



BUSINESS
TRANSITIONS
FORUM

NOV 16 / 17, 2016
CALGARY, AB

CAN YOU AFFORD TO SELL? EFFECTIVELY STRUCTURING YOUR COMPANY FOR TRANSITION

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The Fundamentals:

- Streamlining your corporate structure
- What are you selling? (Shares, assets, hybrid)
- Access to the capital gains exemption
- Multiplying access to the capital gains exemption
- Other Items



The Lifetime Capital Gains Exemption

1. What is it?
 - Approx. \$820,000 indexed to inflation
2. What/who does it apply to?
 - Qualified Small Business Corporation Shares
3. What do you mean by multiplying it?



Other Items to Consider:

1. Streamlining the corporate structure
2. Identifying where the value is
3. Other Items to consider:
 - Deferring Sales Proceeds (spreading out the capital gain)
 - Earnouts
 - Consulting Arrangements



- Classic issue – asset vs. share sale?
- Share sale: pros are mostly in the hands of the vendor – capital gains treatment, eligibility for capital gains deduction (?), simpler transaction for vendor, one level of taxation (if individual shareholder).
- For purchasers, share acquisition is often not ideal given the loss of tax shield (in other words, the purchase price ascribed to shares can not be amortized for tax purposes).
- In some cases, there can be post-acquisition planning that may be able to be done by the purchaser to try to utilize the share purchase as a tax shield.....however, opportunities are very narrow and complex.



- Asset sale: for vendor, tax results really depend on what specific assets are being disposed of, what the tax attributes attached to such assets are and who specifically is disposing of such assets (corporation, individual).
- No ability to claim capital gains deduction for vendor if asset sale (except limited exceptions for farmers and fisherman).
- Best of both worlds for vendor and purchaser? Consider hybrid sale (although advantages of such a structure will be greatly diminished for 2017 forward as a result of changes to the ECP regime as Bob Hagerman will / has discussed).



- Will you be granting any restrictive covenants as a result of your business sale? If so, need to carefully consider tax issues.
- Restrictive covenants can include a wide variety of routine contractual agreements (non-compete agreements, confidentiality agreements, etc.).
- "New" section 56.4 of the Income Tax Act deals with the taxation of restrictive covenant grants.
- Changes were first introduced in 2003 but finally came into law in 2014 with retroactive effect.
- New rules are mind-bogglingly complex!!!



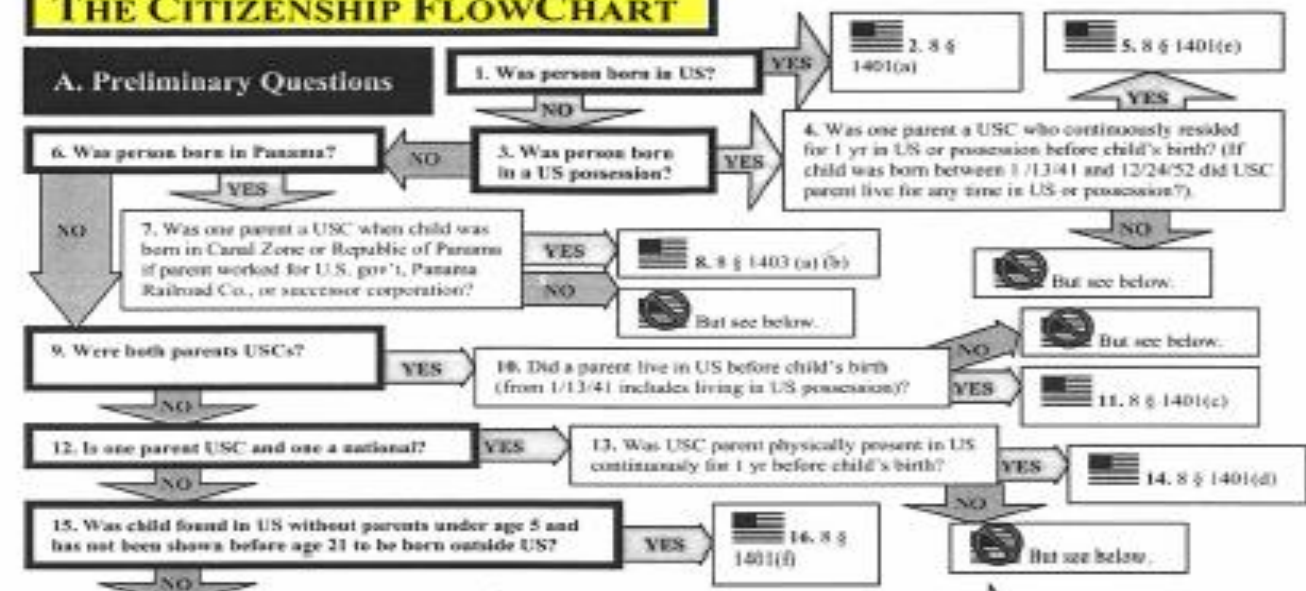
- New restrictive covenant rules are routinely overlooked and not considered in many transactions.
- However, they should not be!
- In a worst case scenario, whatever the FMV of the restrictive covenant grant is, such amount will be fully taxable to the grantor of the covenant.
- There are some very narrow exceptions to the full taxation treatment but you need to VERY CAREFULLY plan for such exceptions. There are no "rules of thumb" with these new rules.....plan, plan and then plan again.



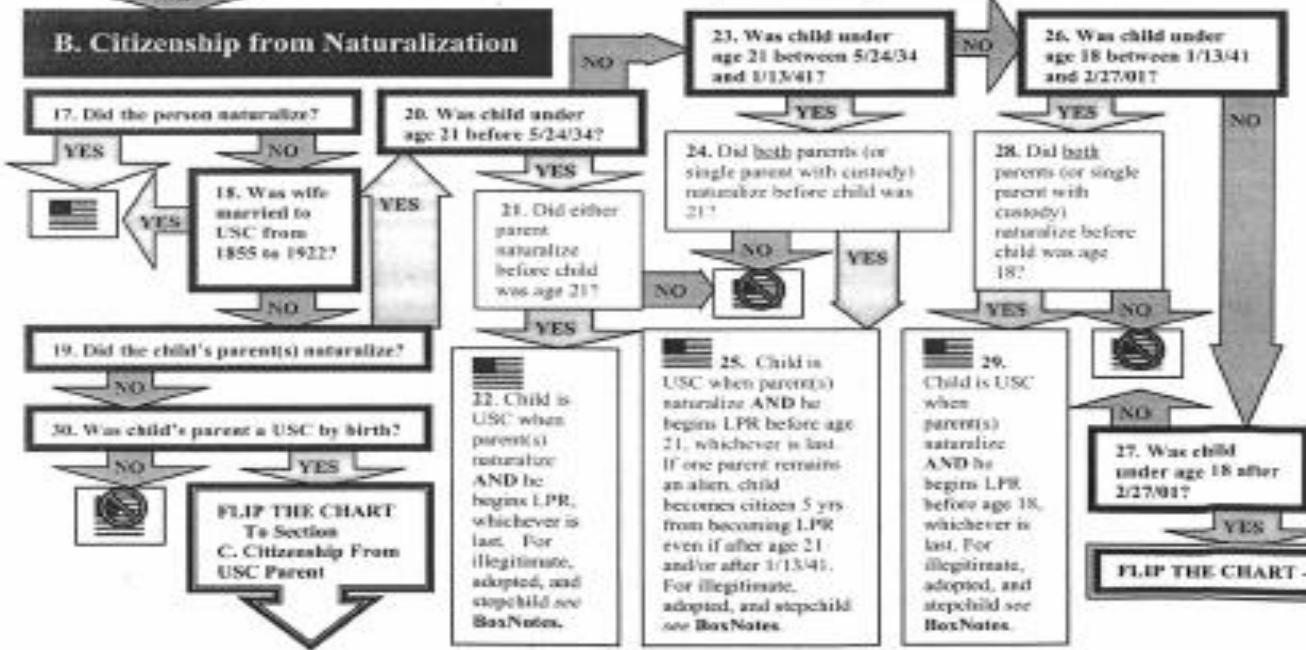
- If you are a US citizen, you are taxed on your worldwide income.
- What if you're a US citizen resident in Canada?
- Need to carefully plan for the appropriate tax results.
- The Canada / US tax treaty will often provide relief but such relief is not absolute.
- For example, a US citizen resident in Canada who sells shares of a CCPC and claims capital gains deduction for Canadian purposes, such a person will be in for a nasty surprise.....the US does not respect the Canadian capital gains deduction and ultimately a high US tax liability will arise.
- Need to very carefully plan for a US citizen who is resident of Canada who desires to sell their business.

THE CITIZENSHIP FLOWCHART

A. Preliminary Questions



B. Citizenship from Naturalization



Terms and symbols:

= Citizenship = No Citizenship

Admitted = an alien's lawful entry into the US after an immigration officer's inspection and authorization (8 U.S.C. § 1101(a)(13)(A))
Alien = any person not a citizen or national of the US. (8 U.S.C. § 1101(a)(3))
Child & Parent = see 8 U.S.C. § 1101(b)(1), (b)(2) and § 1101(c) for definitions
Domicile = a person's legal residence rather than a temporary place of abode or the place a person intends to be his actual permanent place of living. A person may have one domicile but several residences.
Lawfully admitted for permanent residence = status under immigration law of the privilege of living permanently in US as an immigrant (8 U.S.C. § 1101(a)(20))
Legitimate = to put a child born out of wedlock on the same legal footing as one born in wedlock. *Matter of Cabrera*, 21 I&N Dec. 589 (BIA, 1996)
LPR = a Legal Permanent Resident of (or Residence in) the US (8 U.S.C. § 1101(a)(31))
National = one who owes permanent allegiance to the US and includes citizens and those born in outlying possessions. (8 U.S.C. § 1101(a)(21) & (22))
Naturalization = conferring nationality of a state upon a person after birth by any means (8 U.S.C. § 1101(a)(23))
Oath of Allegiance = procedures defined at 8 U.S.C. § 1448(a)
Physical presence = literally means the time a person actually spends in the US
Possession or "Outlying possession" = currently means American Samoa and Swains Island, (8 U.S.C. § 1101(a)(29)), but has included other lands
Residence = a person's general place of abode, his principal, actual dwelling place in fact without regard to intent (8 U.S.C. § 1101(a)(33))
US government employee = includes US education, scientific, philanthropic, religious, commercial, or financial organization
US = continental United States, Alaska, Hawaii, Puerto Rico, Guam, and the US Virgin Islands (8 U.S.C. § 1101(a)(38))
USC = United States Citizen
§ = United States Code
 For questions on any box see **BOXNOTES**

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U.S. Citizenship

1. Born in the U.S. = U.S. Citizen.
2. Born in Canada to two U.S. Citizens = U.S. Citizen.
3. Born in Canada to one U.S. Citizen = U.S. Citizen if:

Born on or after November 14, 1986:

- U.S. Parent resided in U.S. for five years.
 - Two of which were after that U.S. parent's 14th birthday.

Born before November 14, 1986:

- US Parent resided in U.S. for ten years.
 - Five of which were after that U.S. parent's 14th birthday.

US green card holders

- Termination of income and reporting requirements not effective until Form 8854 filed.



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- Bottom line.....as Bob has / will say, plan, plan and then plan again.
- And make such planning early.....not last minute.
- Very limited benefits occurs with last minute planning.



- Win/win sale of Eligible Capital prior to end of 2016
 - Capital Gains and Eligible Capital sales both $\frac{1}{2}$ taxable
 - Capital Gains taxable portion is investment income – possible 51%
 - ECP only 27%
- Hybrid sale of assets/shares
- ECP Bump
 - Replace salary over next few years
 - Strip corporate retained earnings i.e. replace dividends



- Internal transactions
 - Freeze
 - Freeze with redemption over time
 - Gift using capital gains exemption
 - Where does the funding come from?
 - Strip out excess/redundant assets
 - Separate land/building from operations



- Management
 - Freeze with return on invested capital
 - Capital gains exemption
 - Where does the funding come from?
 - Corporate funds or borrowing by management
 - Strip out early excess/redundant assets
 - Separate land/building from operations and lease



- External transactions
 - Funding from third parties
 - Cash, promissory notes, possibly shares (rollover)
 - Assets versus shares or Hybrid
 - Coordinate corporate and personal tax if sale of shares
 - Is land/building included?



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- PLAN, PLAN PLAN AHEAD



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