What happens to my company shares after I die? The importance of buy and sell agreements

Take the following scenario:

Craig and Raymond were high school friends. About 20 years ago, they started a mining supply business. They registered a company with both of them as directors and shareholders in equal proportions. They trusted each other and, therefore, did not feel it necessary to conclude a shareholders agreement or any other contracts to govern their relationship. They believed in resolving matters on a consensus basis as they came up based on the circumstances at the time. This worked for them.

But then something happened that neither of them had planned for. Craig unexpectedly passed away from a heart attack at age 53. He did not have a will. Consequently, his wife and two sons inherited his estate in equal shares, including the shares.

Raymond offered to buy shares from them for what he believed the market value of Craig's shares was. They are not interested in selling. They want to get involved in the business and make a living. They also believe that the business and the shares are worth much more than Raymond is offering.

This is a big problem for Raymond. He never really got along with Craig's wife and two sons; he believes the sons are spoiled and don't know what it takes to build up a business with a lot of hard work.

The said scenario is why every company with a business and joint shareholders should have a properly negotiated and drafted shareholders agreement signed. The shareholders' agreement should, amongst others, cater for an option, alternatively an obligation, for the surviving shareholder or shareholders to buy the deceased shareholder's shares.

Such a clause is also referred to as a buy and sell agreement. If, in the scenario above, such a buy and sell agreement had been concluded between Craig and Raymond, Raymond could have forced the beneficiaries of Craig's estate to sell the shares. He would then be able to carry on with the company and the business on his own.

The beneficiaries, on the other hand, would have received the money and, thus, were also treated fairly. Therefore, a win-win solution.

Furthermore, if Craig and Raymond had taken out life insurance on each other's lives, the life insurance proceeds could have been used to settle the purchase price of the shares, alternatively, a portion of the purchase price. In this regard, a buy-and-sell agreement could cater for the proceeds of the life insurance to be the purchase price; alternatively, the agreement could stipulate that the market value of the shares at the time, determined by an objective evaluation, would be the purchase price payable by the surviving shareholder. In such an event, the agreement could also cater for the balance of the purchase price, if any, to be paid in instalments with interest in a reasonable period not to cause a cash flow headache for the surviving shareholder.

Thus, make sure you get legal advice if you are a joint owner of a business or a company owning a business on a buy-and-sell agreement.

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