Grant Thornton

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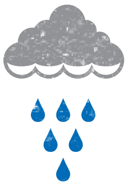
Business Protection

Have you planned for the unexpected?



In the event that a key individual or proprietor becomes unable to work involuntarily; Grant Thornton can partner with you to protect your business's revenue and equity interest by helping create a Business Protection plan.

Why have a Business Protection plan?

Simply put, a well implemented plan ensures that your business will continue to operate effectively with minimal disruptions.

It may be rarely discussed or considered, however one day you will inevitably leave your business; either voluntarily (e.g. retirement or a sea-change) or involuntarily (accident, sickness or death). A funded business protection plan will allow a smooth transition to take place, reducing the likelihood of disruptions to business operations (i.e. revenue loss, credit risk etc.) in the event of an involuntary exit.

Let's take a look at an example case study:-

Mr Frank Goner departs his business on an *involuntary* basis...

Frank and Dean, friends and business partners, run a successful legal practice business that is worth $4M. They own this business in equal shares. Frank specialises in property and owners corporation law and Dean in planning and environmental law.

Tragically, Frank suffers a stroke and can no longer work in the business. As a result, the business starts to lose money. Dean wants to buy out Frank's interest but they can't agree on what the business is now worth. Dean is also unsure as how to pay for the purchase as all of his assets are already held by the bank to secure the business debt.

Frank dies, leaving his interest in the business to his wife. Dean and Frank's wife are quarrelling over what will happen to the business and Frank's share.

Other issues to consider include:

- How is Frank's family going to survive with no income?
- How is Frank's death going to affect the revenue and profit of the business?
- How will the business maintain its credit standing? The firm has lost one of its greatest assets – Frank's expertise in property and owners corporation law. Dean must immediately find someone who can fill that role.
- How will the business loan be paid? Frank's death has triggered an automatic default of the debt and the bank wants payment or to renegotiate the loan.

If Frank had a 'funded' business plan in place, the issues faced by his family and business partner, would be easily resolved.

What is usually covered in a Business Protection plan?

There are 3 basic protection needs that typically apply to business:

Equity Protection

(is your equity interest protected?)

A business protection plan should detail the legal interest each owner has in the business and the rights of each owner. It should also give the continuing owners the right to buy the interests of the deceased or disabled owner, and ensure that the departing owner, or their estate, is paid a pre-determined price for their share of the business.

The plan provides all owners and their spouses with legal certainty should the unforeseen occur. A business protection plan should also detail the likely risks to the continuity of the business and its profits, should you or one of the other owners (or other key stakeholders) leave through sickness, accident or death. The plan should also outline strategies to appropriately manage any identified risks.

Revenue Protection

(is your business revenue protected?)

The sudden loss of a key person can have an adverse effect on the sales and profits of the business, and until a suitable replacement is found, the business could be faced with recruitment costs, possible loss of clients, and negative impact on credit rating and goodwill. If there isn't a suitable replacement within the business it may take substantial time and financial inducement to find and train a successor. Losses may also result, from demand that can't be met, errors of judgement by a less experienced replacement, or through the reduced morale of employees.

Regardless of a business' worth (in terms of equipment, property, inventory, goodwill etc.) the biggest business asset is usually the people whose efforts and skill drive it. Revenue protection is designed to minimise disruption to your business in the event that a key person is no longer there.

Debt Protection

Material things can always be replaced or repaired, but a key person's death or disablement can result in more disastrous consequences than any loss of, or damage to physical assets. Outstanding loans owed by the business to the key person may also be called up for immediate repayment.

A Debt Protection plan can provide your business with the ability to satisfy creditors and maintain its credit status through the period that you or a business owner is unable to work. Having a debt protection plan can provide your business with enough cash to preserve its asset base in order to repay debts, free up cash-flow and maintain its credit standing should a business owner or loan guarantor die or is disabled.

How to implement a Business Protection plan?

Firstly, it is important to establish what the business is worth. Your accountant may assist with this valuation however you may decide that their estimate is not a fair representation.

Once your business value has been determined, you can now explore the 'funding' options for voluntary and involuntary exits.

What are the Funding Options? *(In our example the following would apply)*

Options	Possible Issues	Cost Associated
Borrow funds	Qualifying for a loan? Geared to maximum?	At least $2M plus interest and opportunity cost (growth)
Sell or liquidate business assets	Price? Goodwill (if something happens to the business owner, will the business' value fall?)	$2M plus time and the survivor's lifestyle
Admit new business partner	Compatibility, time delays in finding a suitable replacement	$2M plus recruitment costs
Negotiate vendor terms	Succession suffers if business proceeds aren't available immediately. Cash flow problems for ongoing survivors.	$2M plus interest and opportunity cost (cash flow leads to decreasing revenue)
Sell personal assets	Capital Gains Tax, lack of desire from survivors to sell off personal assets.	$2M plus tax and survivor's lifestyle
Insurance policies	Good health to qualify, underwriting requirements, ongoing change in business values, ability to increase existing policies	Less than 1% of business value (< $20,000 PA)*

*In this above example policies to protect Debt, Equity and Revenue have been implemented for 2 white collar males, non-smokers, aged 45

Grant Thornton can work with you to assist, develop and implement a tailored Business Protection plan.

Often it will consist of adopting a combination of the funding methods outlined opposite. Business valuations can be arranged in addition to the funding via insurance policies. We can also liaise with a suitably qualified solicitor to draft the legal documentation known as the 'buy-sell' agreement. This will tie it all together. To safeguard the future of your business, consider organising a funded protection plan today.

Further information

If you would like to discuss any aspect of this brochure, please contact

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