

# Buy-sell agreements — why are they important?

BY DON STALLINGS

If you own an interest in any closely held business with multiple owners you need a



buy-sell agreement. In the event of death, disability, retirement, disagreement between owners, divorce, insolvency or bankruptcy, loss of professional license, conviction of a crime, desire to sell your interest and withdraw from the business before retirement, etc. you could face the possibility that the other owners will try to take advantage of the situation and acquire your interest at a bargain price. Before any of these events occur,

none of the multiple owners know who might be the one wanting to liquidate their interest. It is more likely a fair value for an ownership interest can be established prior to a triggering event. I have often heard the old adage that it takes fifteen minutes to get in business with someone and a lifetime to get out. There is a lot of wisdom to that adage in regard to a closely held business with multiple owners.

Even if you are the surviving owner there are many reasons you would want a buy-sell agreement. No one wants to have to negotiate a purchase price with a widow or widower. Anyone who has ever had to deal with that situation can tell you that it is not a pleasant experience. A buy-sell agreement can also prevent unwanted outsiders, possibly even a competitor, from obtaining an ownership interest in your company.

One of the most common problems with buy-sell agreements is inadequate consideration for funding the agreement. An agreement is not going to help much if the buying party has no funds to execute it. In many small businesses finding the money to fund the agreement is the major problem. Signing a non-funded buy-sell agreement can create more problems than it solves. Partial funding combined with lender agreements to fund the balance can solve this problem when lenders can be found that are willing to provide loan commitments. An experienced attorney should be consulted to draft your buy-sell agreement.

One of the most important components of the buy-sell agreement is the determination of the value to be paid for the ownership interest. Consulting an experienced valuation specialist in constructing the val-

uation clause is always a good idea. While it is common to see a simple formula for valuation set out in the buy-sell agreement many times "rule of thumb" methods (i.e., five times earnings) are utilized which can sometimes result in unrealistic values.

Not entering into a written buy-sell agreement is simply ignoring a problem. There is no better time for providing for a solution than when you initially become an owner in a multiple owner business. **DBJ**

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