The Navigator

Wealth Management

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC WEALTH MANAGEMENT SERVICES

Year after the sale of your business

Sale of your business – Part 4

This article is the last in a four part series intended to highlight key strategies to consider at different stages of your business. It isn't exhaustive but it may help you to gain deeper understanding of some of the strategies you are already using or that might be suggested to you. Part 4 introduces some tax, financial and estate planning strategies to consider in the year or years after you sell your business.

The other articles in the series are:

Part 1: Preparing Your Operating Company for Future Sale

Part 2: Planning the Sale of Your Business

Part 3: Year of sale of your business

In this article, the terms 'corporation' and 'company' are used interchangeably to refer to a Canadian-controlled private corporation (CCPC). In simple terms, a CCPC is a private Canadian corporation that is not controlled by a non-resident of Canada, a public corporation or a combination and no class of shares of the corporation is listed on a designated stock exchange. This four part series does not apply to public corporations or to businesses operating as a partnership or a sole proprietor.

Please contact us for more information about the topics discussed in this article.

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Tax strategies to consider

The fourth stage of selling your business is the year/s after the sale of your business. You may consider the following tax strategies in the year/s after the sale of your business. Each is discussed briefly in the following sections.

1. Reinvest in a new active business within 120 days after the year of sale to defer the tax on the sale of your business
2. Trigger capital losses on other assets (stocks, US currency, etc.) and carry back the loss to the year of sale (capital losses can be carried back up to three years)
3. If continuing to work for the purchaser, consider incorporating yourself. However, talk to a qualified tax advisor since the tax rules with respect to incorporated employees and personal services business have changed and may not be as attractive as before.
4. Other post sale wealth planning – financial plan, retirement income planning, update Wills, tax planning, etc.

Reinvest in a new active business

If you expect to reinvest some or all of your proceeds from the sale of your business in shares of another active Canadian business in the very near future, you may be able to defer the recognition of some or all of the capital gain on the original sale.

If an individual sells “eligible small business corporation shares”, you may be able to defer the recognition of all or a portion of your capital gain arising on the disposition to the extent that the proceeds are used to acquire “replacement shares”. A replacement share is generally defined as a newly issued share of an eligible small business corporation that you designate in your personal income tax return to be a replacement share and that you acquired in the year of the qualifying disposition or within 120 days after the end of that year.

Eligible small business corporation shares have the following characteristics:

- They consist of common shares issued by the corporation to you, the investor;
- The issuing corporation must be an eligible small business corporation at the time the shares were issued;
- The total carrying value of the assets of the corporation and related corporations cannot exceed $50 million immediately before, and immediately after, the share was issued; and
- While you hold the shares, the issuing corporation is an eligible active business corporation.

To be able to defer the capital gain, you must have held the eligible small business corporation shares for more than 185 days from the date you acquired them.

Generally, an eligible active business corporation is a taxable Canadian corporation, where all or substantially all of the fair market value of its assets are used principally in an active business carried on primarily in Canada by the corporation or by a related active business corporation while the investor holds the shares, or for at least 730 days of the ownership period, if you hold the shares for longer than 730 days. It can also be shares of, and/or a debt issued by, other related active business corporations or a combination of such assets, shares, or debt.

An eligible active business corporation does not include:

- A professional corporation;
- A specified financial institution;

Consider completing a financial plan to understand all your sources of retirement income and to determine whether you have an excess or a shortfall.

- A corporation whose principal business is leasing, renting, developing, or selling real property that it owns or any combination of these activities; and
- A corporation where more than 50% of the fair market value of its property (net of debts incurred to acquire the property) is attributable to real property.

If you are interested in pursuing this strategy, you should speak to a qualified tax advisor to confirm that your corporation and the corporation you are considering investing in qualify.

Trigger capital losses

If you have publicly traded securities that are in a capital loss position, you can consider selling these loss securities prior to year-end to trigger the capital loss. If your current year capital losses exceed your current year capital gains, the net capital loss can be carried back to offset capital gains in the prior three years. For example, if you sold your business in Year 1, the net capital losses in Year 2, Year 3, or Year 4 can be carried back to Year 1 to reduce the capital gains realized on the sale of your business. This may result in a refund of some of the taxes you paid in Year 1 on the sale. The decision should be made in conjunction with the investment merits of the securities you are planning to sell. If you want to repurchase the same security, you may consider waiting thirty days before the repurchasing the same security to avoid the loss being denied under the "superficial loss" rules. Ask an RBC advisor for a copy of our article discussing the superficial loss rules and planning strategies for more information.

Incorporate to provide continuing service to the business after the year of sale

If you are going to work for the purchaser after the sale of your business to assist with the transition, speak to a qualified tax advisor to determine the best way of receiving your compensation going forward – either as an employee or a consultant. If you are considered a consultant, you may be able to incorporate yourself so that the income you earn from the business is taxed at lower active business rates. If you are considered an employee then it may not be advisable to incorporate yourself since the personal services business rules make this option not as attractive due to a higher corporate tax rate and fewer expense deduction opportunities.

Financial and wealth planning

Work with an RBC advisor to manage your sale proceeds to create adequate retirement income to meet your lifestyle needs. Consider completing a financial plan to understand all your sources of retirement income and to determine whether you have an excess or a shortfall. An RBC advisor will take into account your income needs now and in the future and the effect of those needs, your risk tolerance and investment knowledge on asset allocation. This analysis, along with your objectives, will assist them in determining the types of investments appropriate for you. There are a host of different investment solutions available that satisfy different needs, including investments that are designed to be tax-efficient. An RBC advisor, as well as a qualified tax advisor, can assist you with these investment decisions.

If some of your sale proceeds are received by a holding company, there may be tax strategies available to enable your beneficiaries to withdraw funds from the holding company on a tax-free basis after your death. This type of planning should be incorporated in your estate plan. Working with a qualified tax advisor may help you determine the tax strategies that will work in your situation. In addition, they can assist you on an ongoing basis

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to determine the most tax-efficient ways of receiving the funds from your corporation in your retirement.

Finally, remember to talk to your legal advisor to determine if your Will and Power of Attorney may need updating after the sale of your business.

Conclusion

There are a number of planning strategies that may be appropriate in your situation after the sale of your business. Be sure to speak with a qualified tax advisor in order to ensure that you are taking necessary steps to maximize the proceeds from the sale of your business.

This article may contain several strategies, not all of which will apply to your particular financial circumstances. The information in this article is not intended to provide legal, tax, or insurance advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified tax, legal, and/or insurance advisor before acting on any of the information in this article.

Wealth Management

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