

The Importance Of A Buy-Sell Agreement

If you are the part or sole owner of your business and want your interest to remain in the family or be taken over by a key employee or other specified party, a written buy-sell agreement will help accomplish these objectives. A buy-sell agreement is an arrangement that directs the disposition of the business in the event of your:

- Death
- Disability
- Retirement
- Ownership transfer within your lifetime.

Benefits

- Provides a ready market for shares after an owner's death.
- Sets a price for the shares. The agreement may also effectively establish the share value for estate tax purposes.
- Avoids disagreements that could otherwise be caused by unexpected new shareholders.
- Provides cash for the purchase if life insurance is utilized.

Funding

For a buy-sell agreement to work, cash must be available to purchase your business interest from you or your estate. A buy-sell agreement without the cash may be just an empty promise. There are several ways to fund the agreement:

- Cash flow or retained earnings of the business.
- A bank may provide a loan for the purchase.
- Life insurance policy proceeds can provide the needed cash.

Of the three, life insurance is often the most financially efficient tool to provide the cash necessary to complete a buy-sell plan. Life insurance guarantees the money will be immediately available for the purchase. A buy-sell agreement can ensure that policy proceeds are received free of income tax. Also, life insurance funding involves no loan or installment interest.