

## member services

By Caprice L. Collins, Esq.



# Buy – Sell Agreements Explained Rental Property: The Next Generation

**A** humorous take on how families pass on businesses or rental property is reflected in this quip: “Avenge your children; give them equal shares in your business.” What seems like a generous, wonderful thing can be rife with conflict and imbalance if you don’t take steps to implement the appropriate legal framework.

Rental property owners face unique challenges surrounding how to preserve the family real estate and business. This article focuses on the transfer of rental properties after death, and steps you can take to ensure a smooth transition.

### Planning Is Key

Whether your family is running a business or owns rental properties – either through death, retirement, divorce, or just the desire to sell one’s share – it can cause turmoil in the family. But harmony can be maintained, and issues can be anticipated and planned for if everyone agrees in advance how situations will be handled. The key word here is “advance.” Preparing ahead of time means the difference between getting it right and unfortunate hindsight.

Let’s look at buy-sell agreements to prevent problems. Buy-sell agreements, are basically contracts that specify rights among the owners of a family business or rental properties.

Sometimes, a buy-sell agreement is incorporated into a living trust. Other times, it is

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a separate document. Either way, the estate planning attorney needs to coordinate the distribution of the assets between the children receiving their share of the property and those possibly not receiving their share of the property.

Other planning devices, such as Family Limited Partnerships, can be used to distribute shares in real property to family members, but that’s another discussion.

**What Is A Buy-Sell Agreement?**

One might lightly define a buy-sell agreement as a document that staves off family mud wrestling. Legally speaking, it is a contract that serves four purposes.

1. Formalizes who controls ownership of the business or rental properties.

2. Focuses on shareholders’ rights to transfer stock in the business to other people.

3. Determines what circumstances activate those rights.

4. Details how such transfers might be accomplished.

### Who Has Controlling Ownership?

Most buy-sell agreements restrict who may own the business. In family businesses, it is often understood that only lineal family members (or possibly spouses) can be shareholders.

With a buy-sell agreement, you can formalize a contract that will ensure that others – uninterested in the ownership lifestyle – still get their fair share when parents pass away.

### What Are Buy-Sell Triggers?

Some key elements of a buy-sell agreement need to be addressed. A course of action must be determined in the event of certain “triggers.”

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Triggers are occurrences, such as death, disability, retirement, reaching a certain age, or even a divorce, that obligate shareholders (or their estates) to sell shares in a family business. Identified buyers are then required to purchase upon that event.

For instance, let's imagine a family has four children and the parents pass away. They are survived by three children who wish to sell their interest in the business or rental property, and one sibling who wishes to carry on the management of the business or rental property.

The "trigger" is the parents' deaths. What takes place next must be outlined in painstaking detail in your new buy-sell agreement.

## **Succession Plan Elements**

Succession planning, a broader term for the creation of a buy-sell agreement, is only one part of estate planning. Although your Will and Trust may be in great shape, the succession plan for passing on the business or rental property may be a disaster waiting to happen. That's why it's important to use a buy-sell agreement.

How do you know when you've covered all the bases? A good succession plan addresses five basic issues.

1. Retaining or selling the properties.
2. Generational Differences.

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3. Ownership Models.

4. Leadership and Management.

5. Personal/Family Issues.

Remember, buy-sell agreements provide solutions to potential conflicts before they arise, saving tremendous time, pain and expense. Moreover, well-constructed buy-sell agreements can protect both individual shareholders and properties by providing a way to achieve liquidity while keeping demands for funds manageable.

## **The Importance of Shared Goals**

Many families carefully distinguish the roles and responsibilities of members in the business to minimize the chance of familial conflict. The Gallo brothers, Ernest and the late Julio, provide an interesting example. As chairman, Ernest controlled marketing, sales and distribution for the giant winery. Julio was president and oversaw production. Their offices were on separate floors and they did not have daily contact. They managed to mesh effectively through shared goals. Julio's goal was to make more wine than Ernest could sell, while Ernest sought to sell more than Julio could make.

In real property ownership, one person could be better suited to marketing and managing the finances while another may be more talented

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in supervising repair and maintenance.

These examples are important. Consider them carefully when determining who will run what part of the family estate.

## **Establishing a Buy-Sell Agreement**

Creating a buy-sell agreement or Family Limited Partnership can help you achieve tax advantages and control with respect to your family business or rental properties. Equally important is the peace of mind you'll gain when you know your children will be well provided for and your legacy will be passed on in a highly-structured and cost-efficient way.

Every family's goals and situations are unique. You need estate planning strategies specifically created for business or rental property. Don't wait for conflicts to make reaching a buy-sell agreement impossible. Develop an agreement to support your family's business goals.

*This information has been prepared for educational purposes only. This material is not intended as tax or legal advice. For more information, Attorney Collins may be reached at 310-677-9787 or at [clcfirm@aol.com](mailto:clcfirm@aol.com). Collins Law Group is located at 3330 West Manchester Blvd., Inglewood, CA 90305. Our experienced team will show you how to best employ these strategies for your family's greatest benefit.*

