

GIVE YOUR BUY-SELL AGREEMENT A PERIODIC CHECK-UP

Introduction:

A buy-sell agreement can be one of the most important documents for any nonpublic company with two or more owners. A common problem with buy-sell agreements is that once written, they never get a check-up.

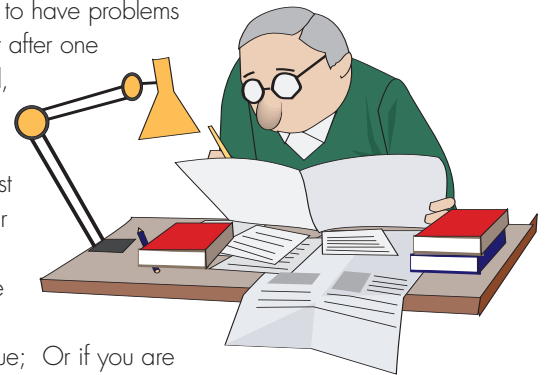
After a few years virtually any closely-held business will be in a different position than what the owners envisioned when starting the business. The customer base may have changed, economic conditions may be different, lines of business may have been added or dropped and indeed the original business aims may have changed completely. Yet the same old buy-sell is stuck in a never-opened file, just waiting until one owner chooses to or is forced to terminate employment, dies or becomes disabled, or becomes involved in a divorce or other legal proceeding. And when it finally gets pulled out of that file, the buy-sell terms may bear no realistic relation to the current financial realities of the company.

Valuation, Valuation, Valuation:

A key aspect of a buy-sell agreement is the method for determining the value of the company or of an owner's interest in the company. The method may be simply an agreed value by the owners, a determination by the company's accountant, or a determination by business appraisals.

If your buy-sell agreement contemplates an annual agreement on value, do the owners really meet annually and agree on the value?

If not, you are likely to have problems reaching agreement after one owner has terminated, quit or been fired from the company; Or when in the midst of a divorce or other legal proceeding in which someone else is pushing for the highest possible value; Or if you are dealing not with a partner of many years, but with a spouse or legal representative; If your buy-sell agreement requires an annually agreed value, but the owners have not been doing that, then you need to start doing it now, possibly with the benefit of professional advice on how to best value your company.



If your agreement requires one or more business appraisers, do you realize the "going price" for a business appraisal these days? Does your agreement specify an independent, local appraiser with recognized qualifications (such as an Institute of Business Appraisers ("IBA") Certified Business Appraiser or Master Certified Business Appraiser)? Otherwise you might be stuck with an appraisal by one of the owner's in-laws or second cousin from the East or West coast. And if your buy-sell agreement contemplates appraisals, what instructions are given to the appraiser? Is the appraiser to determine "fair market value" of the entire company and the departing owner gets her or his percentage? Or is the appraiser to determine the value of the departing owner's interest only, which may be reduced from its proportionate share of total company value if certain discounts are applied? Specific words in a buy-sell in this regard can make a world of difference. The "fair value" of an owner's interest may be more than its "fair market value," whereas "fair market value" of the company as a whole may be the basis of determining "fair value" of individual interests without regard to discounts.

If your buy-sell agreement has a formula value, does the formula still make sense? The formula value may have made sense when the buy-sell agreement was written, given then-current circumstances. But those and other factors may have changed dramatically since your agreement was written.

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Funding and Payment:

There is also the question of how a buy-out will be funded. If funded by life insurance, verify that the insurance has not lapsed and is still adequate in amount. If the buy-sell agreement requires payment in full upon a co-owner's death, and if life insurance proceeds are not sufficient to provide funding, will the company or the surviving co-owners be able to raise the funds to make the payment?

Conversely, if the buy-sell agreement requires payments over a period of time, is the rate of interest up-to-date? Does the payment period continue to make sense given the company's current financial condition and ability to pay? Has the company entered into new credit arrangements that might restrict payment under the old buy-sell agreement?

Other Considerations:

There can be numerous other considerations that arise under a buy-sell agreement. For example, if your company is an S corporation, does the buy-sell agreement cover distributions to pay taxes as well as buy-out commitments? Does it take into account the possibility of ending the company's tax year upon complete buy-out of a shareholder, to avoid having a former shareholder being taxed on income (or potentially having the tax benefit of losses) after he or she ceases to be a shareholder?

Most buy-sell agreements provide for a determination of the purchase price, after which there is a "closing" when the departing shareholder ceases to be a shareholder. A recent case has reinforced that the shareholder continues to be a shareholder until that "closing," even if the closing is delayed for years because of an unresolved dispute as to the proper valuation under the buy-sell

agreement. The shareholder continues to have her or his shareholder rights – including rights to the corporation's financial statements and other records, rights to attend meetings of shareholders and perhaps even call meetings of shareholders, and other rights (potentially even while she or he is working for a competitor) – until that closing occurs. The recent case has given some guidance on how this scenario might be avoided, by carefully tailored buy-sell agreement provisions, even if there is some dispute as to the valuation or other reason while closing is delayed.

In Closing:

If you are an owner of a closely-held business, review your buy-sell agreement every few years. Make sure it continues to make sense for you, your company and your co-owners. If it contemplates an annually agreed value, and that has not happened, engage your co-owners in a discussion to see if you can agree on value. If you have different ideas on how the company should be valued, and cannot reach agreement, that in

and of itself is probably a good indicator that you may want to discuss the process by which value will be determined and make sure that process is spelled out as clearly and as specifically as possible. And if you are a co-owner of a closely-held business with no buy-sell agreement, we would encourage you to get as much information on buy-sell agreements as you possibly can, and raise the topic with your co-owners before your company is faced with a departure, death, disability, or other circumstance in which an owner wants or needs to be bought out.

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RECENT SIGNIFICANT BUSINESS TRANSACTIONS

The Felhaber attorneys in the firm's Business Section were engaged in a multitude of client business transactions over the past few months, including the following:

■ **Rick Salmen, Pat Brinkman and Trina Sjoberg** represented a number of different lending institutions in a variety of commercial loan transactions.

■ Representation of a number of clients in various mergers and acquisitions ranging from the sale of assets of a retail facility, to a complex transaction involving acquisition of numerous car wash operations nationwide handled by **Russ Sudeith**.

■ **Rich Savelkoul** handled a number of business purchase and sale transactions including the purchase of a corrugated boxing company from Georgia Pacific Corp. for over \$1 Million; and the sale of interest in an Anheuser-Busch/Coors distributor for over \$2 Million; **Jennifer Forbes** and **Rich Savelkoul** represented an internet/software company with regard to a sale for approximately \$1 million with earnouts.

■ **Rick Salmen** has represented, and currently represents a number of individuals/business entities, in connection with troubled loan workouts and business bankruptcy issues from both the debtor and creditor perspective.

COPYRIGHT INFRINGEMENT: E-MAIL CIRCULATION OF ARTICLES

Have you seen an interesting article in a trade publication recently and perhaps thought of sending a copy to your co-workers? **Don't do it!** You can certainly email them a summary, or send them a link and suggest that they read the article, but **Do Not Copy** it and attach it to your e-mail.

Liability for copyright infringement can be substantial. The copyright owner may recover either actual damages, the infringer's profits, or statutory damages. Statutory damages can be up to \$30,000 per act and may be increased to \$150,000 per act if "willful."

Various industry groups actively search for "pirates". The Software & Information Industry Association (SIIA) is the principal trade association for the software and content industry. It recently announced the first settlement in its **Corporate Content Anti-Piracy Program**. See http://www.sii.net/press/releases/Antipiracy_KN-settlementrelease.pdf.

Their news release dated August 16, 2007 states in part: "SIIA reached a **\$300,000 agreement to settle copyright infringement claims** against Knowledge Networks, Inc. ... a mid-sized market research company with offices in San Francisco, New York and several other cities. The firm's marketing group had been distributing "press packets" internally to certain employees ... [that] sometimes included ... copyrighted articles owned by SIIA members such as the Associated Press, Reed Elsevier, and United Press International. ... SIIA learned of the infringement though a confidential tip and ... the individual who reported the case to SIIA is receiving a reward of \$6,000 ..."

In one recent court case, *Lowry's Reports, Inc. v. Legg Mason, Inc.*, the court held that Legg Mason was liable for copyright infringement damages in the amount of \$20 Million. Legg Mason had one subscription to plaintiff Lowry's market-trend-analysis newsletter but Legg Mason distributed the newsletter company-wide by e-mail.

In *American Geophysical Union v. Texaco, Inc.*, defendant Texaco was found liable for copyright infringement for photocopying and circulating copies of trade journals and publications in-house to all employees despite the fact that they had paid for only one licensed copy.

Avoid copyright infringement. Do not attach copies of articles to your e-mail or fax copies. Instead send a citation or link with a summary. Adopt a corporate policy to that effect.



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■ **Tom Doyle** and **Tim Hassett** represented Osceola Medical Center regarding acquisition of land, securing construction financing and construction of a new hospital in Osceola, Wisconsin.

■ Representation of various borrowers in connection with several multi-million dollar bank and institutional lender loans. In particular, **Dave Cremons** and **Randy Sparling** assisted a Canadian client and its U.S. subsidiaries with a loan refinancing in excess of \$100 Million.

If you need legal advice regarding a business transaction, please contact **Rick Salmen**, Business Section Chair, who would be delighted to refer you to the appropriate attorney. You may also log onto www.felhaber.com to view our attorney biographies.



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Four Felhaber Attorneys Named Chambers USA Leaders in their Field

Felhaber, Larson, Fenlon & Vogt, P.A. is pleased to announce that four of its attorneys were recently appointed as *Chamber USA Guide* Leaders in their Field.



James Dawson
Labor & Employment



David Eide
Real Estate



Jan Halverson
Labor & Employment



Paul Zech
Labor & Employment

The publication is compiled as a result of thousands of client interviews across the United States, balanced by opinions from colleagues and competitors. The qualities on which rankings are assessed include technical legal ability, professional conduct, client service, commercial awareness/astuteness, diligence, commitment and other qualities most valued by the client.

To learn more about the attorneys' credentials, please visit our website at www.felhaber.com to review their biographies.

Business Report

The Business Report is an update on legal developments. It is not intended to be legal advice and should not be relied upon without consulting counsel.

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