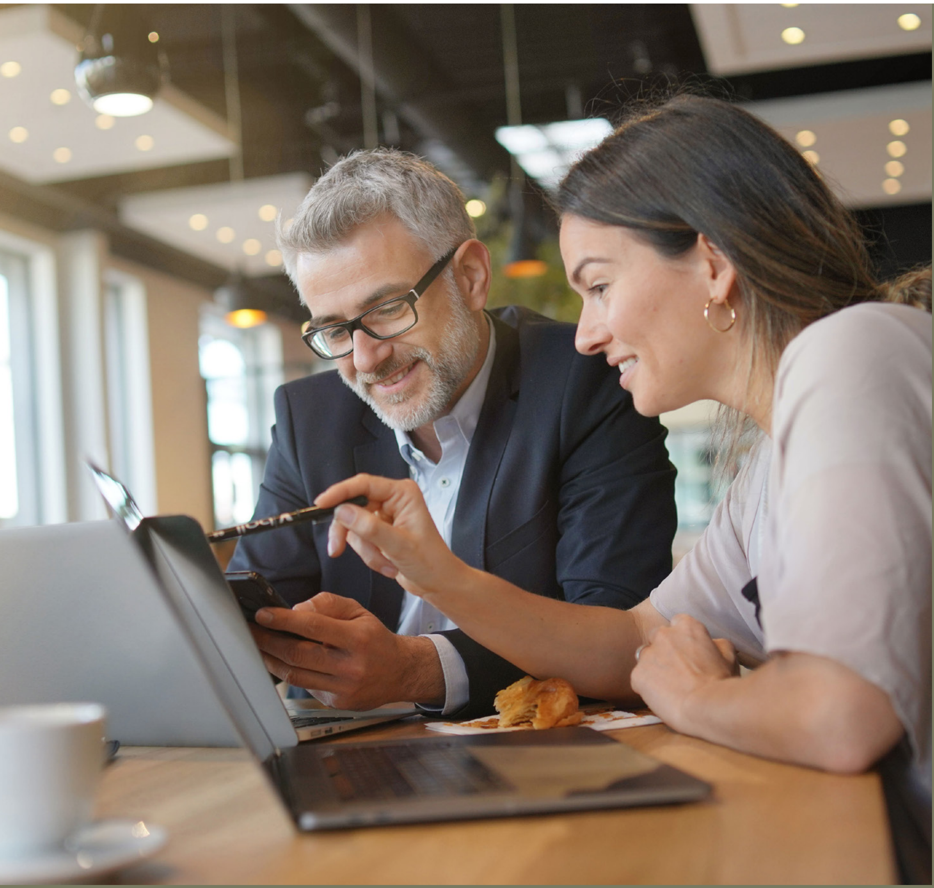
RICHTER'S TRANSITION BOOK
FOR YOUR FAMILY ENTERPRISE

RICHTER

HOW TO TRANSITION YOUR BUSINESS

SIX HOLISTIC STEPS



RICHTER'S TRANSITION BOOK FOR YOUR FAMILY ENTERPRISE

YOUR TRANSITION SUCCESS STORY BEGINS TODAY

Many business owners are unaware of the different options available when it comes to selling or transferring their business. It's clear that owners put an enormous amount of time and effort into growing their companies. However, few put as much time and effort into their exit strategy.

> **For many entrepreneurs, retiring comfortably after a long and successful career is the end goal – but this comes with a lot of necessary preparation, and decision making that must start now.**

Many business owners rely on the impending funds from such transactions to provide for their retirement. However capital gains from a sale alone can severely impact retirement plans. It's crucial to consider all options and plan thoughtfully. Planning now can help you maximize your return, minimize tax, and align future expectations with your current reality. With forethought and advanced planning, implementing proper strategies can help you avoid severe tax implications and allow you to keep the most money possible from the transaction.

Richter's Transition Book covers important steps in the seller's journey to help you take the first step towards your transition plan or sale of the business.

ABOUT RICHTER

Founded in 1926, Richter provides assurance, tax and wealth management services, as well as business advisory services to successful entrepreneurs, executives and business families. Our commitment to excellence, our in-depth understanding of family governance and business issues and our practical problem-solving methods have positioned us as one of the largest independent advisory and consulting firms in Canada.

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STEP 1 –
HOW TO GET STARTED

Ask yourself: Should I stay or should I go?

Planning for the transition of your business does not necessarily mean putting yourself out of a job. Perhaps you enjoy what you do, and you can't foresee a day when you are no longer involved to some degree in the business.

KEY TAKEAWAYS:

- Realizing this from the outset can save you a great deal of heartache in the future – especially if you build this into your plan.
- Oftentimes, as a former owner, you can play a very important role even after the business has transitioned to a new owner, and this can be of benefit to you, as well.

While you were the owner and operator, your attention was divided several different ways, but having sold, you may have more time to focus on ideas that piqued your interest throughout your career. There may be a multitude of special projects, untapped markets or potential product lines that are of interest to you, which time hadn't allowed you to explore previously.

> **As a former owner, you can play a very important role even after the business has transitioned to a new owner.**

If the transition of your business is planned in an organized manner, such projects may provide you with the perfect consultative role to play in the 'new' company. After all, your knowledge, insights and understanding of the existing business can can be valuable to any purchaser.

Conversely, staying on as a 'consultant' to the business might not hold any allure for you. The beaches down south or the cottage up north may be calling your name – and you want to answer that call. You may have an ideal retirement date in mind. What is key here is identifying this in advance, to ensure the smooth transition process that you desire, when you are ready to do so.

Learn more on how to get started with your business transition.

STEP 2 –
HOW TO PLAN FOR TRANSITION

Begin now: Plan your exit strategy

The most significant change in the life cycle of a business is also an inevitable one: the transfer of ownership. This can involve:

- an inter-generational transfer of a family business;
- the sale of a business to its management or employees;
- or a sale to an outside third party.

Oftentimes, this transfer is intentional, but sometimes it occurs due to unexpected circumstances, like death or disability. Regardless of how, or to whom the business is transferred, proper steps need to be taken now, to ensure a successful transition when the time comes.

A successful exit plan can take several years to implement. However, with the necessary diligence, the resulting value of your business will be well worth the investment for you and for the next owner.

You need a plan that is deliberate, and all-encompassing. To navigate what may seem like an overwhelming process, our business advisors can help you map out:

BUSINESS VALUATION

Maximizing the value of your business starts with knowing how much it is worth today. Richter consultants can work with you to develop a professional valuation that will help establish the baseline, and drive decisions that lead to a value's growth for the long term.

TAX PLANNING

Taxation of capital gains resulting from the sale of a business can impact your retirement plans. Yet with proper planning, it is possible to significantly reduce, or even eliminate this tax. Alternative tax strategies should be considered and implemented early on, to minimize taxes at sale time.

TRANSACTION ADVISORY

Intricate endeavors require professional guidance. You only sell your business once. Whether it's performing seller due diligence, providing reliable financial forecasting, or developing a post-acquisition integration plan before the transaction is completed, we take a hands-on and innovative approach to complex transactions for our clients.

STEP 2 –
HOW TO PLAN FOR TRANSITION

ASSURANCE AND ACCOUNTING

Accounting standards and financial reporting requirements are complex. Buyers, banks and other investors derive comfort from financial statements subject to an assurance report, be it a review or audit, from the company's firm of accountants. Richter professionals can also help prepare financial records and advise on proper internal processes and procedures.

ESTATE AND SUCCESSION PLANNING

Estate planning can be a very sensitive matter as finances intertwine with family dynamics. Often these issues lead to paralysis, as all options can appear problematic. Our collaborative approach, and years of experience dealing with families instils confidence from all parties, and helps pave the way for the smooth transfer of assets, including your business, to the intended parties.

Visualize your plan

Artists will tell you that the best paintings are created when the artist visualizes the painting hanging on the wall before they make a single mark on the canvas. The same is true for selling a business. To maximize value, one must start with a vision of what that business is going to look like on the day it is sold.

WHAT ASPECTS OF THE BUSINESS SHOULD YOU BE VISUALIZING?

There are many answers to that question, among which are the size, the structure, the culture, etc. Once you have visualized these aspects of the plan and you have a clear idea in mind, some of the more specifics can then be documented.

- How many team members will be required and in what positions?
- What systems and processes will be required to support volume, people, etc.?
- How much financing will be required in order to achieve your vision?

Studies show that when a goal is put down in writing, it is much more likely to be achieved. It's also true when you're thinking of selling a business.

KEY TAKEAWAYS:

- Documenting your vision and what is needed to achieve it will undoubtedly identify some obstacles or deficiencies along the way.
- The beauty of developing a succession plan well in advance of your target retirement date is that an action plan can address any deficiencies before they become serious issues that affect the salability of your business.
- Plans also clearly communicates the role of each stakeholder and can serve as a contract between stakeholders to support the plan.
- A detailed review of the business's current position and a visualization of its future is absolutely necessary.

STEP 2 –
HOW TO PLAN FOR TRANSITION

> **An action plan can address any deficiencies before they become serious issues that affect the salability of your business.**

An effective action plan will identify the tasks that need to be done, the persons taking ownership of the tasks and deadlines for achieving the goals. The plan should also be flexible, to adapt periodically to the changing needs and objectives of all stakeholders involved. Checking in on the plan will also ensure it's up to date and working smoothly. This helps implement needed changes consistently and ensures buy-in from everyone involved.

Look at the big picture

It's important to think through the instances beyond retirement that may cause a business owner to leave his or her business: divorce, death, or disability.

While unpleasant to consider, planning for the possibility of each instance is necessary. The last thing anyone wants to see is the hasty sale of a business due to an unplanned for, unforeseen circumstance. The best time to plan for a crisis is before the crisis occurs. An estate plan, a pre-nuptial agreement, a buy-sell agreement – all can contribute to a comprehensive transition plan and provide protection for each "what if" scenario.

> **The best time to plan for a crisis is before the crisis occurs.**

EVERYTHING ELSE... AND EVERYONE ELSE...

The starting point in the process is to determine your needs as the owner. What is your expected timeline for exiting the business? What do you need from the business upon retirement? How will the business continue without you?

Once you have considered these questions, it is then crucial to identify the needs and expectations of other key stakeholders in the business, be they other family members, business partners, or even loyal employees, customers and suppliers. Family, business, and ownership systems are all equally important to the long-term success of the business; all should be given equal respect and consideration.

Considering all the central people close to the business, it's important to account for all options in succession. A successful transition involves determining all viable alternatives, given the stakeholder requirements. Options can be grouped into three different levels.

STEP 2 –
HOW TO PLAN FOR TRANSITION

1. **Legal Options** – how will the wealth of the business be transferred? e.g. gift, annuity, buy-sell agreement, partnership, etc.

2. **Funding Options** – how will the transfer be funded? There are many ways to structure a financial transaction: self-funded, insurance, cross purchase, working capital, public offering – viable alternatives will depend on your specific situation.

3. **Managerial Options** – who will ultimately be responsible for leading the business? Will there be more than one leader? How will you transfer your knowledge over to the new leadership? Do you want to be involved with the business after the transfer, or are you willing to walk away?

Selling a business is not an immediate process; it takes time to explore the different options and prepare the business for sale. This is best started well in advance of actual retirement; five years is good, 10 years is even better. Thinking with the end in mind (i.e. your retirement goal), is the only way to make certain that all decisions made along the way are consistent with the said goal. Planning early is the best way to ensure a pain-free, smooth transfer, while maximizing your returns.

Start drafting your transition plan today!

STEP 3 – HOW TO APPROACH THE TRANSITION OF YOUR BUSINESS

Consider all options

Many owners and entrepreneurs suffer from tunnel vision when it comes time to pass the business on. However, there are a number of options for exiting a business and all of them should be investigated thoroughly and considered equally before reaching a final decision.

There are **three main alternatives** for exiting the business.

1. **The Internal Transfer –** There are a variety of options within this alternative. For example, the business may be passed down to a family member within the business, a family member that is not currently involved, key management personnel or a group of employees. For any of these scenarios to work, it is important to gauge the requirements, wishes and competencies of your key stakeholders when contemplating this alternative for your succession. Additionally, there are a variety of methods that can be employed in an internal transfer.

    - Direct sale of shares
    - Redemption of outstanding shares
    - Stock options to new owners
    - Employee Share Ownership Plans
    - “Spin-off” of part or all of the business
    - Recapitalization of the company

    Exploring each option to determine the method that is most advantageous to all stakeholders is crucial.

2. **The External Transfer –** An external transfer is a straight sale to an outside, third-party purchaser. The feasibility of this option depends greatly on how well the business has been prepared for sale.

    - The value of the business must meet the expectations of the owners.
    - There must be a backlog of orders and an asset base to sustain the business.
    - The business must continue to be viable without the ongoing involvement of the former owner.

    An outside purchaser is unlikely to pay top dollar for a business which does not have people, systems, and procedures in place that will allow it to continue to function smoothly.

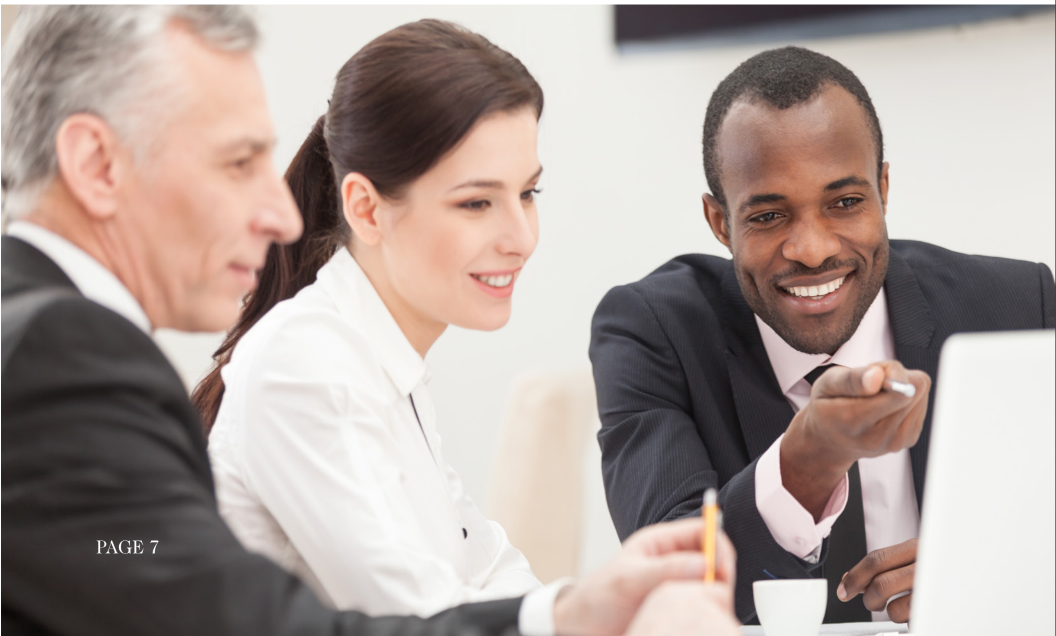
STEP 3 – HOW TO APPROACH THE TRANSITION OF YOUR BUSINESS

3. **Liquidation –** This is generally the 'fallback' option if the other alternatives do not work out as planned. This is generally most common for personal service businesses that are not salable. Advanced planning can still enhance the value received by an owner who liquidates his or her business, although tax consequences still come into play.

   It is also critical to develop alternative plans in case the preferred option is not feasible. By building flexibility into the plan, you are in the best position to deal with unexpected changes that may occur and still realize your goals within the time frame you have selected.

   Of course, the wisest of business owners are those who consult their advisors for professional advice and input. These are often the people who know your business best (after yourself, of course) and who can look at your options through a third-party perspective with a degree of impartiality and detachment.

Don't miss a step! Make sure you have all the information for a seamless transition – talk to one of our experts.



STEP 4 –
HOW TO MAXIMIZE YOUR VALUE

The value of the business is actually inversely related to the amount of time that the owner spends on it.

What it's worth now, and how

Maximizing the value of your business starts with knowing how much it is worth today. It's crucial to assess the current performance of the business and determine if it is ready for transition. Decisions can then be made on what needs to be done to prepare the business.

If you as the owner are still personally responsible for the many daily business functions (finances, strategy, operations management), you are the one holding all the cards, and not many buyers would come to the table willing to bet big on the company once you are gone.

KEY TAKEAWAYS:

- Many educated buyers would see this as a real detriment to any company: once the owner goes, so too does the business knowledge and intellectual property.
- To mitigate this, and enhance the value of your company, you must start a transfer of knowledge and of the day-to-day responsibilities to people you trust.
- Whether it's promoting internal team members and nurturing their potential to lead, or bringing in the right experts to manage such things like the finances or operations, these people become valuable assets that may actually help increase company value and attract the right buyer.

> " To enhance the value of your company, you must start a transfer of knowledge and of the day-to-day responsibilities to people you trust.

While you may think that adding such people means additional costs, more salary, and less profit – this is usually only a short-term problem.

Once you have skilled people in place, performance can increase, and these people can help grow the business further. We saw this happen in an instance where after implementing these changes, the owner sold the business for significantly more than anticipated originally. Why? Because the added management had helped increase profits substantially!

AS A PRECURSOR:

These changes can take roughly two (or more) years to implement. Restructuring to make a company more attractive to an outside purchaser is a great opportunity to consider. Business owners start transferring knowledge and exiting slowly with less pressure. **A detailed action plan formulated to address each area in need of development will help attract the right buyer and lessen the stress of the process along the way.**

Get more information on business valuation.

STEP 5 –
HOW TO SELL LIKE A PRO

Be transparent

Much like your car needs regular oil changes to keep it running optimally, regular audits and careful financial reporting can help ensure your business is running at its peak. It's crucial to have the proper reporting and assurance standards in place at any point in the business cycle, but even more so when you are considering a potential sale.

AUDITS ADD CREDIBILITY TO YOUR FINANCIAL INFORMATION.

1. A quality audit can aid in your decision-making and offer insights into reducing waste, tightening controls or spotting trouble before it occurs.

2. A well-conducted audit is also a key tool when dealing or negotiating with banks, investors, joint ventures or potential buyers.

3. The more open and organized your books are, the better your chances for obtaining financing or attracting the right buyer, whenever that time comes. Transparency adds weight to your selling power.

> “Transparency adds weight to your selling power.

Staying on top of the latest financial reporting regulations is also important in the lead up to a sale. Accounting standards have become much more complex in recent years and if your company doesn't adhere, you may end up facing major challenges that could affect your selling price. To ensure you're compliant, a qualified professional can help your management team through the process on timely and specific issues, or with entire projects, regardless of the accounting standard (ASPE, IFRS, US GAPP), or financial reporting and continuous disclosure requirements under specific securities regulations (AMF, SEC). With the right guidance and meticulous financial reporting structures in place, you will be better positioned to negotiate when it comes time to sell.

Keep up with the paperwork

Before you seek out a qualified buyer, it's important to make certain representations as to the financial status of your company to justify the price you hope a buyer will pay. This price must be derived from realistic information.

How can the purchaser really be sure? What's involved in finding out? What can make the purchaser's own due diligence *assuredly* diligent – and avoid a nasty dispute when the “real numbers” come to light?

By going through the proper due diligence, you will save time and effort – and ensure you close on a deal based on solid, accurate information.

STEP 5 –
HOW TO SELL LIKE A PRO

In some ways the principles of **due diligence** are similar to an audit even though it's decidedly a unique and separate engagement. There are tests, reviews of key information and recalculations, but they are, in general, confined to certain areas.

> "By going through the proper due diligence, you will save time and effort. For many entrepreneurs, retiring comfortably after a long and successful career is the end goal – but this comes with a lot of necessary preparation, and decision making that must start now.

THE 10 MAIN ONES ARE:

1. Tax history – the nature and frequency of reassessments
2. Aggressive accounting – especially concerning overstatement of assets, or not recognizing all liabilities
3. Obsolete inventory in need of a write down (prevalent in many businesses, and a big balance-sheet item)
4. Non arms-length transactions (with relatives or the owner, who might not have taken salary, but rather a dividend)
5. High discretionary expenses
6. U.S. and other tax filing requirements that need to be fulfilled
7. Identities of those on payroll and their clear function – and what would the financial position of the company look like, after adjustments, if family members need to be replaced?
8. Cutbacks in R&D in anticipation of sale
9. Understated income as a result of private company discretionary spending (or at least the vendor's representations that this was the case)
10. Overstated income based on spending cuts before a sale which may impact the future profitability of the business

Accounting due diligence is a necessary part of any successful merger and acquisition process.

STEP 6 – HOW TO KEEP YOUR FAMILY FRONT OF MIND DURING THE TRANSITION

Carrying on your legacy

Are you satisfied with your current succession plan? Have you considered the tax consequences? This last section of Richter's Transition Book covers important aspects to consider when it comes to aligning your business interest with your family interest.

Plan for your success[ion]

All too often, business owners neglect to plan for the succession of their business. While lack of planning is likely to affect how an owner transitions out of their business, there can also be severe implications that could impact the 'when', 'what', 'who' and 'why' aspects as well.

As a business owner, you have worked long and hard to build up a valuable asset and at some point down the road you will likely want to enjoy the fruits of your labour and retire. Between now and then, however, there are a number of questions that need to be answered:

- When do you want to retire?
- How are you going to retire?
- How much will you need in order to retire?
- Who will run the business if you are unexpectedly injured and no longer able to work between now and your expected retirement date?
- Are you going to sell your business, pass it along to another generation or just close the doors and walk away?

IT IS HUMAN NATURE TO GENERALLY FEAR THE UNKNOWN

Issues and questions like the above are often brushed aside, with the intention of dealing with them "later". Addressing your own succession involves answering a lot of difficult questions for you, the many other people involved with the business, and your family. Besides, your time is much better spent managing the day-to-day operations of the company, right? Wrong!

THE OLD CLICHÉ IS VERY TRUE IN THIS CASE – WE ARE OFTEN 'OUR OWN WORST ENEMIES'.

A lack of preparedness for the transition of your business can ultimately harm the company and lead to family conflict and discord. That's why it is so important to find the options that best meet the needs of all involved parties.

- A good succession plan should summarize the decisions made and the rationale behind each decision.
- It should also clearly communicate everyone's role going forward.
- A written succession plan acts as a road map and a contract to ensure everyone involved supports and is accountable to the plan.

STEP 6 – HOW TO KEEP YOUR FAMILY FRONT OF MIND DURING THE TRANSITION

> **A good succession plan should summarize the decisions made and the rationale behind each decision.**

A WORD OF CAUTION

The succession plan is not a static document; many of the assumptions used in the planning process may change over time. However, addressing the hard questions early on means tough conversations down the road can be handled more easily. The succession planning document should be reviewed and updated periodically to ensure that it remains in line with your objectives.

The legacy carries on

Succession planning helps ensure the family business and its legacy will live on for another generation. When it comes to a family business, succession planning can be a sensitive matter. It's truly unfortunate when a divisive issue ultimately ends up affecting the current business negatively. Even more so, disagreements or opposing goals can ruin relationships and destroy family bonds.

> **Succession planning helps ensure the family business and its legacy will live on for another generation.**

Due to the emotional component involved and the in-depth knowledge required of legal, tax, and financial issues, succession planning can be a very complicated process. Working with experienced and independent professional advisors can help accelerate the process and ensure that thoughtful deliberation is given to all issues.

Proper succession planning through an experienced advisor helps:

- facilitate much needed discussions with each family member;
- navigate sensitivities objectively; and
- eliminate the chance of potential conflicts becoming costly issues.

There are many implications that can befall a business owner. Regardless of whether the end goal involves the sale of a business or transfer to a new generation, it's imperative to protect yourself, and all that you've built. A solid plan will prepare you for a realistic exit and help avoid potential conflicts that could damage your company, your finances and possibly, your family's well-being. With proper exit planning, managing the unanswered questions earlier provides for a smoother transition and a happier retirement.

STEP 6 – HOW TO KEEP YOUR FAMILY FRONT OF MIND DURING THE TRANSITION

While as tragic as these instances can be, the impact can go beyond just you as a business owner, and beyond your family, to affect the livelihood of your business, employees, their families, and even your customers.

Prepare for the unexpected: When "What If" Becomes "What Now"

One of the most important – but often ignored – reasons for preparing for the future succession of a business is to minimize the fallout from the unexpected.

It's understandable that preparing for these types of situations usually falls to the end of the to-do list. Just the thought of such circumstances is enough for many to choose to ignore and focus on the tasks of a more immediate nature. Yet, the potential for such instance is there. It's unpleasant to think about what may happen should you as a business owner get seriously hurt in a car accident, contract a life-threatening illness while travelling, or take an unexpected turn that leaves you incapable of managing the business.

Things don't always go according to plan. Therefore, the business has a much better chance of surviving if the owner has made preparations, in advance, for it to continue without him/her there.

HOW? WITH CAREFUL PLANNING THAT ENCOMPASSES ALL ASPECTS TO PREPARE FOR THE 'WHAT IF':

- **Succession Planning** – Develop a strong and capable management team and delegate responsibility to the team.
- **Insurance Planning** – At least bi-annually, life and disability insurance policies should be reviewed to ensure adequate coverage in case of death, illness, or disability. Insurance strategies can often include funding the premiums using corporate assets in certain situations. This planning also involves the preparation and updating of proper wills and powers of attorney.
- **Tax Planning** – A proper corporate structure might allow you to multiply the Capital Gains Exemption on the sale of company shares. As a result, capital gains tax could possibly be eliminated entirely.
- **Exit Planning** – Develop and communicate plans for the business so that key stakeholders (family and senior management) know and understand your wishes. They will then be able to execute them in case of disability or sudden death.
- **Financial Planning** – A solid financial plan could establish family assets in addition to the business investment. This way, debts can be managed to maximize interest deductibility.

Put the plans in motion to mitigate the implications of an unexpected, yet potentially disastrous situation. After all, "What *if*" can turn into "What *now*?" very quickly – but with the right team of proactive advisors in place, you can avoid a nasty outcome.

STEP 6 – HOW TO KEEP YOUR FAMILY FRONT OF MIND DURING THE TRANSITION

Life Insurance

As we've said before, no one likes to think about the worst-case. Leaving your family ill-prepared for the time when you pass on isn't an easy a situation to envision, let alone thoroughly plan for.

There are many reasons why one might consider forgoing a robust life insurance plan. Some may believe it's not needed, thinking they have enough money to cover their family's financial needs after their death without it. Others may simply not view it as a promising investment or necessary spend. So why purchase life insurance?

Every family's situation is unique and individual circumstances are always different – and should be treated as such; however, there are three general reasons that we suggest you consider, when deciding whether to purchase life insurance.

TAXES AT DEATH

When you or a loved one dies, legal representatives file a final tax return to the Canada Revenue Agency (CRA), including taxes owed and taxes on the gain in the value of assets (car, cottage, etc.) transferred. This means that for certain individuals, the final total can be significant. Life insurance proceeds can give your family the necessary liquidity to pay the amount owed.

This is useful when it comes to family businesses. The availability of this liquidity means that a family is not required to sell assets such as a private company, or real estate, in order to generate the liquidity needed to pay the taxes owed.

PHILANTHROPY

By naming a charitable organization as the beneficiary of a life insurance plan, you can ensure that your money makes a difference even after your death. Upon death, it will be transferred to the beneficial charity. This procedure also means that your estate would receive a tax credit based on the amount of your donation. There are many life insurance strategies that can allow you to give generously and minimize the after-tax cost.

ESTATE EQUALIZATION

While questions of fairness in estate distribution can be complicated and lengthy at the best of times, life insurance can help with the process of estate equalization. Life insurance can play a significant role when trying to find balance during the distribution of liquid and non-liquid assets.

Whether you chose to purchase life insurance or not remains a very personal matter. We know that these are difficult conversations to have, because each family is unique and that presents several challenges to overcome. As independent advisors, we do not sell insurance in-house, but rather we advise on what unique

STEP 6 – HOW TO KEEP YOUR FAMILY FRONT OF MIND DURING THE TRANSITION

Life Insurance

ESTATE EQUALIZATION (CONT'D)

strategy is right for you and your situation. We always apply an after-tax perspective to strategies before investments are made; and certain opportunities such as life insurance can assist in not only protecting your family upon your death, but also protecting your wealth to ensure the maximum amount is passed on to family members or causes close to your heart, after you are gone. To help you on this journey, our experts are here to lend an ear and offer professional advice to help you choose the right solution for you and your family.

Don't leave them unprepared. Get more information on succession planning today.

RICHTER

BUSINESS TRANSITIONS TAKE TIME

RICHTER CAN HELP YOU NAVIGATE THE PROCESS SEAMLESSLY

When your business is your life (or at least a huge part of it) there are many considerations and emotions involved. Let our experts guide you through the process.

When we say our approach is holistic, we mean it. It's centered around you. Not just your company; not only your legacy, you. We advise business owners and their families both personally and professionally. Our professionals, (from wealth management, valuations, taxation and estates, to various other service lines) work collaboratively to provide advice that makes the most sense for you and your objectives – because we know that your work affects your personal life, and vice versa – they are of equal importance. Through early, comprehensive planning, our professionals assess every situation and present options to help you make informed, strategic decisions to make the most out of your unique situation.

Interested in learning more about Richter's approach to transition your business? Let's connect

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