THE POWER OF BENCH STRENGTH
When the game shifts into high gear, the right team can help you score a bigger win

LAYING A SOLID FOUNDATION
Bellavita Tile seals a strategy that focuses on long-term success

BUYER BEWARE
What Canadians need to know before purchasing U.S. property
Many would find it difficult to manage one firm leadership role, let alone two, but Scott Crowley has found a way to do it. “To succeed as the Regional Managing Partner of Advisory Services for Ontario and the Eastern Canada Regional Enterprise Risk Services Leader, I’ve learned the importance of aligning the goals and priorities of both roles,” says Scott. “For me it boils down to two ambitions—exceed our client’s expectations through exceptional service and quality and always be on the lookout for innovative opportunities that will help clients achieve what they’ve set out to do.”

That philosophy has generated a track record of excellence that Crowley works hard to maintain. It’s also what helped him define his vision for the future of the advisory services practice in Ontario. “I think our firm is particularly valued within the marketplace for our tailored approach and the calibre of our team. We blend the knowledge we hold of the external environment and our deep technical expertise with the strategic ambitions and capabilities of our clients’ business. This allows us to develop and implement practical and strategic solutions that get them tangible results.”

In his second role as Leader of MNP’s Enterprise Risk Services in Eastern Canada, Scott defines and orchestrates effective governance, risk management, internal audit, business continuity, operational effectiveness and security strategies. “Our solutions help ensure the continuity of our client’s operations so they gain a competitive advantage while staying on track as they achieve their organizational objectives,” says Scott.

Ensuring that the next generation continues to provide the high levels of customer satisfaction that MNP is known for is especially important to Scott. “It is essential for me to help create opportunities that enable our staff to excel personally and professionally,” he adds.

“To offer in-depth solutions to clients in Enterprise Risk, Management and Technology Consulting, Corporate Finance, Insolvency, Business Valuations, Anti-money Laundering and Forensics, requires us to be on the cutting edge of each of our areas of specialty. To be the best, you can never sit still.”
What Canadians need to know before purchasing U.S. property

BUYER BEWARE

With the promise of warmer weather south of the border, an increasing number of Canadians are considering the purchase of a vacation home in the U.S. Whether reserved exclusively for personal use, purchased as a rental property or some combination of the two, there are a number of tax considerations Canadians must be aware of before buying in.

**Estate Tax**

With the majority of vacation properties being purchased by older, often retired Canadians, mortality is a consideration. Unlike Canada, the U.S. levies a substantial estate tax upon death, which is based on the value of your U.S. estate. U.S. assets include real estate, possessions that stay in the U.S. (like a car) and shares in U.S. companies. If your worldwide estate is worth more than $5.34 million, you may be subject to a tax of up to 40% of your U.S. estate’s value.

“Historically, the estate tax was a bigger concern for more people than it is today,” says Kevyn Nightingale, CA, CPA (ON), CPA (IL), TEP, a U.S. Tax Specialist with MNP’s Toronto office. “With the current exemption rate being as high as it is, it applies to fewer people, but with a great impact.”

If you are among those that are subject to an estate tax, there are ways to mitigate your tax exposure. Kevyn notes he has 12 different approaches to help clients reduce their overall estate tax liability – but with so many options, he recommends building your estate tax strategy as early as possible.

**Income Tax**

If you currently own a U.S. vacation home and are considering selling, there are U.S. income tax obligations. The purchaser must withhold 10% of the gross proceeds - the IRS wants to make sure you pay your tax. “As a result, some of your money can be tied up with the IRS for quite some time,” says Kathy Bonazew, CPA, CA, a U.S. Tax Specialist with MNP’s Edmonton office.

There are two options for rental property owners to comply with tax legislation. The first involves the tenant (or agent) withholding 30% of the rent and submitting it to the IRS. More commonly – and effectively – the landlord can choose to file a tax return with the IRS. Filing a tax return allows you pay tax on net income after expenses, instead of on the gross rent. Tax is applied at graduated rates instead of 30%.

“Usually the net income is very small, especially when someone has a mortgage on their property,” says Kevyn. “However, if you use your property personally and for rentals, you’ll need to prorate your expenses.”

Whether you are selling or renting a property, you’ll also need to report your activities on your Canadian tax return. While Canadians will receive a foreign tax credit, there are a number of additional considerations and challenges. For example, you may require a Foreign Income Verification Statement or you may have currency differentials that can cause you to report different figures on each side of the border.

No matter what, speaking with a specialist before you buy can help protect your U.S. assets and shield you from extensive tax exposure.

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For more information on this topic or other related tax issues, contact Kevyn Nightingale at 416.515.3881 or Kathy Bonazew at 780.969.1454 or your local MNP Advisor.
THE POWER OF BENCH STRENGTH

Having a team you can draw on when the game shifts into high gear can help you score a bigger win

Bench strength. It’s defined as the quality and number of players available to help you succeed. For many business owners, their relationship with MNP begins with a relationship with just one player—your accountant, perhaps, or maybe a consultant engaged for strategic planning purposes. But at key points in the game, it can be encouraging to know there are more members of the team waiting to jump in and help.

The power of bench strength is readily seen in the often-complicated process of selling or transitioning a business. “Everyone will need to sell their business at some point, whether that’s to a family member, a financial buyer or a strategic buyer. It makes sense to plan for this transition and find an advisor that has bench strength,” says Wilma Braat, CFA, MBA, a Senior Vice President and Director for MNP Corporate Finance Inc. in Calgary.

For Wilma, working with her colleagues—MNP Business Advisors—who have a history working with the client, is an asset when seeking the right buyer for the business. The Business Advisor has a trusting relationship with the client and understands the needs and objectives of all shareholders.

“We understand the business and how it’s structured. We know the numbers and have ensured that the tax planning for an ultimate sale has been done. All of that makes it easier for me to sell the business in a way that meets the individual goals of the client,” she says.

ENGAGING YOUR FULL ADVISORY LINE-UP

Recently, Wilma was introduced to Jim O’Rourke, President and CEO of OEL Projects Ltd., a Calgary-based engineering firm. Jim and five other shareholders in OEL had been working with Mark Brown, MBA, FCMC, Director of Business Consulting Services for MNP, on a strategic planning engagement.

Jim wasn’t interested in selling his company right away, but Wilma asked what his ultimate goals were. Jim said he eventually wanted to sell the majority of his shares for a specific amount, retain an ownership position, ensure the future of his five minority shareholders and find a partner with the ability to work with the team and take the business to a new level.

Because of her in-depth experience working with the engineering industry, Wilma was confident she could get Jim exactly what he wanted and with her assurance, he was interested in proceeding. Wilma targeted a small number of potential buyers she knew well and was able to negotiate a transaction that allowed Jim to monetize the majority of his shares as well as meet all his other objectives. But, as is common at MNP, she didn’t do it alone.
“Mark had been working on OEL’s strategic plan and had a trusting relationship with the shareholders. Throughout the transition, he was able to counsel the minority shareholders while I worked predominantly with Jim, which ensured we could move the deal along in a timely manner and ensure everyone was informed, involved and ultimately satisfied with the result,” she says.

She also drew on another team player, Jeff Kawamura, CA, Taxation Services, MNP. “When Corporate Finance starts working on numbers, the client wants to know the critical piece—how much will be left after tax. We come in to help determine the best way to structure the transaction so the vendor gets as much as possible out of the sale,” explains Jeff.

In Jim’s case, the tax situation was more complicated than usual because there were six shareholders who bought their shares at different times and prices. In this scenario, Jeff analyzed the situation and presented the best plan to maximize their proceeds now and in the future. He also presented the team with a clear breakdown of the taxes that had to be paid.

The ability to access in-house tax expertise during the sale of a business is important for clients, even if they have done advance tax planning using a process like MNP’s ExitSMART™ succession program.

“When offers come in, we need to analyze them on an apples-to-apples basis to ensure we understand which results in the largest after tax benefit for our client,” says Jeff.

That said, Jeff stresses the importance of tax planning before selling, ideally three years before you want to take your business to market, because some critical tax planning can’t be done after that. For instance, if you want to ensure family members get the capital gains exemption when the business is sold, those members have to own the shares for at least 24 months and sometimes as long as 36 months prior to the sale.

“There are a lot of tax issues that can affect you, so you really need to work with your Business Advisor and our team to help determine the right structure and develop a tax plan so you can maximize after-tax profits,” says Jeff.

THE VALUE OF A TEAM APPROACH

Harnessing the power of bench strength allowed Jim O’Rourke to attain his objectives and get the majority of his equity out of the business earlier than he’d thought possible. He appreciated the team approach.

“Mark helped us find common ground as a group of shareholders and it was extremely helpful that he had the resources for us to draw on,” says Jim. “Wilma was great to work with and it was helpful to have Jeff provide tax advice to some of our existing shareholders.”

In some situations, MNP remains involved with companies after they transition to new ownership, particularly in cases where the business is sold to family or an employee group. For new owners, having a firm that knows the history of the business makes sense and saves time because they don’t have to develop a new relationship and tell their story over and over again.

And that’s the real power of bench strength—working with a team that knows you and is committed to your success. From planning your ideal future with your Business Advisor to engaging MNP Corporate Finance to find the right buyer and execute the deal, to getting tax advice that maximizes your returns, the process goes more smoothly and is tailored to help you achieve exactly what you want.

For more information on this topic, contact Wilma Braat at 403.537.7632, Jeff Kawamura at 403.263.3385, Mark Brown at 403.537.7623 or your local MNP Advisor.
Growth—it’s what every business owner wants from day one. But when it happens quickly, entrepreneurs are often unprepared and find themselves struggling to manage the increase in business. That’s what happened with Bellavita Tile, a company that had increasing demand for its innovative products and is now meeting, and growing, that demand beautifully.

Bellavita Tile is a rapidly growing design, manufacturing and distribution company with a head office in Vancouver and a U.S. division in Texas. The company produces and markets high-end, unique ceramic and glass wall, floor and mosaic tiles and also takes on custom design projects. Founded by entrepreneur and President Duigan Mitchell in 2004, Bellavita initially focused on the Canadian market but by 2009, plans were in place to establish U.S. operations. As the American market began to develop the company grew rapidly—and experienced significant challenges with everything from inventory to cash flow to human resources.

“That is a very common situation for entrepreneurs,” says Eben Louw, CPA, CA, a Business Advisor with MNP in Vancouver. “You get into rapid growth mode but you don’t yet have the people, processes and technology systems in place. How do you determine the moving parts that factor into making the business successful over the long-term as well as the short-term actions that should be taken? What are the priorities and what are the key decisions that have to be made?”

Realizing that he needed better overall direction and someone he could consult, Duigan was referred to MNP. “I wasn’t looking for services from MNP at that time,” he remembers. “But after meeting with Eben a couple of times, I grew confident in what he could bring to the table.”
One of the first things Eben pointed out was that Bellavita Tile was facing impending tax issues in U.S. that needed to be dealt with quickly. Because Bellavita has partial ownership of a factory in China—a separate entity—the tax situation was even more complicated.

Eben drew on David Turchen, CPA, CA, CPA (PA) in Abbotsford and Tim Bloos, CPA, CA, LLB, BCL in Toronto, both Senior Managers in MNP’s International Tax practice, for advice on cross-border structuring. They helped determine the agreements, filings and registrations that were required, which structure would be most tax efficient, and how Bellavita could stay in compliance while expanding.

With that taken care of, Eben and Bellavita’s management team began to look at other immediate concerns. “They needed to make some really big decisions but they didn’t have the right financial information. It was an overwhelming time for them. As a starting point, I took them through a strategic planning process to give them direction and a plan for achieving their goals,” says Eben.

About a year ago, Eben, Duigan and the management team – including Mike Ward, North American Sales Manager, who joined the company in 2008 to open up a customer base in the U.S. – sat down in Abbotsford for a two-day strategic planning session. The process began with establishing Bellavita’s vision and values. While Mike remembers it as exhausting, he also thought the time spent was valuable. “When it comes to business decisions, we reference our vision and values constantly. In fact, I just referenced them this week,” he says.

Eben’s process didn’t just have the team develop a vision statement. Instead, they created a ‘memory of the future.’

“We delve into the future and ask, ‘What does it look like? What are the implications? Are all the components balanced?’ For example, if you have a significant sales goal, you need to have the support in place to achieve that goal. When you delve into that memory of the future in so much detail, you can make decisions later that tie into the memory. It allows you to define the strategy and set priorities,” says Eben.

Next, the team identified their critical success factors and developed a ten-year plan. To support this plan, they also developed one- and two-year plans. A few months later, they met again to determine the key performance indicators to back up their critical success factors.

The result of the entire exercise was one plan that includes both strategic and operational planning, as well as operational metrics. The plan is also fully integrated with the company’s budget.

But plans have a way of falling by the wayside when people get back to business. To ensure that didn’t happen, Bellavita’s management team committed to meeting once a month to go through the critical success factors and key performance indicators to ensure accountability and track progress. They also meet with Eben each quarter to review the ten-year plan and what’s happening in the marketplace, update the long-term plan if required and establish focus for the next quarter.

The plan is also shown to staff and key customers and suppliers so they know Bellavita’s objectives.

“What MNP gave us was a really sophisticated way of setting our goals and establishing the roadmap that would help us reach them,” says Mike. “To grow the way we needed to grow, we needed to determine the things we have to do internally to achieve that.”

The strategic planning process has made it easier for Duigan to focus on his priorities, which often take him to China. “Having very quantifiable, realizable and measurable goals and key performance indicators is fantastic because it got us all pointing in the same direction,” he says. “I am confident that the whole team knows where we’re going and their role in how we’re going to get there.”

Bellavita has continued to grow in spite of the poor economic situation in the U.S. This year, sales are expected to hit $19 million, while by the completion of the ten-year plan, annual sales are expected to climb to $75 million.

It’s a lofty goal but, according to Duigan, it’s realistic and achievable thanks to the work he and his management team have done with MNP.

“We’ve become a lot more focused. I’m a pretty driven guy, but it’s much easier to be driven when you can focus your energy, which we can do now. Having lofty but achievable goals helps drive the rest of the team,” says Duigan.

As the company begins to plan for sales beyond North America, it will also be working with MNP to develop personal action plans for the management team and all employees. This work, which Eben will facilitate, will ensure that everyone at Bellavita understands their own roles and how they contribute to success, while encouraging everyone to support each other in reaching the company’s strategic goals.

Bellavita’s work with MNP has given it a firm foundation on which to grow. While the company is small compared to many of its competitors, innovative products and the ability to make strategic business decisions have positioned the company for an exciting future.
SPOTTING A FRAUDSTER
How to protect your company from internal theft

A receptionist helps herself to office supplies or petty cash. A controller sets himself up as a fictitious supplier and gets your company to pay fraudulent invoices. A CFO manipulates the financial statements in order to maximize her bonus. According to the Association of Certified Fraud Examiners (ACFE), the average organization loses five percent of its revenues to fraud each year. Although the individual amounts taken may be small, the accumulated costs of fraud can be very significant.

“The ACFE found that the median loss to a company was $140,000. That goes up to $180,000 if someone in management is stealing and to $573,000 if the owner or a member of the executive team is the fraudster,” says Jacklyn Davies, CA, DIFA.

Jacklyn leads MNP’s Investigative & Forensic Services practice in British Columbia. Fraud, she says, is a major problem—and it doesn’t matter what shape the economy is in. When business is booming, she sees cases of financial statement fraud in which results are overstated to attract investors or talent to the company. When there’s a downturn, there are cases of making the financial statements look better so the bank doesn’t notice an issue with debt or employees submitting false expense reports to obtain more money.

Two of the most common areas in which fraud occurs are purchasing / procurement and expense fraud—claiming too much on expense reports and ‘double dipping’, which could be submitting a per diem and then expensing the individual receipt. Another trend showing up in audits is theft of time, which may involve people spending personal time on the internet during working hours or actually claiming to put in time they never worked.

“It happens in organizations of all sizes. Where there is money flowing, there is opportunity for fraud,” says Jacklyn.

WHAT DOES A FRAUDSTER LOOK LIKE?
While there’s no way to identify someone as a fraudster based on appearance, those who commit this type of crime do have a few characteristics in common. Typically, fraudsters are trusted, long-term employees who know the business extremely well. They may have personal problems such as a drug or gambling addiction that create the pressure to access more money.

They leave other behavioural signs too. Your employee might be stealing from your organization if he or she:

• Appears to be living beyond their means
• Refuses to take holidays
• Takes his or her computer everywhere
• Exhibits abusive or controlling behaviour
• Has an unusually close relationship with a manager or supplier
• Has a problematic attitude at work
• Often attempts to be alone at work

Essentially, people commit fraud if they have the motivation and opportunity and are able to rationalize their decision, usually with the thought that they aren’t really hurting anyone.
IS YOUR COMPENSATION PLAN ENCOURAGING FRAUD?

If people are taking their time getting things done or if your sales force is selling to customers with poor credit histories, you might want to take another look at your compensation structure. “Paying people hourly might be encouraging them to take longer than required to complete a task. The sales team might only be interested in getting their commission,” says Jeff. “Take a look at your compensation plan to ensure it is creating the intended results.”

HOW CAN YOU PREVENT FRAUD IN YOUR ORGANIZATION?

Fraud isn’t easy to detect. “If somebody is going to defraud you, they have time to plan it out and often it is only discovered by accident, if at all,” says MNP Assurance Partner Jeff Westcott, CPA, CA, LPA, BBA, from the firm’s Toronto – West office. “Prevention is key.”

Prevention begins with setting the tone from the top. If employees see the owner putting personal expenses through the business, they get the message that those kinds of activities are OK. “This gets back to rationalization,” explains Jeff. “If the owner expenses something, he won’t mind if I take this from petty cash.”

Every organization should have a code of conduct that outlines management’s expectations for employees. It doesn’t need to be detailed and should be communicated to every member of the company. It’s also wise to establish a whistleblower hotline so people know they can speak up when they see something unusual, as this is the most common way of finding out about fraud. According to the ACFE’s report on fraud, 43.3 percent of the time, initial detection was the result of tips. Once the hotline is set up, you must determine the protocol for handling complaints.

The next step is to establish good internal controls. These may differ depending on the business, but typically include ensuring the accounting system is password protected and that staff are cross-trained so more than one person knows what is going on in each role.

Segregation of duties is very important; if the same person is responsible for the custody of cheques, recording the transactions in the accounting system and signing off on cheques, there is a higher risk of fraud occurring.

Determining which controls are required is only part of the picture. “You can have all the documented controls you want but if they sit in a binder on a desk and no one applies them, then what managers may think is happening is not happening. Get out there, test the controls and perform unannounced spot checks,” says Jacklyn.

CAN YOUR AUDITOR HELP?

The short answer is that it doesn’t hurt to ask. “If there is fraud, the chance of stumbling on it is low,” says Jeff. “But if you suspect something, bring it to our attention so we can consider it further and discreetly take a look at certain things.”

MNP’s auditors are required to consider fraud both in the planning stage and throughout the audit. They also speak with those charged with governance about fraud and help identify related risks within the business. “If you’re aware of an issue such as a lack of segregation of duties when it comes to payroll and you bring that to our attention, we can make sure to address it throughout the audit,” says Jeff. Jeff also cautions owners and management teams that there is a fine line between fraud and error. The difference is intent and that can be difficult to decipher. Adjustments are made in almost every audit and people naturally assume they are due to error, but savvy owners and managers should take a closer look to ensure there isn’t anything unsavoury occurring.

In reality, no organization can be completely fraud-proof. But keeping an eye out for the signs of fraud, having controls in place, ensuring employees know that stealing is not acceptable and talking to your auditor during the planning stage minimizes the risk.

For more information on this topic, contact Jacklyn Davies at 604.637.1597 or Jeff Westcott at 416.641.4951 or your local MNP Business Advisor.
Often, Lionel Cochey, CISSP, CRISC, CISM, a Senior Manager with MNP’s Technology Risk Services practice in Calgary and Leader of Information Security and Privacy for the firm, is asked the question, “Why do we need security policies?” Lionel adds this is a very good question. The short answer is that security policies—which include policies for information technology, access management, acceptable use, change management, logging and monitoring, back-up and disaster recovery, among others—are critical to an effective security program. Formal policies, procedures and guidelines set the stage for success, telling everyone in the organization, including employees and system administrators, what the detailed expectations are. Simply connecting a firewall or an anti-malware solution is not sufficient anymore to be protected against today’s threats. Policies form the basis of a program that helps protect the organization from internal threats and external attacks, which are becoming increasingly more elaborate and more technologically advanced.

Having an information security program without policies in place is, says Lionel, a very unstable situation. “You might have an experienced IT manager who knows what he or she is doing, but what if the manager leaves or is replaced by a different person?” he asks. “If you don’t have well-documented policies and corresponding procedures and guidelines, the new person may adopt different and unsafe processes that put your information at risk.”

Information security is an increasing concern for organizations of all sizes as owners, management teams, boards and other stakeholders gain a better understanding of the potential impacts of a breach. There are a range of solutions on the market as well as best practices that can be implemented to enhance security but if you’re managing security on a piecemeal basis or simply not putting enough focus on the fundamental components of a security program, you may not be mitigating risk as much as you think you are.

The strength of your information security program depends on the quality of your policy documentation
Another reason to get documentation in place is that compliance requirements and regulations for specific industries are maturing. Until 2013, compliance standards set out best practice security controls for organizations to implement. But recent updates to frameworks such as ISO 27002:2013, PCI DSS version 3 and NERC CIP version 5, set a new expectation to handle security as part of ‘business as usual.’

“You need to have an ongoing security program that proactively monitors security and you need to be very reactive to changes to your environment and the organization,” says Lionel. “A review and update of your controls at a point in time, even if it’s annually, is not sufficient. Your environment and needs will change, as do external threats, and security policy documents and controls should be integrated into the daily operations”.

Developing and maintaining security policies, procedures and guidelines takes time and is complicated. “Today’s organizations deal with many challenges such as higher numbers of increasingly complex threats and the need to secure a variety of IT systems, some of which may be old architecture,” says Trac Bo, CA, CISA, CRISC, ABCP, CGEIT, MNP’s Technology Risk Services Leader. “There are a lot of moving parts to information security,” he adds. To strengthen your security program, you should consider your people (and stakeholders) and the parts they play in the business; define and formalize processes; and implement technology solutions—a tall order when you’re busy conducting business.

“There is a tendency to look for a quick fix—implement a technology solution and move on. Implementing detailed policies and procedures is not glamorous and sometimes organizations forget how important it is,” Trac says. “But if you take the time to define your objectives and understand the relevant IT and security risks, you can take a prioritized approach that will be more efficient, garner support and in the end provide practical policies that address key risks and add value”, he adds.

That means security policies must be tailored to the organization and the environment it operates in. MNP has developed templates based on best practices and experience. After understanding the client’s environment and context, MNP adapts the templates for policies, procedures and guidelines that fit the organization’s unique requirements.

Which security policies are in place will vary. “One organization may need to have 17 policy documents while another may just need a large single standing document,” says Lionel. The important thing is to ensure that the policies address the requirements.

The work doesn’t stop after you have developed a tailored security program that is built on a set of comprehensive and detailed policy documents. Full implementation and adoption across the organization is extremely important, because if the policies and procedures aren’t followed, the program will not be effective. Specifically, achieving adoption should consider that people will have varying levels of awareness about and understanding of the need for information security.

With the support of senior management, and a training and awareness program across the organization it is possible to build up a culture of security so that everyone proactively participates in the protection, detection, and remediation of security threats to the organization’s information and systems.

“It’s an iterative process and a long-term commitment. You want to set milestones, monitor compliance and continue to improve awareness,” says Trac. “Part of how Lionel and his team help our clients is by defining monitoring mechanisms so you can ensure your carefully created policies and procedures are being followed.”

Ultimately, building a strong security program takes dedication, time and effort. But in today’s world, where organizations face threats ranging from a single disgruntled employee to faceless hackers from the other side of the world, doing it right and ensuring you have quality policies, procedures and guidelines in place is a necessity.

For more information on this topic, contact Trac Bo at 403.537.8396 or Lionel Cochey at 403.536.2183 or your local MNP Advisor.
STRUCTURAL MATTERS

In a post-recession market, structure may take precedence over price when planning to sell your business

Prior to 2008, owners selling their businesses often received a significant percentage of the purchase price in cash and headed off into the sunset. The recession changed that. Today’s vendors are regularly asked to accept alternative deal structures such as vendor take backs (VTBs), earn outs, equity in the purchaser and / or holdbacks. Structure, in fact, may now be more important than price when planning to sell a business. “What we’re seeing over the last few years is that the structure of deals are changing and the post-sale business performance risk is being transferred from the purchaser to the vendor,” explains Anne Hinds, CPA, CA, a Partner with MNP’s Transaction Advisory Services in Ontario. “Vendors are being asked to stay on with the business to assist with integration and they’re receiving less cash in favour of other forms of consideration.”

Equity
One trend is to offer to purchase a portion of the company and keep the existing shareholders involved in the business. Over the past two and a half years, MNP’s Wes Priebe, Senior Vice President and Director, MNP Corporate Finance Inc. in Edmonton, has seen a significant shift in this direction, with many purchasers choosing to buy 70 to 80 percent of the company. “If the existing shareholders retain a portion of ownership the transition will be smoother and the vendor may receive a higher value for the percentage of shares retained at a later date if the value of the business is increased through new ownership. But it is very important, especially if the company is privately held, to define when you’ll be able to sell your remaining shares and have an exit strategy,” says Wes.

Earn outs
After the recession hit, the predictability of financial performance has dropped off. Over the past several years, business owners have worked hard to rebuild and generally cash flow is trending upwards. “The concern for the purchaser is whether this trend will continue. That’s where the earn out comes in. For two or three years post acquisition, the purchaser will pay the vendor a portion of the profits on any amount in excess of the financial performance being bought today,” says Wes. The risk for vendors is that they won’t receive anything if growth plateaus, which may not be in the vendor’s control, even if he or she stays with the company. It’s critical to establish proper parameters of the earn out at the time of the transaction in order to minimize risk.

Vendor Take Backs
With a VTB, the vendor carries some portion of the financing which is repaid over two or three years. VTBs were common even before the recession because they are a convenient way for the purchaser to close the gap between the amount of financing raised and the purchase price. The VTB could be a portion of the goodwill – which purchasers can’t get financing for – and vendors must be aware that, in most cases, there will be no security.

Equity in the Purchaser
Another trend is for the purchaser to offer the vendor equity in the purchaser. This gives the purchaser a way to help finance the acquisition but it can transfer risk to the vendor because a portion of consideration is equity in the purchaser’s company, which the vendor probably doesn’t control and so cannot necessarily influence share price. The vendor may also not have a liquid market to dispose of equity in the purchaser, thus reducing the ability to convert this portion of the purchase price to cash. On the other hand, if the purchaser is successful, the vendor can participate in future growth.

Holdbacks
Holdbacks involve holding a portion of the sale price in a trust pending a specific outcome. For example, an acquirer might hold back cash until the receivables bought at the time of the transaction are collected. Holdbacks are typically short-term.
Other reasons to consider structure over price

Many business owners work hard to establish a strong reputation, loyal employees and good client base—and they want to preserve what they’ve built. While strategic buyers might pay more than financial buyers, they’re also more likely to change how the company operates as well as its culture.

“Vendors may have conflicting objectives. They may want to maximize how much they get on the sale of the business for retirement but they might also want to consider a lower sale price if transitioning the company to family or arranging a management buyout. Some might consider a lower sale price if it’s important to find a local purchaser as opposed to an international purchaser. It could save a lot of time and money to think about these considerations before you sell,” says Anne.

Managing the challenges

Owner-managers looking to divest need to prepare for the structures they can expect to see in offers so they can maximize the value they receive. Some steps to consider are:

**Vendor due diligence:** “A self due diligence can reduce the odds of an unsuccessful deal that arises from matters found when the potential purchaser conducts due diligence,” says Anne. This can also help you minimize price reductions because you’ll be able to quantify exposures such as those related to environmental issues or international tax.

**Extract redundant assets:** Canadian owner-managed businesses often co-mingle non-active assets such as real estate, investment portfolios, life insurance and personal property with the active business. Extracting these as far in advance of the sale as possible will allow for more tax planning opportunities.

**Review your value expectation:** There are two types of value gaps. The transaction gap is the difference between what was paid (expected value) and the maximum that should have been paid (true value). The integration gap is the difference between the true value and what was achieved.

Due diligence before the sale and an external review of projections and value expectations can help reduce the transaction gap so you get the price you want. To reduce the integration gap in cases where the vendor retains a stake in the business, question the potential purchaser about their plans for the business.

**Understand what you’re getting into:** Gain an understanding of the value or synergies the purchaser hopes to achieve by acquiring your business and understand your role going forward to ensure those are achieved.

**Improve operations and prepare for employee transitions:** Plan for and implement a smooth post-transaction integration. While this might be construed as the purchaser’s job, taking steps to ease the transition pre-sale can improve your business value and the sale price while easing the transition process.

**Analyze the tax implications:** Vendors may want to sell shares to get the capital gains exemption. Purchasers may want to buy assets to get a write-off against profits. While that may seem to be an impasse, MNP Corporate Finance has options available to help both parties determine what’s best.

“We can work with the vendor or purchaser to negotiate what’s being sold and to determine the most tax-efficient price allocation. Sometimes we can be neutral to one side and have a benefit to the other, while other times there are opportunities for a hybrid share / asset sale,” says Anne.

The price you receive for the business you’ve built is always important, but the structures of M&A transactions today mean that vendors can expect to see less cash and more risk. In this new reality, owner-managers should focus on the things they can control to help maximize the value they receive for their businesses. Working with professionals who can help you analyze your options and determine the best course of action is another good way to reduce your risk and ensure you get the value you deserve.

For more information on this topic, contact Anne Hinds at 416.263.6923 or Wes Priebe at 780.453.5398 or your local MNP Advisor.
Compensation tells a story that staff members and potential employees hear loud and clear, whether management realizes it or not. That story demonstrates what positions the management team thinks are valuable: which skills they want to reward and what they value in each position. If the story doesn’t align with the company’s philosophy and what actually brings value to the organization, the result can be a compensation system that does not support the attraction and retention of the right talent.

“More and more business value is derived from people and knowledge resources, so it’s important to ensure that recruitment practices and compensation strategies position organizations to attract and retain employees with the right skills,” says Heather Lannigan, MIRHR, BBA, CHRP, a Manager with MNP’s Human Resources Consulting practice in Toronto. “The specific skills an individual company will want to attract and reward depend on their overall business strategy.”

More specifically, many organizations are seeking employees with strong technical skills for managing and sharing knowledge as well as excellent teamwork capabilities. While they may have implemented tools to assess for those skills during the recruitment process, they may not be rewarding people for having and using them because of outdated compensation programs including job evaluation and performance management systems.

**UPDATE YOUR COMPENSATION PROGRAMS**

Job evaluation systems, which are used for determining the value of a position in comparison to other positions within an organization, provide an opportunity for organizations to compensate positions based on factors (such as skills or knowledge) that are important to the organization.

“If you’re using an outdated job evaluation system, you may want to review what you are rewarding as the skills and attributes that you valued in the past may have changed as your organization has evolved. To be more specific, today’s economy is a much more knowledge based than in the past. If you’re using an old evaluation system, you may not be valuing the skills and abilities that will make you successful today,” says Yvette Battistolo, BHRD, CHRP, CCP, Leader of MNP’s Organization and People Consulting team in Saskatchewan.

“For example, if your job evaluation system is designed to compensate a skill such as typing speed, it may be time to review the factors you are using to value positions to ensure those compensable factors reflect what is important for your success today. Rather than words per minute, an approach that values the ability to learn new technologies may more closely align with what you wish to value, and as a result, pay for.”
WHEN TO ACT

If you’re having difficulty attracting and / or retaining good people, it’s time to review your compensation program. Otherwise, be proactive and conduct reviews periodically. Yvette recommends the following:

Review your job evaluation system every five years to ensure you’re measuring the right things.

Survey the market every two years to see if salary ranges have changed.

ALIGNING COMPENSATION WITH YOUR ORGANIZATION’S PHILOSOPHY

Another challenge organizations can experience is a lack of alignment between the organization’s philosophy about compensation and how the compensation system is actually being administered. For example, “An organization might intend to link salary increases or bonuses to the achievement of specific objectives but continue to provide salary increases based on length of service,” says Heather. “Another organization might state that it values people who work as a team, but continue to use performance metrics focused on the achievement of individual objectives.”

When designing a compensation program that rewards specific behaviours or the achievement of objectives, it’s critical to determine whether the behaviours or objectives an organization wants to reward are being exhibited. One way to accomplish this is to ensure that targets or goals in an employee’s performance plan are S.M.A.R.T, or: Specific, Measurable, Actionable and Realistic, with clear Timelines.

HOW COMPETITIVE IS YOUR COMPENSATION PROGRAM?

While much of the work of aligning compensation to what brings value to an organization is done internally, organizations may be challenged to attract or retain employees if compensation levels are not competitive with the external marketplace. For this reason organizations often look externally to understand what’s happening in the marketplace. A competitive compensation program is critical for attracting top talent and today’s job market changes at lightening speed.

To stay on top of what’s happening in your industry, you can purchase public surveys that report on compensation. Or, to obtain more specific information, you can design and implement your own customized survey.

“Depending on what information you are looking for, MNP can work with you to identify relevant comparator organizations as well the types of information to collect. We might look at pay rate, benefits or other compensation practices such as bonus systems or reward programs,” says Yvette. “If, for example, a client wants to know exactly how executives in the industry are being rewarded, we can look specifically at that.”

To stay competitive and ensure your organization is viewed as an attractive employer, you need to compensate the right skills by ensuring you have an up-to-date job compensation program and evaluation system that is aligned with your organization’s strategic objectives, goals and compensation philosophy. With such a high level of competition for talent, it’s critical to take a close look at what you’re telling employees you value when compensating them and to take the steps that will help you ensure you’re telling the story you want to tell.

For more information on this topic, contact Yvette Battistolo at 306.751.7696 or Heather Lannigan at 416.515.5062 or your local MNP Advisor.
YOU’VE OUTGROWN YOUR TAX STRATEGY.
Where do you go from here?

Realizing the full potential of your business requires an understanding of the tax challenges you face within your provincial, national or even international markets. MNP’s Tax team delivers the experience and strategies both public and private companies need to minimize your exposure and maximize the returns to your business.

Contact your local MNP advisor or visit MNP.ca to learn more.