

Dealer Transfer Series: After the Transfer-Planning for Future Transfers or Break-Ups

Your dealership just completed a merger. You did everything by the book: took your time getting to know the other organization, set up a new organization, agreed to a fair value and established how the new ownership group would work together going forward. You will now be able to operate cohesively for years to come ... Ok, wake up from your "fantasy". This situation will not happen. As you know, it is nearly impossible to predict the future and events will pop up that impact your organization, whether it is the event itself or the timing of the event. In my last article, I discussed default rules for working together as owners. In this article, I want to address default rules to handle situations when the ownership group changes (or should change). Like rules for working together, rules for ownership changes should be covered by your Buy-Sell Agreement. These rules can involve much detail (especially as more owners or owner groups are involved), but there a few main topics that should always be addressed. **Is**

Permission Needed to Transfer Stock? The most basic principle of a Buy-Sell Agreement is to prohibit transfers of stock without approval of the other owners. Without this rule, your co-owner could transfer his stock to an unknown person (or next generation family member with little experience) and all the effort put into investigating and developing the owner group goes out the window. But, as with most general rules, there are exceptions, including the following:

- Permit transfers, but only if the other owners have a right of first refusal to match the terms.
- Permit transfers between family members as long as the key persons from the family remain active in the dealership (and often retain voting control).

Options to Purchase. Owners can limit risks from changed circumstances by getting an option to buy stock of another owner if certain events occur with respect to the other owner. The most common events are death, disability, divorce and bankruptcy. However, you should consider other key events and determine if those events should trigger options to purchase stock. Two important events that can be overlooked are listed below:

- Retirement. We have seen dealership organizations experience the early retirement of one or more owners and then realize that the retired owner would be able to keep his stock and continue to benefit from future growth in the organization. To limit surprises in this situation, owners should discuss retirement expectations in advance and then build in appropriate purchase options.
- Termination for Cause. Although I hope you won't experience this, you need to be prepared to address owners that turn out to be less than perfect employees. We advise dealers that they should have an option to purchase any stock owned by an employee-owner fired for cause (e.g., violation of a non-compete, embezzlement, consistently ignoring important company policies, etc.).

Price. An option to purchase requires establishing the price for the stock. The most common approaches to price are the following:

- Formula. Price is based on book value of the company or book value plus a formula for approximating "goodwill" or "blue sky" of the dealership.
- Agreed Price. The price is the amount that the owners (or a percentage of owners) establish. We typically see this approach used along with a mechanism requiring a third party appraisal or a formula approach if an "agreed price" has not been set in the last 12 months.

- **Appraiser.** Ownership groups may decide to defer setting price until an option event actually occurs. In that situation, an appraiser will be appointed by the company to determine the price for the stock.

When determining price, also consider if it should be adjusted further in certain circumstances. For example, the price for stock owned by a minority shareholder is often discounted because it does not give the owner control. Other dealerships discount stock values in situations where an owner retires early or is terminated for cause. You can be confident that your ownership group will experience change in the future. Anticipating changes in advance and establishing processes for addressing change will put your dealership in a much better position for continued success and growth even in situations where the timing of change is unexpected.