



MINDING YOUR BUSINESS

Understanding when and how to use assurance in your business – RSA edition

There are a number of highlights and pitfalls surrounding corporate insurance and group cover. This brochure looks at them.

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GROUP MEDICAL AID

Although medical aids are considered a fringe benefit when paid, or partially paid by an employer there are a number of reasons that may make this a good idea in your business.

- ✦ You should be able to get a tax deduction on the cost to company. Speak to your accountant about this.
- ✦ You can ensure that your staff are properly cared for when they are ill, which will reduce the time that they are off work.
- ✦ Many of the large medical aids have wellness days and wellness programs that can help you keep your employees healthy – especially in critical but sensitive areas like obesity, high blood pressure, high cholesterol and HIV where it is not appropriate or legal for a company to get involved. Basic wellness days can be organised for as few as 10 employees.
- ✦ If membership of a medical aid is compulsory and there are more than 15 principal members then late joiner penalties, waiting periods etc. can be waived. This can save your employees thousands of rand.

PENSION AND PROVIDENT FUNDS

The government is intent on reforming the pension/provident fund arena and changes have been happening slowly over time, but there is no doubt that the ultimate objective is to ensure that every employee is contributing to retirement funds, which will not be able to be accessed until retirement. Provident funds were originally introduced to service the low income market, but have become the fund of preference across the board. Pension and provident funds are essentially being merged together in terms of the pensions fund act, many using umbrella provident funds. Over the last 10 years small provident funds and standalone pension funds have merged into larger funds because they have become uneconomical to run. There are still some concerns that the government will insist on the compulsory use of the government's PIC in much the same way as the American social security system. The biggest issue if that should that happen is the sheer volume of investment that would be controlled by a single entity (add all the contributions that are currently made to all the insurance companies at present, and add all the government contributions as well and PIC would very quickly own a large share of the JSE). The next wave of reform is likely to clamp down on the cashing out of pension contributions on resignation from a company. It is likely that the regulations will be changed to enforce preservation of the funds, or transfer to another pension/provident fund until retirement.

When considering where or not to go down this route – here are some pointers:

- ✦ Ensure that the benefit consultant or broker uses a large, well established and well run umbrella fund with a modern, flexible and client centric computer interface system. Standalone funds are not really economical unless you have thousands of employees.
- ✦ Get comparative quotes that have a clear and transparent disclosure of the fees, fund availability and employee access to the information.
- ✦ It might be a good idea to allow your staff to contribute more than the minimum amount.
- ✦ Ensure that your HR staff are trained on the basic options on resignation and the tax implications of cash withdrawal.

GROUP RISK BENEFITS

Providing basic life cover, funeral cover and disability cover goes beyond being a nice to have for your employees, it also protects you as the employer from claims from a disabled employee.

- ▶ Although you may not have a legal requirement to pay out any form of life or funeral cover to the family of a deceased employee you will be approached by the family and if it is badly handled this can adversely affect your staff morale.
- ▶ Funeral cover is very inexpensive and starts at around R20 per month per employee and their family. If you are introducing it for the first time into a company you cannot make it compulsory for new employees, but if you coincide the introduction with the annual salary increase the uptake is usually high.
- ▶ While capital (total) disability cover is inexpensive it takes up to 2 years to pay out, and in the meantime you may be obliged to continue to keep the employee on your books. Depending on the provider and the definitions of disabled the employee may not meet the provider's requirements (in which case he may not meet the government's medical boarding requirements either) and you may be forced to try and retrench the employee (opening up discrimination accusations). Bottom line, this is a nightmare and in the 5 cases I have come across only 1 employee was paid out. My recommendation is to put income protection temporary and permanent disability group cover in place. If the employee is booked off work for more than 3 months then the insurance provider pays out the employee, and this can continue through to retirement if the condition is deemed permanent. Get full disclosure on how and when this is paid out by the different providers. Goedkoop is usually duurkoop.
- ▶ Depending on the size of company and the number of employees joining the group benefit scheme, a 'free cover limit' will apply. This is the amount of cover that will be granted before requiring medical underwriting. For employees that have a medical condition that may preclude them getting life cover out in the free market (diabetes for example), this can be a huge help.

KEY INDIVIDUAL ASSURANCE

If you have an individual who is integral to the company's success – a manager, salesperson or scientist for example – losing them to death or disability can have a huge impact on the company's finances until you manage to replace him or her. Key individual assurance will provide the much needed liquidity to bring in a temp, and go through the expensive process of replacing the individual. Typically the policy belongs to, and is paid out to, the company

BUY AND SELL ASSURANCE

A shareholder's agreement in a private company will address how shares in the company should be bought and sold on the death of one of the shareholders, more often than not it will give the other shareholders the right of first refusal to buy the shares. If the shareholders do not have ready liquidity in order to buy the shares from the estate here are some of the potential consequences:

- ▶ The executor of the deceased shareholder's estate can apply for the liquidation of the company in order to obtain the value of the shares, especially if the estate is not liquid. This creates a

'firesale' situation which can seriously disrupt the company as a going concern, frighten off clients and damage the credit rating of the company.

- Although companies are so-called 'limited liability' entities, most directors will have signed surety in their personal capacity for any facility with a financial institution, even if they aren't aware of it. On the death of one of the shareholders banks are known to call in the facility, and depending on the wording of their small print they are also under no obligation to demand payment from all directors, they often go straight to the estate and claim from the 'low hanging fruit'. This contingent liability should be provided for.
- If the shareholders do not have the liquidity to pay out the executor the beneficiary of the shares may impose their rights as shareholders, demanding a presence on the board, directors fees etc. Once again, this could have a massive effect on the smooth running of the company.
- Although the company will not pay estate duty, estate duty on the value of the shares will be paid by the executor. The shareholder must make provision for this.

Liquidity can be generated in the hands of the 'surviving' shareholders by way of buy-and-sell policies. Essentially all the directors take out life (and sometimes total disability too) assurance on each other's lives that will payout a lump sum equal to the shareholding of the deceased shareholder. This then creates the liquidity to 'buy' the shares back from the executor. It is imperative that this scheme is structured properly, and backed by a shareholders agreement compelling the sale/purchase of shares. The premiums must be seen to be paid by the life assured (otherwise double estate duty may apply). A buy and sell agreement needs to be drawn up and signed by all parties. While this can obviously be done by the company's attorneys most large insurance providers will provide this legal service free of charge.

CONTINGENT LIABILITY ASSURANCE

Contingent liability assurance will provide liquidity to settle loan accounts or sureties the deceased shareholder may have signed.

STRUCTURE OF THE SHAREHOLDER'S AGREEMENT

The shareholder's agreement is likely to require changing to accommodate and enforce the buy-and-sell agreement. It should also address the following:

- The manner by which the value of the company will be determined.
- Provision for the cession of the deceased shareholder's interest in the surviving partners.
- How the premiums will be paid (it is common for the company to pay the premiums which are then charged to the loan account so that the shareholder is 'seen' to be paying the premiums which is essential.
- A description in how the and when the payments will be made to the deceased estate, especially if the amount insured is not adequate to provide liquidity of the full value.

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