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Other Issues

1. Control of the corporation
2. Shareholder agreements
3. Family law issues
4. Estate planning

1. Control of the corporation

- Timeline
- Is the business being sold outright or is a freeze being used or both?
- Is there a transition period where the principal is going to stay on?
- If so, how long?
- Is there an event that will trigger a transfer of control?

1. Control of the corporation cont'd.

- With an outright FMV sale, the purchaser/child will generally want full control. Few issues here.
- With a freeze, who will control?
 - Principal via freeze shares or child(ren) via new common shares?
 - What if wasting freeze implemented?
- What about when a trust is used to hold new common shares?
 - Fear that if a trust holds voting control and there is a change in trustees, CRA may view that as a change of control
 - A change in control can trigger year-ends, restricts carryforward/back of losses

1. Control of the corporation cont'd.

- How to avoid this potential risk?
- Why not consider using “voting only” preferred/special shares?
 - Shares have voting rights granting the holders voting control
 - Shares have nominal redemption/retraction price
 - Limited/no right to dividends
- Shares can be held by principal and sold/gifted to child once triggering event takes place or shares can be held by child to avoid voting control being held by trust

1. Control of the corporation cont'd.

- Risks?
 - Voting premium on shares?
 - CRA has not taken a firm position on this, but it is possible
 - Have not seen it in practise for private companies (save for VC financing/sale arrangements)
- Does price adjustment clause alleviate this risk?

2. Shareholder agreements

- Are shareholder agreements redundant in family business succession?
- May not be “needed” for transition from parent to 1 child...although we always recommend because it encourages dialogue
- However, if transition is to multiple shareholders then it is strongly recommended to set rules of the game before transition takes place
- Surprising how often these discussions raise new issues

2. Shareholder agreements cont'd.

- Can parent enter into Shareholder agreement prior to transition and then force children to become parties to the agreement?
- What happens if certain events take place:
 - Divorce
 - Creditors
 - Death
 - Not fulfilling responsibilities
- Can shares be bought back at a discount?

3. Family law issues

- *Caveat – I'm not a family law lawyer!!
- Reports that estate litigation is fastest growing area of law in Ontario
- Family law litigation is also growing
- How do we minimize exposure for our clients?
- Best option is always marriage/co-habitation agreement

3. Family law issues cont'd.

- Discretionary trusts can be helpful...courts have acknowledged that is very hard to value a beneficial interest in a trust
- Gifts after marriage
 - New common shares can be gifted to married child to rely on exemption from net family property calculation
 - Does the gift of shares to a trust and subsequently distributed to child provide same protection? Mixed opinions.

4. Estate planning

- If shares of Opco are sold outright for cash, no issue with transition in Will of parent
- If child issues promissory note to parent, how is note dealt with?
 - If gifted to purchaser child then very beneficial
 - If split amongst purchaser and other children then more sensitive
- If freeze is used, then what happens to freeze shares?

4. Estate planning cont'd.

- Equalization amongst active and inactive children is very sensitive and complicated issue
 - Family views vary greatly on this issue
 - Every child should get equal value (including value of shares held by parent)
 - Active child has earned what they've got and remaining assets should be split equally
 - Unequal distribution is completely fine
- How to equalize if Opco is primary asset?
 - Case specific

4. Estate planning cont'd.

- Ensure Will drafter knows about trust and shareholder agreement
 - SHA often missed when Wills are prepared
 - What if there are life-insurance shares?
 - Make sure plan is well documented and even encourage post-mortem planning to be discussed during lifetime with family
- Do special purpose trusts (alter-ego and joint spousal) help minimize family law and estate litigation?
 - Certain scenarios where they provide assistance BUT be very wary of the *Succession Law Reform Act* if considering this strategy

Recommendations

- Consider using voting-only shares to ease transition of control
- Avoid voting shares in trusts, if possible
- SHA are strongly recommended to encourage dialogue and set out rules before transition
- Consider family law issues in advance and take steps where needed to minimize risk/exposure

Recommendations cont'd.

- Discuss estate plan well in advance. Involve children/family to identify issues early on.
- Consider post-mortem planning and make family aware of double/triple tax issue so they are aware planning is needed following a death.

QUESTIONS?