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A word concerning personal guarantees

It is quite common for small businesses operating as private limited liability companies to have shares held by two or three shareholder employees.

This happens when a company is growing; it needs more space, equipment, or financing for its accounts receivable or inventory. The shareholders approach a lending institution to borrow the money the company needs.

The lender approves of the company's plans and approves the loan **requiring as additional security the personal guarantees of the shareholders**. Once the guarantees are in place, the lender has access to the personal estates of the shareholders, **over and above the company's assets**.

During the term of the loan, one of the shareholders dies. His/her shares are sold to the surviving shareholders under the terms of a Buy-Sell arrangement. The deceased's executor, having exchanged the shares for cash has no further interest in the company's affairs, but what about the personal guarantee given by the deceased to the lending institution? **It still exists and is binding on the estate**.

The executor would, of course, approach the lender requesting cancellation of the personal guarantee given by the deceased and the lender might agree.

On the other hand the lender might decline the request and would almost certainly do so if the shareholder's death were likely to cause difficulty, or if the death occurred during a general economic downturn that was likely to affect the company's sales or profitability. Why would a lending institution release the guarantee? The estate of the deceased employee is the most liquid security the financial institution has.

Most small to medium sized private companies are indebted to lending institutions in one way or another. The giving of personal guarantees is a widespread practice. Funding Buy-Sell Agreements with life insurance is also a common practice due to its cost effectiveness.

Unfortunately the provision of additional life insurance to retire any company indebtedness and thus eliminate a deceased shareholder's personal guarantee is often overlooked, especially when the provision of insurance is not a condition of the loan.