Centuria Investment Bonds Strategy # 7

Centuria

Using an Investment Bond to fund a Business Succession Plan

Astute business owners realise that taking the time to put a succession plan in place for their business gives them a clearer picture of the future.

Succession Planning - an essential business planning strategy

Planning ahead for the day that you leave your business is an important part of business planning. No matter what your business is currently worth, owners who plan now for the succession of their business can put themselves a step ahead in ensuring the future success and value of the business.

Astute business owners realise that taking the time to put a succession plan in place for their business gives them a clearer picture of the future. They recognise that it prepares the business for acquisition or extending ownership and ensures that the business will continue to serve its clients when they retire or wish sell down part of their business equity when transitioning to full retirement.

After identifying the appropriate successor(s) for the business one of the fundamental issues for business owners is to seek advice on how to identify and establish an appropriate funding mechanism that is both tax effective and supports any buy/sell or key man arrangements that have been put in place with the proposed successors.

One option is to consider funding the plan using investment bonds which offer several benefits including taxation and protection from creditors in the event of bankruptcy.

Why use an Investment Bond?

A ten year investment bond offers key benefits when used as part of a strategy to fund a business succession arrangement. An investment bond is a tax paid structure that, under current taxation law, pays tax on earnings throughout the life of the bond at a maximum rate of 30%. The proceeds of an investment bond are paid out without any additional taxation after year 10; are protected from creditors while held within the investment bond structure and do not form a part of the estate of the bond owner in the event of death. Upon death, the proceeds are paid directly to the bond owner (if different from the life assured), the bond owner's estate or the nominated beneficiary.

As such, investment bonds can be used successfully to provide the business owner with some certainty of transition of their business interests at an agreed price over a ten year time frame.

Tax Considerations

If the investment bond is withdrawn within the first eight years all of the growth is assessable in the bond owner's income tax return. If withdrawn during year nine, two thirds of the growth is included as assessable income and if withdrawn in year ten, one third of the growth will be assessable. Beyond the ten year period none of the growth is assessable to the bond owner.

Ownership Structure

There are two parties to an investment bond and they are the bond owner and the life insured. In the case of funding business succession, the bond owner will be the business successor – the person who will by buying all/part of the business. The second party - the life insured – will be the current business owner. In the event of the death of the business owner before completion of the ten year period, proceeds from the investment will be paid to the bond owner. Note that as per the above, taxation will be a consideration in such an event for the bond owner (business successor) if a death payment is made prior to the end of year ten.

Will the investment bond saving and investment plan be sufficient

Very likely, in the early years of saving and investing via an investment bond, the accrued balance will not be sufficient to fully fund the purchase, or part of it, in the event that the business owner dies. There could be a substantial shortfall and so the business successor should implement a stand-alone life insurance policy(s) on the life of the business owner to facilitate purchase of the business from the deceased business owner's estate upon his death.

Note that the receipt of life insurance policy proceeds might have tax implications and each situation will require tailored legal advice before the stand-alone insurance policy on the business owner's life is established.

Advantages of utilising a bond structure to fund succession

There are a two key advantages to using an investment bond to fund a business succession arrangement:

1. **There is no additional tax payable on withdrawals after 10 years.**
2. **The proceeds of the investment are protected from creditors in the event of bankruptcy.**

Conclusion

If you are an adviser looking for a tax - effective investment to help your clients fund their business succession plans, then investment bonds offer a potential solution which is accompanied by a range of investment options. When anchored to a well-constructed Buy/Sell Agreement, investing in an Investment Bond enables a business owner to establish an agreed business exit strategy while enabling the successor to accumulate the assets needed for the purchase of their share.

7 Reasons to consider an Investment Bond Structure with Centuria

1. Flexible investment options

Investment bonds allow investors to access many asset classes and provide a market-linked investment vehicle to help meet investment goals.

2. No limit on the investment amount

There is no limit on the amount that can be invested to establish an investment bond. Investors can also make subsequent investments up to maximum of 125% of the previous year's contribution without restarting the ten year period. Investors can choose to start new investment bonds if higher amounts are to be invested.

3. No excess contribution tax

Investment bonds can provide a tax effective means of investing and avoid excess contributions tax that may otherwise apply in the case of superannuation contributions.

4. Flexibility

Investment bonds give investors the flexibility to access funds at any time. This can act as a hedge against restricted access to superannuation.

5. Capital gains tax simplicity

Investment bonds provide simplicity as earnings are automatically reinvested in the bond. This means reinvestment dates do not need to be tracked for capital gains tax purposes. Investors can also switch between investment options without triggering personal capital gains tax.

6. Transfer of ownership/ named beneficiary

The ownership of the investment bond can be easily assigned or transferred at any time. The original start date is retained for tax purposes. This may not be achievable within a company structure without creating tax liabilities.

7. Bankruptcy protection

Investment bonds may offer protection from creditors in the case of bankruptcy (subject to certain rules), which may not be possible through a company structure.

Start investing today.

Simple | Flexible | Versatile

For more information contact Centuria on 1300 50 50 50 or visit www.centuria.com.au/investment-bonds to download the PDS.

CA-CLL-25/02/16-00190