

7 July 2020

::= Captain Cicero

C/- Work Club, L8/99 Elizabeth Street  
Opp. NSW Supreme Court  
Sydney NSW 2000

Email: cc@blueocean.law

Dear ::= Captain,

## **Your Legal Health Check – Issues Identified and Suggested Actions**

Thank you for taking our online Legal Health Check. We have analysed your answers and identified a number of issues for your attention.

This letter provides a summary of those issues and outlines the actions that you should take to remedy them.

### **1 Executive summary**

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The table below sets out the key suggested action items and their priorities.

Where you see a reference to a "*Company Incorporation Pack*", this includes the following actions and documents:

- registration of the new company with the Australian Securities and Investments Commission;
- consent to act as a director for each director;
- consent to become a shareholder, and share certificates, for all initial shareholdings;
- establishment of all required registers (eg, register of members, etc); and
- company constitution.

Issues and Suggested Actions	Documents / Advice Required	Importance
<b>Family</b>		
<p>As you are planning on getting married in the near future, it's worth considering whether it is appropriate to put a Binding Financial Agreement in place before tying the knot. This document is essentially a "pre-nup" and can dictate how your existing and future assets will be divided between you and your partner in the unfortunate event of a breakdown of the marriage.</p>	Binding Financial Agreement	High
<p>We strongly recommend that all loans between family members are documented with formal written loan agreements. Undocumented loans between family members can be a major source of family disputes and can lead to conflict in the administration of wills and estates. These loans are usually documented through short-form loan agreements. Promissory Notes (ie, legally binding IOUs) can be used as well.</p>	Loan Agreements and/or Promissory Notes	Very High
<b>Family trust</b>		
<p>As you are a trustee of your family trust personally, you are exposing all of your personal assets to loss in the event that the trust is subject to litigation. We suggest incorporating a new special purpose company to be the trustee of the trust in order to limit your liability. If you will be a director of that company, we recommend putting in place a Deed of Access and Indemnity (see section 2 of Schedule 1 below) to reduce your personal exposure to legal claims that may be brought against you as director.</p>	<ul style="list-style-type: none"> <li>• Company Incorporation Pack</li> <li>• Deed of Access and Indemnity</li> <li>• Documents to replace you as trustee</li> </ul>	Urgent
<b>Estate planning</b>		
<p>You do not have a will that was prepared by a lawyer. We strongly suggest engaging a lawyer to discuss your family and financial situation and prepare a formal written Last Will and Testament for you that is customised to your personal circumstances. In many cases, including testamentary discretionary trust structures in your will is valuable both from a tax minimisation perspective and also for protecting your hard-earned assets from potential bankruptcy and/or family law claims. See section 3 of Schedule 1 below for more detail about why including testamentary discretionary trusts in your will is important.</p>	Last Will and Testament with testamentary discretionary trusts	Urgent
<p>You do not have an Enduring Power of Attorney. An Enduring Power of Attorney is a special type of power of attorney that appoints one or more persons to make</p>	Enduring Power of Attorney	Urgent

Issues and Suggested Actions	Documents / Advice Required	Importance
<p>financial decisions on your behalf while you are still alive, if you are no longer able to make those kinds of decisions yourself (eg, due to illness or injury). This is an important document that everyone should have.</p>		
<p>You have not set up an Enduring Guardianship. An Enduring Guardianship is an appointment of one or more persons to make medical and health-related decisions on your behalf if you become incapacitated.</p>	Enduring Guardianship	Urgent
<p><b>Existing business structure</b></p>		
<p>You run your business as a sole trader. This is exposing all of your personal assets to loss in the event that your business is sued or goes insolvent. The most common legal structure that provides limited liability is a company. Using a company may also have tax advantages.</p> <p>Additionally, you mentioned that you will have one or more business partners or investors in the future. Using a company will make it much easier to bring in other business partners/investors and manage the co-ownership arrangements.</p> <p>Accordingly, we may suggest setting up a new company to be the business vehicle. If you will be a director of that company, we recommend putting in place a Deed of Access and Indemnity (see section 2 of Schedule 1 below) to reduce your personal exposure to legal claims that may be brought against you as director.</p>	<ul style="list-style-type: none"> <li>• Advice on legal structure for your business</li> <li>• Company Incorporation Pack</li> <li>• Deed of Access and Indemnity</li> </ul>	Urgent
<p><b>Business purchase</b></p>		
<p>You haven't yet conducted a full legal due diligence process in respect of the business to be acquired.</p>	Full legal due diligence on the business to be acquired	High
<p>You are contemplating buying a business by way of an acquisition of assets. A formal written Business Sale Agreement containing the main terms and conditions that will govern the transaction needs to be prepared. This agreement should consider all of the important terms described in section 4 of Schedule 1 below.</p>	Business Sale Agreement	Very High
<p>The following additional documents are required in order to formalise the agreement for the purchase of the business by way of an acquisition of assets:</p> <ul style="list-style-type: none"> <li>• <b>Board resolutions of the vendor</b> – Resolutions of the directors of the vendor authorising it to sign the</li> </ul>	<ul style="list-style-type: none"> <li>• Board resolutions of the vendor</li> <li>• Board resolutions of the purchaser</li> </ul>	Medium

Issues and Suggested Actions	Documents / Advice Required	Importance
<p>Business Sale Agreement and Deeds of Novation (see below re novation of contracts).</p> <ul style="list-style-type: none"> <li>• <b>Board resolutions of the purchaser</b> – Resolutions of the directors of the company that will be purchaser authorising it to sign the Business Sale Agreement and Deeds of Novation (see below re novation of contracts).</li> <li>• <b>Powers of Attorney</b> – Powers of attorney may be required if any of the individuals who are to sign documents are unavailable at the relevant time.</li> </ul>	<ul style="list-style-type: none"> <li>• Powers of Attorney for signing of documents (if necessary)</li> </ul>	
<p>The following additional documents are required in order to complete the purchase of the business by way of an acquisition of assets:</p> <ul style="list-style-type: none"> <li>• <b>Transfer of Lease</b> – As the business leases premises that you need or would like to retain, it will be necessary to enter into a tripartite agreement with both the vendor and the lessor for the lease to be transferred to the purchaser.</li> <li>• <b>Novation of contracts</b> – As the business has contracts that you need or would like to retain, it will be necessary to enter into a tripartite document (called a "Deed of Novation") with both the vendor and each of those counterparties for the purchaser to take over the vendor's position in the contract.</li> <li>• <b>New employment contracts</b> – As the business has employees whom you need or would like to retain, it will be necessary to enter into new Employment Contracts with them.</li> <li>• <b>New independent contractor agreement</b> – As the business has staff who are engaged as independent contractors and whom you need or would like to retain, it will be necessary to enter into new Independent Contractor Agreements with them.</li> </ul>	<ul style="list-style-type: none"> <li>• Transfer of Lease</li> <li>• Deeds of Novation for transfer of contracts</li> <li>• Employment Contracts for employees who will remain in the business</li> <li>• Independent Contractor Agreements for independent contractors who will remain in the business</li> </ul>	Very High
<p>You propose to purchase the business through a company. That company needs to be incorporated. If you will be a director of the company, we recommend putting in place a Deed of Access and Indemnity (see section 2 of Schedule 1 below) to reduce your personal exposure to legal claims that may be brought against you as director.</p>	<ul style="list-style-type: none"> <li>• Company Incorporation Pack</li> <li>• Deed of Access and Indemnity</li> </ul>	High
<p>As ownership of the business to be acquired is to be shared, it is strongly advisable to put in place a formal written Shareholders' Agreement between all initial shareholders to</p>	Shareholders' Agreement	Very High

Issues and Suggested Actions	Documents / Advice Required	Importance
govern how the business will be run and the dynamics of the co-ownership arrangements.		
<b>Equity capital</b>		
<p>The business has previously raised equity capital through the issue of securities. It also plans to raise further equity capital from investors in the near future. The following legal documents are required:</p> <ul style="list-style-type: none"> <li>• <b>Resolutions of the issuer</b> – Resolutions of the issuer approving the issue of the securities and authorising it to sign the new certificates.</li> <li>• <b>Certificates</b> – New certificates for all securities. The register of holders of the securities also needs to be updated.</li> <li>• <b>Applications from investors</b> – Forms signed by the investors applying for the securities and agreeing to be bound by the constituting documents of the issuer.</li> <li>• <b>Deeds of Accession</b> – Signed documents (typically called "Deeds of Accession" or "Deeds of Adherence") pursuant to which the investors are joined as parties to the co-ownership agreement between the holders of securities.</li> </ul>	<ul style="list-style-type: none"> <li>• Resolutions of the issuer approving the transactions</li> <li>• Certificates for the issued securities</li> <li>• Applications from the investors</li> <li>• Deeds of Accession from the investors</li> <li>• Review of the documentation for previous capital raises to ensure that the above documents were properly put in place</li> </ul>	High
<b>Loans</b>		
<p>The business has borrowed money from investors but none of those loans have been properly documented with formal written loan agreements.</p> <p>All loans should be properly documented with formal written Loan Agreements / Loan Facility Agreements (as applicable). It is important to ensure that the terms are comprehensively and clearly documented in order to avoid disputes. Formal documentation is also required in order to avoid debt/equity issues with the ATO (see paragraph 5 of Schedule 1 below for more detail).</p>	Loan Agreements and/or Loan Facility Agreements (as applicable) for all existing loans	Urgent
<p>The business plans to borrow additional funds from investors in the near future. Legal documentation has not yet been prepared for those anticipated loans.</p> <p>All new loans should similarly be documented with formal written Loan Agreements / Loan Facility Agreements (as applicable) to ensure that the terms are comprehensively and clearly documented and to avoid debt/equity issues with the ATO (see paragraph 5 of Schedule 1 below for more detail).</p>	Loan Agreements and/or Loan Facility Agreements (as applicable) for all loans	Very High

Issues and Suggested Actions	Documents / Advice Required	Importance
<b>Staff</b>		
<p>Although you don't have any employees at present, you are contemplating hiring employees in the near future. We strongly suggest putting in place a formal written Employment Contract for all future hires. This is crucial to ensure that the potential for legal disputes with employees is minimised and to protect the business from unfair competition and misuse of its confidential information. We recommend that every Employment Contract should consider the important matters described in section 6 of Schedule 1 below.</p>	<p>Employment Contracts for all future hires</p>	<p>Medium</p>
<p>The business should have a formal written Independent Contractor Agreement with every staff member who is engaged as an independent contractor. This is crucial to ensure that the potential for legal disputes with them is minimised and to protect the business from unfair competition and misuse of its confidential information. We recommend that every Independent Contractor Agreement should consider the important matters described in section 9 of Schedule 1 below. We strongly suggest putting in place a formal written Independent Contractor Agreement with all existing and future staff who are engaged as independent contractors.</p>	<p>Independent Contractor Agreements for all current and future staff who are engaged as independent contractors</p>	<p>Urgent</p>
<p>You are contemplating letting go one or more members of staff in the near future and you have some concerns that they may seek to bring claims against the business. If they will agree, you should enter into a formal written Deed of Terminating and Release with each of them to terminate their contract with the business and release all claims that may exist between the parties.</p>	<p>Deeds of Termination and Release (potentially multiple)</p>	<p>High</p>
<p>You mentioned that the business currently has an existing equity incentive scheme in place for remunerating staff with equity. In order to ensure that the incentive scheme complies with the requirements for tax deferral (see section 8 of Schedule 1 below for more detail), we recommend reviewing the existing scheme.</p>	<p>Advice on existing equity incentive scheme</p>	<p>Medium</p>
<p>Every business should have an official set of written policies and procedures that applies for all staff. Not having a comprehensive set of written policies and procedures in place creates uncertainty as to how personnel matters are to be dealt with and exposes the business to potential legal claims from employees and independent contractors as well damages that may result from staff misconduct. We recommend putting in place an Employee</p>	<p>Employee Handbook of policies and procedures</p>	<p>Very High</p>

Issues and Suggested Actions	Documents / Advice Required	Importance
Handbook that includes all of the policies and procedures discussed in section 7 of Schedule 1 below.		
<b>Customers/Clients</b>		
The business has a standard set of terms and conditions for the supply of its services but that documentation was not prepared by a lawyer. In our experience, it is dangerous for businesses to attempt to prepare their own terms and conditions (eg, by copying and pasting from other businesses) without legal assistance. Accordingly, we strongly suggest that the existing set of standard terms and conditions be reviewed. In particular, it is important to ensure that they address the key terms discussed in section 10 of Schedule 1 below.	Review of existing Terms of Business	Very High
<b>Website</b>		
The website does not have a formal Privacy Policy. This is especially important as the business operates an online store and likely collects personal information about customers through the online ordering process.	Privacy Policy	High
The website does not have a formal set of Website Terms of Use. Again, this is especially important as the business operates an online store.	Website Terms of Use	Very High
<b>Commercial agreements</b>		
<p>The business is contemplating the termination of one or more of its existing commercial agreements. All such terminations should be formally documented and, if there are no lingering disputes between the parties, that documentation should include a mutual release of all claims.</p> <p>If there are any lingering disputes between the parties, we suggest exploring whether it may be possible to settle those disputes via a Deed of Settlement and Release (see below).</p>	Deed of Termination or Deed of Termination and Release	Medium
The business is contemplating amending one or more of its existing commercial agreements. All such amendments should similarly be formally documented.	Deed of Amendment	Medium
A number of the transactions contemplated above would typically involve significant legal and/or commercial negotiations. Indeed, you confirmed that the business is involved, or expecting to become involved, in significant	<ul style="list-style-type: none"> <li>• Confidentiality Agreements</li> <li>• 1-Page NDAs (as applicable)</li> </ul>	High

Issues and Suggested Actions	Documents / Advice Required	Importance
<p>negotiations. Such discussions often necessitate the sharing of confidential and commercially sensitive information between the parties.</p> <p>We recommend putting in place a strongly drafted and full-form Confidentiality Agreement in respect of all such negotiations.</p> <p>Where you have concerns that requiring a long-form Confidentiality Agreement might stifle negotiations, we would suggest proposing a simpler, short-form NDA to provide at least some level of protection. We can prepare a short-form NDA that fits into a single page, which is easily digestible by other parties to the negotiations without their requiring extensive legal review.</p> <p>The business does not have any template confidentiality/non-disclosure agreements yet.</p>		
<p>As the business is contemplating entering into one or more joint ventures with other businesses that may involve profit-sharing (as opposed to revenue-sharing) arrangements, we suggest a discussion about legal structuring for the proposed joint ventures. Where a joint venture more closely resembles a new, separate business (ie, rather than a mere collaboration in furthering the existing businesses of the parties), it is generally preferable to structure the arrangement as an incorporated joint venture. This involves establishing a new joint venture vehicle, typically a company, where the profit-sharing arrangements are handled through the ownership of shares in that new company.</p> <p>The documentation required in order to establish a new incorporated joint venture with a company as the operating vehicle includes the documents needed to incorporate the new company, a Deed of Access and Indemnity (see section 2 of Schedule 1 below) for each director of the new company and a Shareholders' Agreement to govern the co-ownership arrangements.</p>	<ul style="list-style-type: none"> <li>• Advice on the legal structure for the proposed joint ventures</li> <li>• Company Incorporation Pack</li> <li>• Deed of Access and Indemnity</li> <li>• Shareholders' Agreement</li> </ul>	High
<b>Intellectual property ("IP")</b>		
<p>The business needs to apply to register its business name, logo and slogan as a trademark in Australia.</p>	<p>Trademark applications</p>	<p>Very High</p>
<p>The business has developed inventions, technology or designs that are or may be patentable/registrable. You have confirmed that such IP is important to the value of the business. However, some of that IP has not yet been patented/registered. We suggest, as a minimum, a discussion about what such IP may exist and the legal and</p>	<ul style="list-style-type: none"> <li>• Review of IP that may be patentable/registrable</li> <li>• Legal and commercial strategy in respect of IP protection</li> </ul>	<p>Very High</p>

Issues and Suggested Actions	Documents / Advice Required	Importance
<p>commercial strategies that may be adopted in protecting it. If desired, patent/registration applications can then be made.</p>	<ul style="list-style-type: none"> <li>Patent/registration applications to be made, if desired</li> </ul>	
<p>It appears that some or all of the persons who were involved in developing the IP of the business have not yet formally assigned their interests in that IP to the business. This is especially concerning because the business relies upon inventions, technology or designs that are or may be patentable/registrable. For example, in respect of patents, without an effective assignment, the individual inventors may be held to be the owners of the invention even if it was developed in the course of their employment with the business. Additionally, you have advised that copyright material forms a substantial part of the value of the business. There may be a similar risk in respect of copyright material, depending upon the terms on which the creators were employed/engaged. The individual creators of copyright material may also have so-called "moral rights" in their works (eg, the right to be named as the creators, the right not to have the material amended, etc) which can only be waived through a formal written agreement.</p> <p>Accordingly, we suggest entering into a formal written document called a "Deed of Assignment of Intellectual Property" with each person who was involved in developing the IP of the business.</p>	<p>Deeds of Assignment of Intellectual Property (possibly multiple)</p>	<p>Very High</p>
<p>The business utilises IP that is owned by third parties. Similarly, the business licenses some of its own IP to third parties. For all such IP licensing arrangements (other than software that is widely published and licensed through End User License Agreements), a formal written Intellectual Property License Agreement covering the terms described in section 11 of Schedule 1 below should be entered into.</p>	<p>Intellectual Property License Agreements (possibly multiple)</p>	<p>High</p>
<p>As IP is valuable to the business, to insulate it from potential claims against the business, it is prudent to place the IP in a separate special purpose company that is not owned by the main operating entity. The only purpose of that separate company is to hold the IP. The operating entity then licenses the IP back from that separate special purpose company. That way, provided that the legal structuring is done correctly, if legal claims are brought against the operating entity, the IP is not at risk because it doesn't form part of the assets of the business.</p> <p>Implementing this will involve:</p> <ul style="list-style-type: none"> <li>establishing a new company to hold the IP;</li> </ul>	<ul style="list-style-type: none"> <li>Company Incorporation Pack</li> <li>Deed of Access and Indemnity</li> <li>Deed of Assignment of Intellectual Property</li> <li>Intellectual Property License Agreement</li> </ul>	<p>Very High</p>

Issues and Suggested Actions	Documents / Advice Required	Importance
<ul style="list-style-type: none"> <li>• transferring the IP from the operating entity to that new special purpose company with a Deed of Assignment of Intellectual Property; and</li> <li>• then licensing the IP back to the operating entity with an Intellectual Property License Agreement.</li> </ul> <p>If you will be a director of the new special purpose company, we would recommend putting in place a Deed of Access and Indemnity (see section 2 of Schedule 1 below) to reduce your personal exposure to legal claims that may be brought against you as director.</p>		

The above is a summary only. More detail can be found in Schedule 1 below and can be provided upon request. Please note the limitations of this report set out in section 12 of Schedule 1 below.

## 2 Next steps

We will give you some time to review and consider the problems and solutions identified in this report. We will then be in touch to arrange a strategy session to answer any questions that you may have and formulate an action plan for remedying these issues.

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In the meantime, if you have any queries in respect of the material in this report, please don't hesitate to contact us.

Yours sincerely,

**James D. Ford**  
Principal Solicitor

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## 1 What you told us about yourself

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### Family

- 1.1 You are not currently married or in a de facto relationship. You are planning to get married in the near future.
- 1.2 There are loans between members of your family that have not been documented with formal written loan agreements.

### Family trust

- 1.3 You have an existing family trust. You are a trustee in your personal capacity.

### Investment properties

- 1.4 You own one or more investment properties, including both residential and commercial real estate. You hold those investment properties in your own name personally. You anticipate entering into one or more commercial leases in the near future. You're not sure whether they will be retail or non-retail leases.

### Estate planning

- 1.5 You do not have a will that was prepared by a lawyer.
- 1.6 You do not have an Enduring Power of Attorney or Enduring Guardianship.

### Existing business structure

- 1.7 You run a startup business as a sole trader. The business is not run through a corporate group.

### Business purchase

- 1.8 You are contemplating buying another business in the near future. The business to be purchased is owned by a company. You are proposing to buy the assets. You have not yet conducted full legal due diligence on that company. You are proposing that the purchaser will be a new company incorporated specifically to hold the assets. That company has not yet been incorporated.
- 1.9 The Business Sale Agreement has not yet been prepared. The business to be acquired has premises leases that you need or would like to retain. The business to be acquired has other existing commercial contracts that you need or would like to retain. Some of the existing employees of the business will be transferring. The business has staff who are engaged as independent contractors and who will be transferring.

### Ownership of the business

- 1.10 You will share ownership with others in the future. It is contemplated that ownership of the business to be purchased will be shared with others. The business has previously raised equity capital through the issue of securities. It plans to raise further equity capital from investors in the near future.

## **Debt funding**

- 1.11 The business has borrowed money from investors. None of those loans have been documented through formal written loan agreements. The business plans to borrow further money from investors in the near future. Legal documentation has not yet been prepared for those anticipated loans. None of the loans are secured or supposed to be secured.

## **Staff**

- 1.12 The business does not have any existing employees. The business is expecting to hire new employees in the near future.
- 1.13 The business currently engages staff as independent contractors. It does not have formal written services agreements with all existing independent contractors. The business is planning to engage new staff as independent contractors in the near future. It is also contemplating terminating the engagements of some current staff who are engaged as independent contractors in the near future.
- 1.14 You are concerned that some of the terminated staff may have claims against the business.
- 1.15 The business has put in place a formal equity incentive scheme for staff. It does not have a formal set of written policies and procedures.

## **Goods and services**

- 1.16 The business provides both goods and services. It does not generally enter into customised agreements with particular clients. Rather, it relies upon a standard set of terms and conditions that applies broadly to all customers/clients. The standard set of terms and conditions was not prepared by a lawyer.

## **Website**

- 1.17 The business operates an online store. The website does not yet have a set of Website Terms and Conditions or a Privacy Policy in place. The online store does not have a Returns Policy.

## **Commercial agreements**

- 1.18 The business is contemplating terminating one or more of its existing commercial agreements. It is also contemplating amending one or more of its existing commercial agreements.
- 1.19 The business is involved, or expecting to become involved, in significant negotiations. Those negotiations include potentially entering into joint ventures with other businesses that involve a profit-sharing arrangement.
- 1.20 The business does not have any template confidentiality/non-disclosure agreements.

## **Intellectual property ("IP")**

- 1.21 The business has not yet registered its business name, logo or slogan as a trademark in Australia. The brand forms a substantial part of the value of the business. The business has developed inventions, technology or designs that may be patentable/registerable. Not all such IP has been registered. It's possible that some of the people who were involved in developing that IP have not formally transferred ownership of that IP to the business. Inventions/technology/designs form a substantial part of the value of the business.
- 1.22 Copyright material also forms a substantial part of the value of the business. It's possible that some of the people who were involved in developing that copyright material have not formally assigned that IP to the business.

- 1.23 The business utilises IP that is owned by third parties (excluding software packages that are widely published and licensed through End User License Agreements). The business licenses its own IP to third parties. None of those licensing arrangements have been formally documented through written IP License Agreements.
- 1.24 As the business is not conducted through a corporate group, we assume that the intellectual property of the business is not held in a separate special purpose company. We note that intellectual property forms a material part of the value of the business.

### **Regulatory matters**

- 1.25 The business has an ABN and you do not need help with registering for GST. All business names have already been registered with the Australian Securities and Investments Commission. All website domain names have already been registered.
- 1.26 The business requires licenses or permits in order to operate legally. You feel certain that all licenses and permits that are required for the operation of the business have been obtained and are current.

### **Disputes**

- 1.27 The business is not currently involved in any disputes other than debt recovery. Similarly, the business is not seeking to recover a debt of \$20,000 or more from any company.
- 1.28 You are not currently involved in any disputes personally.

## **2 What is a Deed of Access and Indemnity?**

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- 2.1 Directors have various duties under the *Corporations Act 2001 (Cth)* (*Corporations Act*) to act in the best interests of the company. Usually, this means acting in the best interests of the shareholders, but these duties can also require directors to take into account the interests of other stakeholders like employees and creditors. The duties include acting with care and diligence, exercising their powers in good faith and for a proper purpose and preventing the company from trading when insolvent. The problem is that directors often have to make difficult decisions that involve judgement calls with limited information in circumstances in which the stakeholders have conflicting interests, so it's not always clear whether they have properly discharged all of these duties.
- 2.2 In some cases, directors can be personally liable for breaches of these duties. This can include civil and/or criminal penalties under the Corporations Act, legal costs incurred in defending themselves in regulatory investigations and/or legal proceedings and even being personally liable for debts of the company. A Deed of Access and Indemnity is designed to help directors defend themselves from personal liability that may arise from their conduct as directors. It ensures that they are given access to the books and records of the company and also indemnifies them from such personal liability. It will typically also require/permit the company to take out, and pay for, directors and officers (often abbreviated to "D&O") insurance on behalf of the director – this is a special type of business insurance policy that insures against such liabilities and costs.

## **3 What are testamentary discretionary trusts and why are they important?**

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- 3.1 A testamentary discretionary trust is a discretionary trust that is created pursuant to a person's Last Will and Testament. A discretionary trust is a structure in which:
- (a) assets are held by the trustee(s) for the benefit of one or more beneficiaries who are typically individuals within a broadly defined family tree; and

- (b) the trustees have complete discretion as to which persons, among that wide class of potential beneficiaries, will receive distributions of income and/or capital from the trust. Unlike a unit trust, which is a fixed trust, the potential beneficiaries under a discretionary trust have no fixed entitlement to any assets of the trust.
- 3.2 There are two main reasons why it is valuable for estate assets to be placed into testamentary discretionary trusts rather than passed to the beneficiaries in their personal names directly:
- (a) **(asset protection)** where you incur debts in your own name, assets that you hold personally can be used to satisfy those debts. Placing ownership in the hands of a trustee that is a separate legal entity (typically a special purpose company incorporated purely to act as trustee) takes those assets out of your hands and insulates them from your creditors.  
  
With a cleverly drafted will and carefully crafted trust terms, where a beneficiary is involved in a marriage or de facto relationship that breaks down, this can also help to protect the assets from claims by the beneficiary's former spouse; and
  - (b) **(tax flexibility)** income earned by the trustee from the trust assets – importantly, including capital gains – can be "streamed" to beneficiaries who are in lower marginal tax brackets. For example, income can be passed through to stay-at-home parents, adult students and even minor children who otherwise have little or no income. In that way, overall tax on the income from the assets can be minimised.
- 3.3 There are other advantages as well – eg, where estate assets would otherwise pass directly to a beneficiary under the will who is a foreign resident for Australian tax purposes, CGT that would otherwise be triggered by that transfer can be avoided by instead placing the assets into a testamentary discretionary trust of which that foreign person is a beneficiary.

## **4 What terms should be in a Business Purchase Agreement?**

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### **Warranties and disclosure**

- 4.1 When buying a business, the biggest challenge facing the purchaser is to know as much as possible about the business before buying it. The purchaser can gather information during an investigative due diligence process that takes place before the agreement is signed – however, much of the information that is important to the purchaser can only be discovered if the vendor discloses it.
- 4.2 To elicit that disclosure, the purchaser should seek to include comprehensive warranties in the Business Purchase Agreement. Warranties are essentially statements about the business that the vendor assures the purchaser are true as at the time when the agreement is signed and often again at the time when the transaction is completed. Where comprehensive warranties are included, the vendor is usually able to notify the purchaser of exceptions to those statements before the agreement is signed. From the perspective of the purchaser, including comprehensive warranties can thereby pressure the vendor to disclose important matters of which the purchaser would not otherwise be aware and which can dramatically affect the valuation and risk profile of the business. Standard form business purchase contracts are typically woefully inadequate in this regard.

### **Specific indemnities**

- 4.3 Where due diligence investigations and warranty disclosures reveal that the business may incur significant liabilities in the future in respect of particular matters, the purchaser may seek to include specific indemnities from the vendor. By providing an indemnity, the vendor takes on full responsibility for those liabilities if and when they eventuate.

## Conditions precedent

4.4 Where the purchaser requires a lease of premises to be transferred or a new lease to be granted, standard form business purchase contracts will usually make completion of the transaction conditional upon the transfer of lease or new lease being granted. However, they often fail to address other crucial prerequisites that the purchaser should require as conditions precedent to the transaction completing— eg:

- (a) conclusion of due diligence investigations to the satisfaction of the purchaser;
- (b) key employees and/or contractors accepting employment/engagement with the purchaser;
- (c) the consent of other contractual counterparties, especially where the contract cannot be assigned without such consent;
- (d) regulatory approvals having been obtained; and
- (e) no events occurring in the period between signing and completion that may have a material adverse effect on the business (this can even extend to include changes in market conditions),

etc. This should be a key area of focus for the purchaser.

## Conduct of the business between signing and completion

4.5 Where conditions precedent are included, there will usually be a gap between the time when the business purchase agreement is signed and the time when the transaction completes. During that period, while the parties are waiting for the conditions precedent to be satisfied, the purchaser will want to ensure that the vendor continues to operate the business in a prudent manner and does not undertake any conduct that could strip value out of the business. To achieve this, the Business Purchase Agreement should include comprehensive obligations and limitations regarding the conduct of the business during that period. This includes, for example, requiring the vendor to:

- (a) continue to operate the business as usual;
- (b) comply with all laws and regulations;
- (c) maintain insurance policies;
- (d) not induce employees/contractors to leave the business;
- (e) not provide any excessive benefits to employees/contractors;
- (f) not terminate any key contracts;
- (g) not undertake any significant new borrowings; and
- (h) not purchase any significant new assets,

etc. This is another area in which standard form business purchase contracts are frequently inadequate.

## Restraints

4.6 There is little sense in buying a business if the vendor can simply 'set up shop' again and compete against you in the same markets. To prevent that, the purchaser should demand strongly-worded non-solicitation and non-compete obligations in the Business Purchase Agreement:

- (a) non-solicitation provisions seek to prevent the vendor from poaching any customers/clients, staff members or contractual counterparties (eg, suppliers, distributors, etc) from the business after the transaction completes; and
- (b) non-compete provisions seek to prevent the vendor from being involved in any competing business within particular geographic areas for a specified period of time after the transaction completes.

As such restraints can be difficult to enforce in practice, it is important for the drafting to create as many different combinations of duration and geographic scope as possible.

## **5 Debt/equity issues**

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Where capital is provided to the business ostensibly in the form of a loan, there is a risk that the ATO may instead treat it as an investment of equity unless certain requirements are met. This can affect whether, for example, amounts paid by the business to the investor are treated as dividends (which are taxable to the investor and non-deductible for the business) or loan repayments/interest, which have different tax consequences. Whilst there are a number of factors that need to be taken into account, making the duration of the loan shorter than 10 years can assist with avoiding such a reclassification.

## **6 What terms should be in an Employment Contract?**

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### **Type of employment and duties**

- 6.1 Every employment contract should specify the nature of the employment (ie, full-time, part-time or casual), the duration of the employment (eg, indefinite or for a specified period) and the duties and responsibilities of the employee. A comprehensive description of the duties and responsibilities is crucial when it comes to assessing the employee's performance for remuneration reviews and/or any termination of the employment.

### **Remuneration**

- 6.2 It is important to clarify whether the employee's stated salary/wages are inclusive or exclusive of superannuation and additional amounts such as allowances, leave loadings, shift loadings, overtime and penalty rates. Also consider what expenses of the employee will be reimbursable and whether any discretionary monetary bonus may be added based on performance.

### **Performance and remuneration reviews**

- 6.3 Detailed provisions should be included addressing when and how the employee's performance will be reviewed, what assessment criteria will apply and what disciplinary action may be taken in the event of underperformance or misconduct on the part of the employee.

### **Non-solicitation and non-compete**

- 6.4 Also consider putting in place reasonable non-solicitation and non-compete provisions for staff who will have access to any proprietary know-how or key suppliers/customers of the business:
  - (a) non-solicitation provisions seek to prevent a departing employee from poaching any customers/clients, other staff members or contractual counterparties (eg, suppliers, distributors, etc) from the business; and
  - (b) non-compete provisions seek to prevent the employee from being involved in any competing business for the duration of employment and for a period of time after the employment ends.

- 6.5 Non-compete provisions need to be cleverly constructed to aid enforceability as the enforcement of non-compete provisions in employment contracts is notoriously difficult.

### **Intellectual property and confidentiality**

- 6.6 It is absolutely vital that employees of the business are not able to lay claim personally to any of the valuable intellectual property of the business. To achieve this, every employment contract should include thorough provisions that assign ownership of all of the intellectual property that the employee develops in the course of employment to the business.
- 6.7 Additionally, as employees are inevitably exposed to the inner workings of the business, confidentiality provisions are also extremely important. The confidentiality clauses should be strongly worded to aid enforceability, especially as a breach of confidentiality may provide the business with its only remedy in circumstances in which the non-compete provisions turn out to be unenforceable.

## **7 What matters should be addressed in employment policies and procedures?**

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- 7.1 Every business needs a comprehensive set of employee policies and procedures. These work hand-in-hand with your employment contracts to define the business culture, set expectations and clarify the rules for all employees. Adopting a proper Employee Handbook will help you to meet your legal obligations, enable managers to make reliable decisions and promote a culture of fairness. This can avoid disputes and grievances caused by confusion and inconsistencies in how staff are treated.
- 7.2 Your Employee Handbook needs to be customised to suit the particular environments in which your staff will be working and the tasks they will be performing (eg, dress code, food safety, manual handling, working outside, etc). Depending upon the particulars of your business, some or all of the following policies may be required:

- Code of Conduct
- Dress Code
- Internet Policy
- Recruitment Policy
- Induction Policy
- Training and Development Policy
- Probation Policy
- Occupational Health and Safety Policy
- Alcohol and Drugs Policy
- Equal Opportunity and Anti-Bullying Policy
- Pregnancy at Work Policy
- Flexible Working Arrangements Policy
- Leave Policy
- Parental Leave Policy
- Performance Management Policy
- Performance Improvement Policy
- Summary Dismissal Policy
- Grievance Policy
- Conflicts of Interest Policy
- Intellectual Property Policy
- Environmental Policy

## **8 Employee incentive schemes and tax deferral**

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- 8.1 An employee equity incentive scheme enables the company to remunerate key staff members (employees and/or contractors) with equity. There are 2 main reasons to do this:

- (a) the company can hire key staff members and grow the team without needing to raise funds to pay their wages; and
- (b) giving key staff members a stake in the ownership of the business aligns their incentives with those of the shareholders and helps to motivate them to be loyal to the business and work hard towards increasing its value.

8.2 However, without careful structuring, the employee or contractor may be taxed on the value of the equity incentives in the year in which they receive them, even though the employee/contractor does not receive any money with which to pay that tax at that time. To avoid this unintended outcome, the ATO has made it possible for the payment of such tax to be deferred well into the future, provided that the equity incentive scheme meets certain key requirements. Such schemes are called "tax-deferred employee share schemes". Please note that, also they are referred to as "employee share" schemes:

- (a) the equity incentives can also be in the form of options; and
- (b) the incentives can also be given to staff members who are engaged as contractors.

8.3 A common structure for such incentive schemes is an Employee Option Plan that enables the exercise price of the options to be set at any level, including nil. With this structure, tax on the value of the incentives will be deferred until the earliest of:

- (a) the time when the options have been exercised, there is no risk of forfeiting the resulting shares and there are no ongoing sale restrictions;
- (b) cessation of employment; and
- (c) 15 years from grant.

8.4 In order for the plan to be eligible for such tax deferral, it must be carefully drafted to ensure that the conditions of Division 83A of the *Income Tax Assessment Act 1997* (Cth) are met.

## **9 What terms should be in an Independent Contractor Agreement?**

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### **Scope of the services**

9.1 Just as an employment contract should clearly describe the role and responsibilities of the employee, an Independent Contractor Agreement should comprehensively define the scope of the services and the standards and duties with which the contractor must comply in providing those services. This should include being honest and diligent, maintain professional standards and abiding by the policies and procedures of the business.

### **Deadlines**

9.2 It is important to set clear deadline dates for completion of the services. Time overruns inevitably lead to cost overruns and are a frequent cause of disputes.

### **Fees**

9.3 The parties to an Independent Contractor Agreement have considerable flexibility in crafting the fee structure. Fees may be specified as a fixed price or calculated by reference to hourly rates. A deposit may or may not be payable. If the services are divided into phases, the arrangement may provide for a single fee that applies to all phases or a separate fee payable for each phase. The contractor will be required to provide a tax invoice prior to each payment.

9.4 The contractor should be responsible for its own costs to the extent possible. Reimbursable expenses should be agreed in advance.

## **Intellectual property**

- 9.5 The business will want to ensure that any and all intellectual property created by the contractor in the course of providing the services will be owned by the business. The Independent Contractor Agreement should include comprehensive drafting that vests ownership all of such intellectual property in the business and enables the business to freely use such intellectual property. To the extent that the material produced by the contractor includes literary, artistic or similar works in which copyright may subsist, the agreement should include a waiver of the contractor's "moral rights" (ie, the right to be named as the creator of the material, the right not to have the material amended, etc).

## **Restraints**

- 9.6 As with an employment contract, non-compete obligations in an Independent Contractor Agreement can be similarly hard to enforce in practice. For this reason, the non-compete clauses should be structured as cascading provisions that create multiple combinations of durations and geographical ranges – that way, if combinations with long durations and broad geographical ranges are struck out by the court, other combinations will remain and be enforceable.
- 9.7 Non-solicitation obligations, which prevent the contractor from interfering in the relationships of the business with its staff, customers/clients and contractual counterparties, should also be included.

## **Confidentiality**

- 9.8 If the non-compete obligations turn out to be unenforceable, the business may need to rely upon the confidentiality provisions in the Independent Contractor Agreement to prevent the contractor from using information that it obtained about the business to compete with it. For this reason, we generally advocate for strongly-worded, long-form confidentiality provisions to be included in the Independent Contractor Agreement.

## **Termination**

- 9.9 The business will want the flexibility to terminate the engagement at any time by notice to the contractor. This should be additional to the rights of the business to terminate for misconduct, underperformance or other breach of the agreement by the contractor.

## **10 What terms should be in a Services Agreement?**

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- 10.1 With an Independent Contractor Agreement, the business is the recipient of the services, whereas, with a Services Agreement, the business is the service provider. This means that, from the perspective of the business, the considerations in respect of its terms of business are essentially the inverse of its considerations for an Independent Contractor Agreement.

## **Scope of services**

- 10.2 Whether the business enters into bespoke Services Agreements with each customer/client or operates off the back of a standard set of Terms of Business, the considerations for the business are largely the same – however, the process for defining the scope of the services will be very different. With a bespoke Services Agreement, the scope of the services will need to be specified in the agreement, whereas, when operating with a standard set of Terms of Business, the scope of the services will usually be set out in a separate document such as a quote or pitch/proposal.

- 10.3 The Services Agreement can also be structured as a "master" or "umbrella" document, with the scope and details of each individual engagement being specified in a separate document such as a "job form".

### **Fees**

- 10.4 The service fees may be structured in various ways (eg, fixed price or hourly rates, deposit or no deposit, phases or no phases, etc). From the perspective of the business, the fees charged for out-of-scope work will be of crucial importance. Defining the scope of the services clearly is therefore crucially important, as that will determine whether any particular services are included within the base fee or additionally chargeable as out-of-scope work. We suggest including an hourly rate for out-of-scope work, even in fixed-price engagements.
- 10.5 If possible, the business should require a deposit at the commencement of each engagement. The deposit should be non-refundable in the event that the customer/client breaches or repudiates (ie, abandons) the agreement.

### **Ownership of intellectual property**

- 10.6 In many engagements, the customer/client will require that ownership of all material that the business develops in the course of providing its services will be owned by the recipient. However, that is not always the case, and if the business will be retaining ownership of such material then that should be clearly stated in the agreement.

### **Non-disparagement**

- 10.7 In an age in which the reputation of a business is defined largely through its online reviews, including a non-disparagement clause can help to protect the reputation of the business in the event that an unsatisfied customer/client would otherwise seek to use a negative online review as leverage against the business.

## **11 What terms should be in an IP License Agreement?**

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### **IP rights**

- 11.1 The agreement must clearly and comprehensively define the intellectual property rights to which the license relates. This may include registered IP (such as registered trademarks, patents, etc) and/or unregistered IP (such as unregistered trademarks, copyright, etc). Relevant particulars and detailed descriptions of the IP need to be specified in the agreement.

### **Type and scope of license**

- 11.2 The license may be either:
- (a) exclusive – in which case nobody other than the licensee can commercialise the IP, including the licensor;
  - (b) sole – which is like an exclusive license except that the licensor retains the right to also commercialise the IP; or
  - (c) non-exclusive – in which case the licensor is permitted to commercialise the IP itself and grant further licenses to third parties.
- 11.3 The scope of the license also needs to be clearly stated. The scope can be defined by reference to particular activities, geographical territories, industries and/or goods or services.

## **Duration and termination**

11.4 The duration of the license, which may be perpetual or for a finite period of time, must also be specified in the agreement, along with the termination rights of the parties and the processes that must be followed for termination.

## **License fees**

11.5 The license fees may be structured as a single lump sum, ongoing fixed amounts or royalties based on the revenue generated by the licensee through its commercialisation of the IP. Where the licensee fee is calculated as a percentage of revenue, the relevant revenue metric and the inclusions/exclusions to be applied in calculating it (eg, GST, shipping costs, refunds/rebates, discounts, commissions, etc) need to be carefully considered and defined.

## **Assignment and sub-licensing**

11.6 The agreement should specify whether the licensee is able to transfer the license to a third party and/or grant its own sub-licenses to third parties.

## **12 Limitations of this report**

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### **Your information**

12.1 In providing this report, we have relied upon the information that you provided in our online Legal Health Check form. Our analysis is confined only to that information and we have not undertaken any investigations as to the accuracy or completeness of that information (eg, we have not conducted any searches of any public registers or reviewed any additional documents).

### **Taxation considerations**

12.2 All tax-related information provided in this report is of a general nature only and we make no representation, and can provide no warranty or guarantee, that any particular tax and/or other financial outcomes will be achieved. Tax advice needs to be tailored to your individual circumstances, which requires knowing information beyond that which you have provided to us. You should obtain your own tax advice from a separate tax specialist.

### **Reliance on this report**

12.3 This report is addressed to you (Captain Cicero) only and should not to be shared with anyone else, other than your spouse and professional advisers, without our prior written consent. Nobody should rely upon this report, including you, without first entering into a formal engagement with our firm.