

BUY-SELL AGREEMENTS FOR START-UP COMPANIES - a.k.a. "Founder's Agreement" by James Burk, Esq.

What is the Buy-Sell Agreement?

Buy-Sell agreements are agreements by which interest holders of an organization agree to place restrictions on the transfer of their interests in the Company. The agreement, also called a "Founder's Agreement," creates a guideline for the event where an interest holder ("Member") who controls a significant (though it need not be significant) interest in the Company, wishes to sell his/her interests in the Company. In the cases of small companies such as closely held corporations, founders who do not wish to let a member distribute his/her interests to parties outside the Company use the Founder's Agreement.

For the purpose of this summary, interests in a company (Corporation, Limited Liability Company, Partnership, etc.) will be called "Shares."

What Types of Agreements are there?

1. **Redemption Agreement:** The member agrees to first offer all shares to the Company before selling the shares to a third party. If the Company does not purchase the shares at the price and terms fixed by the agreement, the member becomes free to sell the shares to an outsider.
2. **Cross-Purchase Agreements:** The member must offer all shares to the other Company owners in certain specified situations
3. **Hybrid Agreements:** The member must first offer the shares to the other owners. If the owners do not purchase all of the shares, then the Company has the right to buyback the shares. The member may then sell the shares to a third party. The order and extent of the right of first refusal can vary among agreements.

What may be in the Buy-Sell Agreement? (Some examples of what may be included)

1. Right of first refusal
2. Amount of shares and the price of the interest to be purchased: fixed or market based?
3. Whether the Corporation will purchase life insurance to cover the buy back upon the passing of the member
4. What triggers the buy-back: termination with or without cause, sale, early
5. Force the member to sell or grant right of the exiting member to force the owners to buy his/her interest or force the Company to buy
6. Restriction against competition
7. Tag along clause: requiring the owner who buys the shares of the majority interest holder to also buy the shares of the minority interest holder

In spite of our intentions, we never know what the future may bring and cannot say with certainty what our partners or we will be doing in five years. The Buy-Sell Agreement outlines the method by which the Company will maintain control throughout changes in ownership.

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