FINANCIAL **FACT SHEET**

WEALTH PROTECTION AND A BUSINESS SUCCESSION PLAN

IT'S IMPORTANT TO PROTECT WHAT YOU'VE WORKED LONG AND HARD FOR

Business risk insurance provides a vital safety net for anyone who operates his or her own business, or in partnership with others.

A business succession agreement should be an important consideration in instances where:

- two or more parties share ownership of a business – eg. they (or their trust, spouse, etc) each own shares in a company or units in a unit trust that carries on the business;
- one business principal dies or becomes disabled and the continuing principals want to ensure they are able to purchase the outgoing principal's interest; and
- the outgoing principal wants to ensure his/her estate is paid a fair value for that financial interest.

With a business succession agreement in place, a smooth transfer of ownership can be implemented.

INSURANCE FUNDED BUY/SELL ARRANGEMENTS

An insurance-funded buy/sell arrangement is beneficial where:

- a buy/sell agreement has been executed; and
- the business owners are using life insurance to provide either all or part of the funds to purchase an outgoing owner's interest.

HOW A BUSINESS SUCCESSION AGREEMENT WORKS

The following example illustrates how a business succession arrangement works:

Andrew, Brian and Colin equally own shares in ABC Pty Ltd. A Buy/Sell Option Agreement is in place that gives each of them the option of forcing the sale of their shares to the others if any one of them dies' becomes totally disabled, or suffers a major trauma event.

After a brief and unexpected illness, Andrew dies. Brian and Colin exercise their option to purchase Andrew's shares from his estate. (Note: Andrew's wife, as executor, could have exercised the option to force Brian to buy. It doesn't matter who takes the first step).

With the business valued at $1.2 million, each of the partners' shares are worth $400,000. Andrew also had a life insurance policy in place for $300,000.

The $300,000 is paid to Andrew's estate leaving $100,000 to be paid equally by Brian and Colin. The agreement gives Brian and Colin time to pay this additional amount.

Upon payment, Andrew's wife (his executor) must transfer his shares to the surviving partners. The best outcome would have been for Andrew to have had an insurance policy of $400,000.

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WEALTH PROTECTION AND A **BUSINESS SUCCESSION PLAN**

WITHOUT A BUSINESS SUCCESSION AGREEMENT

Where two or more people are carrying on a business, a business succession (buy/sell) arrangement ensures a fair outcome should one of them die or become disabled.

Problems can arise in the absence of such agreements, as highlighted in the following examples.

EXAMPLE 1

Peter Jones and Robyn Smith operated a marketing firm, PR Communications Pty Ltd.

When Peter died, his wife (as executor of Peter's estate) offered to sell Peter's share of the company to Robyn for a fair price.

Robyn declined the offer and began to set up her own marketing agency. Over a period of six months, Robyn succeeded in capturing most of PR Marketing's clients.

The original company became worthless, with Robyn effectively gaining Peter's share of the business for nothing. Ultimately, Peter's wife and family were the ones who suffered financially.

EXAMPLE 2

Ian and Rebecca were business partners supplying support materials to universities, technical and trade colleges, and schools.

When Rebecca died, Ian offered to buy her shares in the company from her estate.

Rebecca's will left everything equally to her two sons, Richard and John, aged 19 and 24 respectively. Unfortunately, the sons fancied themselves as businessmen and rather than selling their mother's share, they insisted in taking an active role in the business.

After a year of indecision, arguing and no growth, the business failed – a truly sad conclusion.

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