

# Alert

## WILLS & ESTATES

### COVID-19: Business Succession Planning

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The COVID-19 pandemic has had a devastating impact on many of us. One thing that it has undoubtedly highlighted is that none of us are immortal and it has forced many business owners to think critically about whether they have suitable plans in place in the event that they pass away or become incapacitated.

While succession planning has always been important, many people tend to overlook it as being something that they'll 'get around to later'. However, as many businesses are now finding out, that can have catastrophic consequences if tragedy strikes when unprepared. We have witnessed significant disputes between families and owners that have resulted in substantial financial losses, the distressing breakdown of previously strong relationships and ultimately the closure of successful businesses. In our experience, the time and monetary outlay required to plan is almost always the cheapest and most prudent path to take.

Given the current uncertainty we now face, businesses who have yet to do so should strongly consider putting a business succession plan in place now. Those who already have a plan in place should review it and ensure it is up-to-date, functional and achieves the desired outcomes.

#### The succession planning process

Business succession plans should be tailored to suit each business. Owners need to consider and identify the individual needs of the business to determine the desired outcomes before putting in place the documentation to achieve those outcomes.

A comprehensive business succession plan should have procedures in place for not only the death of any of the directors or owners but also their incapacity, whether temporary or permanent. While mechanisms for passing control and ownership of assets are important, the plan should but also consider possible taxation implications and other risks, for example potential inheritance claims, that could potentially defeat the desired outcome being achieved.

#### Decision-making powers

While the passing of ownership of business assets and entities upon death is often at the forefront of people's minds, one of the most important issues that should be considered is how the business would continue to make decisions in the event of the death or incapacity of one of its owners?

For example, if the business is carried on by a sole trader, have appropriate documents been entered into to confer on one or more persons the power to make decisions on behalf of the owner in the event of death or incapacity? Is that power conferred on a person or persons who have the appropriate skills to make decisions in respect of the business?

If the business is carried on by a company (either in its own right or as trustee of a trust), are there other directors who can continue to make decisions in the event of the death or incapacity of one of them? Does the constitution of the company contain a suitable mechanism to allow for the appointment of a replacement director? Is the director also a shareholder? Who has the power to exercise the rights of the shareholder in the event of incapacity or death?

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## What documents do I need?

While circumstances will be different depending on the objectives of each business owner, there are several tools that are commonly used to achieve the desired outcomes in the event of death or incapacity. This list and the examples given are not exhaustive, but some examples of the tools available include:

### Your Will

- A Will is often the first document considered for the purposes of succession planning. Ensuring the provisions of a Will have been updated to accurately reflect and accommodate the wishes of the testator with respect to their assets and interests in other entities, and to ensure that its terms are consistent with the terms of any other succession planning documents, is critical. This includes ensuring that appropriate persons are appointed as executor, given that this person or persons will have control over the estate assets during administration of the estate. Inappropriate dealings with the assets by the executor could not only defeat the succession planning objectives, but may also trigger unintended tax consequences.

Where circumstances have changed since a Will has been drafted, existing Wills should be reviewed, and either a new Will or Codicil put in place to address this.

### Enduring Power of Attorney

- Granting powers of attorney may be used to ensure that an appropriate person or persons have the right to exercise the powers of the individual, including rights attached to any shares in a company (whether conducting the business in its own right or as trustee of a trust), during any period of incapacity. Consideration should be given to the powers granted to the attorney and, in particular, whether the powers should be restricted at all to protect against an attorney potentially exercising the powers in a manner inconsistent with the overall planning objectives.

Consideration should also be given to the limitations of such powers, particularly where the business structure contains one or more companies, as an attorney cannot exercise the powers and duties of the grantor in his or her capacity as a director of a company.

## Shareholders Agreement and Company Constitution

- Where assets are owned by a company, a Shareholders Agreement or Company Constitution is a valuable tool to customise the rules relevant to the conduct of the company to suit the specific needs and objectives of the parties. These are useful both where the company owns assets in its own right, and where it does so as trustee of a trust. Issues that are commonly addressed in these agreements include:
  - o the right to appoint and remove directors, including alternate directors;
  - o who can make decisions and what percentage of votes are required to pass a resolution;
  - o whether any shareholder or director will have a casting vote or right of veto in respect of any decisions;
  - o rules around the issue of new shares and prohibitions against diluting the shareholding of any shareholders;
  - o exit strategies and rules and procedures that must be followed if any party wishes to dispose of all or part of their interest or in the event of certain events such as death, incapacity or retirement;
  - o policies as to declaration and payment of dividends;
  - o rules around borrowings to be undertaken by the company and/or contribution of capital; and
  - o dispute resolution procedures.

### Option Agreements

- In some instances, call options can be used to secure the right of another party to acquire ownership interests in an entity in the event of certain events such as incapacity or death of an existing owner. These are most often used when unrelated individuals enter into a business together to protect against disputes arising between the continuing owners and the representatives of the deceased or incapacitated owner in relation to the buyout of that owner's interest.

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Call options can also be useful to secure a family member's right to acquire a certain asset on the death of the existing owner if there are any concerns of an inheritance claim or other issues arising during the administration of the estate that may defeat the passing of that asset to the intended person.

While the grant of a call option is unlikely to trigger any tax implications, the exercise of the call option will, and therefore this needs to be taken into account as part of the broader succession plan.

### Trust Deeds – Appointments and variations

- Where a business is run through a discretionary trust, consideration needs to be had to both control of decision making at the trustee level, as well as mechanisms to ensure appropriate distribution of income or capital of the trust. Relevant issues here include:
  - o where the trustee is a company, putting in place a shareholders agreement or other document to regulate decision making of the trustee company and other relevant issues;
  - o ensuring that the role of appointor is passed to appropriate persons to protect against an existing trustee being removed and a new trustee appointed who may not act in the best interests of all beneficiaries; and
  - o distributor provisions to ensure equitable distribution of income and capital between beneficiaries.

### Superannuation

- In some instances, assets such as premises from which the business is conducted are held in a self-managed superannuation fund. As the death of a member triggers a cashing event in the fund, if this event is not properly planned for,

the fund may be forced to sell or otherwise dispose of the property in order to fund these payments. A comprehensive business succession plan should therefore include a strategy in relation to dealing with any business assets held in a self-managed superannuation fund.

### Restructuring

- Where current ownership structures do not adequately accommodate succession planning objectives, it may be possible to utilise various tax concessions including the small business CGT concessions, and the small business restructure roll-over to enable ownership to be restructured with minimal tax implications.

### Social distancing restrictions

The current social distancing restrictions in place do not mean that it is too late to do any of the succession planning that you need to do. We can put measures in place to overcome the social distancing restrictions through the use of technology. There are strict requirements of witnessing Wills to ensure validity in accordance with the *Wills Act 1936* (SA) and we encourage our clients to discuss this with us so that we can provide options based around each client's personal circumstances. It is not too late to put necessary documents in place, and if you need to get on top of your succession planning, we urge you to contact us to discuss your circumstances.



MORE INFO

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