Buy Sell Agreement

View Legal

WHAT IS A BUY SELL AGREEMENT?

A buy sell agreement is a contractual arrangement between members of a jointly owned business (for instance, a company). The agreement is structured so that subject to certain events relating to the departure of a principal, the continuing principals are given the option, or in some cases are obliged, to purchase the interest of the departing principal.

NEED FOR A BUY SELL AGREEMENT

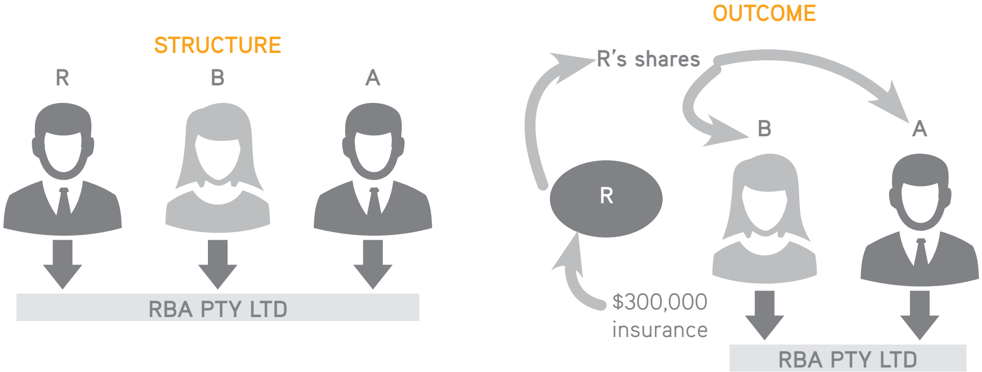
There is often insufficient capital available for the remaining principals to buy out the exiting principal without suffering financial hardship.

If one of the principals in a business dies, significant commercial difficulties can arise.

It deals with the value and valuation of the equity in the business from the beginning, avoiding the awkwardness and unpleasantness that often accompanies buying out an exiting principal or their estate where no preagreed arrangements are in place.

ADVANTAGES OF A BUY SELL AGREEMENT

Example:



The buy sell agreement that is implemented gives each of the principals the option of forcing a sale of shares to the other principals, should a principal suffer a triggering event. Buy sell agreements are normally designed to ensure that equity in a business remains closely held. With any contractual arrangement, a buy sell agreement can override the provisions of an individual principal's will. Buy sell agreements reduce the likelihood of members being 'in partnership' with unwanted 'partners'.

KEY ISSUES TO BE CONSIDERED IN PREPARING A BUY SELL AGREEMENT

- The triggering events can include:
  - death
  - TPD
  - trauma
  - bankruptcy of a partner
  - divorce of a partner
  - retirement at a compulsory retirement age, or earlier
  - dismissal from the partnership
- Valuation of the outgoing partner's interest
- Payment terms
- Insurance funding arrangements (generally only available for triggering events such as death, TPD and trauma)

SUMMARY

The potential consequences of the unexpected exit of a principal are generally unfavourable, reinforcing the reasons why buy sell agreements are so important for the sustainability of a business.
Where two or more unrelated people are carrying on a business, a buy sell agreement helps to ensure a fair outcome when triggering event takes place and provides certainty for each principal's personal estate plan as price or valuation mechanism is established on a reasonable basis and set out in writing in a buy sell agreement.