



Until death do you part

Writing a will...the life of your business depends on it

A business is like a marriage – the last thing you want to think about when it's going well is what will happen if something goes wrong. But conflicts can arise, tragedy may strike and no-one lives forever. By Domini Stuart.

Whatever takes you out of your business, if you haven't made provision for those you leave behind, your legacy could be heartbreak, disappointment and even financial ruin.

Who should benefit?

Business owners are no exception to the rule that everyone should have a Personal Will - a document which allows you to make binding arrangements for the distribution of your assets on your death. Along with your home, car, bank account, shares in public companies and jewellery, if you're running your business as a private company, your personal Will can also set out who should inherit your shares in that company.

For example, if you were running a small business through a company with one other person, and 50 per cent of the shares were in your own name, you could pass these shares on to your spouse or one or all of your children.

The problem is that they may not be interested in the business and want to have nothing to do with it. Even worse, they may want to have *everything* to do with it but lack the necessary skills.

"If you were suddenly left without your business partner, you'd almost certainly want to continue running the business in your own way," says Norbert Schweizer, principal of the law firm Schweizer Kobras. "What you wouldn't want is to find

yourself trying to work with someone you don't know, maybe you don't like, or simply isn't up to doing the job."

This is why you also need a Business Will.

What should become of your business?

"'Business Will' is actually a commonly-used term for business succession," says Schweizer. "Its job is to make provision for involuntary departure like death or disability, and can also cover voluntary departure such as retirement. Whether you have a fatal heart attack or simply decide you'd rather move on, your Business Will should make it clear who owns the business, the interest at stake and who is entitled to take over that interest or buy that share of the business."

A crucial thing to establish early on is how the business will be valued. One way is to base it on EBIT (earnings before tax and interest). Another is for the remaining partner and the deceased partner's beneficiaries simply to come to an agreement. If they can't agree, a professional business valuer, an accountant or someone from a relevant professional body might be called in.

However, no simple dollars and cents analysis can take account of the fact that the departure of one of the partners could, in itself, change the value of the business considerably.

"Two of my clients have a garden landscaping business," says Schweizer. "One is a real go-getter, very good at bringing in new business. The other is more of a back office person, taking care of the day-to-day administration. In this case, the go-getter would be much more difficult to replace. Harsh as it sounds, the business would be worth a lot less if the go-getter died than if his partner died."

The Business Will should protect both the rights of a surviving partner by giving him or her the right to buy a deceased partner's share in the business. It should also protect the rights of the family of the deceased partner to benefit from the business.

The perceptions of these two parties can be very different.

"A woman whose husband has been in a business for 25 years might believe she's entitled to a payout of, say, \$2 million," says Schweizer. "Meanwhile, her husband's partner might claim that he has been carrying him for the past 15 years and that, without him, she wouldn't even have had an income in that time. In his eyes, he owes her nothing.

"If there's no Business Will and they can't agree, they could end up in court. Meanwhile, of course, the business is suffering."

In order to avert these kinds of situations, a Business Will generally takes the form of put or call options. A call option gives the buyer the right to buy. A put option gives the seller the right to make the buyer buy.

This then raises the issue of how that buy-out will be funded. If the business is worth \$1 million, where will the deceased partner's family find \$500,000?

“It’s common for both partners to take out insurance to cover the payout, but this isn’t always possible,” says Schweizer. “In one case I am presently handling, a client has a medical condition which means insurance isn’t an option. In this case, his partner’s beneficiaries have agreed that they would accept payment in instalments over a three-year period.”

Managing conflict

A Business Will can be written in tandem with your Personal Will as either a succession deed or, more commonly, as a Shareholders’ or Partnership Agreement.

One of the key differences between a Personal Will and a Business Will is that a Personal Will can only take effect when you die, whereas a Business Will, and particularly a Shareholders’ Agreement, is effective as soon as it is signed and can be invaluable while everyone is still alive.

If there’s a conflict within the business, for example, a Shareholders’ Agreement can provide guidelines for how it might be resolved. It could include preventing an acrimonious partner from leaving the business, setting up in competition and approaching your most profitable clients. And it could also prevent someone like our go-getting landscape gardener from walking out of the business and leaving his partner, who may be less able to continue the business alone yet still have made significant capital investment, with nothing.

When Stephane Thomas wanted out of his retail optometry business he had a taste of the complications that can ensue.

“I started the business with one partner who stayed for two years before moving on,” says Thomas. “That was fine – there were no problems in making the transition to another partner. But then things started to go down hill.

“In fairness, I can see that many of the difficulties started when I developed other interests.” Thomas is co-inventor of an environmentally-friendly portable fireplace that burns methylated spirit. “Retail is a seven-days-a-week commitment and I wasn’t giving it my full attention. I can understand why my partner was getting frustrated.

“In the end I decided to exit the business in order to concentrate on the fireplaces, and the simplest way to do that was to sell my share to my partner. Even though we had a Shareholders’ Agreement in place it was still messy – it took a long time for us to agree on a fair price and we stirred up quite a bit of ill will in the process. In the end we managed to settle without having to enforce the agreement, but it was reassuring to know we had it there as a last resort.”

The experience hasn’t put Thomas off working with a partner. He and Uwe Backes now head up The Fire Company, selling their EcoSmart® Fire in Australia and overseas. However, he has been careful to put a comprehensive Business Will in place. “You want to believe that a partnership will work forever, but you have to be realistic. If things do go wrong, being prepared could save the business.”

Shareholders' Agreements are not something to tackle on your own. "If they aren't properly drawn, they can leave everyone in limbo, and eventually destroy the business," says Schweizer. "At the moment, in another case I am handling, we're working with five directors from the same company. One developed problems which prevented him from functioning in his role and, in the end, he was fired. He wants \$1 million as a payout. The others say that the business is worth less without him and that depreciation has further eroded its value – that his share is effectively worth nothing."

"Unfortunately, the agreement they had in place when they approached us wasn't specific about who should pay, or how a director's share should be valued. In these circumstances it was worthless. Four years after the man was fired, they still haven't reached an agreement. Now the business is in the process of being wound up."

There is a rule in law that allows a court to wind up a business if it can't be properly governed. Where an agreement can't be reached, the receiver will be called in to sell everything. "This is a loss to everyone," says Schweizer, "personal and emotional as well as financial."

Keeping it in the family

Family businesses bring a new dimension to the issue of succession.

According to Monash University's Family and Small Business Research Unit (FSBRU), many family-owned businesses are run by ageing founders and operators who have given scant consideration to the complexities of passing on their company.

"We believe business operators need to take a holistic approach to succession planning," says FSBRU director Associate Professor Rowena Barrett. "You can look at succession planning from the financial, taxation and legal points of view. But unless you also factor in the individuals, you are destined to fail."

The FSBRU advises that effective succession planning involves balancing expectations of management and staff with what is best for the business. An eldest son or daughter might expect to be the heir apparent - but what if a younger sibling is more suitable?

"The best person to take up the reins may not be a family member at all," says Dr Barrett. "Business operators should also look at the relationships involving management and other employees. The person the boss thinks would be best to take over may not be popular with the other staff. That person's appointment could lead to lowered morale, reduced output, a decline in the company's profits and, ultimately, even send the business to the wall."

How much will it cost?

"A simple Personal Will doesn't cost much at all," says Schweizer, "but, when you're in business, it's isn't likely to be that simple. If your business is turning over \$1-\$3 million each year, you will probably have a trust or two, self managed super, enough assets to make tax planning an issue as well as asset protection. In this case your Personal Will is likely to cost anything from \$1,500 to \$3,000. You will also need to

have your will reviewed from time to time, and especially if there are any significant changes to your circumstances like marriage or divorce, and this will incur further costs.

“Your Business Will, written in conjunction with a Shareholders’ or Partnership Agreement, will then cost about \$2,500, bringing the total cost to around \$5,000. This may seem like a cost you can put off when you’re facing the expense involved in setting up a business, but this is really the best time to put your succession plans into place. There’s less likely to be a dispute when your business hasn’t started making a profit. And \$5,000 is really a very small price to pay when you think of the pain it can help avoid.”

Before you put off making a will, here are a few more points to consider

- A surviving business partner could be left struggling to cope with the pressure of keeping the business running without a key player while trying to manage personal grief and do the right thing by his or her deceased partner’s family.
- If your partner died, you could find your business part-owned, and part run, by his or her partner. How well would you work together?
- A Business Will is the perfect way to pass on the secrets of your business – key information such as supplier agreements, intellectual property, arrangements with customers and agreements with staff.
- A Will can ensure that your assets are distributed in a tax-effective way, reducing the impact of tax and other charges on you beneficiaries.
- If you are the sole director of your company, your executor has the power to appoint a new director to keep the company running until the new shareholders decide on its future. If there’s no Will, someone close to you would have to apply to the local Supreme Court for letters of administration. This could take weeks or months and, in the meantime, the business may be unable to trade.
- If you want to keep your business in the family but aren’t sure who should replace you in the top job, you could have your family members independently assessed. This way, you will gain a clear a picture of their skills and talents.

Online information

<http://www.pt.nsw.gov.au/page.cfm?page=25&category=1>

The Public Trustee - an independent and impartial Executor, Administrator and Trustee for the people of NSW.

http://www.google.com.au/search?q=cache:MydtkaT8CE0J:www.eqt.com.au/pdf_files/EQU%2520087%2520Broch_29_aw.pdf+facts+about+Wills&hl=en

Equity Trustees (EQT) – a public company independent of outside interests offering a wide range of will-related services.

http://aussielegal.aol.com.au/Will_splash.asp

AussieLegal - Australia's leading consumer legal information and law firm referral service.

http://www.makeyourwill.com/index.htm?aaaaaGn006Pwriting_a_will

MakeYourWill.com – if you're considering creating your own Personal Will