

irongroup lawyers



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Estate Planning for Business Owners

Introduction

Do you have clients who own businesses? If so, the following issues should be considered when it comes to advising them on their estate planning strategies.

Business Ownership

A business can be owned by different types of entities and how the business is passed on after death differs according to the type of entity. For example:

1. An individual who owns a business can pass it on to a beneficiary via a Will.
2. If an individual has a partnership interest it can be passed on via a Will if the partnership agreement allows it. If there is no partnership agreement then it can be passed direct to a beneficiary however whether the surviving business partner is happy with that is another issue - we will address this later.
3. Assets in a trust do not form part of an estate & cannot be transferred via a Will. Therefore if a trust owns the business (or a share in it), you can only change the Appointor of the trust (via a Comprehensive Will) and then leave a Statement of Wishes requesting what they do with the assets. You cannot directly transfer the business.
4. If a company owns the business, the shares in that company must be transferred via the Will. Again though - you need to "look through" and determine what entity owns those shares. Again, if it's a trust, the Appointor may need to be changed via the Will.

Co-owners in a business

As noted in point 2 above, when a business is co-owned, the death of a partner can cause a number of problems for the remaining business partner/s.

If the deceased's share is passed on to a beneficiary, will the surviving business partner be happy with that new partner? In most instances it will be the deceased partner's spouse, who may or may not be capable and/or willing to work in the business. In these instances, a Buy Sell Agreement, sometimes called a Business Will, is essential to address these issues.

Internal Loans - owed to the business

There are two types of loans that a business owner might need to address in a Will. The first of these are "internal loans" ie where the owner has borrowed from the business, as any loans to the individual need to be repaid on death.

Let's say one child is inheriting a business, worth \$500K and the other child is inheriting \$500K cash. It appears fair, however when you realise the deceased owed \$200K to the business, one of the beneficiaries (the new business owner) will have an additional claim on the estate for that \$200K debt.

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If the two siblings get along, it may not be a problem as the debt can be forgiven (subject to the Debt Forgiveness Provisions) but what if they don't? Or what if one of them is going through a divorce and their ex-spouse insists on a repayment of the loan?

When it's a co-owned business, similar problems arise. Let's say the deceased business partner owed the business \$250K. With a Buy Sell Agreement in place, the deceased's share is passed to the other partner however their estate will still be liable for the \$250K loan repayment.

The partners may have decided to "forgive" any debt or they may have decided to take out extra insurance to cover the debt. Either way this will need to be covered off in the Buy Sell agreement.

If they don't have an agreement in place, the deceased's share in the business will pass to a beneficiary via the Will and the estate will still be responsible for the debt. Again, insurance may be an option.

External Loans - owed to a 3rd party

Banks often require guarantees from business owners, usually with joint and several liability. In the event of the death of a partner, the bank may call up the loan.

In addition, an estate cannot be wound up until any guarantee signed by the deceased is extinguished ie the estate has a contingent liability it needs to clear.

How do you resolve this? One solution is for each partner to take out insurance to cover the external debt.

Those policies can be personally owned or owned by the business. If personally owned, the estate can be required to lend the money to the business to pay down the debt so the bank can release the guarantees. That loan however, will need to be repaid at some stage.

Alternatively, if the business owns the policies they can pay down the debt direct. The bank can then release the guarantees and the estate can be wound up.

How does Irongroup's Estate Planning service work?

We can meet with the client or it can all be done over the phone - it's up to them.

Here's what usually happens...

1. With the client's approval, you phone or email us (info@irongroup.com) their name and phone number and we call to arrange a phone or office appointment.
2. During this appointment we collect personal information from them and begin to build up their profile to help identify estate planning solutions.
3. We then send the client background information on Wills & the decisions they might need to discuss with their family eg choice of executor, guardians etc
4. We contact them a third and (usually) final time and finalise their estate plan. The Will is prepared & mailed out for signing.

Do your clients need advice?

If you have clients who need estate planning advice please give us a call.

With our depth of experience, fixed prices and phone or office appointments, we can help you look after your clients' estate planning needs.

More information?

For a copy of our 11 Common and Costly Estate Planning Traps email us on info@irongroup.com.

If you have a query or would like help with estate planning please call one of our lawyers on 03 8621 9000. We'd be pleased to help.