

LEGAL ASPECTS OF BUSINESS SUCCESSION AGREEMENTS

Why do you need a Buy and Sell Agreement?

In any business with more than one owner, it is important that the proprietors ensure that the death, permanent disability, trauma (heart attack or stroke), retirement, conviction of serious crime or marriage breakdown of one of the owners does not result in a continuing party finding himself working with a partner of another owner or at worst, a dissolution of the business.

It is therefore important to have a Business Succession (Buy - Sell) Agreement in place. Such agreements can set up a procedure to enable business owners' interests to be effectively transferred during their lifetime in the situations outlined above.

Whether the business is run by a joint venture, partnership, trust or company, the business and its owners need to make specific arrangements for an orderly transfer of the business to the surviving owner(s). In one sense this type of agreement is a business "will".

Equally important, there needs to be provision for the continuing owner(s) to purchase the former owner's interest at an agreed valuation. Other options may include the sale of the business in total, introducing a new equity partner or franchising the business.

Basic Facets of a Buy and Sell Agreement – Generally, the agreement is comprised of the following:-

- **Leaving the Business** – If an owner leaves (whether by death, trauma, permanent disability, retirement, expulsion or other reasons stipulated in the Agreement), the departing owner agrees to give a call option in favour of the continuing owner. This essentially means the continuing owner can call for the sale of the existing owner's share in the business. At the same time, each owner grants an existing owner a put option by which the continuing owner(s) can be required to buy the existing owner's share of the business for an agreed sum.
- **Insurance** – A Buy Sell Agreement should include the requirement of the individual owners or the business to take out and maintain life, trauma and/or permanent disability insurance to fund the purchase of a deceased owner's share. The agreement should also stipulate how the insurance premiums are to be paid.
- **Valuation** – It is vital to set out how an existing owner's share is to be valued. This will avoid quarrels and uncertainty at the time of the sale.
- **Indemnity** – The departing owner may be indemnified from the remaining owners(s).

Conclusion

Buy and Sell Agreements are an essential mechanism for business planning. Failing to plan may result in problems such as the family of the departed proprietor demanding an involvement in the business, lending institutions limiting the continuity of finance and the departed proprietor's family accepting less than what the business is worth. Having such an arrangement in place permits the owners of a business to make decisions about the continuity of the business in the face of significant events as outlined above, whilst allowing them to continue operating the business.

Aspects of taxation and asset protection must also be considered, and it is strongly recommended that business advisers, including accountants and lawyers, are involved in the process, to ensure rights and obligations are respectively protected and honoured.

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