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# Family Business Forum

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Business Transfers

Experiences from Belgium and Western countries

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## SESSION I

How to secure the income of the entrepreneur when he will retire or withdraw from the family business ?

- Case study
- A company owner is retiring and leaves the management function (and possibly the ownership of the company) to his heirs
- How to define the relationship with children and ensure additional income and a « decent life » in retirement ?



## SESSION I

### How to secure the income of the entrepreneur when he will retire or withdraw from the family business ?

- Preliminary comments :
  - sharing experiences
  - necessarily subjective and personal feelings
- Securing an revenue for the founder/ company owner after retirement = is one of the various stages which are part a long term vital strategical issue of the enterprise
- Need to have a STRATEGIC PLAN over TRANSMISSION ISSUE
- Need to formalize agreements in a valid legal and enforceable manner :
  - ➔ Avoids future potential conflicts over
  - ➔ “what was said and what was not said” or
  - ➔ “what was promised or not”

## SESSION I

### How to secure the income of the entrepreneur when he will retire or withdraw from the family business ?

- Need to use reliable technical tools and legal expertise needed : consider investing time and money
- Various options to be considered:
  - Owner keeps the ownership till his decease, but as he leave management function, he gets full or part of the future rights to dividends (“shareholder’s rights to be fixed in a shareholder’s agreement if needed); are there legal instruments that will allow him to keep a (periodical) control of the enterprise and/or to keep the power to appoint or dismiss directors or use veto rights ?
  - Owner sells its business or the shares the company to heirs, but he grants to his heirs sufficient time to pay part of the price over an agreed period (share purchase agreement “S.P.A” with partial payment upon closing)
  - Owner makes a gift of his shares of the company to heirs, but keeps the right to be paid fully or partly with future dividends flows
  - Other possible choices and combined mixed options

## SESSION I

### How to secure the income of the entrepreneur when he will retire or withdraw from the family business ?

- ➔ Identify and verbalize : wishes, realistic business plans, draft agreement and have a healthy communication process
- ➔ Preparation and time needed : from 2 to 3 years process, starting preferably at least 5 to 10 years before the contemplated retirement age
- ➔ Pitfalls of the "Valuation exercise": do not make it "an endless issue"
  - Need to have common assumptions over future;
  - Do not leave the full process in hands of "experts in valuation"
- ➔ Need to reach an agreement over various things and not only about the "value" (or "price")
  - The "envy" of heirs to take over (motivations)
  - Will the owner keep any control over the management or not ? To which extent ?

## SESSION I

### How to secure the income of the entrepreneur when he will retire or withdraw from the family business ?

- How to proceed ? (continued):
  - Create a positive environment about the transmission issue
  - Integrate the "emotions" in the process
  - Anticipate different situations on behalf of the heirs :
    - heirs who are fully active in the business and others non active heirs
    - Make a clear distinction between the income linked to the mere ownership of the family company and the income linked to activity and work of the heir
    - Consider having non active heirs leaving the company or being secured as well
    - Integrate the various tax and legal constraints (example in Belgium for compulsory civil law, tax costs, etc.)

## SESSION I

### How to secure the income of the entrepreneur when he will retire or withdraw from the family business ?

- Keep some flexibility :
  - ➔ future flows to be generated from the family business are uncertain and may range significantly over the time :
  - Need to integrate the financing aspects : realistic business plans need to be prepared in order to assess if the business may generate sufficient net income flows to secure the retiring owner
  - need to fix the minimum future flows to be obtained by the leaving founder
  - Need to share “risks” between leaving founder and heirs
- If appropriate : try to obtain from a non related third party (or non family third party) an offer over the business (being aware of “pro’s and contra’s)

## SESSION I

### How to secure the income of the entrepreneur when he will retire or withdraw from the family business ?

- Key factors for a successful transfer of an enterprise:
  - 1) Leaving owner is discharged from his responsibilities and may find a new role
  - 2) The new manager is competent and motivated (technical skills and human skills)
  - 3) Parties have good relations (high level of confidence, respect and mindset)
  - 4) Clear agreements over the management model and shareholdings issues
  - 5) The new manager builds a team with both non family members and family members active in the company
  - 6) Management is performed in a professional way
  - 7) The transmission results in a correct division of the family estate
  - 8) The steps of the transmission are integrated in a precise planning

## SESSION I

### How to secure the income of the entrepreneur when he will retire or withdraw from the family business ?

- Illustrations and lessons learned from Belgian experiences
- Debate and Questions and answers

## SESSION II

### The « Family » Council : why, how and when ?

- Case study
  - After the decease of the company founder and owner, the business is inherited by the family members – his legal heirs, who are now supposed to jointly bring decisions about the company's future.
  - Why a family council ?
  - How to form the family council ?
  - When ?
- What are the important elements all family council members should agree on, in order to avoid the possible disputes in the future ?

## SESSION II

### The « Family » Council : why and how ?

#### A) Formation of a Family Council

First fundamental remark : the non legal aspects of transmission = MYTHS & TABOOS

→ : what is typical on all family business .

- The **three dimensions** of a family business → in full interdependence : possible conflicts between roles and interests

	3 different registers	Needs	How	Method
1.	It is an enterprise	to be managed	Professionalism	structure
2,	It is a family	To be compliant with emotions	Communications skills between different generations	resilience
3.	It is an asset	A return – a valuation-protection	Process of benchmarking	Expert's assistance

## SESSION II

### The « Family » Council : why and how ?

#### A) Formation of a Family Council

- Why ?
  - Need to organize and structure the relationships between the family members with respect to the daily management of the enterprise and its future development
  - In case of conflicts → danger for the continuity of the family business that may disappear very quickly → negative consequences for all family members
  - Need to avoid some pitfalls linked to communication issues
  - Need to address the complexity of legal and tax rules
  - Need to “channel” emotions and subjective feelings

## SESSION II

### The « Family » Council : why and how ?

#### A) Formation of a Family Council

- How ?
  - Some references in “Corporate Governance rules “(Code “Bysse 2”)
  - Written document “ Family Charter”
  - To be agreed and signed by all family members
  - Legally binding or not ?
  - Flexible to a certain extent ?
- When ?
  - It should be done and prepared ideally before the decease of the owner/founder, or prior his retirement

## SESSION II

### The « Family » Council : why and how ?

#### B) Key topics to be addressed in the “Family Charter”

- 1) Key family values and continuity of those values : a “vision” - the “culture”
- 2) Transfer of the shares and the liquidity
- 3) Rules regarding careers of family members within the enterprise (as manager or not)
- 4) Rules regarding income and other benefits for family members active in the enterprise
- 5) Setting up of financial objectives and strategical plans
- 6) Training and coaching of family members
- 7) Rules regarding communication of information between family members – balance between transparency & confidentiality
- 8) Procedures → decisions process making with the Family Council : Chairman and secretary – periodical meeting (once a year at least)

## SESSION II

### The « Family » Council : why and how ?

#### B) Key topics to be addressed in the “Family Charter”

9) Roles and scope of actions of the Family Council → role of General shareholders assembly → role of Board of Directors

10) Defining who may become and stay member of the Family Council: what about spouses of family members ?

11) Majority rules for specific decisions such as :

- Appointment/dismissal of directors;
- Recruitment/ dismissal of family members:
- Dividend policy – Investments policy
- Amendments to the Family Charter;
- Resolution of conflicts;

12) Agreements about votes with the legal bodies : shareholder’s meetings and board of directors’ meetings – need to check legal validity  
– local company law prohibitions

## SESSION II

### The « Family » Council : why and how ?

#### B) Key topics to be addressed in the “Family Charter”

13) Rules to be eligible to management bodies (needed experience, competences and diplomas, etc.)

14) Rules about transfer of shares:

- prohibition to sell (limited in time)
- justified by the genuine interests of the company

15) Clauses regarding admission/ refusal/ exclusion to quality of member of the Family Council

16) Representation rules to meetings of Family Council

17) Rules : place and roles to non-family members in the enterprise

Etc ... tailor-made exercise

→ Family Council has various roles:

- Place for communication – dialogue & consultation – stability & balance



## SESSION III

### Selling and/or buying a business : how to prevent the various risks ?

- The risks for vendor/ buyer → Preliminary remarks
- The life cycle of the process : from day 1 to closing deal
- **Preparation phase** : SWOT analysis (Strengths- Weaknesses- Opportunities-Treats) – Business Plan – preliminary assessment of value – Identify the deal breakers ? What is “icing on the cake” ?
- **Selling/Buying phase** :
  - a) Non disclosure agreement (“NDA”)
  - b) Letter of Intent covering : timing-due diligence- exclusivity- binding character or not and to which extent – some milestones about price-declaration and warranties- continuity in good faith-end of negotiation
  - c) Sale purchase agreement and closing conditions

## Letter of intent “L.O.I.”

### Vendor

- Confidentiality to be described extensively
- Need to stick to a timetable and deadlines
- Interest to grant or not exclusivity to a candidate buyer?
- Proceed to an assessment of the quality (financial and reputation) of the candidate buyer

### Buyer

- Need to avoid unprecise intentions and to create unreasonable hopes : could constitute a fault
- respect of non disclosures and confidentiality obligations : need to control the process of internal and external persons involved in the process
- Importance to obtain an exclusivity period !

## Due diligence

### Vendor

- Need to take care of an efficient process to enable respect of confidentiality : data rooms, communications, secured exchange process of documents
- Due diligence process may not jeopardize the normal life cycle of the business activities: controlling time and scope

### Buyer

- Importance of the preparation phase process in order to define : a) priorities b) scope of the due diligence (general or focused)
- Need to control efficiency and costs of due diligence : methodology to optimize both internal and external expert resources

## Sale Purchase Agreement « S.P.A. »: Preamble - Recitals

### Vendor and Buyer

- Allows to contextualize preliminary facts and contacts
- may serve to clarify points or,
- avoid misunderstandings
- express goals of respective parties

### Vendor and Buyer(cont'd)

- Insert comments regarding motivations and/or economical justifications of the transaction as well as the ways and forms agreed between the parties
- In some cases it may have legal consequences

## SPA : conditions of closing

### \* buyer gets financing

#### Vendor

- Get transparency from buyer in his financing process → to exclude risk of misconduct in case of withdrawal
- put pressure on buyer to be liable to agreed deadlines (with penalties and interest charges if not observed)

#### Buyer

- Needs to anticipate all financing aspects with his bank (interest charge rate, duration of credit, warranties, etc.)
- Optimize financial flows and treasury (including tax costs and incentives)
- Validation of financial leverage
- Check if financial assistance schemes are possible : use money of the target company to finance part of the acquisition

## SPA : conditions of closing

### \* management issues

#### Vendor

- Eventually : key personnel and workforce must continue to work a certain period – if not : effect on payments modalities and warranties
- Check possible split of price (earned income or capital gain on shares ?)

#### Buyer

- Secure position and/or conditions for leaving of key management
- Tax and social optimization opportunities to be explored (options on share, incentive plans, etc.)

## SPA : conditions of closing \* shareholder's agreement

### Vendor

- In case one of the vendors becomes part of the team of management after the sale or in case a vendor keeps a minority shareholding
- Choice open to have (or not) a link between the obligation to continue to work within the target during a certain period and price to be paid (or its timing)

### Buyer

- allows to articulate conditions of the deal in view of achieving continuity of some key people
- Way to set up preemption rights, conditions of agreement for new shareholders, rights of forced exit, etc.
- Possibility to reduce part of price against grants of options on shares of buyer

## SPA : conditions of closing \* other topics

### Vendor

- Secure prolongation of suppliers key agreements, major and strategic distribution agreements, etc.
- Renewal of permits, authorizations or other administrative or legal documents

### Buyer

- Get the vendor's commitment about period between end date of last approved accounts and closing date
- Allow withdrawal in case of negative outcome from due diligence process audits and audits

## SPA : price and payment arrangements

### Vendor

- Set up the objectives :
  - Price or payment modalities?
  - Balance Cash and/or earn-out ? Cash and vendor's credit ?
  - Level of price against timing or minimum or no warranty ?
- Consider performing an external audit before any contact with candidate buyer

### Buyer

- Cash optimization during the cycle : try to split payments in slices dated
- Need to secure the effectivity of warranties : escrow account, etc..

## SPA : Effects of closing \* various

### Vendor

- Discharge of directors mandates
- All responsibilities with respect to legal, financial and tax have to be left to buyer
- Take care of potential legal rules resulting in liability to payments of taxes, social contributions, or VAT of the target on behalf on vendors

### Buyer

- Sequential legal formalities : dismissal and appointment of directors, general shareholders meeting, ,share register, etc.
- Matching responsibility of vendors until closing
- Need to clean private arrangements and to pay out vendor's debts towards the target upon closing

## SPA : commitments upon closing

### Vendor

- Declarations and confirmations : sincere, complete and honest
- Non concurrence : geographical limits - duration
- Confidentiality
- Obtain relief for personal cautions given to cover targets debts

### Buyer

- Strictly execute payments obligations and others obligations
- Obtain possibility to resell as soon as possible
- Obtain relief of cautions given by the target for private debts of the vendor

## SPA : Warranties

### Vendor

- Secure effective payments of differed sales price (third party deposits, reserve ownership resolution clause, etc.)
- Special care while drafting terms of warranties, common blocked accounts, etc.

### Buyer

- Obtain classical warranties to indemnify damages for buyer for period before closing : operational risks, compliance with tax ,social , environmental laws, etc.
- Need to set-up deadlines, period covered by vendor's warranties, procedure of recourse in case of claims

## SPA – conflictual issues

### Vendor

- Procedures for conflict solutions and prevention: conciliation, mediation, (third party experts tiers, mediator, ...)
- importance of notifications et delays
- Evidencing facts and documentation of the process : burden of proof !
- Arbitrator or usual judicial jurisdictions?

### Buyer

- Same concerns and vendors, but :
- Anticipate documentation process of proof :
  - Stipulate presumptions;
  - Assessment process of factual elements
  - Danger of referring simply to the due diligence performed by buyer

## Signatures and valid representatives

### Vendor

- Importance to check upfront the identity and valid mandates of persons facing-up as representatives of candidates buyers
- → written evidence

### Buyer

- Make sure persons involved from vendor's side are well empowered to conduct as sale process
- Check of proxies and mandates

## Enclosures to SPA

### Vendor

- Interesting to provide full and complete documentation
- Provide full list of potential litigations and/ or claims from third parties against the target
- Unknown risks ?
- Investing in a set up of qualitative legal compulsory documentation → Added value in transmission process

### Buyer

- Be attentive to communications from vendor assumed to be complete and sincere : « *the devil is in the details* »
- Presumption : what is not disclosed = responsibility of vendor
- Need to document that factual elements are known by buyer or are deemed to be known by buyer

## As conclusions : lessons learned

### Seller's concerns

- Knowing more about the buyer's agenda
- Communication = key : create envy
- Managing the selling cycle
- Provide to buyers solutions to face legal and tax risks inherent to the target's business
- Anticipate psychological dimensions and play with your "paintbrush"

### Buyer's concerns

- Importance of gathering valid and reliable preliminary information about the target
- Set on beforehand the acceptable limits and conditions of a successful take-over
- Consider daring proposals that you would normally not accept if you were the other party's advisor



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