## SHAREHOLDER AGREEMENT
## QUESTIONS TO BE ANSWERED

PLEASE READ CAREFULLY – ESPECIALLY HILITED AREAS

Every Shareholder Agreement has to consider three important factors.
What happens when:

1. A shareholder dies
2. A shareholder is disabled
3. A shareholder departs from the business

1. The easiest solution is when a shareholder dies. The Shareholder Agreement provides for life insurance on the lives of the principals. This can be either a corporate redemption or a cross-purchase agreement if there are two shareholders, or a trusteed cross-purchase if there are more than two shareholders. In this instance, there are going to be at least three shareholders, but one of them is retiring, and will be paid out of corporate earnings. Therefore, I would recommend a corporate redemption agreement. The Corporation owns all of the insurance policies, and holds all of the shares, which have been endorsed in blank. When a shareholder dies, the Treasurer pays the insurance proceeds to the Shareholder's Estate and the shares are returned to the Treasury.

   The only question to be decided here, is how much insurance to buy??? If you value the business at $600,000.00, then each insurance policy represents the shareholder's percentage of the whole. If more insurance is needed for the shareholder's family needs, it can be purchased as part of the Estate Plan, and placed in an Irrevocable Insurance Trust, which renders the insurance proceeds both income tax-free and estate tax-free. The tax benefit to buying more insurance in the Estate Plan, and not in the Shareholder Agreement, is that you avoid some capital gains tax on the death of the shareholder. Also, since Sue is older than Steve, the difference in premiums is a significant factor.

2. When a shareholder retires or becomes totally disabled, there is a trigger date when the shareholder must sell his shares back to the business. A disabled shareholder can only receive a salary for a reasonable period of time (usually 6 months to one year) before he becomes a drag on the business. The partners have to decide how long to carry a disabled shareholder, and how to pay him for his shares when the trigger date arrives. If there is group disability insurance (which you should look into, the payments are reduced by that monthly insurance payment.
   Question: How long should the disabled partner draw a salary, and how

many years for the buyout, and do you pay interest on the unpaid balance??
Question: For a retiring partner, how many years for the buyout, and do you pay interest on the unpaid balance??

There is a type of insurance called "disability buy-out" insurance which provides for these types of events, but this insurance is often expensive. The more reasonable course, is for the business to pay to the disabled shareholder the value of his shares, over an extended period of time (10-15 years), with those payments being reduced by any disability insurance that the business carries. The monetary burden on the business is determines by the value of the shares at the trigger date.

3. A shareholder departing from the business is the most troublesome provision. There are two types of departure – Voluntary and Involuntary.

Voluntary departure can be either retirement (discussed above), or the desire by a partner to quit and do something else. If the partner leaves, this places a great burden on the other partners and the business, as the departing partner is entitled to either all or part of the value of his shares, and the business has to spend a lot of money and effort finding someone to replace him. This would suggest that either the departing partner take a very long payout (20-25 years), without interest, or receive a percentage of the value of his shares over a shorter period of time. It is unwise to fully reward a departing partner for messing up the corporation.

Question: Do you discount the value of a departing partner's shares – if so, by how much, and how many years is the payout; and do you pay interest.

A partner departs involuntarily, if he is fired for some criminal act against the business or is indicted for some other criminal offense, then he should take a very serious discount on the value of his shares, since he has damaged the business by his own acts. A discount of 70-90%, without interest, would not be unreasonable.

Question: What is the discount, and how long is the payout; and without interest??

There will also be provisions in the Agreement covering divorce and Bankruptcy, and all spouses MUST SIGN THE AGREEMENT

All these scenarios have to be examined, and decisions have to be made on the treatment of each scenario. I will be happy to discuss all of this with you so as to assist you in making these decisions.