



THE FACILITATED

BUY SELL AGREEMENT

OVERVIEW

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The buy-sell agreement is a foundational shareholders' agreement for any business with two or more shareholders. Its purpose is to manage the biggest risks a company and its shareholders face: the unexpected loss of a managing shareholder.

HOW IT WORKS: The buy-sell agreement provides clear terms for transferring shares upon certain triggering events such as the death, disability, retirement or other voluntary and involuntary departure of a shareholder. Although a buy-sell agreement will include many detailed provisions, its principal provisions involve the valuation of shares that will be transferred following a triggering event.

RECOMMENDED ACTION: The best time to value a business is now, as you contemplate the creation or updating of a buy-sell agreement. The only time that all of the parties' interests are aligned is now, before a trigger is pulled. Waiting to value the business until after a triggering event means you are putting off an agreement on the value of the business until after the parties' interests have diverged.

FUNDING OPTIONS: Funding the buy-sell upon the death of a shareholder is another key provision the parties must consider. Life insurance is the most effective manner of managing this risk, but it is not always an available option, such as when one of the parties is uninsurable. In this event, agreeing now on detailed terms of the buyout that will follow the trigger event should be clearly resolved and submitted to writing in the agreement.



Few things are more likely to throw parties into litigation than a disagreement over the value of the business after one of the shareholders leaves the firm, whether voluntarily...or involuntarily by death or disability. Disputes following departures can threaten the stability of the business, and cause pain and confusion in a family at a time that is often already painful and confusing.

THE PROBLEM: Lack of communication. Partners do not have sufficient clarity about their choices.

THE SOLUTION: A facilitated conversation that addresses all of the relevant questions, allowing all parties to make fully informed decisions.

DANGERS TO AVOID:

- New owners not included in the agreement
- All relevant trigger events not defined
- Fixed price agreements not up-to-date
- Confusion caused by formula agreements – failure to clearly define earnings and adjustments and “management” of earnings to influence results
- Shock at costs and delay of multi-appraiser approach
- Standard of value and level of value not adequately defined
- “As of date” not specified
- Funding mechanisms and terms not specified

TOOLS TO HELP:

The following questionnaire is designed to help you prepare to have an informed conversation with your advisors about the terms of your buy-sell agreement.



BACKGROUND QUESTIONS

- Why are you considering a buy-sell agreement now?
- Have you been party to a buy-sell agreement in the past? If so, what happened?
- Are you comfortable with your knowledge on buy-sell agreements?
- What is the ownership breakdown of the company? Please include shareholder name, percentage owned, and shareholder age.
- Have all shareholders paid for their shares?
- Do you know the value of your business? If so, what is it, and how did you arrive at the value?
- Has your business been professionally appraised? If so, when and for what purpose.
- Do you have a succession plan? Is it in writing?
- Have the shareholders who will be party to the buy-sell agreement completed their estate planning? If so, does it include life insurance?

STATUS QUESTIONS

- Does one shareholder or a discrete group of shareholders have a controlling interest in the business? If yes, do you intend to keep it this way?
- Will all shareholders be party to the agreement?
- Do any shareholders have personal guarantees on the corporate debt? Who?
- Does the age difference between shareholders make conversation about your buy-sell agreement difficult?
- Do you have a board of advisors or a board of directors?



TERMS AND TRIGGERS

- Upon which events would you like your agreement to trigger the transfer of shares? Please list “triggering events” you wish your buy-sell to address such as death, disability, firing, retiring, or otherwise voluntarily leaving.
- If you die while owning shares of the company, what would you like to happen to your shares?
- Would you like to limit or at least have the right to approve new shareholders?
- Do you expect/plan for any of the shareholders to sell their interest upon retirement, and if so, would you like this addressed in your buy-sell agreement?

TRANSACTION – VALUE

- Do you prefer valuing the shares of the company before or after a trigger is pulled?
- Which standard (definition) of “value” would you like your buy-sell agreement to use, such as fair value, fair market value, book value, investment value, owner value, economic value, intangible value, or insurable value?
- Do you expect all shareholders to receive the same value for their shares after a triggering event, even if they own a minority interest? Specifically, do you expect that applicable discounts for lack of marketability and/or control should be applied, or should the minority interest be valued on a pro rate basis?
- Do you have an opinion on how you expect/want to fund the purchase of shares subject to the buy-sell following a triggering event?
- Do you expect the buy-sell agreement to be part of your succession plan discussion?
- Are there any other business objectives you would like your buy-sell to address?

OUTCOME

- Does your business (exit) plan contemplate the sale of your business to a third party, and if so, when?
- What impact will the market perceive of a change in ownership, if any?
- Are your decisions in your buy-sell agreement likely to create any rifts among the shareholder group?