotiate better /more-realistic Purchase Price sooner. Also consider getting an independent valuation of the Business.
 - Ensure that the Buyer has prepared a business plan, with cash flow budget projections together with sufficient working capital including but not limited to payment of acquisition costs (e.g. transfer duty, stock, advisors costs as well as sufficient working capital)
 - Engage appropriate professionals to undertake due diligence as well as assist with ultimate Settlement.



Sale Contracts and Purchase Price

- Terms Sheets, Heads or Agreement and Information Memorandums:
 - Indicative/ 'Non-binding' vs. Binding...
 - Expressions of Interest and 'Agreements to Agree'.
 - Exclusivity vs. "competitive tension".
- A 'Standard' contract (by whom?) vs. bespoke contracts (note: Business Sale Contracts are commonly prepared by the Seller's business broker for the Seller, and quite often with no legal and/or accounting advice or input first...)
 - Therefore Seller can sometimes be unnecessarily legally and and/or financially exposed or under-protected e.g. poorly-worded vendor finance terms, weak deposit provisions, no pre-sale 'seller legal due diligence' etc
- Apportionment the Purchase Price (and competing tensions between buyer and seller relating to same)
 - e.g. P&E (\$400k) and goodwill (\$600k) = \$1m PSAV
 - tip: need such in any event, for tax records and Duties assessment*

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Sale Contracts and Purchase Price (cont.)

- Buyer – apportionment *to maximise upfront tax relief*:
 - Trading stock; then
 - Depreciable assets (includes patents, designs, copyrights); then
 - CGT assets that may expire, cancel, cease to exist; then
 - Other CGT assets.

- Seller – apportion *to maximise concessions*:
 - Pre-CGT assets (real property: goodwill?); then
 - CGT assets; then
 - Pre-CGT concessions available (general discount, Small Business Concessions); then
 - Trading stock and depreciable assets (disposed of at settlement versus execution of contract); then
 - Other CGT assets where no concessions available.



Deposits and Vendor Finance

- How much?
 - Usually no more than 10% of purchase price and commonly much less (but for the Seller, ensure that its not a nominal amount too)
- Up-front and refundable until/if settlement?
- Single or 'phased deposit(s)'?
- **Vendor Finance Arrangements (VFA):**
 - Firstly, why!?
 - How much a part of the purchase price (and whether a Deposit has also been paid).
 - Also recommend the VFA term be shorter and rate of interest be higher than commercial lending rates, and maybe an 'early repayment' incentive provision.

continued.....



Deposits and Vendor Finance (cont.)

- VFA must be as a full written loan agreement with term, interest rate, repayment schedule, warranties, insurances & certificates of currency, access to premises, provisions of financials, verification and audit , *plus securities!*
 - (e.g. PPSR over all of the business assets i.e. an ALLPaP. Not just over, say, stock etc)
 - Plus consider third party-guarantees (with securities too?)
- Where does VFA 'rank' with other financiers and secured creditors?
- *'Irrevocable Privacy Disclosure Consent'* from Buyer/Borrower whilst any monies is still owing to Seller/Lender under VFA Loan Agreement (including surviving upon material default or termination)
- To the VFA Seller: Do you just want your money or the (probably trashed) business back if the has Buyer defaulted?
 - i.e. Retirement vs. Reversion back into the business!?



Due Diligence (DD)

- Financial Statements.
- Depreciation Schedules.
- P&E inspection.
- ‘Communications details’ (e.g. website, emails phone and fax. Note: who “owns” the mobile numbers for the key employees/ sales managers’ phones?)
- Key Contracts.
- Has also the business’ systems and procedures been captured in good, written manuals and IT infrastructure?
- Does DD change the ‘value’ of buyer’s ‘initially agreed’ (but lesser-aware) Purchase Price?
 - Note *for Seller*: be careful, which (if any) of their employees can be contacted by the Buyer during or as part of DD!



Special Conditions

- Why have them and how do they work (usually used to 'vary 'standard'-from Sale Business Contracts)
- *For Buyer* they may:
 - also want/ seek to have greater oversight or even control over the Seller's conduct of the business (other just retaining the status quo) before Settlement; and
 - with sometimes, even having paid a (sizeable) non-refundable deposits e.g. Seller not enter into any new contracts with Buyer's express permission... etc
- Importance of 'paramountcy' of documents and the legal applicability of same as to any conflict or ambiguity between provisions/clauses.
 - e.g. Special Conditions apply first, then Schedules, then General Conditions and then Annexures.



Employees

- Are they written or 'on a handshake' employment arrangements?
- True 'contractors' vs. employees?
- True 'casuals' vs. permanent part-time?
 - Note: even casuals can & do accrue Long Service Leave Entitlements.
- Details of all Employment contracts, start date, roles, positions, hours (hint: get payroll system data)
 - Also obtain HR records (e.g. performance warnings and notices – subject to Privacy Act consent and compliance by Seller.)
- Are you taking all, some or none of the current employees?
- 'Transmission of employment' employees :
 - Same or 'better-off overall' test met.
 - Accrued entitlements amortisation (60 -100%?) offset against Purchase Price
 - i.e. Personal, Annual and Long Service Leave
 - Accepting passed-probation or anew employment contracts?



Key Contracts

- Are they written or 'on a handshake'?
- Are there any 'third party- masters' ?
 - e.g. Lessor, Franchisor, Bank, Key Suppliers, Key Employees, Key Licensors etc
- Careful financial analysis/forecasting of P&E provisioning, Leases (and premises re-fit/updates), Franchise Agreement, Employee bonuses etc.

Key Clients

- Key Clients means all prior and existing clients and referrers associated with or material to the conduct of the Business.
- Ensure where practical and possible that you formalise contracts with key clients.
- If you plan on selling the client database as a business asset, you may be 'trading in personal information', which means the *Privacy Act 1988* will apply. Ensure that you have the consent of clients prior to the completion of the sale.



Intellectual Property, Confidential Information and Goodwill

- Business name vs. Domain Name vs. Trademarks
- Other IP e.g. registered or unregistered (but registrable?) designs, patents, circuit board layouts, etc...
- How good is the business' current NDAs, Employment and Contractor Agreements in relation to this? (if none, then ensure robust Vendor warranties...)
- Are you buying 'goodwill'?
 - If so, highly-recommend/ need –
 - Registered Business and Product & Services' Trade Name(s)
 - Related IP registration,
 - Clear identification of clients,
 - Vendor Handover; and
 - Vendor & Vendor Covenanter's Restraints of Trade
 - Particularly more so the latter, and longer, if it applies to 'services-based' business otherwise consider 'earn-out'/'rise & fall' type provisions (in addition Retention Sums)*.

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Intellectual Property, Confidential Information and Goodwill (continued)

What is 'goodwill'

"Goodwill is the product of combining and using the tangible, intangible and human assets of a business for such purposes and in such ways that custom is drawn to it. The attraction of custom is central to the legal concept of goodwill. Goodwill is a quality or attribute that derives among other things from using or applying other assets of a business. It may be site, personality, service, price or habit that obtains custom. It is more accurate to refer to goodwill as having sources than it is to refer to it as being composed of elements. Goodwill is a composite thing. It is one whole. It is an indivisible item of property that is legally distinct from the sources from which it emanates. It is something that attaches to a business and is inseparable from the conduct of a business. It cannot be dealt with separately from the business with which it is associated."

- *Commissioner of Taxation v Murry [1998] HCA 42 at 85.*

What can be identified as the key components or sources of 'goodwill':

- Skill & reputation of employees
- Business names
- Brand (trade marks, design)
- Trade secrets/processes/confidential information
- Identity of the clients
- Identity of the suppliers
- Location
- Standards of service



Buyer Finance Applications

- Ensure sufficiently 'loose' (if you are Buyer) and 'tight' (if you are Seller) e.g. so once key date(s) passes they can terminate contract to maybe get a (better?) third party purchase offer etc.
- Fundamental differences between:
 - *(conditional) finance approval/letter f offer vs.*
 - *unconditional finance approval vs.*
 - *funds available for settlement.*
- Should provide a (redacted) copy of finance approval to seller's agents, so the Buyer financier's specific 'conditions precedent' can be incorporated in Sale Agreement.
- IMPORTANT Note *for Buyers*: if say a Buyer's related persons privately borrow money from a bank against, say, their home or other equity, and then 'on-loans' such to their new Buyer-entity...
 - **Need formal Loan agreements with security asap!!**



Third Party Approvals and Key Persons

- Usually (or should be!) in 'conditions precedent'.
- If Key person doesn't agree to join Buyer:
 - does sale still proceed; or
 - is it dealt with by the Purchase Price Adjustment and/or Retention Sum*?
- For *the Seller*- Remember to also check for any 'director's guarantees' that should be released on assignment of any key contracts
 - Albeit less so a risk than with equity sales, if Seller supplier paid-out at Settlement etc)



Adjustment of Purchase Price

- After, if at all possible, Due Diligence
- P&E agreed to be higher than written down-down value. What are the tax consequences to Seller.
- Debtor and Creditors
 - Obviously, the creditors will be the Seller's sole responsibility (subject notices with new ABN / bank account details etc to relevant clients, suppliers etc)
 - With Debtors- are they sold be sold to the buyer. Usually not, but need to ensure to a prompt accounting for and on-payment by the seller if it (incorrectly) receives such
- Note to Sellers: watch for if the sale price comprised possible equity in lieu of ca\$h for purchase price e.g. no cash for payment CGT (if any) etc.



Stock-take and Valuation

- Estimated Stock' level to be at settlement – practical inconvenience to buyer if not maintained
- Aged and Good condition stock?
- Stock-take adjustment mechanism and still proceeding with settlement.

Vendor Warranties and Indemnities

- Remembering the Buyer should be effectively buying the business' assets and not any of seller's liabilities.
 - SAVE FOR: specifically agreeing maybe to take on certain business liabilities such as the assignment of lease, equipment lease, transferring employees etc
 - Be very careful and certain with these, as they can have serious ramifications for both parties
- How long for and what happens if Seller wound-up?
- For *the Seller*: consider 'Vendor Warranty Insurances'.



'Claw-backs' and Retention Sums

- Pros & cons of each
 - Clawbacks are essentially warranty claims which:
 - have to be proven then quantified by Seller; and
 - if not accepted by Buyer, sued upon in Court!

Therefore, it can be like 'arguing uphill' by the Seller, for their residual purchase -price monies owed money...

- Where & how Retention Sums should be held e.g. Buyer's agent trust accounts or interest-bearing account (especially long term), Joint bank account, Bank Guarantee?
- For purchasing an accounting 'services'-based business and Seller's clients may not be as 'sticky' to the business as they may be to, say, the Seller covenantor...
 - Then, in addition to robust Restraints of Trade and appropriate handovers etc.
 - Also consider a retention sum that suitably 'adjusts' for a possible diminution in the client-base (but may also allow for a 'top-up' or 'replacement' clients by the Seller?).

continued.....



'Claw-backs' and Retention Sums continued

- Deferred Payments

PURCHASE PRICE

Subject to the Deferred Payment set out in schedule Item (1) below, the purchase price shall be ONE MILLION FOUR HUNDRED THOUSAND DOLLARS (\$1,400,000), being the aggregate of:

- A. First Vendor's Goodwill \$1,350,000; and
- B. Second Vendor's Plant and Equipment \$50,000.

LESS all the Key and Transferring Employees' accrued employment entitlements (e.g. annual, long-service, sick leave etc)

(1) Deferred Payment

The Vendor agrees that the Purchaser shall withhold the sum of SIX HUNDRED AND FIFTY HUNDRED THOUSAND DOLLARS (\$650,000) from the Purchase Price ("the Retained Payment"), which shall be payable to the First Vendor on the anniversary of 2 years from the Completion Date ON THE CONDITION that:

(b) If for any reason, other than as a result of the:

- (i) The Purchaser does not competently provide its professional services to the Clients; or
- (ii) the Clients terminate the engagement of the Purchaser because of:
 - A. the Purchaser failing to provide sufficient and/or satisfactory service; or
 - B. for inaccuracy of the provided services provide; or
 - C. the Purchaser charging an hourly rate lower than rate currently billed to the relevant Client; or
 - D. the Purchaser has raised the Business' fees by more than Fifty percent (50%).



GST

- Going Concern (GSTR 2002/5): when is a 'supply of a going concern' GST-free?
- Asset Sale or GST-applicable transaction.
- GST application and indemnification by Buyer (i.e. Purchase price + GST)

Settlement

- Settlement "Date" - recommend the later of:
 - Parties' desired , specific date; and
 - Say, (at least) 2 business days after last of the conditions precedent met or waived by Buyer.
- Vendor to prepare Settlement Statement.
- PPSR Discharges.
- Electronic Transfer Funds (EFT), or Bank cheque? Note: now also New Payments Platform (NPP) and PayID with some banks www.nppa.com.au



Default and Termination

- Need clear process set-out and appropriate provisions.
- Consider also 'Dispute Resolution' clause.
- Consequences for each party if they cause termination.
- What provisions 'survive' termination? e.g. confidentiality, right to sue for breach, damages etc

Post-Settlement matters

- Hand-over, announcements to staff and introductions to key clients and suppliers.
- 'Time of the Essence' and 'Further Assurances' provisions.
- Maintain a good Documents' Register relating to the entire Sale and Purchase transaction.
- Note: Post-Sale of Business litigation is, unfortunately, more common than you may think!



Transfer/ Stamp Duty

- Under the s.23 of Duties Act 2008 (WA) all transaction records must be lodged for assessment within two (2) months of the date of the dutiable transaction.
 - Penalty tax of up to 100% of the duty will be imposed where transaction records are not submitted by the due date
- Watch for s.280(2) of Duties Act 2008 (WA) “Unlodged instruments, duty of non-party to lodge”:
 - *If, after the expiry of the time provided under section 23 within which an instrument referred to in subsection (1) is to be lodged for duty endorsement, a person who is not a party to the dutiable transaction effected by the instrument —*

continued...



Transfer/ Stamp Duty (cont.)

- (a) *has possession or control of the instrument; or*
- (b) *acts under the instrument,*

that person must, as soon as practicable, lodge the instrument or give notice of the instrument to the Commissioner.

- Penalty: a fine of \$20 000.
- Concession Rate - eligibility for sales of dutiable property i.e. business assets of \$200k and under)
- Note s.88A - Conditional Agreements, and (very) conditional 'no duty payable' and s.107 Cancelled Contracts of Duties Act.



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