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Now's The Time To Buy

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Bargains can be had, but be sure to do your homework before bidding on a restaurant.

Investors with liquid financial resources are finding seemingly endless opportunities to acquire businesses and assets at prices significantly lower than those of recent years. One industry with more than its share of businesses available for sale is the restaurant industry. The opportunity may be tempting, but it also can be a trap for the unwary.

HOW'S THE 'HOOD? It's important to consider the surroundings before buying.

In every restaurant acquisition a number of due diligence items must be carefully investigated by the acquirer. Some of these items require even greater scrutiny in the current challenging economic environment:

Location, location, location: As with real estate, the location of a restaurant will largely dictate its success or failure. This is even more true in a bad economy. Diligent investigation of the surrounding location and clientele during all hours of service should be conducted. The makeup of the surrounding businesses, including expected growth or retraction and proximity of competing restaurants, should be taken into account.

Financial due diligence: Financial statements and tax returns should be reviewed by an accountant or consultant with experience in the restaurant industry. While current financials will likely show declining operating results, it is important to evaluate whether other non-market-related factors are contributing to the decline. There may be opportunities, for example, to eliminate or curb expenses that can provide an immediate boost to the operating results. More importantly, there may be evidence of a declining customer base or brand loyalty that will be more difficult to overcome.

Vendors: The restaurant's vendor contracts and relationships should be reviewed. If a restaurant has been struggling, it is very likely that invoices owed to existing vendors are long overdue and as a result the relationships have soured. The acquirer should consider specifying in the purchase agreement that a portion of the purchase price will be used to settle some of these payables. If the purchase price will be insufficient to satisfy the payables, the potential purchaser will need to consider whether he or she will be able to mend the relationship sufficiently to ensure adequate coverage of the restaurant's needs postclosing.

Employees: Employee salary and benefits costs should be analyzed. A restaurant with high employee turnover, union involvement, wage and hour compliance issues and significant workers' compensation insurance and health insurance costs can wreak havoc on the overall profitability of the restaurant.

Liens: Personal property and real property records should be searched to determine what liens have been recorded against the property. The acquirer will want to ensure that these liens are removed prior to closing the acquisition.

Ownership of intellectual property: Ownership of intellectual property, including brand tradenames, trademarks and recipes, is particularly important when buying restaurants from an established chain. The acquirer needs to be sure that he or she will have continued and uninterrupted use of the intellectual property going forward and will be able to transfer ownership of the intellectual property upon sale to another party. This can often be accomplished by negotiating a franchise agreement or license.

- **Lease:** Assuming the lease is assignable, the acquirer will have the most leverage at the time of acquisition to negotiate an extension or modified terms to the existing lease for the restaurant location with the landlord.
- **Permits:** Permits and licenses, including liquor licenses, will need to be transferred or acquired prior to closing.
- **Inventory:** Inventory, particularly liquor and wine inventory, should be carefully counted at the time of entering into the purchase agreement and provision made for required levels to exist at the time of closing the acquisition. Gift card/certificate programs and other potential “hidden” costs should also be reviewed.
- **Noncompete:** A determination as to whether immediate competition by the former owners would adversely affect the business should be made. If competition is an issue, a carefully drafted noncompetition agreement should be signed.

Matthew Ertman *is a partner in the Los Angeles and San Francisco offices of the law firm of Allen Matkins Leck Gamble Mallory & Natsis LLP. He has extensive experience in representing companies, including restaurant companies, in corporate finance transactions and regularly advises public and private companies in mergers and acquisitions, joint ventures, strategic alliances and partnership arrangements. He can be reached at* mertman@allenmatkins.com.

How Will You Pay for That Property?

So you've found a sweet operation. But you're not sure you can line up financing. These days, it's best to think outside the box in money matters, says Chad Simmons, author of *Business Valuation Bluebook, 4th Ed*. (Facts on Demand Press, 2009). Your options:

1. Look at seller financing. You make a down payment of between 30-40 percent of the business's value, and pay the rest over a few years with interest.
2. Try family loans. “Loans from the older to younger generations of entrepreneurs can benefit both — as fixed income for one and opportunity for the other,” Simmons says.
3. Think smaller. Now might be a good time to cut back on the capital you invest in any business. You may be able to expand it when the economy rebounds.
4. Pay cash. If you have the cash on hand or can scrape it together, buying the business straight out can be wise. It reduces risk dramatically, and it also gives the buyer negotiating muscle.
5. Find an equity partner. Lots of people, usually called silent partners, want to invest in a small business but don't necessarily want to run it.
6. Offer a performance bonus. You and the seller agree on a value lower than the asking price, and the owner gets a bonus if the business meets certain goals during the first few years.

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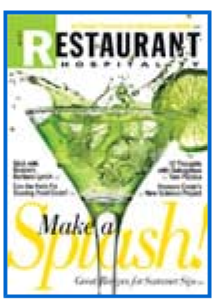
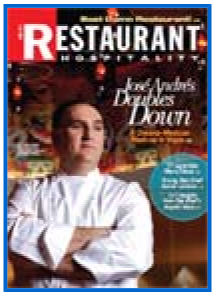
- 

- 

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