Effectively Structuring Your Company for Transition

Presented by:
Trevor Thomson, CPA, CA
Partner, Taxation Services, BDO Canada LLP
&
Danvir Roopra, CPA, CA
Partner, Taxation Services, BDO Canada LLP

tthomson@bdo.ca
Tel: 403 266 5608

Suite 620
903 - 8th Avenue SW
Calgary, Alberta T2P 0P7
Canada
www.bdo.ca

- Trevor is a Partner in BDO’s west region, with over 22 years of professional experience providing taxation and business advisory services to privately-owned and public businesses, including private equity and related funds.
- Trevor has provided advisory services to clients in a wide range of industries, including private equity, engineering, real estate/construction, resource, aviation and related industries. He has successfully assisted a number of clients with mergers and acquisitions, transaction advisory, corporate reorganizations, estate planning, equity compensation and related advisory services.
- Trevor is a member of BDO’s taxation service line and national Transaction Advisory Team. He has been and continues to be involved in the community as a volunteer board member of a number of charitable organizations, including as Chair, Vice-Chair, Treasurer and board member at large. Trevor has been a presenter at Canadian Tax Foundation conferences and other industry presentations. Similarly, Trevor has authored papers on various taxation topics for the Canadian Tax Foundation.

droopra@bdo.ca
Tel: 604 646 3373

600 Cathedral Place
925 West Georgia Street
Vancouver, BC V6C 3L2
Canada
www.bdo.ca

- Danvir is a Partner at BDO Canada with over 12 years of experience in public practice. He works closely with the Transaction Advisory Team and is the lead M&A Partner in charge of tax due diligence assignments.
- Danvir has assisted numerous domestic and multi-national clients in various fields with their Canadian tax due diligence. This includes assessing an organization's tax exposure in areas of income tax, indirect tax, payroll and international tax, as well as providing recommendations on tax structuring to help clients minimize current and future tax exposure.
- Danvir is a Chartered Professional Accountant (CPA, CA) and holder of a Bachelors of Commerce (Accounting) from the University of British Columbia.
- Danvir is a member of the Institute of Chartered Accountants of British Columbia and the Canadian Institute of Chartered Accountants. He is also a group study leader and in-residence tutor for the CPA Canada In-Depth Tax Course sponsored by the Canadian Bar Association and the Chartered Professional Accountants of Canada.

Agenda

- Structuring and other tax considerations when considering a potential sale or recapitalization
  - Assets
  - Shares
  - Hybrid
  - Full or partial dispositions
  - Deferrals

- Avoid major pre or post- close surprises
  - Vendor tax due diligence
  - Other

- Post-closing transition

Structuring Alternatives

- Assets
- Shares
- Hybrids
- Full versus partial dispositions
- Deferrals

Structuring Alternatives – Asset Dispositions

- Often the preferred method for purchasers

- Benefits:
  - Due diligence is typically less involved
  - Can sometimes get a higher price
  - Easier to facilitate with those buyers that prefer flow-through structures (for example private equity / others)
  - Sometimes provides for simpler structuring in closing a transaction for both the purchaser and seller (for example, in selling a division or part of a business within a corporate group)

Structuring Alternatives – Asset Dispositions (continued)

- Drawbacks:
  - Often carries a higher tax burden for the business owner as no capital gains exemption, restricted ability to deal with earn-out payments in a tax efficient manner and due to lack of full integration between corporate / personal taxes
  - Still have to deal with the corporate structure post-closing.

Structuring Alternatives – Share Dispositions

- Often the preferred method for business owners that are selling

- Benefits:
  - Usually results in less tax for business owner due to lower tax rates, access to the capital gains exemption and usually better tax treatment on earn-out payments
  - Allows the business owner the peace of mind in potentially not having to deal with a post-closing structure
  - Better ability to access deferrals of tax
  - Buyer can sometimes access preferential tax balances (i.e. losses, etc.)

Structuring Alternatives – Share Dispositions (continued)

- Drawbacks:
  - Due diligence is usually more involved as the legal and tax due diligence is more rigorous.
  - Buyers sometimes want to pay less as it is not as tax advantageous for them
  - If significant issues are identified on legal / tax due diligence, there can be a higher chance that the deal fails as a result

Structuring Alternatives – Hybrid Dispositions

- Often the preferred method when the purchaser and the seller cannot agree to an asset or share transaction

- Benefits:
  - Can bridge the gap between the buyer and the seller
  - Variety of structuring options depending on the particular situation

Structuring Alternatives – Hybrid Dispositions (continued)

- Drawbacks:
  - More complex to implement and can have a higher tax risk profile
  - Often does not give the selling business owner everything he/ she wants (but often neither for the buyer either)

Structuring Alternatives – Full versus Partial Dispositions

- Some transactions are partial dispositions or include components of "roll-over" equity

- Benefits:
  - Provide the ability to "take two bites from the apple"
  - Potentially provides ability to defer portion of gain

Structuring Alternatives – Full versus Partial Dispositions (continued)

- Drawbacks:
  - Partial dispositions often require ongoing involvement post-closing
  - Can be complex depending on the particular situation

Structuring Alternatives – Deferrals

- Depending on the particular circumstances, there are a number of potential deferrals:
  - Proceeds not received all at closing
  - Contingent consideration
  - Roll-over equity
  - Re-investment

Vendor Tax Due Diligence – Introduction

- Vendor tax due diligence brings forth potentially deal-breaking issues that a prospective buyer could find
- Two types of vendor tax due diligence reports:
  - A report that can be provided to prospective buyers
  - A report for management and shareholders only

Vendor Tax Due Diligence – Benefits

- Health check from a tax perspective
  - Helps with control over the sale process and could potentially lead to a higher sale price
- Independent view from a tax perspective
  - Removes necessity for a buyer to have access to all records to complete own diligence as reliance can be placed on vendor tax due diligence report
- Early detection of potential issues to correct or quantify before going to market

Vendor Tax Due Diligence – Typical Risk Areas

- Employee vs. Contractor Issues
  - Lack of independent contractor agreements
  - Lack of understanding of CRA review criteria

- Cross Border Movement of Employees
  - Travel to foreign jurisdictions or inbound travel from foreign parents/foreign subsidiaries

- Transfer Pricing
  - T106 form penalties
  - Lack of contemporaneous documentation
  - Competent Authority

Vendor Tax Due Diligence – Typical Risk Areas (Continued)

- Central Management and Control Issues
- SR&ED/Other Government Incentive Programs
  - Assistance with SPA language on refund entitlement
- Clarity on IP Ownership/Trademarks
  - Lack of legal agreements
- Part XIII Tax Considerations
  - Lack of withholdings on payments to non-residents

Vendor Tax Due Diligence – Typical Risk Areas (continued)

- Foreign Reporting
  - Lack of filing of foreign reporting forms:
    - T106s
    - T1134s
- CRA Audit Issues
  - Lack of clarity on issue(s) and adjustments etc.
- US/International Tax Issues

Vendor Tax Due Diligence – Timeline

- Typical timeline depends on a number of factors
  - Involvement of specialists
    - Transfer Pricing
    - International Tax
    - GST/HST/PST
    - SR&ED
  - Number of complex issues

- If issues are found, we work with management to address the items before going to market

Avoiding Surprises - Other

- Plan early and carefully
- Ensure tax advisors working together and in conjunction with other advisors
- Involve tax advisors that are familiar with acquisitions and dispositions of businesses
  - Buyers often have more in-house experience in buying / selling businesses as compared to the sellers
- Consider all alternatives

Post-closing planning

- Optimal tax planning post-closing depends on a number of items:
  - How much pre-planning was done in advance of a sale of the business?
    - Utilization of trusts
    - Other family or third party shareholders
    - Number of capital gains exemptions utilized
  - Charitable intentions
  - Plans to re-invest versus personal cash needs
  - Investment holding companies
  - Insurance