KEY ELEMENTS OF A *"HIT BY A BUS"* EXIT STRATEGY

BUY/SELL AGREEMENT

A buy/sell agreement is a document that re-allocates business ownership, or the part ownership of a business, when someone can no longer be an owner or wants out of the business. The buy/sell agreement is basically a Will for your business and lays out exactly how the business will be divided up in the event of a dissolution, a partner wanting out, a divorce or in the case of our discussion the death or disability of a co-owner.

The agreement spells out exactly who will own what in the event that a partner leaves the company either planned or unplanned. In the event of death or disability, rather than leaving these decisions to be fought over with family members and partners or with the courts, a buy /sell agreement spells out a reasonable sale price for a member’s ownership interest, how it will be paid for and even how the business will be run and managed.

One of my MBA classmates has an envelope that says, “To be opened upon my death” that spells out exactly what his wife should do if he were to die unexpectedly. In the next few posts, I’ll discuss key elements of a buy/sell agreement.

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LIFE INSURANCE

One of the easiest and most efficient options to buy out a partner and settle with their estate in the event of a death is with a life insurance policy. With two partners they simply each get a Life Insurance Policy and name one another as the benefactor of each policy. The buy-sell agreement and death clause in the operating agreement stipulates a predetermined value for the business interest and that the insurance proceeds will purchase the business interest of the deceased owner's interest at the predetermined value. The win / win with this structure is that the family of the deceased owner will receive cash instead of non-marketable company stock and the surviving owner is immediately freed up to carry on the business without the deceased owner's family getting involved in the business or a fight over the valuation.

If there are multiple shareholders or partners, then the terms of the agreement would spell out the percentage of the insurance settlement each surviving partner would receive.

As always, consult experienced and trusted advisors to set up the terms, structure and required legal documents.

DECEASED PARTNER

The most emotional and complex part of developing a Hit By A Bus Strategy is replacing the deceased owner's contribution to the business. We were called in to advise a surviving partner after his partner a long-time college friend died unexpectedly. The good news was that they had a buy/sell agreement & an insurance policy that funded the buyout and transfer of the deceased partner's shares.

They were great partners who complimented each other's skills and together built a very successful construction company. The surviving partner was a CPA who handled the business, finance and accounting side of the company. The deceased partner was an engineer who handled the construction and technical side of the business.

They were both very involved in the day to day operations of the company and took pride in the fact that they worked long and hard. They trusted each other and watched each other's back. However, when the technical partner died, there was no one who could step up and fill his shoes. Quotes started getting behind, business was lost, quality suffered and the business began to deteriorate.
By the time we were called in it was too late and the only choice the company had was liquidation. What could have been done?

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"OPEN UPON MY DEATH" ENVELOP

In the situation that I last described the technical partner died unexpectedly and he was such an integral part of the business that it did not survive without him. As I get older, I see this situation occurring more often and typically there is no contingency plan in place.

One of my colleagues has an envelope that says, “To be Opened Upon my Death.” It contains a copy of his current will, letters to his family, detailed plans for his funeral, instructions for transferring all of his personal accounts and plans for the continued operation of his business. While this can be hard to discuss, a plan like this can save a lot of emotional grief, expense, and even the business.

One of the best ways to gauge the survivability of your business is to ask yourself how long could the business survive without me? Do you have a strong enough management team to step in and run the business without any hiccups or would the wheels start to fall off after a few weeks?

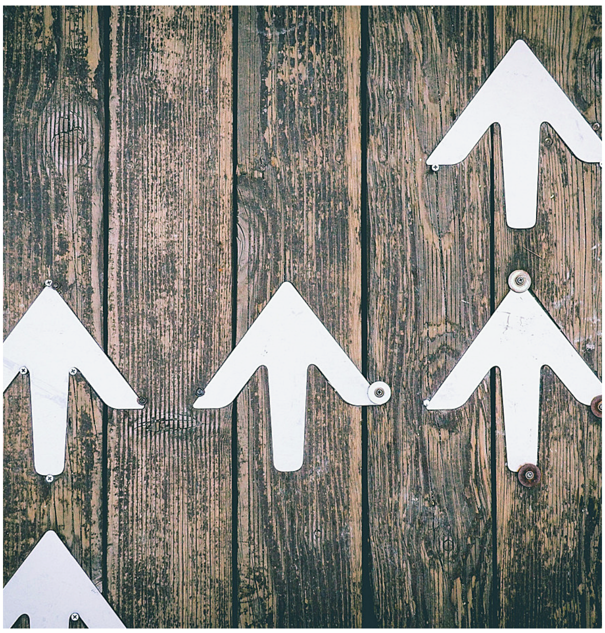
Selling the business can be an option as well. While there are no set answers for what should happen in every case, all business owners should have a plan and trusted advisors/management team in place to execute a “Hit by a Bus” strategy. Start working with your advisors on your “Open Upon my Death” envelope today!

PUT TOGETHER A PLANNED BUSINESS EXIT

Check out the next series in the Key Elements of an Exit Strategy. It will discuss the common types of planned business exits. Like most answers in the real world, the right plan and strategy depends on the specific goals and objectives of the individual Business Owner. Some have family members to pass the business on to, others will depend on the exit to fund retirement, some may have a management team who has been groomed to take over the business, others may have to liquidate the business due to changing market conditions.

Exit and business succession strategy and planning come in all shapes and sizes. The main key is to be in the small minority of business owners who actually have a plan! Price Waterhouse Cooper's estimates that nearly 88% of business owners do not have a succession plan in place. The series will explore common exit options and some of the nuances of each.

Check it out on our Resources Page under "Planned Business Exits"



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