

Case study: The Importance of a Buy/Sell Agreement

John R. was a very successful advisor who had built a thriving practice in northern New Jersey. John was the sole earner for a family of 5, with a stay-at-home wife looking after their 3 children.

John was an excellent advisor and business owner; however he left one critical aspect of his business uncovered. He never put a buy/sell agreement in place to protect him and his family in case of death or disability. Typically these agreements are established and funded by life insurance, so that if there is a triggering event, funds are immediately available to buy the firm to benefit the heirs and not put strains on the cash flow of the business to ensure a smooth transition.

In John's case, the unexpected happened. He became ill and eventually passed away. While he did have instructions to transfer his accounts to his licensed sales assistant, the lack of a buy/sell agreement prevented his spouse from receiving any money from the account transfer. Per NASD rules, the sales assistant was the only person who could pay the widow anything for the business.

In the case of the sales assistant, she didn't have the financial means, nor the entrepreneurial or management skills to effectively manage the firm, so the spouse and the sales assistant actively canvassed in search of a buyer who could purchase the business from the sales assistant and then compensate the spouse.

Through this process clients had begun to wonder about their long-term relationship with the firm and then eventually wander. Once a buyer was found, the business had suffered a nearly 80% attrition of clients, leaving the widow with only a tiny fraction of what the business was worth at the time of death.

While John's case is a very sad story, it could have been less tragic had there been advance planning and a buy/sell agreement in place. Even for sole-practioners, there are solutions that can work, such as working with another advisor in the local area to partner on such an agreement.