



LEVERAGE

Legal and technical update: June 2018

Note from the editor

Sharon Hamman (née Teubes), Senior Legal Adviser: Advice and Wealth Management

As I write this I realise that we are at the halfway mark for 2018 and the financial year end of the group. How time flies; it stops for nobody ... statements we start saying more often the older we get. Why is it that time starts going faster as we grow up – who remembers those long school holidays where the days felt like they would go on forever?

My theory is that we get busy and that inevitably we end up paying less attention to the time and other small things – the things that actually make our lives worthwhile. So let us stop for a moment and reflect on what we keep ourselves busy with and make a conscious decision to be busy with what gives us joy and what creates positivity around us – if each one of us do this what an amazing place the world will not be!

In this issue, we hope to give you some food for thought and hopefully some useful information to make sure that you spend your time with your client

well. Ulanda Weilbach takes us on a journey and shares some insights on a topic I know she is very passionate about. Once again, this will show us the value our legal advisers have and the spectrum of knowledge and experience that they can bring to the table.

Chris Weyers and Odette Kriel both put on their financial planning and marketing hats this month, to assist you in being effective when seeing a business client. Arthie Kander, our fiduciary specialist will summarise the information to show you the impact business planning has on personal planning, which will prove that an action in one area of the plan has a ripple effect into the others.

Happy reading!

momentum

Taking business assurance to new heights: One of our best kept secrets

By Chris Weyers, Legal Adviser: Advice and Financial Planning

If your clients do not have this benefit, the question should be why not?

As a legal adviser, I am often requested to assist in restructuring buy-and-sell arrangements, involving three or more shareholders in the event of a co-shareholder having passed away. This is when the real problem of insurability of the surviving shareholders arises. The cover was taken out years ago when they were healthier and younger. The question then arises whether the surviving shareholders will be able to take out additional cover in line with the restructured buy-and-sell arrangement.

A simple case study will illustrate the point.

Success (Pty) Ltd is valued at R12 000 000 and the shareholders are as follows.

Peter Rabbit	33%	R4 000 000
Snow White	17%	R2 000 000
Rumpel Stilken	50%	R6 000 000

Mr Stilken passes away suddenly and fortunately there was a properly structured buy-and-sell arrangement in place and the shareholding is as follows after the fulfilment of the agreement.

Peter Rabbit	66.67%	R8 000 000
Snow White	33.33%	R4 000 000

Once the buy and sell transaction is concluded, certain steps must be taken to ensure the arrangement is amended to reflect the new structure.

The role of the financial adviser

The financial adviser will have to review the buy-and-sell and restructure the arrangement to align the remaining cover with the new scenario.

However, there can be a MAJOR problem: Lack of insurability

Should the surviving shareholders no longer be insurable, additional cover will not be available to make provision for the increased shareholding.

Mr Rabbit did in fact have a triple heart bypass recently and as a result would be uninsurable according to all insurers.

What is the solution?

Momentum Myriad's Future Cover

What is it? I have never heard of it.

If a death claim was admitted on one of the policies under the buy-and-sell agreement (of which this policy forms part), then the policyholder has the option to increase the benefit amount on the remaining policies under the agreement by the insured life's share of the claim amount, without any proof of health or insurability.

Show me the fine print? This is too good to be true!

The requirements are as follows:

- The original buy-and-sell agreement (a new one will be drawn up free of charge by the Momentum).
- There must be three or more policies forming part of the arrangement prior to the claim.
- All the individual policies funding the buy-and-sell arrangement have to be Momentum Myriad policies.
- The option must be exercised on all the policies forming part of this buy-and-sell arrangement.
- The policyholder does not have to increase the benefit amount by the full amount available. However, the percentage of the available amount by which the benefit amount is increased must be the same for each of the remaining policies under the buy-and-sell arrangement (for example, 50% of the amount available).
- Any specific exclusions and/or loadings that exist on the remaining policies will also apply to the increase in the benefit amount.

Take note: Future Cover is only available on the Death Benefit.

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The outcome

Mr Rabbit can increase his existing death benefit on his Myriad policy from R4 000 000 to R8 000 000 without any underwriting, and Mrs White can increase her death benefit from R2 000 000 to R4 000 000 without any further underwriting.

The advantages

The business succession strategy remains intact in terms of death irrespective of insurability or lack thereof by the surviving shareholders. This unique benefit is only available to Momentum policyholders and results in peace of mind for both the client and adviser.

This unique benefit fulfils Momentum's philosophy of enhancing the lifetime financial wellness of people, businesses and communities. Do not wait until it is too late!

A day in the life of a legal adviser

By Ulanda Weilbach, Legal Adviser: Advice and Financial Planning

As a legal adviser responsible for Momentum Financial Planning (MFP), I am involved with financial planning, risk management, including client complaints and implementing business practices to limit complaints.

Most cases that end up with the Ombud are largely decided on what was recorded in the record of advice (ROA). Where there is no ROA, the finding will generally be against the financial adviser.

Today, most financial advisers pay attention to the ROA and ensure that it is finalised, but what about past clients where no or a substandard ROA was created? Recently, the Ombud suggested that this risk can be addressed as part of the review process. At this opportunity, you can reconfirm and record the purpose of all the product solutions that was implemented over the years. Where no ROA exists you can use

the review to request that the client confirm that the products meet their requirements; when the client confirms this, it becomes the new ROA. If the product no longer meets the client's needs, then steps can be agreed upon to ensure that the client is given an appropriate product solution which is in line with their financial needs at the time.

Recent complaints show that clients expect the financial adviser to provide advice about their wills (a will is not defined as a financial product by the Financial Advisory and Intermediary Services Act [FAIS Act]). Therefore, it is prudent to address the client's will when conducting a financial plan. If the client already has a will, this can be recorded and the matter can be closed. If no will exists, then it provides the perfect opportunity to do a liquidity analysis and draw up a will.

In closing – always remember to do the ROA!

Turning credit loan accounts into financial planning opportunities

By Odette Kriel, Legal Adviser: Advice and Financial Planning

Background

During times of economic slow-down businesses often look inward to improve the business' overall financial wellness. For instance: Debts and spending are minimised, and unsuccessful ventures are reconsidered. In the same vein, prudent business owners will agree that although a credit loan account owed by the business to the business owner may be interest-free, there is an opportunity cost to this debt not being utilised to the benefit of both parties. I will illustrate how a credit loan account can be utilised to the benefit of both the business owner and the business.

A credit loan account is created when an entrepreneur starts a business with their own money to pay for start-up essentials such as salaries, rental, business license costs, etc. Business owners who do not have their own cash, borrow money from banks or credit providers.

A credit loan account is stated on the balance sheet of the annual financial statements as a liability. Therefore, it negatively affects the credit worthiness of the business as it is a debt.

Solution 1:

Repayment of the loan upon the death of the business owner

The credit loan account is an asset in the deceased estate of the business owner. The executor of the deceased estate will demand repayment from the business, for the benefit of the business owner's estate beneficiaries. If the business cannot repay the debt, then the executor

will issue a summons against the business and will go as far as liquidating it in order to ensure repayment. When the business owner started the business, the idea was of course not to cause the business' demise in this manner.

The business must apply for life cover on the life of the business owner, pay the premium and receive the proceeds upon death. The parties should enter into an agreement that will ensure that the proceeds are in fact used to settle the loan account debt. This solution ensures that the business owner's beneficiaries benefit from their life's work and that the business debt is removed from its balance sheet ensuring improved creditworthiness.

Solution 2:

Monthly repayment of the loan account to the business owner

The business can repay its debt to the business owner in monthly amounts if it has sufficient cash. The repayment to the business owner is not included subject to income tax and is a settlement of a capital debt. As a result, the business owner will not be liable for income tax on these amounts; therefore, the business owner could receive a tax-free 'salary' until the debt has been settled.

Solution 3:

Redemption by way of 'gearing'

In this instance, the business will need a good credit rating. It borrows an amount equal to the business owner's loan. Once it receives the funds from the bank, it pays back the

debt to the business owner. The business owner invests the funds into an endowment fund policy and cedes the policy to the bank as security for the loan. After five years the policy matures and the business owner uses a portion thereof to lend to the business to settle the debt to the bank and retains the growth that is in excess of this outstanding debt.

The benefits of this solution are that the loan is turned into a growth asset instead of a stagnant debt and it provides investment diversification outside the business. After five years, it is fully accessible and is able to provide tax-free capital to the business owner.

Solution 4:

Redemption by way of recurring payments

Here the business elects to repay the debt out of business profits. The business owner invests the amounts received into an investment in their own name. Depending on the business owner's preference, the investment can either be an endowment policy or a unit trust investment. This method will also ensure that a stagnant asset is turned into a growth asset in the hands of the business owner that can aid the personal financial plan.

As a business client's financial adviser, you can contribute to the business' success by guiding your clients to use these proactive solutions for credit loan accounts. A business which is financially well and prospers is a great advantage to the business owner's family and ensures that they leave a memorable legacy.

Business continuity and estate planning

By Arthie Kander, Senior Fiduciary Specialist: Momentum Trust

Business owners spend enormous energy in filling gaps to achieve their business aspirations by planning and persisting toward growing and preserving their business value to achieve a lifetime business exit goal. Hard work and perseverance serves them in achieving these goals. The process of administering deceased estates of business owners has evidenced gaps in many business exit plans in the circumstance of death.

Some practical aspects necessary for the continuity of a business after the death of the business owner is the ability for the business to pay creditors and salaries as well as to deliver on contracts. The inability to attend to these key issues may result in discontinuance of services and materials required for performance; uprising of staff and possible union actions against the business and loss of clients which will have a detrimental long-term effect on shareholder value and business profit. Family members may also reap the **short end** by becoming deprived of income and capital to maintain their lifestyles.

Another possible challenge for a business after the death of a business owner is one of control and transition of ownership. The sudden death of the business owner (who is also the key person) can affect profitability of the business without the required skills needed to run the business. Without adequate planning, the death of the business owner can also result in a situation which forces heirs and business partners (who may be complete strangers with no particular interest[s] or skill[s]), to work together. Life assurance (such as a key person policy) will minimise the risk by providing financial liquidity to allow

for employment of skills to keep the business running, while the buy-and-sell policy will provide liquidity to the business partners so that they may purchase the deceased partner's shares while the family can receive the cash value of the business interest as part of their inheritance.

Business owners can achieve peace of mind by developing business continuity arrangements (like buy-and-sell arrangements) and instructions to the executor and financial planner, to lessen potential losses to both their family and business. It is also imperative that the business owner nominates a seasoned professional, well versed in the practice of administration of deceased estates to ensure seamless management of the deceased's affairs within the business. The executor can proceed with issues such as transacting on a business bank account by making payments to creditors and salaries to ensure continuity of day to day activities in the business.

The business owner can leave a business continuity instruction (BCI) as a guide. The BCI can be used to address business matters about whom to contact and for what information. The BCI will also explain who should fill which roles in the business, and how the ownership should be handled upon death. The BCI can also guide the family towards the vision as to how the respective financial resources of the family and business might interact to keep things going. In short, the BCI should be a way to communicate with the family, executor and financial planner, information that they will need to know in order to keep things going until finalisation of the business owner's deceased estate.

About Leverage

Momentum Leverage is prepared by the Momentum Legal Advisers: Financial Planning and Fiduciary Specialists from Momentum Fiduciary Services. For financial advisers, please contact your legal adviser or fiduciary specialist should you have any questions. For clients, please contact your financial adviser should you have any questions.

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