

As Your Business Changes, Update Your Buy-Sell Agreement: The 30,000 Mile Checklist

Today, we look at all the types of changes (in you, your partners, your company, your finances and your industry) that can transform that vigorous buy-sell you created years ago into a lumbering, but potentially dangerous, dinosaur. In this issue you'll also find a checklist that will help you assess the viability of your buy-sell agreement.

People Change

Shareholders are living, breathing creatures. In addition to all the "bad things" (or transfer events) that we discussed in previous issues, shareholders will age. As they do, they may adjust how much they want to work or what goals they want to work toward. If shareholders are all of a common age, they may share these changes or they may not. If one shareholder is older than one or more of the others, the commitment to work long hours or the long-term ownership goals of the older and younger shareholder can diverge. Should that happen, the only effective recourse may well lie in the provisions of a well drafted, comprehensive and current buy-sell agreement.

Companies Change

The most common change in the life of a successful business is its increase in value. When the company isn't worth much, shareholders may be able to buy each other out if certain events occur. As the company becomes more valuable, however, shareholders cannot put together the resources necessary to cash each other out.

Also, over time, the ownership of companies changes as new owners buy in and older ones sell out and retire. As these changes occur, the ownership proportions can change in ways not intended or planned by the majority shareholders. The buy-sell agreement can respond by allowing ownership, but not voting control, to shift to the younger, incoming generation of owners.



**Michael Wildeveld, CEPA, M&AMI,
CM&AP, CM&AA, CBI, CBB**
michaelw@veldma.com

Veld Mergers & Acquisitions
www.veldma.com
1 Park Plaza, 600
Irvine, CA 92614
[310-652-8066](tel:310-652-8066)

Industries Change

Like it or not, the industries we are in affect the value of our companies. If we're in a niche or "hot" industry, buyers will pay more for our companies and values reflect that demand. If there is a great deal of industry consolidation going on, the value of your company will reflect that. Similarly, industries go through boom and bust cycles and if the company is enduring the bust part of the cycle, its value reflects that downward pressure as well. Buy-sell agreements can be drafted to reflect not only rapid changes in value, but also corresponding changes in the terms (length of buyout, amount of down payment, mandatory vs. optional purchase, etc.) of any purchase. This tends to prevent one owner from "gaming" the buy-sell agreement by selling out when value peaks.

Buyout Requirements Change

When you created your buy-sell agreement, you made decisions about whether particular events would trigger an optional or a mandatory buy out. You made those decisions based on then current factors. As the foundation for those decisions may have changed so too do your preferences. For example, you now may prefer that a child or a key employee acquires your ownership when you retire or die, rather than the other co-owner.

The Ability to Sell Out Changes

When your company was worth very little, it would have been highly unlikely for an unrelated third party to approach you with a lucrative offer to buy. Now that your company may be more valuable, however, the possibility that a third party would make an offer is a real possibility. Does your buy-sell agreement adequately address this? What if one owner wants to sell and the other doesn't? Does it make a difference whether you are the owner who wants to sell or the owner who doesn't want to sell?

Given all the moving parts, it makes sense to review your buy-sell agreement at least every year. The following checklist is designed to give you and your advisors a snapshot of your buy-sell agreement. The purpose is to help you identify those areas that should be updated for all the reasons discussed here.

Buy-Sell Transfer Event Checklist

Death of a Shareholder:

Is it included in the Agreement? Yes No

Buyout: Mandatory or optional Mandatory Optional

If buyout can be funded, is it? Yes No

Is the funding adequate? Yes No

Is the ownership proper? Yes No

Disability of a Shareholder:

Is it included in the Agreement? Yes No
Buyout: Mandatory or optional Mandatory Optional
If buyout can be funded, is it? Yes No
Is the funding adequate? Yes No
Is the ownership proper? Yes No

Divorce of a Shareholder:

Is it included in the Agreement? Yes No
Buyout: Mandatory or optional Mandatory Optional
If buyout can be funded, is it? Yes No
Is the funding adequate? Yes No
Is the ownership proper? Yes No

Bankruptcy of a Shareholder:

Is it included in the Agreement? Yes No
Buyout: Mandatory or optional Mandatory Optional
If buyout can be funded, is it? Yes No
Is the funding adequate? Yes No
Is the ownership proper? Yes No

Retirement of a Shareholder:

Is it included in the Agreement? Yes No
Buyout: Mandatory or optional Mandatory Optional
If buyout can be funded, is it? Yes No
Is the funding adequate? Yes No
Is the ownership proper? Yes No

Involuntary Termination of Employment:

Is it included in the Agreement? Yes No
Buyout: Mandatory or optional Mandatory Optional
If buyout can be funded, is it? Yes No
Is the funding adequate? Yes No
Is the ownership proper? Yes No

Business Dispute Among Owners:

Is it included in the Agreement? Yes No
Buyout: Mandatory or optional Mandatory Optional
If buyout can be funded, is it? Yes No

Is the funding adequate? Yes No

Is the ownership proper? Yes No

The information contained in this article is general in nature and is not legal, tax or financial advice. For information regarding your particular situation, contact an attorney or a tax or financial professional. The information in this newsletter is provided with the understanding that it does not render legal, accounting, tax or financial advice. In specific cases, clients should consult their legal, accounting, tax or financial professional. This article is not intended to give advice or to represent our firm as being qualified to give advice in all areas of professional services. Exit Planning is a discipline that typically requires the collaboration of multiple professional advisors. To the extent that our firm does not have the expertise required on a particular matter, we will always work closely with you to help you gain access to the resources and professional advice that you need.

This is an opt-in newsletter published by Business Enterprise Institute, Inc., and presented to you by our firm. We appreciate your interest.

Any examples provided are hypothetical and for illustrative purposes only. Examples include fictitious names and do not represent any particular person or entity.

©2022 Business Enterprise Institute, Inc. All rights reserved.