GUEST COLUMN

Succession Planning — "Keep It Simple Stupid" May Lead To Failure

By Andrea Pontoni

Succession planning is a term that has gained momentum over the years, primarily because of demographics and the aging population.

The primary objective for the planner is to transfer his or her business to a family member, employee or unrelated party, while ensuring a smooth transition and maintaining value. The objectives may differ when transferring a business, primarily because the value factor may be less or more important depending on the purchaser.

I view an adequate succession plan as having, at a minimum, the following components. Additional components may enhance a plan.

STRATEGIC

- Who will be the successor — family member, employee, unrelated third party?
- What will be the criteria in determining the appropriate successor?
- Who will manage the process?
- How will the existing management team be utilized in the succession plan?
- Over what time period will the business be transferred?
- What is plan B if plan A falls apart?
- And many more questions . . .

BUSINESS VALUATION

- What is the value of the business for purposes of the transfer?
- Who will determine the value of the business? **Are they independent?**
- Who will be scrutinizing the valuation (Government Tax Agencies, Family Members, Creditors etc.)?
- What are the implications for an unreasonable value?
- What is the amount required for a successful retirement by the current owner?
- Is there an opportunity to monetize/convert any personal goodwill (typically very little or no value to a third party) to commercial goodwill (has value to a third party)?
- And many more questions . . .

TAX – STRUCTURAL

- Has consideration been given to maximizing the utilization of the capital gains exemption and the appropriate tax structures?
- Has consideration been given to reducing the tax burden through the use of individual pension plans, employee bonuses, triggering losses to offset gains etc.?
- Is a tax freeze required?
- The use of holding corporations in a structure in order to defer tax?
- The use of trusts? The main reason to allocate income while maintaining control.
- And many more questions . . .

LEGAL

- Has an updated Will and Power of Attorney been prepared?
- Have the corporate minute books been updated?
- Have all significant corporate agreements (leases, supplier, customer etc.) been formalized or updated?
- Is there a shareholder's agreement in place? Has it been updated?
- Is there appropriate life insurance in place?
- And many more questions . . .

Even though all of the above points are critical in an effective succession plan, given my background as a valuation and tax professional, I offer the following insight with respect to the valuation and tax aspects of the plan.

Contrary to the belief of some individuals who try to portray themselves as experts, a business valuation is a complex process.

Be careful of individuals who try to minimize the business valuation process, as they often do this to compensate for their lack of credentials, which may demonstrate lack of in-depth knowledge, training and experience, required to do a proper business valuation. Further, you often pay the same fee or more for the service.

As well as having an understanding of the business and industry it operates in, there are many methodologies and variables which are assessed in completing a business valuation.

An unreasonable conclusion or exclusion of these variables, could lead to an improper or unreasonable value.

The implications of an unreasonable value from a succession planning perspective, to name just a few, are. . .

- It may eventually lead to a failed succession plan due to unreasonable value expectations. Also, conflicts within families may occur as a result of these expectations;
- It may be difficult to finance a transfer because the value is unreasonable; and
- **Canada Revenue Agency** may impose gross negligence tax penalties on the taxpayer ("you") and third party advisor penalties, in particular on transfers to related parties.

I highly recommend that you engage a qualified and experienced **business valuation** professional for this aspect of the succession plan, as this, without sounding biased, is **one of the higher risk areas in succession and tax planning.** You may want to consider a **Chartered Business Valuator ("CBV")** in Canada or an **Accredited Member in business valuations with the American Society of Appraisers ("ASA")**, recognized both in the U.S. and globally as an authority in valuation matters.

One of the typical goals in succession planning is tax minimization. The wonderful world of tax has many paths you can take with respect to structures.

The old **Yogi Berra** saying — "When you come to a fork in the road, take it" — may be wise in certain situations, however, it should not be followed in the world of tax.

Before taking the road that best fits, you will be required to assess your options. This can only be done by understanding your objectives and the objectives of the person or entity you are transferring your business to.

In my experience these objectives and the associated tax plans, tend to vary if the individual is related or unrelated, among other factors. Getting the best value for your business is step one, keeping the most value after paying the government their share, is step two.

Again I highly recommend that you engage a qualified and experienced tax professional for this aspect of the engagement. You may want to consider a professional who has completed the **Chartered Professional Accountants of Canada's in-depth tax specialty program** and has some years of experience.

Planning the next stage of your life can be an enjoyable and exciting time if done properly. So be sure you understand your objectives and what you want for your family and your business, going forward.

Also, make sure that you engage qualified and experienced advisors to assist with the succession plan. As **Hunter S. Thompson** puts it "Anything worth doing, is worth doing right." X

__Andrea Pontoni__ holds an __Honours Bachelor of Commerce Degree, is a Chartered Professional Accountant (CPA),__ Chartered Accountant (CA), __Chartered Business Valuator (CBV)__ with the Canadian Institute of Chartered Business Valuators, __Accredited Senior Appraiser (ASA) in business valuations__ with the American Society of Appraisers and Certified in Financial Forensics (CFF) with CPA Canada and the American Institute of Certified Public Accountants. Andrea has also __completed the three part Chartered Professional Accountants of Canada's in-depth tax specialty program.__ Andrea has over __27 years of experience,__ with 17 of those years at two national firms where he held senior positions including that of a partner. His practice includes providing advice on business valuations, personal and corporate taxation, economic loss quantifications, accounting, financial investigations, financial forecasts, business planning and corporate finance matters to clients varying in size and industry. He can be reached by calling __519-890-6288__ or by emailing: __apontonicacbv@cogeco.ca.__ For more information on his background visit his website: __www.PontoniBusinessAdvisor.com.__