

Why Your Business Needs a Buy-Sell Agreement: 6 Essential Reasons

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Learn how a buy-sell agreement safeguards your business against unforeseen events and ensures a smooth ownership transition.

By Brad Wright

Running a business is a complex endeavor that requires careful planning and foresight. One of the most critical yet often overlooked aspects of business planning is succession planning. One way to ensure leadership continuity or legacy is by establishing a buy-sell agreement. A buy-sell agreement is a legally binding contract that outlines how ownership interests will be transferred in the event of an owner's departure due to death, disability, retirement or other circumstances. Having such an agreement in place is essential for protecting the business, its owners and their families. Here are six key reasons why every business owner should ensure they have a buy-sell agreement.

1. Ensuring Business Continuity

A buy-sell agreement provides a clear framework for what happens when an owner exits the business. Without one, disputes among remaining owners or heirs may arise, potentially leading to business instability or even dissolution. By clearly defining the terms of ownership transfer, a buy-sell agreement ensures that operations can continue smoothly without disruptions and costly legal battles.

2. Providing Financial Security

A buy-sell agreement helps ensure that an owner's family or estate receives fair compensation for their share of the business. If an owner suddenly passed away or became incapacitated, their heirs may struggle to liquidate their ownership stake. The agreement facilitates a structured buyout, often funded by life insurance or other financial

instruments, to ensure that the family is not left without financial support.

3. Maintaining Control of the Business

Without a buy-sell agreement, an owner's shares could be passed on to an unintended party, such as a spouse, children or external investors, who may not have the necessary expertise or interest in the business. This could disrupt decision-making and affect the company's strategic direction. A buy-sell agreement allows existing owners to retain control by preventing unwanted third-party involvement.

4. Establishing a Fair Valuation Process

One of the biggest challenges in transferring ownership is determining a fair price for the departing owner's shares. A buy-sell agreement typically includes a valuation method, such as an appraisal process or a predetermined formula, to ensure fairness for all parties. This prevents undervaluation or overvaluation and streamlines the buyout process.

5. Facilitating Retirement and Succession Planning

For business owners planning to retire, a buy-sell agreement provides a structured exit strategy. It ensures that there is a clear process for selling shares to remaining owners or a designated successor, allowing for a smooth transition without negatively impacting the business's stability.

6. Protecting Unforeseen Events

Unexpected events such as bankruptcy, divorce or disability can have significant implications for business ownership. A buy-sell agreement includes provisions that protect the company and its stakeholders from potential financial and operational disruptions caused by these events.

Conclusion

A buy-sell agreement is an indispensable tool for business owners who want to ensure stability, continuity, and fairness in the event of an ownership transition. It safeguards financial interests, should minimize disputes, and provides a clear roadmap for handling changes in ownership. By proactively putting a buy-sell agreement in place, business owners can protect their investment and secure the future success of their enterprise.

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