LET'S NOT GET PERSONAL

ALL TRADIES ARE ENCOURAGED TO ENSURE THEIR ASSETS ARE PROTECTED, WRITES **MARTIN CHECKETTS.**

In our last article, we touched on the topic of keeping your business dealings separate from your personal affairs. In short, you don't want a rogue client or supplier making a claim against your business and then find that your family home or personal assets are exposed to that claim.

As we explained then, there are some basic steps every tradie should consider taking in order to ensure that this cannot happen. This is known as 'asset protection' and it's our topic for this month.

CONTEXT IS EVERYTHING

Asset protection is a response to three different types of potential threats. You may have heard this term used in the context of family law disputes (for example, divorces) or succession matters (for example, challenging a will). The focus of this article is asset protection in a business context, such as in response to disputes with creditors or clients. It's important to keep in mind that the tips we are discussing here in a business context may not be helpful in a family or succession strategy and may even work against you. So, always take note of the context and seek professional advice before getting in too deep.

PERSONAL GUARANTEES – NO SURE THING

When you're starting out, keeping your business dealings completely separate from your personal affairs is likely to be a noble but impractical goal. Inevitably, suppliers will demand personal guarantees and the balance of power between the two of you dictates that the supplier will get their way. Initially, at least – until you're powerful enough to dictate a few terms of your own!

Another concern is that the wording of these guarantees can be extremely onerous. For example, your obligations may not cease when an order has been fulfilled and paid; some guarantees continue indefinitely, whether you are still involved with the company or not. It may seem bizarre that you can still be pursued by a creditor after you have, for example, sold your company but that is the nature of a personal guarantee and we have seen examples of courts enforcing guarantees in these circumstances.

Depending on your buying power, it may not be possible to negotiate the terms of a personal guarantee and the big suppliers are likely to leave the smaller tradies with a 'take or leave it' type ultimatum. If that's the case, your best course of action is to meticulously document every personal guarantee you enter into and keep this 'front of mind' if you are intending to sell the business. In that scenario, the buyer should be required to procure a release from the guarantee as part of the sale process or provide an indemnity against any future claim from the supplier.

WORST CASE SCENARIO

The nightmare scenario for any tradie is losing the family home as a result of a business dispute. And if you are holding the family home under your own name, you are leaving yourself open to that exactly that outcome.

Tax looms large as a major consideration in this context. If your home is in your own name, you can generally claim the Primary Residence exemption for capital gains tax purposes and you will lose that exemption if you move the property into another ownership structure such as a trust. You would also generally need to pay stamp duty upon any such transfer.

One possible way to reduce this risk is to buy the family home in the name of your spouse - on the proviso that your spouse is not themselves a business proprietor and dealing with exactly the same challenges as yourself. You may also be able to claim stamp duty exemptions and reliefs through transferring the family home to your spouse. However, this strategy may not be without risk – for example, if you have funded the mortgage repayments then a creditor may argue that your spouse actually holds the family home on your behalf.

Alternatively, it is sometimes possible to establish more complex structures whereby you can protect the family home through a mortgage in favour of a trust or other entity that you control. This type of strategy should not be implemented without professional advice.

This brings us to a key point when bringing your spouse into the equation: you need to have a clear understanding of which of you is 'playing defence' – i.e. protecting your assets - and which one of you is 'playing offence' – i.e. running the business and taking on any exposure associated with the business. Confusing these roles would entirely defeat the purpose of your strategy.

You don't want a rogue client or supplier making a claim against your business to find that your family home is exposed to that claim.

The classic example of conflating offence and defence is to appoint a spouse as a director of your business while the house is in their name. Directors frequently attract personal liabilities and the list of instances in which directors can be personally liable is growing rapidly: for example, if your business is found guilty of an OH&S breach or a breach of environmental protection legislation or if you personally breach duties under the Corporations Act.

CONCLUSION

The structures which underpin a defensive strategy are often complicated and require professional advice from an expert to implement properly. The basic principles, however, are simple: keep your defensive strategy well clear of your offensive strategy; if you can't avoid personal liabilities such as guarantees, track them meticulously and, above all, remember that what works in a business context is not necessarily going to work in a divorce or a family dispute context. The 'enemy within' scenario is an entirely different topic for another day.

Please note that this article provides general comments and guidance only, and does not take into account your particular circumstances. Always seek independent professional advice before implementing any asset protection strategy.

Martin Checketts
Martin Checketts heads up the Private Advisory Team at national law firm Mills Oakley. He specialises in business succession and asset protection.