



## Bart Basi

Dr. Bart A. Basi is an expert on closely-held enterprises. He is an attorney, a Certified Public Accountant, and President of The Center for Financial, Legal & Tax Planning, Inc. He is a member of the American Bar Association's Tax Committee on Closely-Held Businesses.

# THE BUY/SELL AGREEMENT: A NECESSITY IN MULTI-OWNER BUSINESSES

Fastener Distributors are often owned by multiple owners in the form of partnerships, S Corporations, and Limited Liability Companies or LLCs. Because of their multi-ownership nature, members and shareholders tend to grind when their interests are opposed to one another. These disagreements can occur for many reasons, but they typically include, death, divorce, and retirement. It is thus the reason why we have buy-sell agreements.

Buy/sell agreements typically arise in succession planning for executives, including those executives involved in closely held corporations, and those involved in non-corporate types of entities, such as partnerships and proprietorships. The agreements are intended solely for the purpose of the liquidation of the executive's business interest; that is, buy/sell agreements provide that when an executive retires or dies, there will be a party or parties available to purchase these business interests from the estate, at a price which has been previously arrived at.

Although the disposition of the executive's business interest is by no means the only consideration in succession planning, it is an extremely important one, one which is often overlooked or oversimplified.

### Purpose of Buy/Sell Agreements

**[1] PLANNING** A buy/sell agreement before death can help resolve the most serious problems the estate of a closely-held corporation owner usually faces: the lack of liquidity to pay estate taxes, the valuation of the stock for estate tax purposes, a market for the company, and the transfer of control to specific individuals.

**[2] VALUATION** An important factor to consider in drafting buy/sell agreements is the provision for valuation of the business interest for estate tax purposes. The estate tax basis is normally the fair market value at the date of death. However, Revenue Ruling 59-60 states:

"Where the option or buy/sell agreement is the result of voluntary action by the stockholder, such agreement may or may not, depending upon the circumstances of each case, fix the value for estate tax purposes."

In the absence of such an agreement, the IRS may step in and fix the value according to its own formula. The value the IRS applies may have no relation to the consideration, which the estate receives for the interest. It is thus much more beneficial to have the estate tax basis agree with the price actually received by the

estate by having a buy/sell agreement that establishes the value of the business.

**[3] FAVORABLE MARKET** As mentioned above, the proceeds of a sale of assets may have no relation to the value the IRS places on the business interest for tax purposes (if the sale does not reflect the fair market value of the interest). Thus, a favorable market must be provided for the stock interest, and one of the best ways to accomplish this is to utilize a buy/sell agreement.

**[4] CONTROL** The owner may want to direct control of his interest to certain desired individuals, i.e., other stockholders, surviving partners, family members or key employees. He may want to keep unwanted beneficiaries or outsiders from acquiring a controlling share of the interest. A buy/sell agreement is the best way to insure that the results are those which the owner actually intended.

