7 THINGS you need to know about SUCCESSION PLANNING

1. What is succession planning?

Succession planning is the development of a strategy for the transfer of ownership, management and financial responsibility of a business. Whether you are passing the business down the family, retiring or selling up, you need to have a plan in place for when you leave. Succession planning might sound simple, but in reality, it should not be seen as a single event but as a well-thought-out process that takes years to coordinate and implement across all areas of your business.

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2. Developing your succession plan

The key to succession planning is starting early. Set a realistic timeline with measurable targets along the way to ensure a smooth transition to new ownership. Having an exit strategy in place also means you can reap the maximum benefits of the transfer and avoid losing money from unforeseen taxes or complications. Hiring an expert can help you navigate the challenges that arise with succession planning, such as Capital Gains Tax (CGT).

A question you will need to ask yourself is how much of your wealth is tied up in your business? Consider if you require the profits from selling your business to fund your retirement. This will impact your choice to either sell, simply close down or pass your business down to your child or another trusted individual.

When transferring your business to another, you will need to decide who is the best person to replace you. Could they be a family member or a trusted employee? Regardless, your successor must be an individual who is introduced to the business early enough for them to gain an in-depth knowledge and develop key relationships with long-term customers, employees and suppliers. They must be a natural-born leader, have quality communication and management skills, and the relevant industry expertise to guarantee the competence required for an effective change-over.

When developing your plan, consider the following questions:

- Will you transfer both ownership and management of the business to your successor?
- Will your successor require training and mentoring before taking over your business?
- Will any family members be involved in the business?
- When will you review your succession plan to ensure it is still relevant?

LEE & LEE

HEAD OFFICE:
HYPER CENTRE
SUITE 5, GROUND FLOOR
50-56 SANDERS STREET
UPPER MT GRAVATT
QLD 4122

TEL (07) 3103 8551
FAX (07) 3349 8208

EMAIL
info@leeandlee.com.au

WEBSITE
www.leeandlee.com.au

PARTNERS
Tony Lee
Peter Lee

SERVICES
Property Tax Specialists
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3. Succession planning with a co-owner

In the event of your partner's death, retirement or disablement, a buy-sell agreement will ensure you are not financially caught off guard.

A standard buy-sell agreement is a contract binding the surviving partner to purchase the deceased or disabled partner's share. The executor of the estate will instigate and conclude this process. Within the agreement, you must precisely define what circumstances will trigger the contract's provisions as well as an agreed payment method. Regarding the price of the shares, you may decide on a price together while drafting the contract, or a valuation based on market or book value after the trigger event activates the contract.

To fund a potential acquisition, taking out permanent life insurance policies may be an advantage. To gain CGT exemptions consider trustee ownership of the policy. You may also gain this exemption under individual ownership provided you meet certain legislative requirements. If you put the policy under your business or cross insure your partner you will be ineligible for CGT exemptions.

4. Building your business value

Many owners rely on the proceeds from selling their businesses to fund their retirement. However, many of those owners will come up short and place their retirement in jeopardy. Particularly, those businesses in the baby boomer era, which has resulted in more businesses being up for sale than ever before, creating a buyer's market.

It is critical for an owner to implement strategies to maximise the value of their business and ensure that value is independent of any one individual. To maintain or increase the value of your business, you must build strong business systems, protect intellectual property and construct financial and legal mechanisms for the transfer of assets. Ensure your business also has knowledgeable staff, effective training protocols and a stable client base. These are the elements that will add real commercial value to your business when it comes time to sell.

5. Mentoring your children for succession

Your child must only be your successor when it is the best commercial decision for your business. Foster discussion with your child early on so they know they have a choice in the matter. Before skill, they must have the drive to want to be your successor.

Multiple children only complicate the matter because you are crossing commercial and emotional issues. Communicate to them that this is a commercial discussion and not a family one. It may take multiple discussions and some tough decisions with your family over a long period to ensure everyone understands this and to flesh out which child is right for the role. It may also be advantageous to bring in an external third party to maintain an arm's length in the discussions.

Initially, your child should gain independent work experience in other companies before transferring to your business so they can bring new insight and knowledge. Maintain a professional demeanour and hire your child for an existing specific role to demonstrate to your staff their succession is based on merit.

6. Tax considerations for family business succession

Passing down the family business can cause tax implications that may shape the future of your business and how you execute its transfer. Recording all tax consequences will help assess opportunities for carried-forward losses.

Disposing or transferring of a business will cause CGT implications. You may apply for all applicable CGT concessions until there is nothing payable. To qualify for these concessions your small business' aggregated annual turnover must be less than $2 million, your asset must be closely connected with your small business, and your net business assets must not be larger than $6 million.

Re-organising your small business as a family trust will also allow you to avoid immediate tax implications when transferring your business assets to family members. By making yourself a trustee, you can gradually yield control of the family business by transferring assets at your leisure, allowing for a smoother transition.

7. Transferring your business checklist

To finalise the process of exiting your business after the contract for the sale or transfer is completed, you must tie up the administrative and financial loose ends.

Your ABN will need to be cancelled or updated online via AUSkey or Manage ABN Connections. The transfer of all business records regarding customers and assets like domain names and websites should occur in a timely fashion.

You also need to finalise your accounts payable and receivable. Ensure you pay outstanding bills, cancel registrations, lodge any final tax returns and make GST adjustments on final activity statements.

Property leases, as well as permits and licences, should be transferred to the business owner immediately. You do not want responsibility for property agreements while the business is not under your name. Keep in mind that flexibility of lease agreements vary and certain permits and licences can take up to 12 months to change.