NORTHWOOD
Financial Services cc
Authorized Financial Services Provider No. 13296

BUY-AND-SELL (B&S) ARRANGEMENTS

Step 1: Understand what B&S arrangements are and why they are essential:

<u>The B&S arrangement:</u>

A B&S arrangement is an agreement wherein a departing member agrees to sell his interest in the business to the remaining member/s in case of his death, disability or on the occurrence of some other event (e.g. dread disease).

The remaining members (in their individual capacities) will own and pay the premiums on a policy that regards the life of the departing member. In case of the occurrence of one of the aforementioned events, the remaining members will be paid the proceeds. They will use the proceeds to buy the interest from the departing member or his executor.

The arrangement is reduced to writing in a B&S agreement.

<u>Reasons why B&S arrangements are essential:</u>

- In the occurrence of an event (e.g. the death of a member) an outsider (usually the member's spouse) will acquire his interest in the business in terms of his will and the spouse (who in all probability knows nothing about the business) will have a say in how the business is run and this could lead to:
    - Conflict between the new member and the remaining members
    - The business being unable to obtain credit since creditors will be unsure of the future prospects of the business
    - Investors refusing to invest in the business
    - Drop in staff morale
    - Drop in goodwill
    - Eventual liquidation of the business
- Cover provides the remaining members with the necessary funds, which they would not otherwise have, to purchase the interest.
- The departing member (or his estate, after the member's death) will receive a price for his interest that is fixed in the contract (i.e. it is not dependent on a willing buyer in the market).
- In the case of the death of a member, the cover that pays to the existing members, which they must then pay to the executor in return for the deceased's interest, will be exempt from estate duty if:
    - The other member/s held a like interest to the deceased at the date of death
    - The policy was taken out with the purpose of acquiring the deceased's interest
    - None of the premiums were paid by the deceased

Step 2: Prospect for Business Entities:

Every single business entity needs a buy-and-sell arrangement. This includes sole proprietorships, CC's, partnerships and companies.

In the case of a sole proprietorship (which always has only one owner) or in the case of a CC with one member, the agreement can be concluded between the owner/member and an outsider (successor). The successor can be the business's keyperson, a relative or even a competitor. To avoid estate duty on the death of the owner / member, the outsider should be given a share in the business (since he must hold a like interest to the deceased at the date of death).

Virtually every client is a prospect. He may either be a member in his own right or will be an employee in the business (i.e. he can refer you to the members). Prospecting should therefore begin with one's existing client database. Other methods of prospecting may include cold calling from the Yellow Pages, attending business expo's and joining business forums.

Step 3: Advice on the correct policies and underlying agreement:

<u>Products:</u>

Life Cover or Life Cover with OOD and Future Protector

The value of the interests of the members will increase over time as the value of the business increases. Life Plan and Cover Plan allows you to do this.

The members must decide which benefits to add: do they want to sell their shares on death, disability and/or dread disease?

N.B. Be careful with adding physical impairment and severe illness benefits to the agreement. A client may not necessarily want to sell his interests after having a heart attack. (Please revert to legal advisor)

<u>Agreement:</u>

A specimen agreement can be obtained from blueprint online. These agreements are just examples and have not been drafted to suit the particular situation of the clients. Clients must see an attorney to have their agreement drafted but may present this specimen to the attorney as an example.

Step 4: Calculate the premiums payable:

3 shareholders: Sally, Mike and Steve have a 40, 35 and 25% interest (respectively) in a company worth R 1 000 000. Policies will be affected on each of their lives with the others as premium payers:

Life Covered:	Sally	Life Cover:	R 400 000;	Premium: R 1 000
Premium Payer:	Mike	Premium:	35/60 x 1 000 =	R 583
Premium Payer:	Steve	Premium:	25/60 x 1 000 =	R 417

Follow the same logic in respect of the other 2 policies.

Step 5: Pass Underwriting:

Underwriting agents will request a statement of the proportionate interests held by the members in the business. They may also request a balance sheet to verify the value of the business and a copy of the agreement as evidence of insurable interest.