Stephen Larsen and Co

TAX AND BUSINESS ACCOUNTANTS

SPECIAL BULLETIN

Due Diligence Action Checklist

Buying a business requires careful consideration of various choices. A business can be purchased either through purchasing the business's assets or through purchasing the shares in the company or interests in the trust.

It is important to ensure that a thorough due diligence review has been conducted before a decision to buy is made. The review should find out as much information about the business as possible, which you can then discuss with your adviser. You should also consider how embarking on a business venture would fit with your personal circumstances.

This checklist highlights common areas that must be considered when buying a business.

Item	Yes	No
Where the business is conducted through a company		
1. Has a company search been done to verify the vendor?	☐	☐
2. Are all companies' office requirements up-to-date?	☐	☐
3. Does the company have any overseas operations?	☐	☐
Financial health		
4. Have you obtained the last four years financial statements of the business?	☐	☐

TIP: The financial Statements should contain a breakdown of:

- liabilities (including contingent liabilities);
- inventory; and
- accounts receivable and payable.

Item	Yes	No
5. Have you obtained information on the business's capital structure and, where possible, obtained a current list of vested interests (such as shares, options, warrants, etc) and outstanding debt instruments?	☐	☐
6. Have you obtained an up-to-date copy of the business's credit report, if available?	☐	☐
7. Has a comparison between the business's gross profits and the industry trends been done?	☐	☐
8. Have you considered the financial projections and major growth drivers of the business in the next four years?	☐	☐
Taxation considerations		
9. Have you obtained the last four years tax returns, including supporting schedules and workpapers of the business, such as Fringe Benefits Tax returns, etc?	☐	☐
10. Have you obtained confirmation that all tax obligations such as income tax, GST, PAYE are up-to-date and paid?	☐	☐
11. Have you familiarised yourself with the tax obligations of the entity to be purchased?	☐	☐
TIP: If the business is conducted through a company, consideration must be given to the duties of a director under the tax law.		
12. Have you reviewed all correspondence with Inland Revenue as to whether the business has any private tax rulings, amended notices of assessment, etc, that may apply?	☐	☐
13. Are you aware if the business is currently being audited by Inland Revenue or has been audited in the last four years and, if so, what its outcome was?	☐	☐
14. Have you considered whether the purchase of the business will be a supply of a going concern, i.e. GST-free?	☐	☐
ALERT: Where a business is sold through an asset sale, the purchaser does not inherit any tax liabilities of the business. However, where a business is sold through the sale of units or shares, the purchaser inherits the tax liabilities of the business. Where a business is sold through the sale of units or shares, it will not qualify as a supply of going concern, i.e. the purchase of the units or shares will be an input taxed financial supply.		
If you are buying a business through an asset sale		
15. Has a fixed asset register been obtained detailing all the assets being sold?	☐	☐
TIP: The register should detail the following information about the assets: • the original purchase price; • the purchase date; • the depreciation method used; • the depreciation rate used; • the effective life of the asset; and • the written down value.		
16. Have you checked the ownership and condition of the assets being sold?	☐	☐
17. Where the assets are leased by the business, have you obtained copies of the leases?	☐	☐
TIP: If you are taking over the existing leases, consideration should be given to whether the leasing terms are reasonable.		
18. Are the assets adequately insured until settlement of the purchase?	☐	☐
19. Has the purchase price been apportioned across the assets being purchased?	☐	☐
ALERT: If the purchase contract for an asset sale includes the purchase of the business's trade debtors, you will not be able to claim an income tax deduction for bad debts.		
If you are buying a business through a sale of units or shares		
20. Have you obtained a listing of all current shareholders or unit holders?	☐	☐

Item	Yes	No
Employee obligations		
21. Have you obtained a list of the employees, including their salary and other entitlements?	☐	☐
22. Are you aware of all employment conditions, including key workplace agreements, any incentive bonus plans, staff rotation policies, disciplinary procedures, standard of conduct, etc?	☐	☐
23. Have all outstanding employee entitlements, such as medical insurance guarantee and annual leave, been accounted for?	☐	☐
24. Are you comfortable with the current business culture, the level of staff relations and turnover over the last four years?	☐	☐

> **ALERT:**
> Where a business is sold through an asset sale, the purchaser can choose not to take on the employees of the vendor (except in the case of specified categories of employees under section 69A of the Employment Relations Act 2000). However, where a business is sold through the sale of units or shares, there will be a continuity of employment and the buyer is responsible for any employee liabilities accrued.

Item	Yes	No
Trading stock		
25. Does the trading stock include any obsolete stock?	☐	☐
26. Has the trading stock been valued at market value?	☐	☐

> **TIP:** Where the purchase of the business includes trading stock, the trading stock must be valued at market value on the day of disposal, which is normally the date of the purchase contract.

Item	Yes	No
Business premises		
27. Have you sighted copies of all real estate lease agreements, deeds, mortgages and any relevant documents to the premises?	☐	☐
28. If the same business premises are to continue, has the vendor facilitated a lease assignment and all documents signed by you?	☐	☐
29. If there are improvements to the business premises, has a register been obtained detailing the improvements?	☐	☐

> **TIP:** The register should detail the following information:
> - the cost of the improvements; and
> - date of construction or acquisition.

Item	Yes	No
Other considerations		
30. If you are acquiring the business with other people, do you have the necessary agreements in place?	☐	☐
31. Are the business operations subject to any government regulations? If so, are all relevant government licenses, permits or consents up-to-date?	☐	☐
32. Does the business have any pending or ongoing lawsuits, or any recently finalised litigation cases?	☐	☐
33. Have you given thought to whether the structure (company, partnership or trust) that the business operates through is suitable for your needs?	☐	☐

> **TIP:** The structure of the business will determine your legal obligations. Factors that should be taken into account when considering whether the structure of the business is suitable for your needs include asset protection and succession planning.

Item	Yes	No
30. Have you searched the local council and other government agency records to ensure there are no plans or council orders that could disrupt the business or lead to a potential drop in sales?	☐	☐
31. If a restrictive covenant, earn-out clause or claw-back clause is included in the purchase contract, have you ascertained the legal and tax implications?	☐	☐
32. Have you identified the key customer and supplier contracts and the likely impact a change of ownership might have on these agreements?	☐	☐
33. Have you examined current production, distribution, sales and marketing strategies of the business and the likely impact of a change of ownership?	☐	☐

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