

EXPLANATORY MEMORANDUM

Business Succession Planning

A business succession plan is part of a business contingency plan. It helps business owner's deal with their interest in their business if they need to exit their business because they have suffered a traumatic accident, become disabled or tragically die.

Having a business succession plan in place is essential for the continuation of the business and to ensure that the business owners receive full value for their interest in the business. A business succession plan allows the parties to agree on how various decisions will be made following the occurrence of an event. For example, how the exiting partner's interest in the business will be valued.

THE IMPORTANCE OF A BUSINESS SUCCESSION PLAN

These events, if not planned for, can destroy the business and probably the livelihood of the proprietors and their families. Specific problems that may occur include:

1. the estate/family of the departed proprietor may demand involvement in the business with the existing shareholders or partners.
2. the estate/family may make unrealistic demands on the value of their equity or may want the business wound up and the proceeds distributed.
3. creditors may call in outstanding amounts, particularly where the departed proprietor had a significant impact on the perceived credit worthiness of the business.
4. lending institutions (banks etc), may limit the continuing availability of finance if they perceive that the business' financial capacity has diminished.
5. the departed proprietor's estate/family may be placed in the position of accepting less than what the business is really worth.
6. clients and customers may take their business elsewhere if they perceive a reduction in the ability of the business to service their needs.

DEATH ONLY?

Death is commonly nominated as the trigger for a business succession plan but there are others. Total and Permanent Disability (TPD) and Trauma may also be used as insurable trigger events. In comparison to the value and protection they give, the insurance premiums are relatively cheap.

Following the death or disablement of a partner two needs immediately arise:

1. the continuing partner needs to take control of the exiting parties interest quickly and at a reasonable price to protect the business; and
2. the dependents of the exiting partner need to be relieved from the operation of the business and the certainty of knowing they will receive full value for the business interests of the exiting partner.

A Business Succession Agreement together with the correct insurance policy will meet those needs. All too often we devote our efforts to wealth creation, wealth preservation and wealth distribution (tax effectively) but ignore wealth succession and yet often the cost of control of wealth succession is negligible.

A Business Succession Agreement will assist in protecting your client's control and the value of their business if a partner dies. It enables your client's estate and dependents to obtain full, hassle free value for the partner's share in their business if your client dies.

Whilst a properly structured and funded Business Succession Agreements can't stop any of the above occurring it can ensure that there is adequate compensation in the event of their happening.

The prime purpose of a Business Succession Agreement is to ensure the efficient withdrawal of a partner from a business (or from jointly held property) without the need for expense, legal advice or proceedings. Put simply, it makes good business sense.