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FAMILY BUSINESS SHAREHOLDER (BENEFICIARY) EXIT STRATEGY

Do you have protocols in place should a family member, who is a shareholder or beneficiary (if the shareholding is vested in a trust); wish to exit the family business?

The BEST PRACTICE is to have a SHAREHOLDER AGREEMENT with clear protocols to deal with the rules that will apply if a family member-shareholder wishes to exit the family business. If the shareholding is vested in a Trust, a BENEFICIARY AGREEMENT should dictate similar protocols.

Consider:

1. The SHAREHOLDER AGREEMENT should prohibit the family member-shareholder to sell his/her shares to an outsider without the consent of the other family member-shareholders. The BEST PRACTISE is that THE REMAINING FAMILY-SHAREHOLDERS should have the FIRST OPTION to buy the shareholding.
2. To PAY FOR THE SHAREHOLDING might place FINANCIAL STRESS on the family business. Clear protocols should be in place to safeguard the family business against financial hardship.

   Typical practices are:

   - To do a fair valuation of the value of the business by a NEUTRAL VALUER to determine the value of the shareholding.

   - The essence of a family business is "to keep the business in the family over generations." If you break this rule, there should be penalties.

     Typically, it means that the exiting family member-shareholder will receive a reduced value of his/her shareholding of 75% and sometimes even lower. Determine this upfront in the shareholder agreement and reach consensus.

And added penalty will be for the exiting family member-shareholder to carry the administrative costs to remove the shareholder in official documentation, e.g. updating the trust deed, AND to pay any taxes, such as Capital Gains Tax.

Insights from ANDRE BRESLER, MANAGING PARTNER, BENCHMARK INTERNATIONAL. **Bresler@benchmarkintl.com | https://www.benchmarkintl.com/za/**

"Family businesses are often times amongst the most well operated and efficient businesses, however without the execution of a good succession plan or exit strategy, some client's struggle to find an outcome that is aligned with all family members and their individual agendas.

Shareholder dynamics are an ever-changing phenomenon in any business, but nowhere more pronounced than in family businesses where the decision to either exit or transition the business to the next generation is most often fraught with complexity and emotion."

~ Exiting a family business as a shareholder might be for acceptable reasons, such as funding your retirement. If this approach is catered for in the shareholders agreement, the family should plan, and not penalise the outgoing shareholder. ~

Continues Bresler, "Benchmark International has many years of experience and innumerable successful transactions concluded with family businesses in many forms. Whilst an outright sale is often the only consideration owners contemplate some recent transactions demonstrate the value of realising a retiring shareholder's value through a partial sale, whilst simultaneously injecting fresh growth capital into the business to support the growth, expansion and diversification aspirations of the next generation shareholders that remain."

Concluding remark

The ultimate test will be FAIRNESS. The transaction must be fair to the family business and the family member-shareholder, who wishes to exit. IF NOT, it will haunt the family because *something that is not fair will never be final.*