

Risk Management for Businesses

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However, a business owner does not have to accept all risk. A prudent risk management approach will assist a business owner to eliminate unnecessary business risks and give rise to a greater chance of success in business. In this article we discuss some of the most simple ways to manage business risk.

When it comes to mitigating risks in a business, the first thing to consider is the entity used to carry on a business. There are various different corporate entity structures, each with their own advantages and disadvantages. However, both a company and a limited partnership are commonly used because they offer limited

liability. Both entity types enjoy a separate legal personality distinct from the business owner and, accordingly, offer a degree of protection to the individuals behind them. The owner of the business is only liable for the amount of capital they agree to contribute. A business owner may have additional liability, however, where they provide guarantees (for example, to a bank, landlord or supplier).

A dual entity structure provides for the key assets of a business to be held separately to the operating entity, further reducing risk. Under this structure, an entity is created for the purpose of acting as the holding company (HoldCo). The HoldCo operates as a “safe harbour” and owns any valuable assets (such as property, intellectual property, equipment, etc.), with a second entity being created to act as the operating company (OpCo). The OpCo serves as the public face of the business and is where the day-to-day operations occur. As the OpCo undertakes all the trading of the business, it similarly holds all the liabilities and risk for anything that goes wrong.

The HoldCo would allow the OpCo to use its assets by way of a lease or a licence. This means that the HoldCo and all of its assets are protected against creditors or any other liabilities should any legal, insolvency, or other proceedings be brought against the OpCo. If the business gets in trouble, the business owner has the option to sacrifice the OpCo and to continue to hold the valuable business assets.

Another common risk management strategy is to secure shareholder loan funding to the company under a general security agreement. This strategy will only be effective if the business is properly solvent at the time the security is put in place. Having this structure will enable the business owner to rank ahead of some unsecured creditors in the event of business failure. Any such security agreements need to be put in place early and must be registered on the Personal Property Securities Register.

Customers are the lifeblood of the business, but when things go wrong a customer claim or legal proceedings can pose a significant risk for a business. Having robust terms and conditions and/or customer contracts can greatly reduce this risk. Good terms and conditions mitigate risk in a number of ways, including by defining clearly what the business will do or supply, identifying things that the business will not be responsible for, and limiting overall risk (for example through monetary caps and exclusions of types of liability). Terms and conditions should be paired with appropriate insurance policies where cover can be obtained at a cost that is

acceptable to the business.

If you are looking for ways to minimise your business risk, please contact our Paul Tustin or Claudia Riddle.