



Who's on Deck? Broker Succession Planning

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It happens—an unexpected illness, car wreck, or license revocation or suspension of a business entity designated broker or an individual broker. When these occur, what happens to the brokerage business and sponsored agents will depend on swift action being taken.

Having a succession plan in place before the unexpected occurs is the best way to minimize disruptions in business operations. Different laws and issues come into play when creating a succession plan for business entities and individual brokers.

Interplay Between Laws

When the broker in charge of a brokerage becomes incapacitated, dies, or is otherwise ineligible to act as a broker, whether it is a designated broker or an individual broker, at least two of the following areas of law kick in.

- **Texas Real Estate Commission (TREC).** Under the Texas Real Estate License Act (TRELA), for a business entity to act as a broker (i.e., sponsor agents, collect commissions, take listings, etc.),

The Takeaway

A broker's business can be interrupted when the broker suddenly dies or becomes incapacitated. The best way to avoid this is to have a succession plan in place ahead of time. Different factors must be considered for business entity brokers and individual brokers, but both are far better off with a plan than without one.

its designated broker must be an active licensed broker in good standing [TRELA 1101.355]. TREC rules specify that if the designated broker of a business entity dies, is suspended, or has his license revoked or otherwise inactivated (including expiration of his license), the licenses of the entity broker and all sales agents sponsored by the entity broker immediately become inactive. Likewise, an individual broker's death immediately causes all of her sponsored sales agents to become inactive [TREC

Rule 535.121]. Although TREC works with brokerages in these situations to expedite the approval of a new designated broker or transfer sponsorship of an individual broker's sales agents to a new broker, technically, under the law, there is no grace period. Therefore, quick action is critical. If the brokerage does not have a succession plan in place, business will undoubtedly be interrupted.

- **Business entity structure and management.** The laws related to business entity formation and management are applicable only to business entity brokers. Those laws set out the structure for ownership and management of the entity. However, each business entity's management authority for appointing the designated broker will most likely be contained in the entity's management documents, like bylaws for corporations, operating agreements for LLCs, or partnership agreements for partnerships.

Understanding the ownership structure and who has authority to appoint a new designated broker is important when applying to TREC to change the designated broker. Having the wrong person sign the TREC change form or improper entity authorization documentation will cause delays, and, as previously noted, longer inactivation of sales agents and possible loss of listings and clients.

- **Estate and probate.** Taking a dead broker's estate through probate or getting authority to act on behalf of an incapacitated broker takes time in the best of circumstances. The spouse or other heirs of the broker will be dealing with their grief and any arrangements that must be made. Their first priority will not be upcoming closings or sales agents' license status. While an executor will be appointed and an heir will eventually inherit ownership of business assets, it is likely that neither of them will be a broker who could take over the business in compliance with TREC requirements.

Timing for implementation of estate and probate laws should influence an individual broker's succession plan, but it may also be relevant for a business entity. A business entity could be impacted if the deceased or incapacitated designated broker is also the sole owner of the entity or a person whose authority is needed to appoint a new designated broker. A plan that can be put into action right away, before the probate process is complete, helps maximize the amount of commissions realized by an individual broker as the business is wrapped up or maintains continuity of business for

an entity broker. It also benefits the sales agents and heirs left behind.

Brokerage Ownership and Appointment Authority

One of the key advantages of being a business entity broker is that the entity can exist perpetually, changing owners and designated brokers over time. In other words, the brokerage can continue to operate for generations.

A successful succession plan for a business entity must start with a good understanding of the entity ownership structure and appointment authority. In particular, a business entity owner must know who the governing body for the entity is and who has been granted the authority to appoint the designated broker under the entity's governing document. Keep in mind that the designated broker must be an officer of a corporation, a manager or member of an LLC, or a general partner of a partnership. Many governing documents refer to officers, managers, members, or partners, not specifically to a "designated broker." In some cases, the designated broker is also a director or owner of the entity. If the designated broker is the only owner, the only person authorized to appoint a new designated broker, or is part of a group that requires unanimous consent to appoint a new designated broker, the business can be at high risk of major business interruption or even dissolution. In these situations, governing documents will need to be amended before a succession plan can be viable.

The October 2019 issue of *Tierra Grande* includes an article entitled "Covering your Assets: Business Entities Limit Personal Liability." It compares the various entity types, as well as the documents required by TREC for each entity type. A summary chart of entity type, governing body, and governing documents is included here for convenience.

Business Finality of Individual Broker

Unlike a business entity broker, an individual broker's business ends when the broker dies or otherwise becomes incapacitated or inactive. Not only do the sales agents become inactive immediately, those agents must find a new sponsoring broker. Any listing the individual broker had pending automatically terminates. While the estate of a deceased broker may collect commissions on transactions where the commission had been fully earned, many clients will have to find another broker to complete their transactions.

Comparing Business Entities

Entity	Ownership Structure	Formation Documents	Governing Body	Governing Document
Corporation	Shareholders	Certificate of Formation (Articles of Incorporation)	Board of directors/ corporate officers	Bylaws
LLC	Members	Certificate of Formation	Members or manager (choice must be stated in Certificate of Formation)	Operating Agreement
General partnership	General partners	General Partnership Agreement	General partners	General Partnership Agreement
Limited partnership/limited liability partnership	At least one general partner and limited partners	Limited Partnership Certificate of Formation	General partner	Limited Partnership Agreement

Source: Kerri Lewis

A “succession plan” for an expected departure of an individual broker, such as retirement, is really just a sale of the broker’s business assets and marketability of the broker’s established name. A plan for the unexpected termination of the brokerage can take two forms. Both involve making an arrangement with another broker. One plan is to have a conditional sales contract for the business assets and established name that is triggered by certain events. It could be based on a prenegotiated amount or formula. Another is more of a “I’ll scratch your back if you’ll scratch mine” type of arrangement. This is where two individual brokers agree to step in for the other in the case of an unexpected tragedy and help finish pending business, usually for little or no commission.

The goal of either plan is to let sales agents and clients have an immediate broker to go to for sponsorship or completion of a transaction and allow any commissions earned by the broker to date to be paid to the broker’s estate. Keep in mind that because there is no continuation of the individual broker’s license, sales agents would have to agree to be sponsored by the other broker. Likewise, clients would have to agree and sign a new listing agreement with the other broker.

Nothing in this article should be construed as legal advice for a particular situation. For specific advice, consult an attorney. 📌

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Succession-Planning Pointers

For Business Entities

- Check the entity's governing documents to see who has authority to appoint a new designated broker.
- If it is the same person as the designated broker, contact an attorney to amend the governing documents to add another person to the ownership and/or governance of the entity.
- If it requires unanimous consent of all of the directors, members, or partners, and the designated broker is one of those parties, contact an attorney to amend the governing documents to allow the remaining directors, members, or partners to appoint a new designated broker.
- Identify a successor designated broker either from within the brokerage or outside. Let that person know the plan, and get his agreement to step up when needed.
- Identify the documents needed to change the designated broker at TREC. These will include:
 - o a Change of Designated Broker form, signed by the appropriate governing person/people;
 - o an authorization document from the entity appointing the new designated broker, signed by the appropriate governing person/people; and
 - o either documentation that the new designated broker owns 10 percent or more of the entity or proof of errors and omissions insurance in the amount of at least \$1 million per occurrence.

- Create a written succession plan detailing the name of the designated broker who will be on deck and the documents that will be required to make that happen. Have the governing body sign off on it.
- Keep the plan in a place known to the governing body.

For Individual Brokers

- If the brokerage is intended to continue after the individual broker becomes incapacitated or dies, restructure as a business entity immediately.
- If the individual broker's business assets and name have value and the broker can identify a willing future buyer (business entity or individual), contact an attorney to negotiate and write up a conditional sales contract that is triggered by certain events (retirement can be one of them).
- Alternatively, find another individual broker who may be in the same situation and suggest a reciprocal agreement to step in and finish up pending transactions. The terms of this agreement should be clear and preferably in writing, especially if there is some compensation involved. Depending on how detailed this agreement is, the services of an attorney might be useful.
- Let sales agents and family members know what plan will be followed if something unexpected were to happen.

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