
ASK A LAWYER

Elements of a basic business agreement

Q. I am going into business with two colleagues. What basic business agreement should we have?

The owners should enter into a stockholders agreement (if the entity is a corporation) or an operating agreement (if the entity is a limited liability company).

This accord will establish the "rules of the road" for management and succession issues of the business.

Generally, the pact will establish the percentage interests of each party, the designation of officers or managers of the business, and the amount of capital contributions that will be required.

The agreement provides the rules governing the transfers of interests that may occur during life,

upon disability and upon death. The agreement can provide that an owner is free to transfer his interest to a bona-fide purchaser; however, the other shareholders or members would be given a right of first refusal to acquire that interest to eliminate a transfer to a third party.

The agreement could also provide for a continuation of compensation for a specified period if a shareholder or member becomes physically or mentally disabled. The amount of compensation paid by the company can be reduced by available disability insurance proceeds.

After a fixed period, often one or two years, the interest of the disabled party is required to be sold to

the remaining shareholders or members at a price determined under the agreement.

The accord should provide that in the event of the death of a shareholder or a member, the deceased party's interest must be purchased by the company or the remaining shareholders or members. This buyout is often funded with life insurance.

In the absence of such an agreement, a shareholder or member's interest is freely transferable.

A shareholder could transfer his or her interest to a party not known by the other members. Also, in the event of a death, in the absence of such an agreement, the shares or member interests will pass to the member's heirs and the

remaining members will find that they have a new partner in the family of the deceased member.

This can be avoided by a properly drafted shareholder or operating agreement. — *Henry M. Matr* is chairman of the Corporate, Finance & Business Transactions Department at Cole, Schotz, Meisel, Forman & Leonard, P.A., the largest law firm in Bergen County. *This is not intended to be legal advice, which can only be given after the attorney understands the facts of a particular matter and the goals of a client.*

Do you have a business question for a lawyer? Send it to BusinessNews@northjersey.com.
