

## Business Succession Planning: Buy-Sell Agreements

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What would happen if you or one of the other owners of your closely-held business left the business, either voluntarily or due to his or her death? Without a proper estate plan, the result could be disastrous for you or the ones you leave behind. In many cases, a buy-sell agreement is the solution.

Typically, a buy-sell agreement provides that the remaining owners and/or the business itself are required to purchase the ownership interests (or are given a right of first refusal over them) if certain "triggering events" take place. The common triggering events include death, disability, retirement, termination of employment, and bankruptcy. A buy-sell agreement also generally sets the price or a method for determining the price of the ownership interests. It may also limit who can purchase the ownership interests and

provide a funding source for the purchase of the ownership interests.

The primary purpose of a buy-sell agreement is to protect both the owners who exit the business (or their estates) and the owners who remain. For example, when an owner of a closely-held business dies, the remaining owners or the business itself may not have sufficient funds to pay fair market value to the deceased owner's estate for its ownership interests. In addition, there may be no market to sell the ownership interests. In this situation, without a buy-sell agreement, the decedent's family may realize very little from the business that the decedent worked hard to build.

From the remaining owners' perspective, they may find that the involvement of the deceased owner's family in the business hinders their continued operation of the business. As a result, they may be eager to purchase the ownership

interests. Without a buy-sell agreement, the price for the interests and the terms of the sale may be set by the Probate Court. Likewise, the continued operation of the business may be subject to Probate Court review and approval. Even if the Probate Court is not involved in the matter, the remaining owners may find that the deceased owner's family has an unrealistic opinion of what the ownership interests are worth. Sometimes this is based on what they were told years earlier by the now deceased owner. If the parties are unable to negotiate an appropriate price and terms, the remaining owners may find that the continued operation of the business is subject to the review and approval of individuals who were never involved in the business.

A buy-sell agreement is intended to resolve these types of issues. Specifically,

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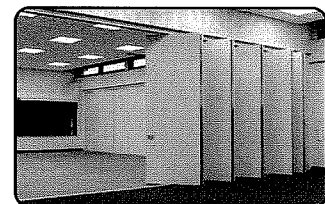
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a buy-sell agreement typically determines the price for the ownership interests by either selecting a formula that the parties must follow to determine the fair market value of the ownership interests, or requiring an independent appraisal to determine the value. Sometimes, a buy-sell agreement enumerates an agreed price, which the owners are required to update periodically. A buy-sell agreement also typically sets the terms for the purchase of the ownership interests. For example, it can provide for a predetermined schedule of payments or the terms for a promissory note if payments are to be made over an extended period of time. Often, a buy-sell agreement is combined with life insurance to provide a source of funds for the remaining owners to make the required payments. A buy-sell agreement also typically restricts who can own the interests. For example, it may prohibit the transfer to certain family members or require that each remaining owner be given the opportunity to purchase a pro rata share of the decedent's ownership interests.

In addition to resolving the issues surrounding the death of an owner, a

buy-sell agreement can resolve similar issues in situations in which one of the business owners withdraws from the business, either voluntarily or involuntarily, i.e. an owner resigns, his employment is terminated, he becomes disabled or files for bankruptcy. Although the general issues are the same (sale price, payment terms, and transfer restrictions), the owners of the business may want the issues resolved differently. For example, the owners may want an immediate payout to the family in the case of the death of a business owner. On the other hand, they may want a withdrawing owner to receive payments over an extended period of time. This might provide a disincentive to owners who are considering whether to withdraw and protect the business from being required to make a substantial payment upon the withdrawal of an owner.

A buy-sell agreement may also include terms that are intended to reduce the likelihood of protracted and expensive litigation. In either the situation of a deceased owner or a withdrawing owner, the chances of litigation are high if there is no buy-sell agreement and the parties are unable to negotiate satisfactory terms for the transfer of the ownership inter-

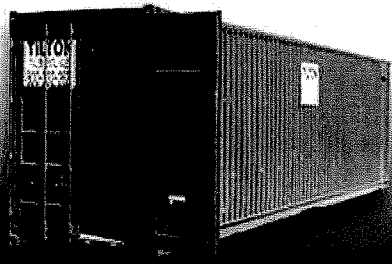
ests. Sometimes, a buy-sell agreement requires the arbitration of disputes and attempts to prohibit court litigation.

In the case of a family run business, a buy-sell agreement can ensure that the children who are active in the business remain the majority if not the sole owners of the business. This is often important because businesses owned by siblings who are active in the business and siblings who are not active in the business commonly have problems because their interests may differ substantially. For example, the siblings who are not active in the business may want to maximize short-term profits at the expense of the long-term health of the organization, whereas the siblings who are active in the business may wish to maximize their compensation at the expense of profits. A buy-sell agreement also addresses the income tax, gift tax and estate tax consequences associated with the transfer of ownership interests. The tax consequences are largely dependent on the type of business organization, i.e. corporation, limited liability company or partnership, and the type of buy-sell agreement established by the owners, i.e. cross-purchase agreement or redemption

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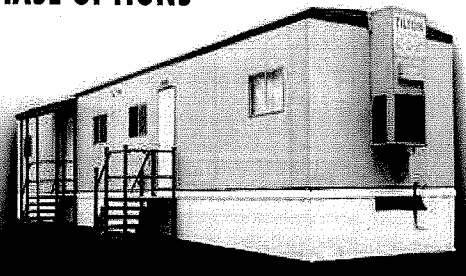
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agreement.

Although the establishment of a buy-sell agreement may seem complicated, it typically only requires the business owners to make a few important choices. In contrast, a closely-held business that does not have a buy-sell agreement often faces significant problems that are difficult to resolve at a critical time for the business, the remaining owners, and the departing owner or the family that is left behind.



## Contractors Should be Aware of ALL Options for Workers Compensation Coverage

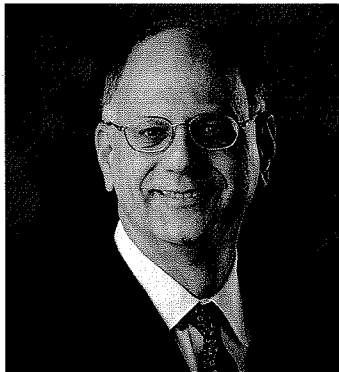
When it comes time for contractors to begin planning for the renewal of workers compensation coverage, insurance brokers work to bring their clients the most appropriate program. Currently, there are many options available in the fully insured commercial insurance market, including dividend programs. However, there is only one self insured group trust available to contractors – the ABC New Hampshire Workers Compensation Self Insured Group Trust. Interestingly, brokers typically do not inform their clients of this option even though it may be most appropriate and it may be an exciting new approach to effectively manage one of the most significant expenses and operational issues a company has.

A self insured group, or trust, is a legal entity established to provide workers compensation coverage to a select group of employers. There are many benefits to the trust partnership. One is Investment

Income. Premiums for all insurances are paid “up front” prior to any related expense being incurred. Also, any claims that may occur have a “long tail”. This means workers compensation claims can remain active for years after an injury. The “up front” premiums and “long tail” with active claims create significant cash flow from the funds that are held in investments. With the ABC Self Insured Group Trust the investment income flows to the trust partners rather than to an insurance company. For example for 2008 the ABC Self Insured Group Trust has budgeted for approximately \$300,000 in investment income. In addition to investment income there is Profit. Rather than paying an insurance company a premium that will never be returned, the premiums from partners in the ABC Self Insured Group Trust are retained and managed by the

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