

The Titan Times Newsletter

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Masterful Quotes

"Stop chasing the money and start chasing the passion."

-Tony Hsieh

"You can have anything you want if you are willing to give up the belief that you can't have it."

-Robert Anthony

"To change one's life; start immediately. Do it flamboyantly. No exceptions."

-William Hames



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Buy-Sell Agreements:

Entity vs. Cross Purchase Agreements

A Buy-Sell Agreement assures a smooth transition of ownership and business continuity in the event of a departure of a partner or equity owner. It is a legally binding contract that establishes how the departing owners' shares may be reassigned (obtained by the remaining partners) should that owner die or otherwise leave the business involuntarily, such as by death, disability, insanity, or bankruptcy. It typically also provides a mechanism for an orderly business succession should an owner decide to transfer his interest due to a voluntarily event, such as retirement. Any such event is referred to in the context of a Buy-Sell Agreement as a triggering event. They are also commonly drafted to restrict owners from selling their interests to outside investors without approval from the remaining owners.

Without such an agreement, there can be legal battles and contestation. For example, if a partner dies without an agreement, their shares may be passed automatically to their spouse, who may decide to keep them. Or, the spouse may want to sell them, but the remaining partners do not have the funds available to buy the shares, resulting in the spouse turning to an outsider.

In addition to controlling ownership of the business, Buy-Sell Agreements spell out the means to be used in assessing the value of a partner's share. This can have uses outside the question of buying and selling shares. For example, if there is a dispute among owners about the value of the company or of a partner's interest, the valuation methods included in the buy and sell agreement would be used. (continued)



2023 Federal Legal Holidays

January 2
New Year's Day
(observed)

January 16
Birthday of Martin Luther
King, Jr.

February 20
Washington's Birthday

April 17
District of Columbia
Emancipation Day
(observed)

May 29
Memorial Day

June 19
Juneteenth National
Independence Day

July 4
Independence Day

September 4
Labor Day

October 9
Columbus Day

November 10
Veterans Day (observed)

November 23
Thanksgiving Day

December 25
Christmas Day

The two most common types of Buy-Sell Agreements are Entity-Purchase and Cross-Purchase Agreements. Under an Entity-Purchase Agreement, the business purchases an owner's entire interest at an agreed-upon price if-and-when a triggering event occurs. If the business is a corporation, the plan is referred to as a Stock Redemption Agreement. In the context of a partnership, it is called a Liquidation of Interest.

Life or disability insurance is often used as a funding source within Agreements. The business owns and is the beneficiary of insurance on the lives of each stockholder, and upon death or disability, it uses the proceeds to purchase back that individual's share of ownership. If whole life insurance with cash value is used as part of the Agreement, the cash value is recorded as an asset of the business on the balance sheet. It is important to note that, depending on the structure of the corporation, there are different tax implications to consider when using an entity-purchase plan.

The use of a Cross-Purchase arrangement requires each stockholder to purchase and own life insurance on the lives of the other stockholders. Each owner would pay the premiums and be the beneficiary of the policy. The face amount of the insurance would be calculated based on the other's ownership interest. Upon the death of one owner, the insurance proceeds would be used to purchase the ownership interests from the deceased owner's estate or family.

Sometimes, a "Trusted" Cross-Purchase arrangement is preferred in which a trust would own one policy on each Partner/Owner and represent the others in the transaction, eventually distributing the deceased individual's ownership to the remaining partners/owners. Disability buy-sell insurance can also be used in a Cross-Purchase Agreement to facilitate transfer of ownership upon the total disability of one of the individuals.

Business continuity is important, especially when there are multiple partners or important equity holders involved in the running of a business. A Buy-Sell Agreement is a legal remedy for establishing a clear plan of how to distribute the shares of a departed or deceased partner to the remaining ones. In the case of a death, life insurance policies are used to fund the buyout of shares from the deceased's estate.

Did You Know?

- A 5% increase in customer retention can raise profitability between 25% to 85%.
- Firms perceived to have better customer service can charge more for their products and services while maintaining higher market share and returns on sales than the competition.
- Only 2% to 4% of customers who are dissatisfied ever complain to a business about poor service.
- 68% of the customers who leave and do business with a competitor do so because of poor customer service and/or supplier indifference.



Strategic Drivers of Business

Strategic drivers of business are forces, both internal and external, that shape an organization's business strategy. Strategies that fail to adapt to forces such as technological change, competition and regulations are recipes for disaster. By no means comprehensive, below we discuss eight such drivers, to set you on the right path:

Organizational Effectiveness: Does the company have an organization chart, complete with job titles, descriptions, compensation and reporting relationships? Customer service and cost control begin and end with your employees. Evidence of management reporting and written evaluations of employee performance is a positive indicator of success.

Cost Identification and Control: Do you know the cost of your product or service? Identifying logical centers where costs accumulate and establishing a reporting system to capture, report and evaluate those costs is mandatory to controlling your cash flow and profits.

Establishing Selling Prices: Do you set your selling prices based on knowledge of your internal costs compared to the competition's prices? Gathering market information about your customers and competitors is vital to properly setting the selling price of your product. Market price information MUST then be compared to your internal cost of producing that same product. Establishing selling price is the most important function impacting cash flow and profitability.

Planning, Directing and Controlling Operations: Are you tuned into the pulse of your company at all times? Key activities and management reports should be part of the company's culture. Activities such as budgeting, rolling sales and profit forecasts, marketing and strategic planning should be regular processes. Key reports should include monthly financials compared to budget, daily quantity and value of the order backlog, customer, vendor, and employee issues if any. Most important is a daily cash position and 90-day cash forecast. Establishing quality and timely reporting is mandatory for continued success. influence and/or industry trends, are there any consumer trends (think changing fashions and hot new fads)?

Inherent Business Risk: Are you aware of key risk factors that affect your business each day? Identifying risk factors and instituting processes to minimize those risks are fundamental to management maintaining control of the business. Certain external factors cannot be controlled, but internal responses can be put in place to deal with both foreseen and unforeseen outside circumstances to minimize damage to your business.

(continued)

Nature of Competition: How strong are your competitors? Do you know if your industry is considered a monopoly or oligopoly, or is it ultra-competitive? Obtaining detailed information on your competition is a key driver to success for your company. Knowing the relative strengths and weaknesses of your competitors will significantly influence your ability to set selling prices to maximize profitability and cash flow.

Business Growth: Do you know what is behind the recent trend in your revenue? Understanding both the internal and external factors that drive your revenue, and ultimately your bottom-line growth, are key components in the strategic direction of any company. Is your industry generally in a growth or decline mode? Are you strategically positioned to achieve growth because of management influence and/or industry trends, are there any consumer trends (think changing fashions and hot new fads)?

Industry Growth: What are the key data points used to track the general health of your industry? Knowing how your overall industry is performing, the long-term prospects of your industry and how your company compares to the overall industry are key management tools that should drive the direction of your business.

The Intangible Appeal of the Company: Do you know how outsiders view your industry and what factors are weighed most heavily in making that judgment? Are you aware of key factors that differentiate you from your staunchest competitors? Identifying and enhancing unique qualities of your business and/or industry that may not show up on your financial statements can have a considerable effect on the value of your business. Is the business perceived to be desirable because of social, comfort, intellectual or economic reasons? Some businesses are just fun and/or stimulating because of unique characteristics of the business or its industry.

At Titan Business Development Group, LLC, we encourage our clients to keep (and update) written analysis of these (and many more) drivers on a continual basis. This exercise applies to both sole-proprietors and larger companies alike. Identifying these drivers will help you draft and update your business plan(s) – which should be prepared at least annually, to guide operations for the upcoming period/year and to adjust as necessary in response to changes in both internal and external activities and forces. Don't hesitate to reach out to us if you would like assistance.



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