



The Balancing Act for Business Owners

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Balancing the issues that confront small business owners is an extremely difficult task. This paper has been prepared to identify the key issues that may affect business owners who wish to maximise the full value from both their business and personal wealth.

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Persons reading this material should obtain appropriate professional advice relevant to their particular circumstances in evaluating its accuracy, currency, completeness and relevance for their purposes.

Foreword

Running a successful business and managing the growth of personal wealth is not easy for business owners of Small to Medium-sized Enterprises (SME).

Most business owners are so busy working within their business that they do not have many opportunities to look outside their business for wealth creation.

As a result, many of these business owners may simply not afford the retirement lifestyle they desire.

Market research and independent interviews confirm the challenge time-poor business owners have in balancing professional and personal wealth management.

This paper explains how this situation arises and outlines steps business owners can take to regain control of their financial future.

The solution is a new form of partnership. A partnership that constantly reassesses best financial directions, that brings accountability to best achieve financial objectives, that increases capabilities and options with appropriate expertise and that is built upon a trusted relationship. This is the role of a SME's Principal Adviser.

Executive Summary

Small business owners face a challenge that is unique to business owners.

Many small business owners will fall short financially and not achieve the maximum return from their business because of the dual challenge they face in running a successful business whilst managing and growing their personal wealth.

This is the harsh reality for a time-poor and ageing market looking to financially reap the rewards of years of hard work and dedication.

Given the growing complexity of the financial services industry, business owners can benefit from using the skills of a professional adviser to help navigate their way through the maze of financial issues.

But it is absolutely essential they employ the right adviser.

The right adviser is one who understands the unique relationship between business and personal wealth decisions so a comprehensive strategy can be designed to include:

- business planning
- tax
- estate planning
- retirement
- succession planning
- investment management
- debt structuring
- cash flow management

However, identifying such a financial adviser is not an easy task.

Some financial advisers focus only on one piece of the puzzle, such as superannuation or investments, and therefore do not adequately take into consideration a client's complete financial situation.

The sad truth is the traditional financial services industry is ill equipped to assist business owners in managing and growing their wealth because they focus on transactions rather than building long term, consultative relationships.

What business owners need are financial planners who specialise in their market, who understand that a large portion of business owners' personal wealth is in the value of their business or the property it occupies and that this can create a lot of unique wealth creation issues needing specialist planning. Therefore a complete approach to financial planning is required, collaborating with a range of experts to help manage the complete financial situation.

Such financial advisers operate as Principal Advisers. They use a consultative approach with their clients and provide customised choices and solutions specifically tailored to individual client needs.

Introduction

Most business owners are so busy working within their business that they do not have time to properly plan their financial future.

“They get so consumed with their job and their career and their clients, so what gives is their own personal financial planning,” says Jeff Patterson, Chair of The Executive Connection.

“A lot of owners feel somewhat guilty that they take time away from their business to focus on their personal affairs.”

Jeff Patterson, The Executive Connection

This time-poor characteristic of business owners seriously limits their ability to maximise the full value of their business.

Ironically, the business is their livelihood yet it is the factor that most limits a business owner’s ability to successfully plan financially for the future. Most business owners often have the ability to manage their affairs but the question that often needs to be addressed is, “is this the best use of their time, talent, skills and resources?”

“They are inclined to only think of their business and how they can increase its wealth without thinking of how they can take money out and create personal wealth,” says John Menzies, Chair of The Executive Connection.

“This limits their options in how they retire. They’re not as free in their choices.”

But of course there is a real need for business owners to build wealth outside of the business to provide some finances for retirement. In some cases, it may make more sense financially and strategically to divest a business owner’s assets, and invest outside of the business rather than building all the assets in the business. Business assets can be at risk of attack from predators and/or creditors.

“By putting more money into your business you may not get a return,” says Menzies. “You need to weigh up if you are better off to put the money elsewhere to build wealth.”

The result is a frustrating situation common to many business owners.

“I have recently sold part of my business,” says Chris, a business owner and member of The Executive Connection. “As a result, I now have more than 50% of my wealth in passive investment assets yet I spend more than 95% of my time still managing my business interests, which I am experienced in doing, and 5% of my time attending to my personal assets, which I have no experience with, and this scares me.”

Preventing this business owner from seeking financial advice was his concern over:

- who to trust
- whether a financial adviser would act in his best interests; and
- what control he would maintain over his own financial future.

Challenges affecting business owners today

1 Recruiting and retaining staff

Many business owners are now finding it increasingly difficult to attract and retain good staff.

Macquarie Bank's Economic Report February 2008 forecasts unemployment at 4.1%. Couple this figure with the fact that Generation X and Generation Y expect to have three different careers in their working life, and you have a highly transient workforce.

Given these factors, experts say if you get three years from an employee you are doing well. The X and Y generations have less loyalty to employers, and staff are simply not as concerned with issues such as job security.

While recruiting the right staff has arguably always been a challenge for business owners, a small job market truly means there is even less choice.

"I think unemployment being at record low levels puts a lot of pressure on the entire employment market and therefore that pressure may result in a compromise when hiring staff," says Patterson.

Many business owners are now saying that the lack of suitability in attracting qualified and motivated staff is a major inhibiting factor to the growth and security of their businesses.

Some even say they are forgoing commercial opportunities because of their inability to attract and retain suitable staff.

2 Leveraging the business

In the past, business owners have relied upon borrowing money or refinancing to facilitate expansion and growth. But with volatile interest rates, many businesses could find themselves in a credit crunch.

"Until recently, the credit market has been very loose and financial institutions have been offering a lot of variety of product," says Patterson. "Owners can be seduced by being able to get money too easily. They may not be as rigorous in working out as to how they will repay or in analysing the return on investment from these borrowings."

Even if a business is 100% family owned or in a 50/50 business partnership, this structure may limit their growth because they are totally dependent on cash flow.

"Once you get a successful business formula then what do you do?" asks Patterson. "You are sort of capped-out to some extent because you don't have the resources to grow further than where you are." These challenges feed into the ultimate goal of trying to move a business away from being owner-reliant.

3 Technology and the pace of change

While technological change can significantly enhance the way business owners conduct their business, it also requires a time investment to get the best out of the technology that's available.

The reality is that for many business owners, technology is another drain on an already time-challenged entrepreneur.

It can leave them with even less time to focus on the critical issues of maximising cash flow and correctly structuring their financial strategy so their personal goals are set and aligned with the goals of the business.

Although technology has facilitated improvements in the procedures and operation of many small businesses, it has also sped up the transfer of products and services.

As a result, family business owners in this modern world have to operate much faster to keep pace with the innovations that affect the future viability of their businesses.

A third generation food manufacturing business which has operated in Australia for over 85 years has experienced this challenge first hand.

“Not only must our business now produce a quality product at a reasonable price, it also has to accommodate the changing tastes and habits of Australian shoppers,” says Peter the managing director.

“Meanwhile, two of the major supermarkets basically dictate to us the success of our new products through the control of in-store placement and shelf space fees.”

“More recently, our business has had to compete with a greater push from supermarket chains to establish their own generic brands. This in turn has reduced our manufacturing margins and eroded the benefit of our brand power”.

4 Managing Personal Wealth

Given the factors highlighted above, getting good financial advice can make the difference between living how you want to live and not being able to afford to.

It is worthwhile considering the risk of not getting financial advice.

Tax is an obvious example. In an ever changing legislative environment, the rules around superannuation and tax structures such as discretionary trusts are constantly evolving.

So too is the range of investment products now on offer. Hedging and short-selling are two popular investment techniques, but both have recently been in the spotlight as contributors to the unstable balance sheets of significant blue chip companies.

The current global credit crisis and the collapse of the sub-prime mortgage market, as well as the fallout in equities, property and fixed interest markets all highlight the potential for danger and the complicated nature of investment markets.

And while regulation of the financial services industry has increased since the introduction of the Financial Services Reform Act in 2002, the potential for financial disaster has perhaps become more widely appreciated.

As a result, there has been a real push towards the simplification of superannuation and ensuring financial advisers are properly licensed to advise on particular structures such as Self-Managed Superannuation Funds.

But the onus is still very much on investors to know and understand the investment products they use and the financial strategy to which they agree.

Therefore a lot of what good financial advisers do is educate their clients on financial options and strategies, empowering them to make their own decisions but ensuring these decisions are in context with their stated long term objectives.

5 The Time Trap

Often successful and smart business owners will know they have issues regarding their estate plan or tax structures. However, because it is an important but not urgent matter, it therefore ends up taking a lower priority than the day to day issues in the business.

Even if a business owner feels they *do* have the time to manage their personal financial affairs it may be that they have yet to truly discover what really is the best use of their skills, talent and resources.

Author Wayne Dyer is famous for writing about his work with people with terminal illness. Perhaps his most quotable remark has been that:

“... none of those people, confronted with their final days, said they wished they’d spent more time at the office.”

This could be extended to highlight that no one would regret limiting the time to manage their own investment portfolio.

"I pay someone else to manage my money so I can do all the things I can't pay someone else to do: exercise, go to kids' sports games, spend quiet time at home, take holidays, grow personally, improve my professional skills, enjoy my retirement, volunteer my time to causes, meditate, read great books, have dinner with friends – why would I do anything myself that I could pay someone else to do?" the delegators mantra.

Use the following questions¹ to help you understand what is truly important to you.

Take a piece of paper and write down your thoughts as you answer each of these questions in order.

Question 1:

Imagine you are financially secure, and you have enough money to take care of your needs, now and into the future.

The question is ... how would you live your life? What would you do with the money? Would you change anything? Let yourself go.

Don't hold back your dreams. Describe a life that is complete, that is richly yours.

Question 2:

Consider visiting the doctor who advises you have 5 -10 years left to live. The good part is you won't ever feel sick; the bad news – you will have no notice of the moment of your death.

What would you do in the time left to live? Will this change your life and, if so, in what way?

Question 3:

This time the doctor shocks you with news that you have only one day left to live. Notice what feelings arise as you confront your very real mortality.

Ask yourself: What dreams will be left unfulfilled? What do I wish I had finished or had been? What do I wish I had done? What did I miss?

6 Business Succession

In April 2004, CPA Australia's Small Business Succession and Exits survey² highlighted the continuing trend of business owners looking to leave their businesses in a relatively short time frame.

¹ Questions provided by the Kinder Institute

² To view the Succession Survey go to https://www.cpaaustralia.com.au/cps/rde/xchg/SID-3F57FECB-5875EA2B/cpa/hs.xsl/726_7914_ENA_HTML.htm

Some 40% of surveyed participants said they intended to leave their business in the next five years. Thirty percent of the business owners were over 50 years of age.

As mentioned earlier, leaving a small business is fraught with difficulties. Most businesses are owner-dependent and do not have a succession plan or exit strategy.

The Report findings:

30% believe it would be difficult finding a buyer for their business, mainly due to the specified nature of the business, the expertise needed and the limited market.

Yet despite this, the 2004 survey revealed 50% of business owners planned to use their business as the primary source of funding for their retirement. That is, although the majority of businesses have no exit strategies and are highly concerned over where to find a buyer, business owners continue to rely on their business to finance their retirement.

The report concluded:

Given that many business owners expect some difficulty in selling their business, many business owners may not be able to achieve their expectations to fund their retirement with their business assets.

Of course one of the major challenges with succession is the assumption that a family member will both want and be able to continue the family business.

"Often the parents have the idea that the children will come into the business but the children have seen their parents work seven days a week, 70 hours per week," says Karen Doyle, member of Family Business Australia. "Often the children do not wish to carry on the business."

People's expectations have shifted tremendously. The business owners of tomorrow do not want to be slaves to a business. They understand the importance of a balanced lifestyle that includes family, friends, relaxation, holidays and good physical health.

The Solution

The close link between business and personal wealth management decisions means to get full benefit from an advisory service, business owners need to source a financial adviser who takes a holistic approach to their finances.

Frank and Glenda are a case in point.

They own and operate a real estate and mortgage broking training business. Frank wants to move out of the day-to-day running of the business, while Glenda wants to remain general manager before selling the business within five years.

The couple own two-thirds of the business and the remaining third is owned by Frank's brother. Although the couple agreed to buy-out the brother's share based on current revenue and valuations, they were unsure how to structure the buy-out.

To provide good financial advice to Frank and Glenda, an adviser needs to understand the business issues as well as the couple's personal goals and aspirations.

This requires an in-depth understanding and analysis of a business owner's lifestyle, goals and financial circumstances. This enables the development of a complete and strategic financial plan.

Using a financial adviser in this manner means thinking of the adviser as a personal chief financial officer who helps a business owner make decisions about their money.

A valued financial adviser will help lay the foundations of a business owner's financial house with a personalised wealth plan tailored to their needs. And as a financial architect, a personal chief financial officer can deal modularly with additional components of a business owners overall financial picture.

This might include estate planning, retirement planning, cashflow analysis, business succession and risk management.

Finally, if an adviser is not able to handle any issues in-house, they should have the resources and contacts to assist a business owner in identifying experts who can address these specific needs.

The result is a complete financial plan and management strategy that enables business owners to maximise the full value of their business.

**Winning is not complicated.
People complicate it.
If you surround yourself with
the right people, you win.**

Dick Vermeil
Coach – Super Bowl Champions XXXIV, St Louis Rams

Conclusion

The complexity in the lives of successful business owners makes managing business and personal wealth almost impossible.

Firstly you will need to decide whether you are a 'do-it-yourselfer', collaborator or delegator.

While seeking advice is a possible solution to this challenge, the reality of having a number of disparate advisers with conflicting advice can add to the problem rather than ease it.

What business owners need is a Principal Adviser who takes a leading role and coordinates the different advice professionals.

The advice should be impartial and should help to work through the maze of opportunities and complexities.

The result is a solution that is time efficient, coordinated in its approach and links the business and personal goals of the business owner.

Choosing the right adviser

If you are going to disclose your entire financial picture, including your values, goals, assets and liabilities – and delegate the creation and implementation of a tailored financial plan – you want to work with someone you can trust.

Choosing a trusted adviser is not dissimilar to hiring a key employee to the business. However, be wary of advisers who promote themselves by reference to the industry or organisation awards or recognition they have received. One of the key problem areas for the entire financial services industry is that as a general rule, recognition in

most organisations equates to the level of production or revenue (product sold) which can often be misinterpreted as competency. The ability to sell products or generate billable hours must not be considered the most important factor in determining competency.

The adviser should interview you, not the other way around. During this initial interview process you should evaluate the adviser to determine if he or she can provide you with the access to an 'A' team of collaborative expert advisers. Check that the adviser demonstrates an ability to project-manage all the components of your financial life and ensure effective implementation of the strategies agreed upon.

One of the important challenges when choosing an adviser is to recognise who is truly knowledgeable in a given area versus who is marginally competent.

Even the most independent, self-reliant business owner should be able to realise that the strategies, tactics, tools and timing required to achieving financial goals are complicated and require the interdependent use of expert advisers. Therefore, you will need multiple advisers from a variety of disciplines.

As in most business arrangements, you will pay for what you get, and conversely, probably get what you pay for.

Integrity is a key component in any successful long-term relationship. We should only do business with people of impeccable integrity, whether we are clients, or advisers.

Questions to consider

We have listed below some things to be aware of when interviewing an adviser and questions to help you evaluate your adviser and their team.

- 🌀 Does the adviser seem thorough and detail orientated?
- 🌀 Does this person ask lots of relevant questions?
- 🌀 Is the response to your financial information non-judgmental and supportive?
- 🌀 Does the adviser have a standard process for delivering advice which can be articulated in the first meeting?
- 🌀 Does the administrative support seem efficient?
- 🌀 Does the adviser allow you time to express yourself and listen carefully to what you have to say so as to understand you completely? Do they also hear what you leave unsaid? (Beware if during the first meeting an adviser is quick to jump into strategy discussions or talk technically. This approach is often used by a 'salesperson style' adviser who is keen to demonstrate their knowledge quickly to enable them to introduce and sell a financial product often before fully understanding the context of the issues you may face.)
- 🌀 Does the adviser work with other professionals and can they provide details of these other advisers and their particular expertise?
- 🌀 Can the adviser provide you with client testimonials and case studies of the work they have completed?

Further reference and recommended reading

Values Based Financial planning by Bill Bachrach ISBN 1-887006-03-6

The New Retirementality by Mitch Anthony – ISBN 978-1-4195-3724-0

Seven Stages of Money Maturity by George Kinder –The Kinder Institute

The Wright Exit by Bruce Wright

Copies of this paper are available from www.fitz.com.au

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About Fitzpatricks Dealer Group

Fitzpatricks Dealer Group is a financial services firm dedicated to providing the support, training and tools for its network of branded and non-branded financial advising firms, to deliver a client focussed approach to financial advice.

The group has been built by Advisers for Advisers and supports the development of services valued and sought after by their high net wealth clientele.

Fitzpatricks Dealer Group and their Advising firms provide a strategic level of financial advice for their clients, who consist of business owners, professionals and corporate leaders.

For more information please contact Fitzpatricks Dealer Group.

About the Authors

David Carney is Managing Director and Adviser of Aspect Partners. His mission is to help clients use their wealth to achieve their most important life goals, such as establishing legacies for their families, contributing to their communities or pursuing their passions. He specialises in helping owners of family business build wealth that is independent of their business income.

David is a CERTIFIED FINANCIAL PLANNER™ practitioner, a status that requires comprehensive knowledge and continuing education. He lives in Sydney with his wife, Kylie, and their two children, Hayden and Madison.

Alf Priestley has been in the financial services industry for over twenty years and also holds formal financial planning qualifications.

Over his career, Alf has developed a particular niche and expertise in providing all-encompassing solutions to manage all aspects of the financial affairs of his CEO and Professional clients.

In this, he has worked with some of Australia's leading tax, legal and lifestyle planning specialists, to create strategies and structures that not only build and protect his clients' assets - from creditors and predators, but also enhance their quality of life. As such he has been referred to as a wealth and lifestyle structure specialist.

Alf conducts interactive workshops in which he draws on his experience to share insights, tricks and traps. He provides guidance on how CEOs, business owners and professionals might structure their affairs to more effectively enhance their life and safeguard their wealth and legacy.

Alf currently speaks at a number of key business leaders' forums, and was recently the recipient of an Outstanding Performance Award for a major business owners' group.

Alf has a B. AgSc, DFP, CFP.

David and Alf are both authorised representatives of Fitzpatricks Dealer Group Pty Ltd, ABN 33 093 667 595 AFSL 247 429.