
BLACKTECHSTARTUP EDUCATION

Buy a Small Business Without Buying a Problem

Find, normalize and diligence an operating business before price seduces you: customer concentration, owner dependence, earnings quality, liabilities, technology, contracts and a written acquisition decision memo.

Find, normalize and diligence an operating business before price seduces you: customer concentration, owner dependence, earnings quality, liabilities, technology, contracts and a written acquisition decision memo.

Buying cash flow can be smarter than inventing it—but only if the cash flow is real

Buying an existing business can give you customers, employees, supplier relationships, operating history and cash flow on Day 1. It can also transfer years of hidden problems. Start with an acquisition thesis before browsing listings: industries you understand, geography, minimum and maximum owner earnings, recurring versus project revenue, customer concentration limit, required licenses, number of employees, technology dependence and how many hours you are willing to work. A thesis stops you from buying whatever seller tells the best story.

For Black entrepreneurs, acquisition can be an ownership path that does not require inventing a venture-scale startup. It can also be a way to acquire a customer base, permits, skilled workforce or distribution that would take years to build. But do not treat “existing business” as “proven business.” Your job is to reconstruct the economics from evidence.

Normalize earnings before you discuss price

Request at least three years of business tax returns, profit-and-loss statements, balance sheets, bank statements and current year-to-date financials. Reconcile revenue across tax returns, accounting records, bank deposits and payment processors. Then build normalized seller earnings or EBITDA by separating real operating expenses from legitimate owner-specific adjustments. Every add-back should have evidence. “The next owner will cut this expense” is not an add-back unless you can operate without it.

Build a monthly cash-flow view, not merely annual totals. Identify seasonality, one-time pandemic-era anomalies, deferred maintenance, unpaid owner labor, under-market family wages, future rent increases, customer prepayments and working-capital needs. A business that reports \$300,000 of seller earnings but needs \$200,000 of inventory and major equipment replacement can behave very differently from the headline.

Diligence the customers, not just the financial statements

Create a customer-concentration schedule showing the top 10–20 customers, revenue, gross margin, tenure, contract status, renewal dates and the person who owns the relationship. If one customer represents 35% of revenue, your purchase is partly a bet on that customer staying. With permission and at the appropriate stage, design a confirmation plan so key relationships are tested before closing or immediately after under controlled communication.

Review lost customers and churn, not just current wins. Ask what percentage of revenue is recurring, contracted, repeat-but-not-contracted and one-time. Inspect pipeline quality and whether sales depend on the owner’s personal reputation. Revenue that cannot survive the seller’s departure should be discounted or protected with transition terms.

Measure owner dependence as a replacement cost

List everything the owner does in a normal month: sales, estimating, supplier negotiation, hiring, quality control, technical work, licenses, emergency response, bookkeeping and customer relationships. Estimate what salary and time it takes to replace each function. If the owner works 60 hours but the P&L shows no market-rate manager compensation, reported earnings overstate what an absentee or semi-absentee buyer will keep.

Ask which credentials, licenses, guarantees, vendor accounts, certifications and personal relationships are tied to the owner. Verify transferability. A company can lose practical operating ability even when the legal entity transfers cleanly.

Run legal, tax, asset and technology diligence in parallel

With qualified advisers, review entity ownership, liens, litigation, employment obligations, leases, supplier agreements, customer contracts, licenses, insurance claims, taxes, intellectual property, equipment title and environmental or regulatory risks where relevant. For a technology-heavy business, inventory domains, cloud accounts, source-code repositories, software licenses, administrator credentials, cybersecurity incidents, backups and whether contractors properly assigned IP.

If the deal is a franchise, federal rules add a specific disclosure process. The FTC says a prospective franchisee generally must receive the Franchise Disclosure Document at least 14 days before signing a contract or paying the franchisor or affiliate. Read all 23 disclosure items and speak to current and former franchisees; do not let the brand substitute for diligence.

Use an LOI to buy diligence access—not to stop thinking

The letter of intent should capture price framework, cash/debt/seller-financing concept, asset versus equity structure being considered, working-capital assumptions, diligence access, exclusivity period, transition expectations and major contingencies, while counsel clarifies which provisions are binding. Do not make the diligence period so short that a seller's urgency becomes your risk.

Create a deal-breaker list before signing the LOI: unverifiable revenue, unresolved tax liens, a key customer unwilling to continue, required license that cannot transfer, undisclosed litigation, seller refusing normal records, or earnings that collapse after market-rate replacement labor. Predetermined gates prevent sunk-cost psychology from turning a bad deal into “we have come too far to quit.”

Your acquisition decision memo

Before financing, write a two-page memo with: purchase price; normalized earnings; required working capital; immediate capital expenditures; top customer concentration; owner-dependence replacement cost; key legal/regulatory risks; three downside scenarios; seller transition plan; why you are a better owner; and the maximum price that still meets your required return after debt service. If the deal only works with perfect assumptions, it does not work.

Guide 61 owns financing and closing. Do not negotiate a loan first and then convince yourself the business is worth buying because a lender might fund it. First prove the asset. Then choose the capital.

Research behind this guide

Use the primary and authoritative sources below to verify current rules, prices, eligibility and program details before acting. Terms can change.

SBA — Buy an existing business or franchise



SBA — Plan Your Business



IRS — Publication 334, Tax Guide for Small Business



IRS — Form 8594 Instructions



FTC — Consumer's Guide to Buying a Franchise



FTC — Franchise Rule



Important: This guide is educational information, not individualized legal, tax, investment, employment, security or compliance advice. For decisions with material legal or financial consequences, use a qualified professional who can review your facts.

SHARE THIS GUIDE ↗

POWERED BY: BLACK TECH STARTUP

blacktechstartup.com