

# FINANCES

## SPECIAL REPORT ON SUCCESSION PLANNING

# Expert advice eases path

Fourth in an eight-part series, to run in Financial Post each Thursday, on business succession to help promote awareness of the importance of proper planning for transferring a business, the many steps involved and how to go about the process.

BY MEGAN MARTIN

When planning for business succession, developing proper tax planning with professionals who specialize in the field is essential.

"The tax implications involved in business transfers are far too complex to handle alone, consulting with a tax specialist is a must," says Martin Lord, a lawyer specializing in tax, estate, wills and trusts at Robinson, Sheppard, Shapiro.

"The process must be planned many years ahead of time."

There is more than one way to structure a succession but it seems that a discretionary trust is a flexible tool that should be put in place in most instances.

"At a certain point in time, when the owner has accumulated enough value, he or she may wish to transfer the future value of the company to the next generation or, failing suitable family successors, to management employees," Mr. Lord says. "In my mind, a succession without a trust is almost impossible."

An estate freeze can be carried out without immediate tax cost by having the owner



Tax lawyer Martin Lord says part of the process of successful business succession includes expert advice on tax planning.

convert their common shares into preferential shares having a fixed value equal to the shares converted.

"In other words, the owner's value will no longer fluctuate but the Canada Revenue Agency insists that certain conditions tied to the shares be satisfied, such as the ability to redeem the preferred shares at will," Mr. Lord says. "New participating shares should

be subscribed by a discretionary trust, the beneficiaries of which will be the next generation."

For Canadians it is possible to sell shares of a Canadian controlled private corporation and realize a capital gain of \$750,000 tax-free, in certain instances. The capital gain realized by the seller can be exempted if his shares are Qualified Small Business Cor-

poration Shares (QSBCS). If the business is passed to family members, the trust will allow the business owner the opportunity to decide within the next 21 years of the trust who will be the chosen child or children to receive shares and continue the business. However, business owners should note that sales to family members don't qualify for the QSBCS exemption if a cor-

poration is interposed as the buying entity.

"The belief that family successions qualify for that is one of the biggest misconceptions," Mr. Lord says. "The tax system doesn't help to support business transfers to generations of families, it actually favours selling to third parties."

The exact same sale structure will result in a different tax outcome for family mem-

bers versus a third party. In one case it is considered a capital gain and in the other it is considered a dividend that does not qualify for the QSBCS exemption.

"Consulting with a tax lawyer will help business owners have a tax treatment for their succession that will appeal to the owners and successors alike and find alternative tax benefits if the tax exemption doesn't apply," Mr. Lord says.

But tax considerations are only one element of the succession process.

"You have to make sure that you have a plan that is all encompassing and is understood by the other parties involved in the process."

It's not a bad idea to have an independent legal adviser helping out the next generation of ownership as well, just to ensure their interests are respected, he added.

"What you'll see very often is the parent who owns 100 per cent of the common shares and then converts them to preferred shares with an established value," Mr. Lord says. "But that value needs to be fair for both the seller and buyer; I've been in situations where the price set was too high because what the parent thought was fair wasn't accurate."

Tax strategy is a huge element of succession planning that needs to be properly structured, but well planned successions have to go beyond that and make sure that all the stakeholders are taking part in the procedures.

"It should never be a one-party process," Mr. Lord says. "It should be a collaboration over many years."