GOOD MORNING!

Welcome to the

Exiting Your Business Seminar

May 5th, 2016

Crowe Soberman™

Selling Your Business

Presented by:

Neil Maisel, B.Comm, CPA, CA, CBV

May 5, 2016

Selling Your Business

- Getting it ready for sale
- Benefits of Valuing the Business

Selling Your Business

Getting it ready for sale

- Start the wheels in motion several years before you actually want to sell
- Clean up the house
- Consider upgrading the work your accountant does
- Inside or outside buyer?
- Consider/Identify who the buyers are that would most likely be prepared to pay the highest price – Special Purchases
- Prepare reasonable Budgets/Projections/Forecasts

Selling Your Business

Benefits of Valuing the Business

- Need to decide what level of Valuation Report needed
- Valuation by Qualified Business Report Valuator will identify areas of interest for the buyer
- Will serve as roadmap for negotiations
- Provides a head start on the due diligence process

Crowe Soberman™

Questions?

You've found a buyer! ....now what?

By: Elisabeth Colson
B.A.(Hons.), LL.B.

My Focus

- Corporate considerations, from the pre-planning stage to Closing.
- Sabina's presentation will follow and will focus on post-sale tax structuring.

Things to Consider

1. Starting to think about your exit

a) What is motivating your exit?

b) What are your goals?

c) Will you be involved post-exit?

d) Get your house in order

2. Structuring the deal

a) Is it an asset sale or share sale?

Things to Consider (cont'd)

3. The purchase price

   (a) How will you be paid?

4. Due Diligence

   (a) What is it and how does it work?

5. Negotiating the purchase price

   (a) Typical heads of negotiation

   (b) Assumption of liabilities?

Things to Consider (cont'd)

6. Papering the deal
   (a) Starting point
   (b) Conveyancing documents
   (c) Employment agreements
7. For the buyer: Paying for the business
8. Making it public – when and how?
9. Closing

Starting to Think About Your Exit

(a) What is motivating your exit?

(b) What are your goals?

(c) Will you be involved post-exit?

(d) Get your house in order: what needs to be done to optimize your sale proceeds?

Starting to Think About Your Exit (cont'd)

These considerations help form your idea of your "ideal" purchaser, of your own must-have deal points and how you find the purchaser.

All this takes time. Pre-exit planning can take 2 years or more.

Structuring the Deal

(a) Is it an asset sale or share sale?

The fundamental differences and how they impact your due diligence process:

- Asset sale
- Share sale

The Purchase Price

(a) How much do you want, and how will you be paid?

1. Keep your personal goals in mind as you consider these questions.

Due Diligence

(a) What is it and how does it work?

1. Asset sale
2. Share sale
3. Aspects common to both cases

Negotiating the Purchase Price

(a) Typical heads of negotiation

(b) Assumption of liabilities

Papering the Deal

(a) Starting point:

1. Confidentiality Agreement
2. Letter of Intent or Deal Memo

(b) Conveyancing documents:

1. Purchase Agreement
2. Ancillary documents

Papering the Deal (cont'd)

(c) Employment Agreements

1. Asset sale: Purchaser is a successor employer.
2. Share sale: Existing corporation continues as the employer.
3. New employment agreements are encouraged.

Paying for the business

(a) For the buyers: Paying for the business

1. High-level view of bank financings
2. How the vendor can help

Making it Public

(a) Making it public – when and how?

1. The usual options
2. It is a business decision

Closing

Once all the outstanding issues are resolved, all the paperwork is signed and you have your money…..

See Sabina to strategize as to how best to keep as much of it as possible out of the government's coffers.

Devry Smith Frank LLP
Lawyers & Mediators

www.devrylaw.ca

Tax considerations in buying and selling a business

Sabina Mexis, LL.B., TEP

March 9, 2016

Things to consider

1. Structuring the deal – pre sale considerations
   a) Is it an asset sale or a share sale?
   b) Tax considerations
      i. Acquisition of Control
      ii. Loss of CCPC status
      iii. Triggering the Association Rules

Things to Consider (cont'd)

2. Capital Gains Exemption

   a) Eligibility

   b) Multiplying the capital gains exemption

Structuring the Deal

a) Is it an asset sale or a share sale?

A purchase and sale transaction generally involves 3 parties:

1. Vendor
2. Purchaser
3. Target corporation

The tax implications of structuring the deal are significant considerations and may be different for each of the parties to the transactions.

Structuring the Deal (cont'd)

i. Share sale

- offers the potential benefits of a capital gains exemption claimed by the vendor and the possible utilization of non-capital losses by the purchaser but results in some additional administrative complexity due to the deemed year end that arises from the acquisition of control of the target company

Structuring the Deal (cont'd)

ii. Asset sale

- Generally permits the purchaser to achieve a step-up in the tax basis of the assets acquired and avoids a deemed year end but subjects the vendor to potential double taxation at the corporate and at the shareholder level as a consequence of the distribution of after-tax proceeds

Structuring the Deal (cont'd)

b) Tax considerations:

- Share sale: ability to access the capital gains exemption
- Asset sale: purchase price allocation is fundamental as it directly drives the tax implications to all parties on an asset-by-asset basis
  - Vendor will generally want to maximize capital gain and minimize recapture
  - Purchaser prefers to maximize future tax shelter by allocating more value to depreciable assets with the highest CCA rates

Pre-sale considerations

i) Change of control issues on a share sale

- In structuring a share sale, we need to be mindful of the potential for triggering multiple year-ends during the closing process
  - Subsection 249(4) of the ITA deems a year end to have occurred immediately prior to an acquisition of control of a corporation
  - If one of the consequences of a proposed acquisition is that the target corporation will either become, or cease to be, a CCPC, then subsection 249(3.1) can also apply to create an additional year end.

Pre-sale considerations (cont'd)

Acquisition of control

- Subsection 249(4) applies where control of a corporation is acquired by a person or group of persons
- This provision triggers a year end immediately prior to the acquisition of control
- A new taxation year then commences at the time of the acquisition of control
- Subsection 249(4) refers to acquisition of control NOT change of control, therefore a transaction whereby a shareholder loses control, but no other person acquires control, does not give rise to a deemed year end

Pre-closing acquisition of control

- Paragraph 251(5)(b) of the ITA provides that where at any time a person has a right under a contract, in equity or otherwise, either immediately or in the future, and either absolutely or contingently to acquire shares of the capital stock of a corporation, the person shall be deemed to have the same position in relation to control of the corporation as if the person owned the shares at that time
- Where a vendor and purchaser enter into a binding purchase and sale agreement to sell shares of a target corporation at some time in the future, paragraph 251(5)(b) will apply to deem the purchaser to own the shares at the moment the purchase and sale agreement is executed

Pre-closing acquisition of control

- One way to avoid the application of paragraph 251(5)(b) is to not sign the purchase and sale agreement until the actual closing date
- The vendor and purchaser should instead proceed on the basis of a non-binding letter of intent, with the binding APA to be signed at closing
- This is not always a realistic alternative given various business considerations

Pre-closing acquisition of control

- As a result, executing a binding purchase and sale agreement with a prospective closing date can prematurely trigger an acquisition of control for income tax purposes and a number of adverse tax consequences can arise from so doing, including a deemed year end under subsection 249(4)
- The association rules can also unintentionally be triggered which may affect the allocation of the small business deduction and investment tax credits for the taxation year prior to the closing date

Loss of CCPC status

- Signing an APA with a prospective closing date can also result in the premature loss of CCPC status if the purchaser is a non-resident or a public corporation
- For example, an APA with a future closing date may provide the purchaser with a paragraph 251(5)(b) right as of the time that the agreement is signed and delivered and not just on the closing date
- A binding LOI may also be sufficient to trigger paragraph 251(5)(b)

Loss of CCPC status

- In order to avoid the loss of CCPC status on signing, where the buyer is a non-resident or a public company, it may be beneficial to structure the transaction as a “sign and close” whereby no binding agreements are signed until the closing time
- If one of the consequences of a proposed acquisition is that the target corporation will either become, or cease to be, a CCPC, then subsection 249(3.1) can also apply to create an additional year end.

Loss of CCPC Status - EXAMPLE

- TargetCo is a CCPC with a December 31 year end
- On October 1, it enters into a binding LOI to sell all of the shares of TargetCo to an arm's- length non-resident purchaser ("ForeignCo")
- The LOI contemplates a due diligence period during which the definitive agreements would be drafted.
- The closing is scheduled for December 1st
- ForeignCo acquired the TargetCo shares through the use of a single-purpose Canadian acquisition company and amalgamated the acquisition company with TargetCo immediately after closing

Loss of CCPC status – Analysis of example

- As soon as ForeignCo entered into the binding LOI, it had a conditional right to acquire control of TargetCo.
- For the purposes of determining TargetCo's CCPC status, ForeignCo is deemed to own those shares that it has a conditional right to acquire (ss. 251(5)(b))
- Even though actual ownership of the shares remained with TargetCo's shareholders until the closing date, TargetCo ceased to be a CCPC immediately upon the execution of the LOI
- Since there was no actual acquisition of control, subsection 249(4) did not apply on the date of execution of the LOI
- However, since there was a loss of CCPC status on that date, subsection 249(3.1) triggered a year end on October 1st immediately prior to signing the LOI.

Loss of CCPC Status – Analysis of example

- Assuming that the transaction closed as scheduled, there would have been an acquisition of control on December 1st
- By virtue of 256(9), the acquisition of control would be deemed to have occurred at the commencement of the day on December 1st thereby resulting in a deemed year-end at the end of the day on November 30th.
- Furthermore, if the amalgamation agreement did not set out a specific effective time for the amalgamation, then the amalgamation would have been deemed to have occurred concurrently with the acquisition of control resulting in a year end on November 30th.
- If Amalco wanted a calendar year end, there would be another short taxation year from December 1 to December 31.

Triggering the Association Rules

- Signing an APA with a prospective closing date may inadvertently trigger the association rules which also could impact the ability of the target corporation to access the small business deduction and investment tax credits
- Paragraph 256(1.4) is a similar rule to paragraph 251(5)(b) which applies for the purposes of the determination of association.
- Under subsection 256(1.4), where a person has under a contract a right to acquire shares of the capital stock of a corporation, for the purposes of determining whether a corporation is associated with another corporation, the person is deemed to own the shares at that time

Triggering the Association Rules

- It is possible to mitigate the associated corporation risk by, for example, having representations and warranties in the APA that the purchasing corporation is not associated with any other corporations for purposes of the ITA
- Consideration should also be given to the purchaser providing a covenant that if the target corporation does become associated with any corporation in the purchaser group, all concerned parties will take the necessary steps to ensure that allocation of the business limit will be in favour of the target corporation to enable it to claim the maximum small business deduction prior to closing

Capital Gains Exemption

(a) Eligibility

1. Allows a vendor, if qualifying, to receive up to $813,600 (for 2015) of capital gains on the disposition of qualified small business corporation shares tax free
2. First step is to determine whether the share is a share of a “qualified small business corporation” (subsection 110.6(1) ITA)
3. Two-part test:
   - Holding period test
   - Asset test

Capital Gains Exemption (cont'd)

Holding period test:

1. For the 24 months prior to the disposition, a QSBC share must have been owned by the individual, the individual's spouse or common-law partner or a partnership related to the individual; and
2. For the 24 months prior to the disposition, the share may not have been owned by anyone other than the vendor, or a person related to the vendor

Asset test:

1. For the 24 months prior to disposition, the corporation must have been a CCPC, and more than 50% of the fair market value (FMV) of its assets must have been used principally in an active business carried on primarily in Canada by the corporation or a related corporation;
2. At the time of disposition, all or substantially all (90%) of the FMV of assets must be attributable to assets used principally in an active business carried on primarily in Canada

Capital Gains Exemption (cont'd)

(b) Multiplying the Capital Gains Exemption

1. If the taxpayer is contemplating a share sale, then consideration should be given to adding family members as shareholders (either directly or through a family trust) in order to gain access to multiple capital gains exemptions.
2. Provided that the shares of the corporation qualify and all other conditions to claim the CGE are met, the gain can be allocated between each shareholder (or beneficiary of the trust) who could then shelter their portion of the gain with their CGE.

Post-sale tax considerations

(a) Tax elections

Numerous tax elections exist to reduce tax otherwise payable on the sale transaction

- Section 167 *Excise Tax Act* – provides that where a vendor sells a business to a purchaser, they can jointly elect for GST / HST to not be payable on the purchase price
- Requirements:
  - i. Vendor makes a supply of a business or part of a business; and
  - ii. The recipient acquires all or substantially all of the property necessary to carry on the business
- Election must be filed on or before the due date of the purchaser's GST return for the given reporting period

Conclusion

- The foregoing represents just some of the complexities and tax issues that need to be considered in planning for the purchase and sale of a business
- Tax considerations apply at virtually all stages of the purchase and sale process, therefore tax advice before the transaction is entered into is critical.

THANK YOU!

QUESTIONS?

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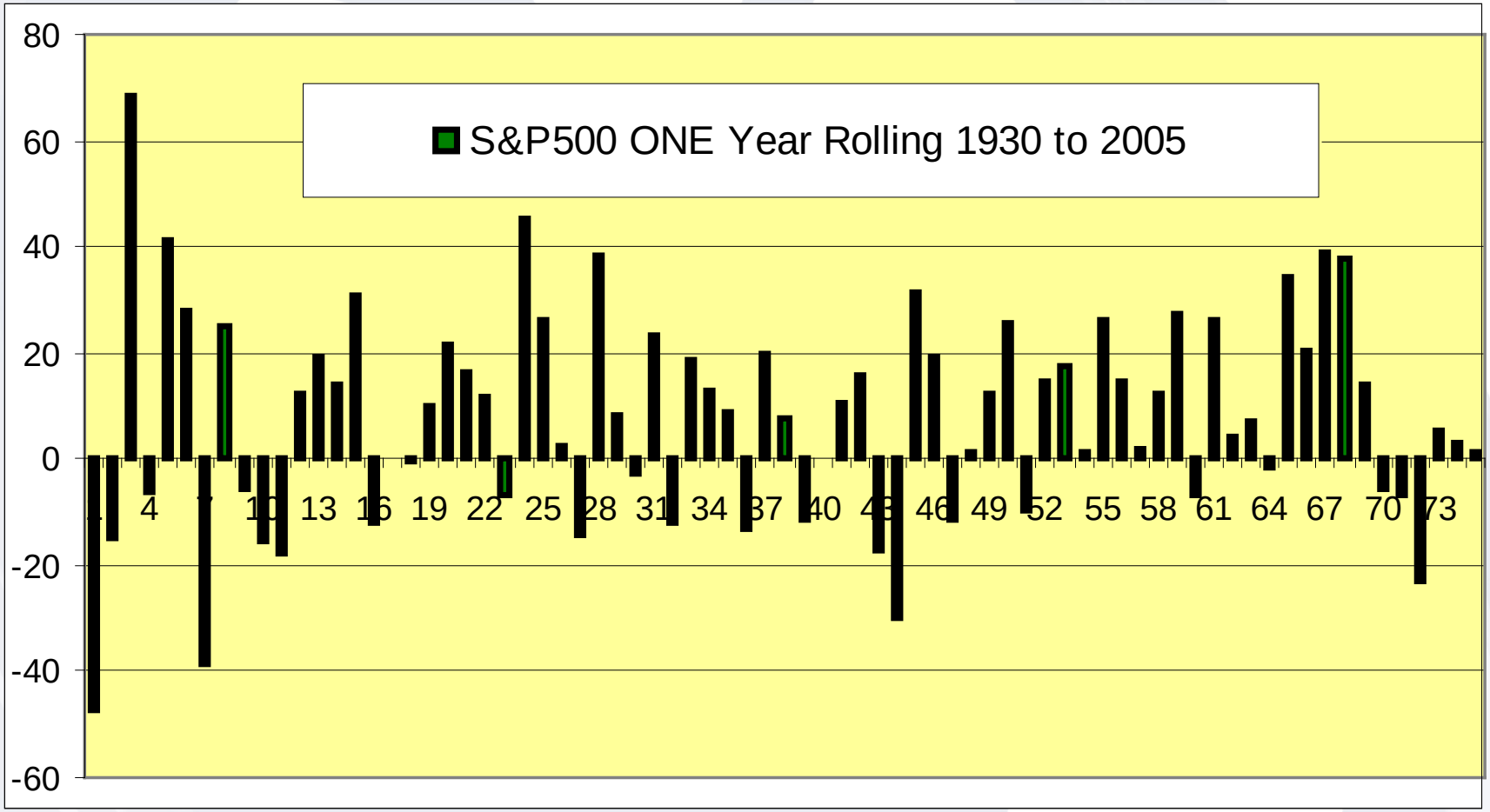
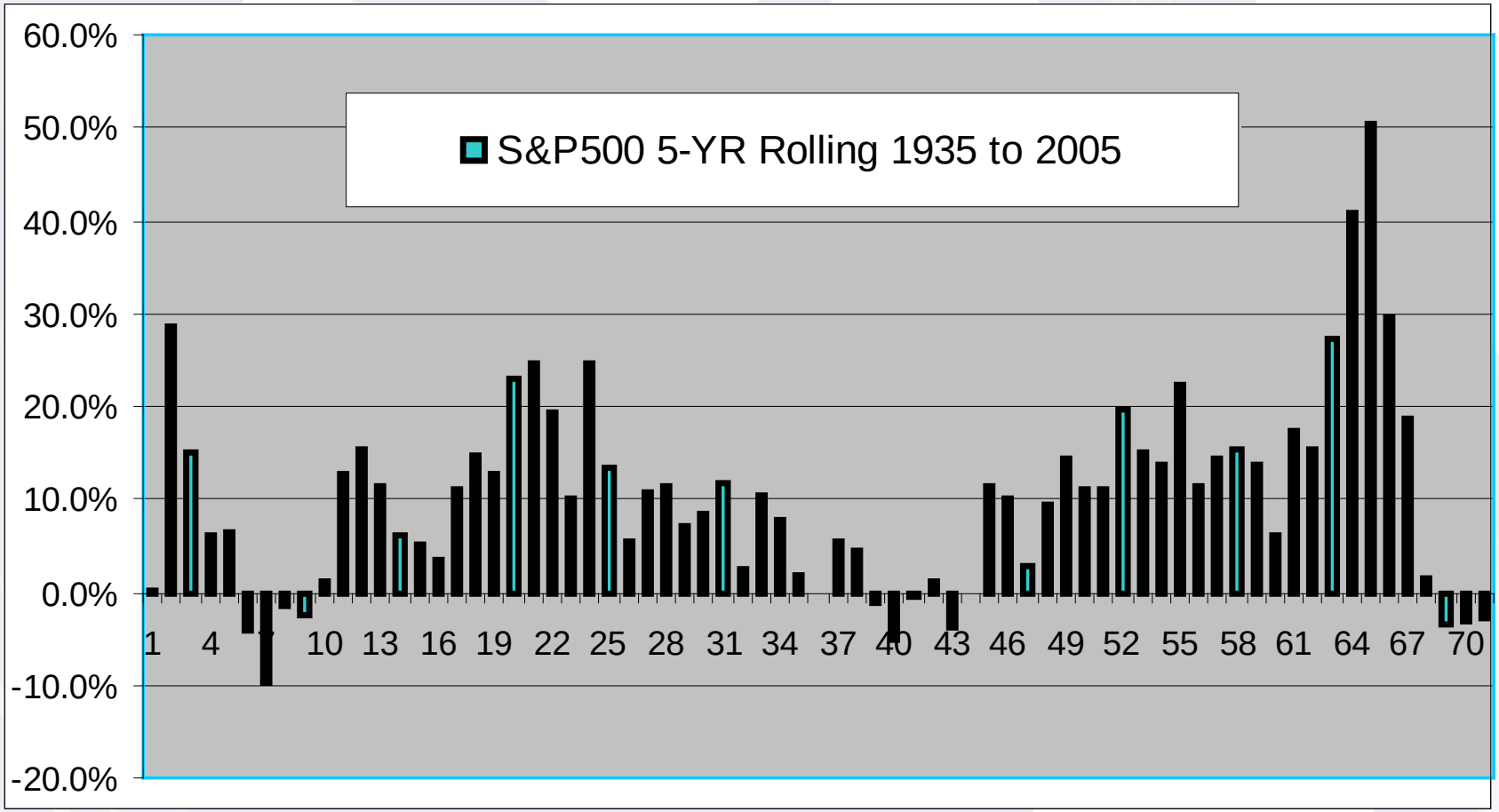
What we will cover

- Why the overwhelming majority of business owners fail to generate decent investment returns outside of their business: failure to understand the stock market
  - Strategies that billionaires use to make money that you can copy
  - How to protect your investments from next down market
- Paying unnecessary tax
  - Strategy of growing your corporate investments tax free

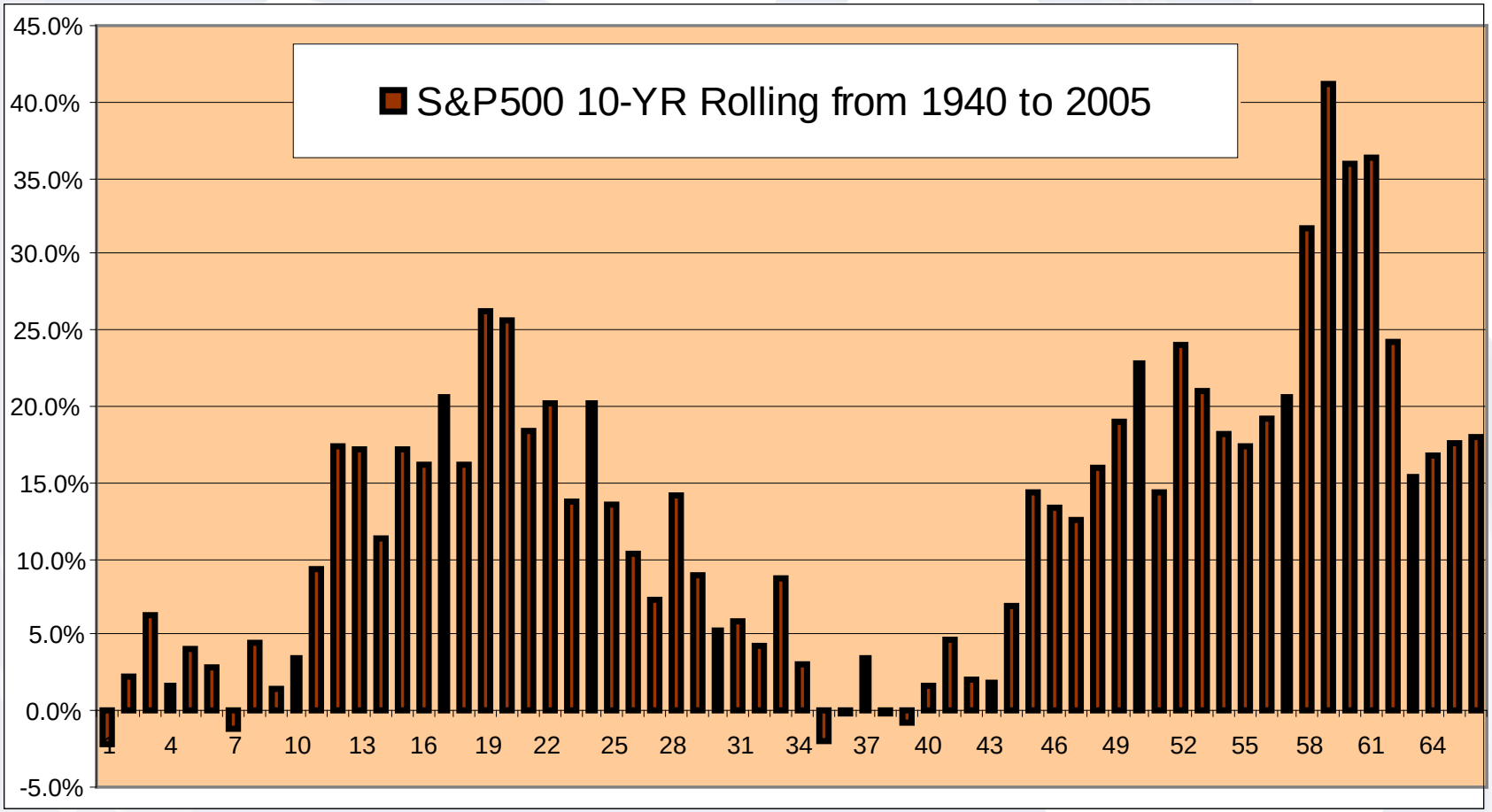
S&P500
ONE YEAR HOLDING PERIODS



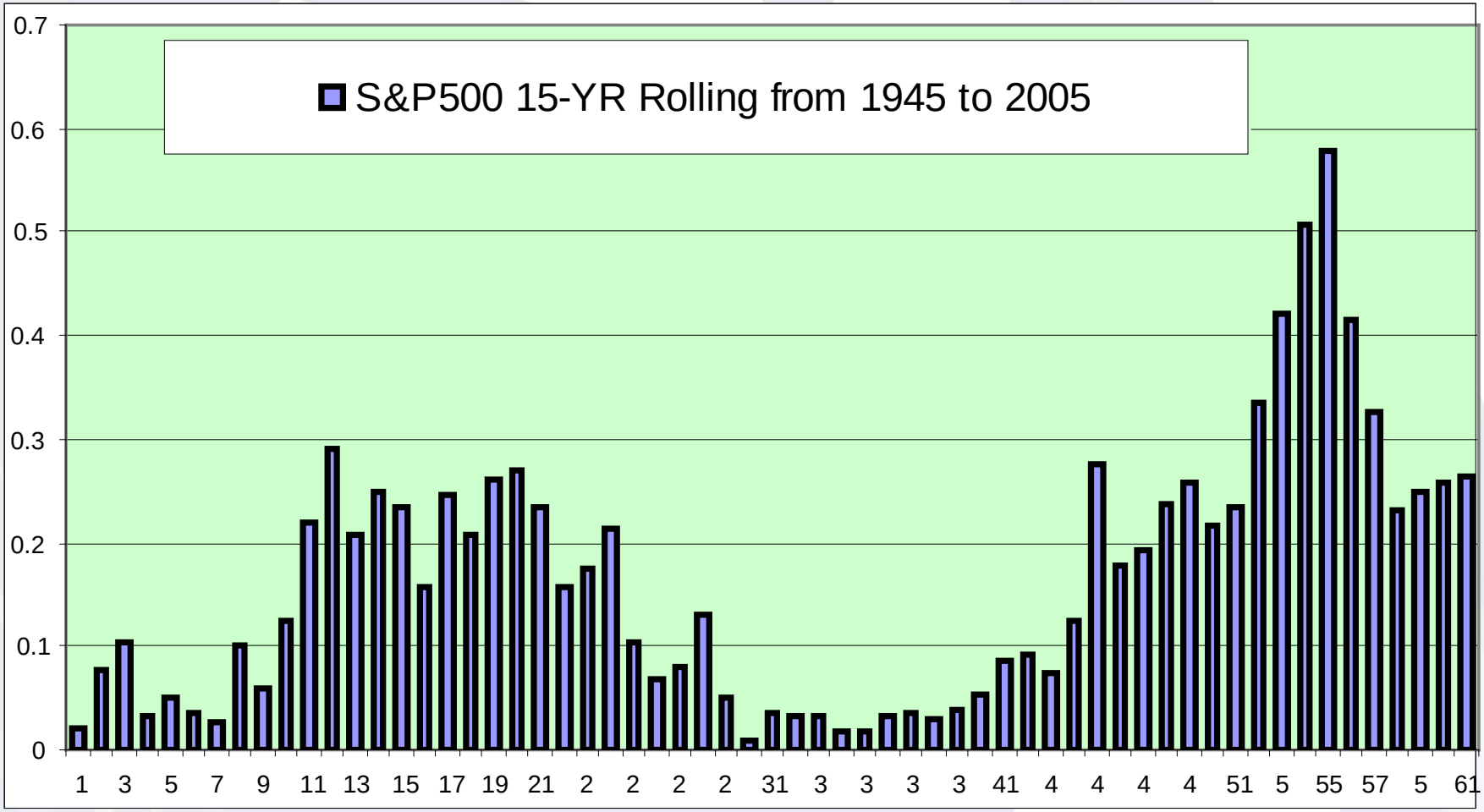
S&P500
FIVE YEAR HOLDING PERIODS



S&P500
TEN YEAR HOLDING PERIODS



S&P500
FIFTEEN YEAR HOLDING PERIODS



Conclusion: To make money in the stock market you need a minimum of a ten year time frame.

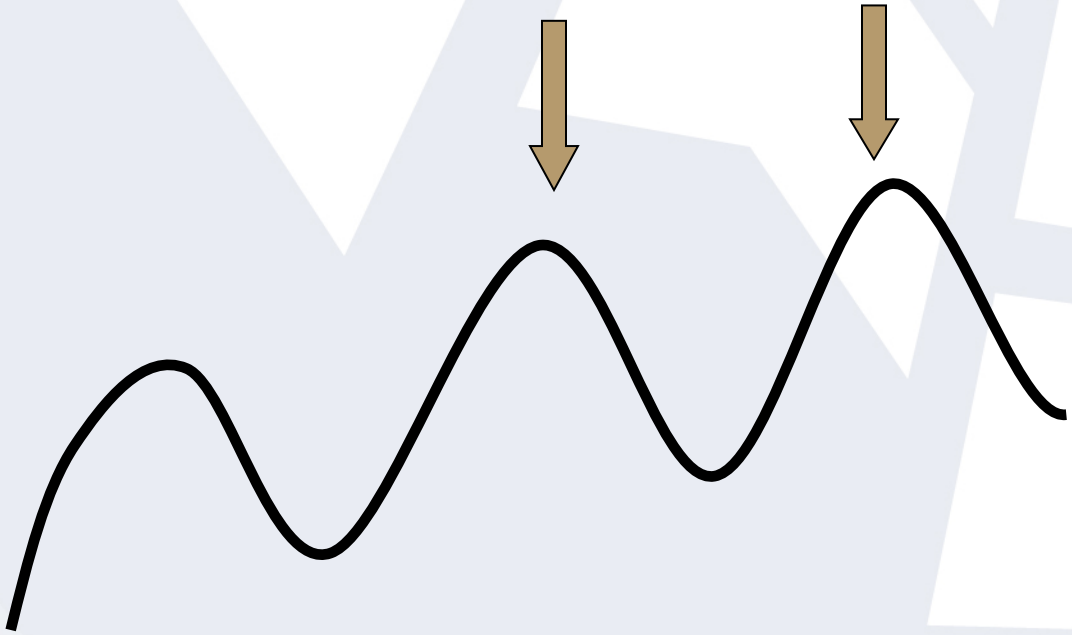
WHY OWN STOCKS?

- Stocks have out-performed every other asset class over any longer period of time (15 years) including bonds, cash, T-bills and **real-estate!**
- Since 1963 the TSX has returned 10.03%
- Best rolling 12 Month Period: 89.9%
- Best Calendar Year: 44.8% (1979)
- Worst Calendar Year: -32% (2008)
- % Positive Calendar Years: 73%
- % Negative Calendar Years: 27%

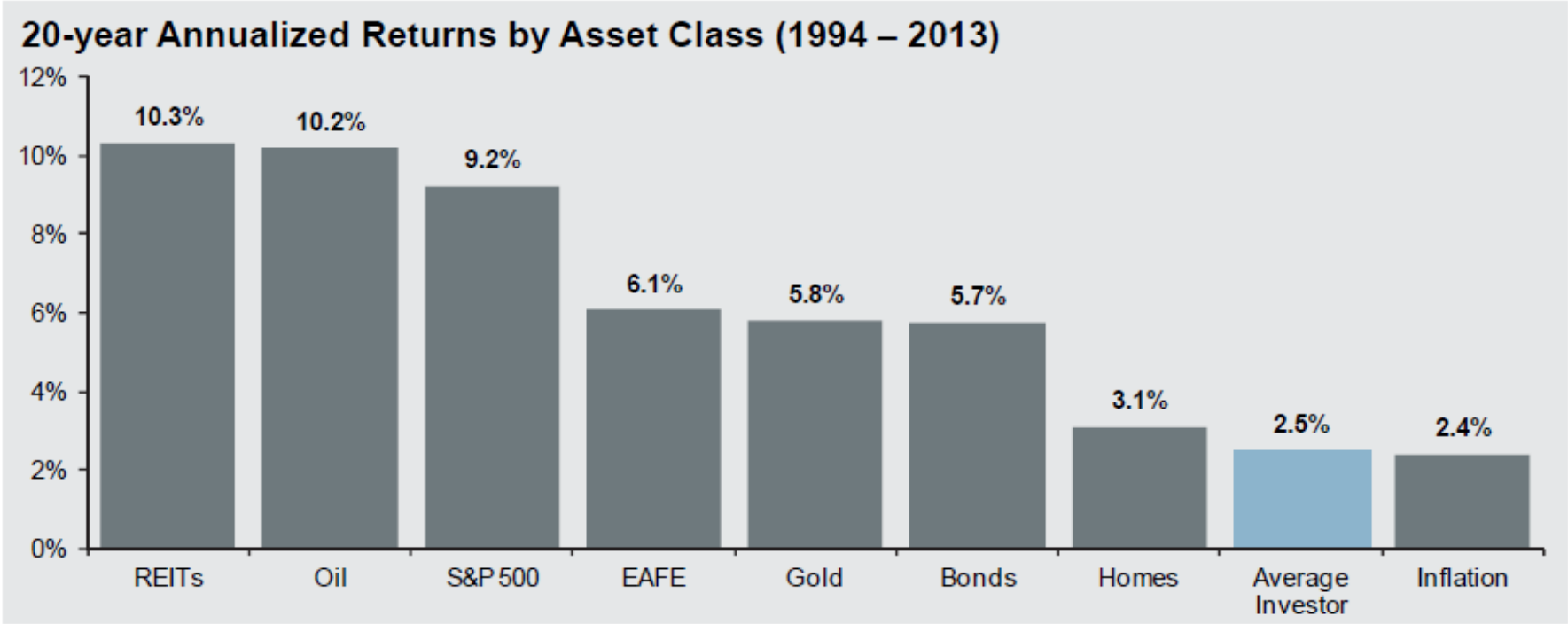
***You should expect to lose money every 3 years on your stock investments on a calendar basis**

Common Mistakes Buying Stocks

How to Help Avoid Buying at the Top of the Market



Average Business Owner Investor Earns Very Low Investment Returns



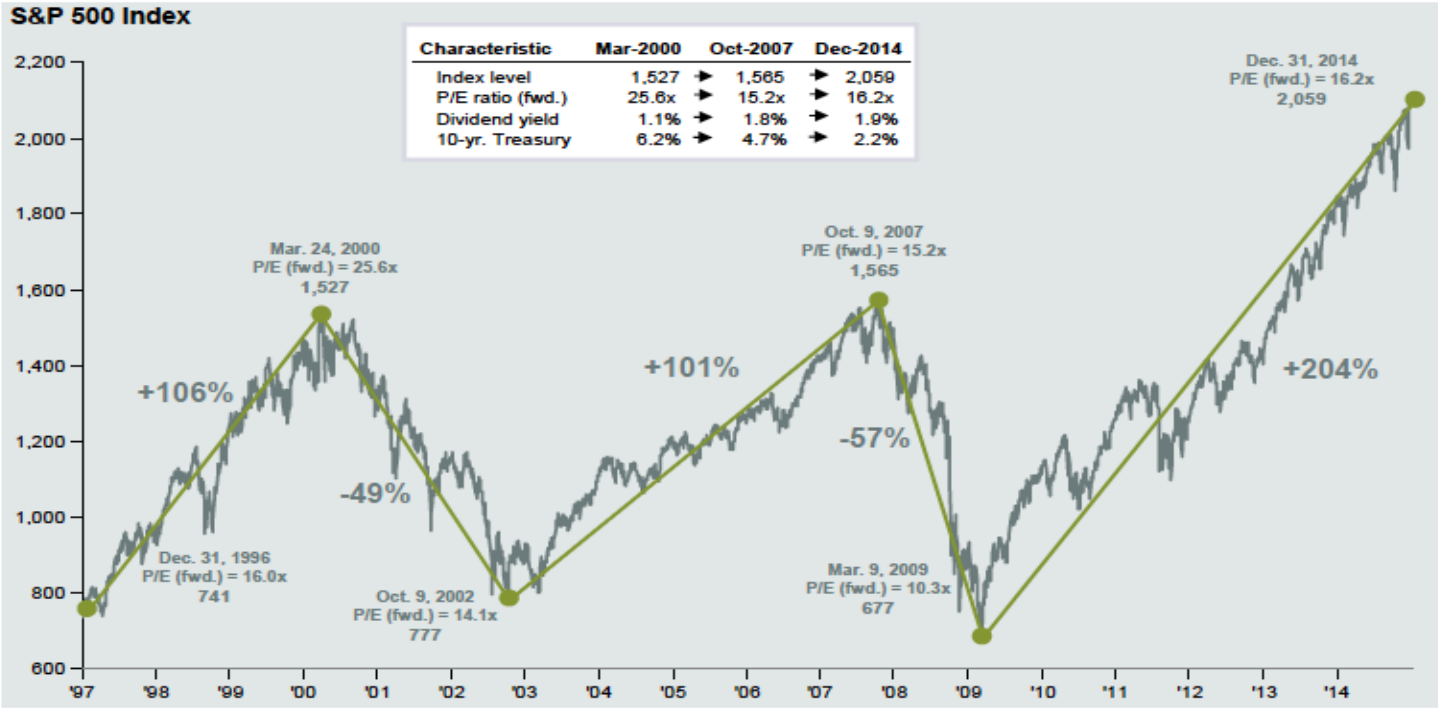
Source: Dalbar, 2013

Life of the Market

MARKET INSIGHTS

S&P 500 Index at Inflection Points

Equities



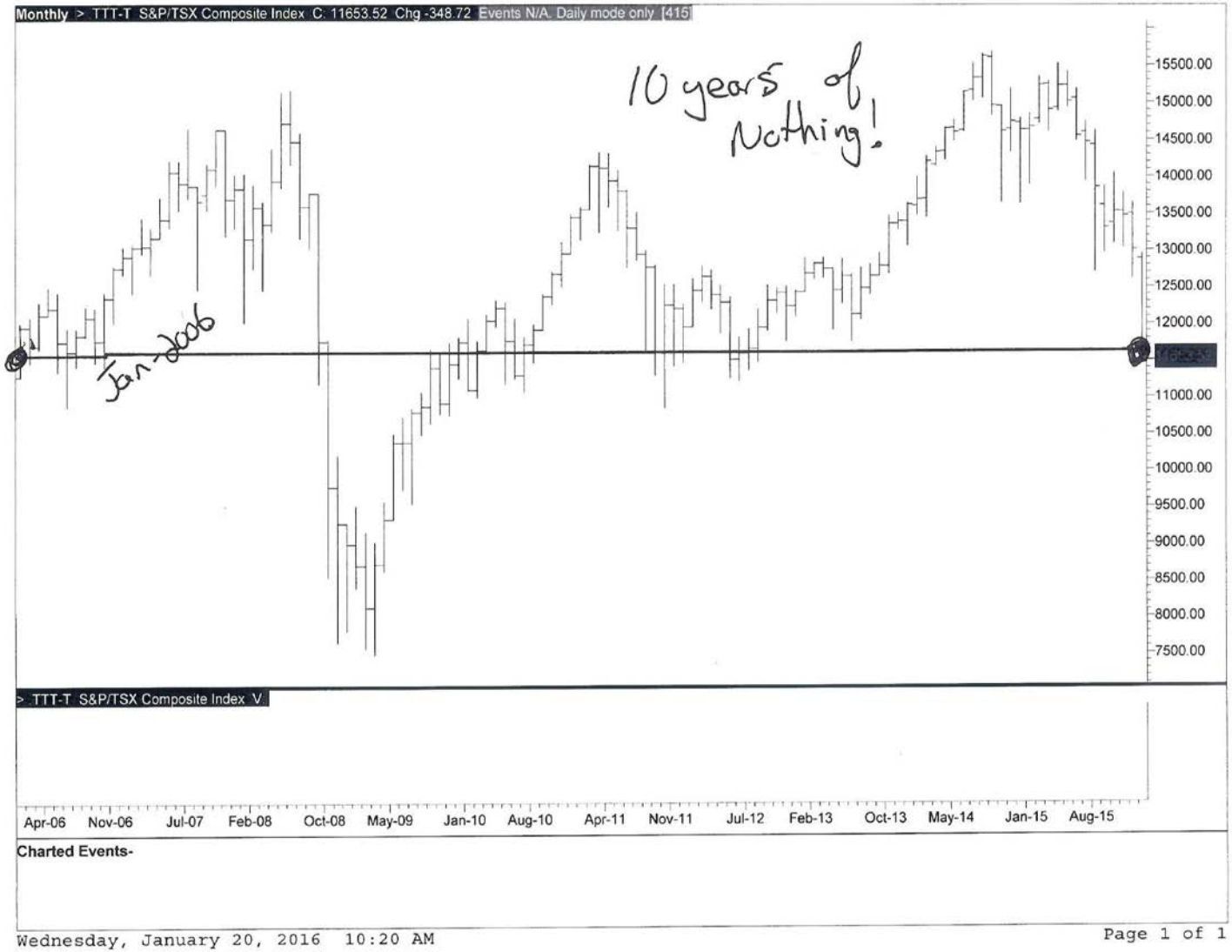
Characteristic	Mar-2000		Oct-2007		Dec-2014
Index level	1,527	→	1,565	→	2,059
P/E ratio (fwd.)	25.6x	→	15.2x	→	16.2x
Dividend yield	1.1%	→	1.8%	→	1.9%
10-yr. Treasury	6.2%	→	4.7%	→	2.2%

Source: Standard & Poor's, First Call, Compustat, FactSet, J.P. Morgan Asset Management.

Dividend yield is calculated as the annualized dividend rate divided by price, as provided by Compustat. Forward Price to Earnings Ratio is a bottom-up calculation based on the most recent S&P 500 Index price, divided by consensus estimates for earnings in the next 12 months (NTM), and is provided by FactSet Market Aggregates. Returns are cumulative and based on S&P 500 Index price movement only, and do not include the reinvestment of dividends. Past performance is not indicative of future returns.

Guide to the Markets – U.S. Data are as of 12/31/14.

J.P.Morgan Asset Management


Monthly > TTT-T S&P/TSX Composite Index C: 11653.52 Chg -348.72 Events N/A Daily mode only [415]
10 years of Nothing!
Jan-2006
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May-09
Jan-10
Aug-10
Apr-11
Nov-11
Jul-12
Feb-13
Oct-13
May-14
Jan-15
Aug-15
Charted Events-
Wednesday, January 20, 2016 10:20 AM
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2nd Rule to stock investing, you need to follow a model or discipline

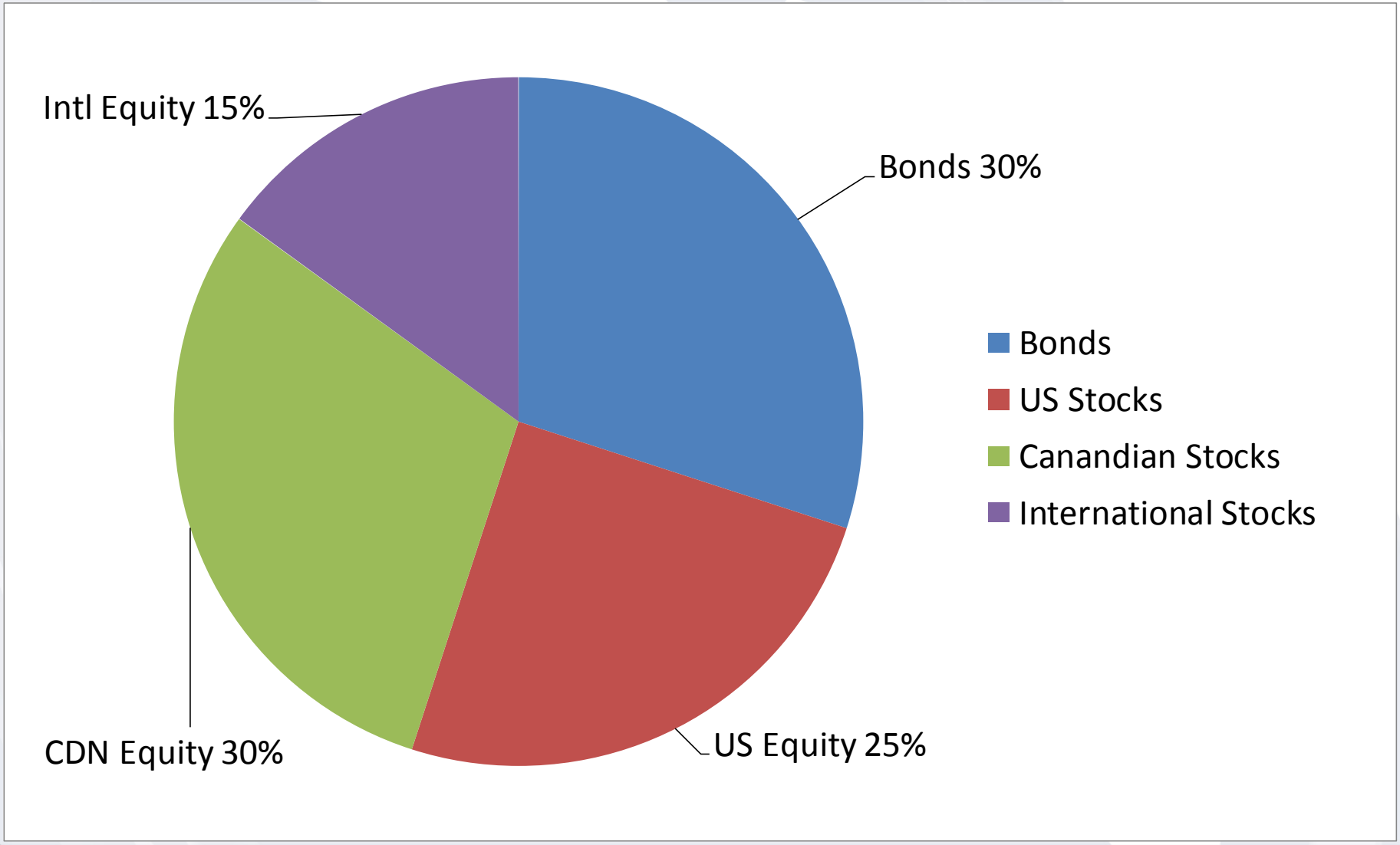
Models and disciplines take your emotions out of the Equation. Here is a discipline that many billionaires follow:

1) Set up optimal asset mix

2) Rebalance regularly to get back to that mix.

Most people require an advisor to ensure they follow the discipline when their emotions are preventing them from doing so.

Optimal Asset Mix



Tax Saving Strategies

The single largest factor, outside of market performance that erodes your capital is…tax!

2016 Corporate Investment Tax Rates On The rise

- Interest income increases from 46.17 to 50.17%, 9 % increase
- Capital gains increases from 23.09 to 25.09%, 9% increase
- Canadian dividends increases from 33.33 to 38.33%, 15% increase!!

Corporate Tax Exempt Investing

- The use of a tax exempt life insurance allows your corporate investments to grow without any report of build up to the taxman. No T-slips.

Conclusion of tax exempt insurance

- Tax free compounding of your corporate earnings
- Money comes out of your corporation tax free on death
- Rules changing in 2017, need to act now

THANK YOU

for attending the

Exiting Your Business Seminar

May 5th, 2016