issue 8 | march 13

scoop

entertaining the law

Dequetteville Chambers
1 Dequetteville Terrace
Kent Town South Australia 5067
phone +61 8 8132 5000
facsimile +61 8 8363 1633
admin@baggiolegal.com.au

Business succession: Plan now or perish later

Inter-generational, and inter-owner, business succession poses an enormous challenge for businesses and advisers. A changing of the guard in a business can occur for any number of reasons – retirement, lifestyle, health, TPD or death to name a few. It is not a question of if – it is a question of when.

Left to their own devices, many clients will fail to plan for their exit from the business. It is our job as advisers to alert them to the perils of this inaction, and address it.

Do you have clients without any clear road map to ensure their business passes smoothly to the next generation or the surviving business owners?

Business succession, in circumstances where the stakeholders are alive and competent, is a complicated enough subject matter. Not only must we deal with the usual commercial, legal and tax issues for a business transaction, we often have to be mindful of personalities, family dynamics and hierarchies.

And then there is business succession occurring upon death or TPD. This makes *inter vivos* business succession look easy! Take all the challenges of *inter vivos* business succession, add grief, financial hardship and uncertainty, death of a business principal and family leader (and the consequential loss of critical knowledge and guidance) and a little self-interest and stir!

Over the years, we have developed a comprehensive toolkit and skills for SME business succession. At its core is the important truth that business succession is not an old fashioned conveyance of property. It is a business transaction, with all the complexities of a business transaction, and more. And this requires skill, experience and judgement to execute properly.

Here are some tips and traps you might bear in mind when advising your clients in this area:

- Got the insurance but no buy/ sell agreement in place
  We see this a lot. Your client has diligently taken out life/ TPD insurance to fund an orderly buy/sell arrangement upon death/ TPD. But no legally binding buy/ sell agreement has been implemented between the business owners. When triggered, the affected business owner's family will enjoy the windfall insurance *and* continuing ownership of the business. Obtaining insurance is only part of the story – a well drafted legally binding buy/sell agreement is essential in these circumstances.

scoops

Have you reviewed your terms of trade and credit applications since the implementation of the Personal Properties Security Register (PPSR)?

The implementation of the PPSR has meant that many different forms of "security" which previously did not require notification will now be ineffective without registration (for example, retention of title arrangements, consignment sales arrangements and leases)

Andrew Baggio
LLB MTax BA GCLP FTIA

William Chau
LLB BCom(Corp. Fin.) GDLP

- Loan accounts/ trust entitlements
  It is fair to say that many lawyers struggle with loan accounts, a simple concept to you accountants. It is essential that loan accounts are addressed in any business succession whether *inter vivos* or testamentary. The continuing owners need to know that no past owner/ successor will demand payment in the future of an old book entry loan that should have been wrapped up years ago. The same applies for trust entitlements. How well do your existing buy/ sell agreements deal with loan accounts/ trust entitlements?

- Business premises in SMSFs
  Your clients have their business premises in a SMSF but wish for the premises to pass to their children as business owners upon their death/ TPD. Have they implemented a structured process to ensure this occurs including, for example, reversionary pension arrangements and/ or liquidity facilities for the SMSF?

- Gross up for stamp duty (and tax)
  Unfortunately stamp duty is, and will continue to be, a feature of our landscape in SA. Have you advised your client to gross up its insurance coverage to fund any stamp duty (or tax) impost that may apply upon a transfer under a buy/ sell agreement? (Have you even quantified these imposts?) If not, these liabilities will have to be raised from own funds or borrowings - which may come as a surprise to all concerned!

- Family farm concessions for stamp duty
  The Commissioner happily takes a benevolent view when it comes to inter-generational *inter vivos* transfers of farm assets. But the devil is in the detail here. Upon analysis, we often discover ‘family farm’ trust deeds have a much broader range of potential beneficiaries than the stamp duty exemptions permit. This requires amendments, and possibly, resettlement issues arise. This is best avoided at the outset by utilising a well drafted and family farm friendly trust deed.

- Powers of attorney/ wills
  Your client has a rock solid buy/ sell agreement applicable upon TPD… but has failed to implement an enduring power of attorney to operate at that time. Who will sign the transfers, bank documents etc. necessary to implement the transaction? Will it be necessary to seek Court orders to address this at that time? This is an example of a simple piece of paper avoiding all sorts of complications and expenses down the track.

- Documentation
  Your client has implemented a buy/ sell agreement for his business interests applicable upon death/ TPD but wishes for the business premises (or farmland) to remain with the family group as a continuing legacy. No formal lease has ever been negotiated or signed. This needs to be addressed. If no lease exists, the continuing owners will have no security of tenure and, perhaps, no place to conduct their business!

- Release of guarantees/ indemnities
  Your client has exited the business. During his tenure at the business, he executed a number of guarantees/ indemnities to landlords, suppliers etc. Unless specific releases are obtained from these obligations, they continue to exist – sometimes even for your client’s executor and beneficiaries. If releases are not possible, the continuing owners should indemnify your client and his successors to shield them from liability as much as possible.

- Retained profits
  Your client dies and the buy/ sell agreement is triggered. Does the agreement deal with whether or not your client (or his estate) will receive an interim distribution of retained profits? Or will this be left to chance?

We at Baggiolegal are commercial lawyers that ‘speak’ tax, and tax lawyers that ‘speak’ commercial. We are experienced in all aspects of business succession. Please contact us to discuss any business succession issues that arise in your practice.