

# FORE SIGHT

PRACTICAL IDEAS FOR BUSINESS MANAGEMENT

## MAXIMIZING VALUES

### What's Driving Value in Your Business?

Business owners often talk about their companies like parents talk about their children. Their businesses, like their babies, are worthy of attention and investment because they will grow into something bigger and more mature — their owners' pride and joy.

But there's also a more concrete growth goal for these businesses: value. Owners are interested in maximizing the value of the company so that they can pass it along to the next generation as a legacy, or sell it and reap the rewards of their hard work.

What builds value in a company? There are several value drivers common to every business. Value drivers are the elements that owners can focus on to create and sustain value by reducing risk and enhancing growth. Here are a few to consider:

**Great People.** Good management is crucial to long-term success. The company needs leaders with strategic vision and the skills and talents to implement it. And if the business owner is leaving with the sale, a strong "second in command" must be in place to continue to lead. Many businesses are built on relationships, so having the right people in the right jobs is a must.

Owners interested in securing value through their people must look at their management team with a critical eye. Are they a solid group, skilled in the

appropriate disciplines and dedicated to pushing the company forward? Are they being compensated in a way that will keep them on board? A strong management team is what will keep the company moving in the right direction.

**Strong Cash Flow.** They say that "cash is king," and when it comes to building value in a company, cash indeed reigns. Good cash flow affords a company the ability to invest in new equipment, technology and research. It provides a buffer when times are slow, and it supports growth and vibrancy throughout the life of a company. When it comes time to sell, buyers are looking for cash flow to assist in financing the transaction and providing a return on their investment.

There are several ways to improve cash flow in a business. For example, good inventory management will keep cash free for other uses. Billing and

collecting quickly — and stretching payables — will keep cash moving. Also, watch competitors' prices. It may be that you're not charging enough for your products and services.

**Healthy Customers.** Healthy companies need a base of healthy customers. This means that the company should be working with many diverse and strong customers, not just a few key ones. If the company is too reliant on too few customers, its future may be in danger if a major customer starts buying from a competitor or incurs financial difficulties.

One way to build value through customers is by expanding the company's operational abilities. Expanded product lines, increased capacity and better service can deepen relationships with existing customers and attract new ones.

Paying attention to these drivers can lead to a more valuable and generally more sound company — important factors when it comes time to sell or move on.

*If you would like to discuss how to increase the value of your company, please contact Young Parkyn McNab LLP.*



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# Money Talk: How to Manage Compensation Expectations



Family business compensation. Is there any subject more emotionally fraught?

No matter who's making what in terms of salary, money is a topic many closely held business owners would like to avoid. For many, it's a question of discerning what is "fair." How much should family member employees be paid? What about family members who are shareholders, but not employees?

Keep in mind that all salaries for all employees should be based on market rates. Bonuses and dividends are a separate issue. Here are some ideas to help ease compensation decisions and discussions:

**Ask for assistance.** Look for a human resources specialist who regularly deals with tricky compensation issues. He or she can advise owners about best practices and serve as a sounding board for decisions. Ask a financial specialist to weigh in on salary, bonus and dividend tax implications (see sidebar). In most cases, compensation for family members who work in the business will be different from those who are shareholders but not employees.

**Define roles and responsibilities.** Job descriptions are a must. In addition to clarifying duties, they also serve as a basis for performance evaluations. Linking a salary range to job descriptions is a painless way to set standards and expectations.

**Codify the rules.** Family employment policies can go a long way toward taking the complexity out of compensation. For example, it is wise to create a clear

set of rules about qualifications for family employees in terms of education and work experience. Compensation policies can also be explained in a family employee handbook, with industry benchmarks and market rates as salary guides. Bonus and dividend policies should also be spelled out.

**Lead by example.** Compensation should always be reasonable. A too-rich set of perks can backfire. For example, personal travel and entertainment, club memberships and expensive cars will be denied by CRA as deductible business expenses. "Reasonable" is also a valid concept when it comes to behavior and work ethic. Owners must lead by example.

Remember, a family and a business are two different institutions, with different rules and notions of fairness. There is no textbook approach, only some guiding principles, and communication is key to defusing tensions and managing expectations.

*If you would like to discuss your company's compensation policies, please contact Young Parkyn McNab LLP.*

## IMPACT OF CHANGING TAX RULES

For many years, the integration of corporate and personal tax rates favoured the payout of year-end bonuses to owners to reduce a company's pre-tax profits to \$200,000 — what used to be the upper limit on income taxed at the preferred small business rate. In 2006, the upper limit increased to \$300,000, and is now \$500,000. In addition, the tax rate has been reduced on dividends paid out of profits taxed at the higher corporate rate.

This equitable tax treatment of dividends has reduced the incentive for corporations to "bonus out" higher levels of income to shareholders. While these changes have resulted in more business reinvestment, they may have left management with less in terms of current remuneration. Update company compensation policies to reflect these new rules; explain revised policies to family employees and shareholders so that they understand the reasons behind the changes.

# The Ins and Outs of Selling to a Third Party

Considering selling the company? It may seem a given that the family business will be passed down to the next generation of owners. But if no one in the family is interested in or qualified to take over - or if selling to a third party might be the best way to maximize value - it may be time to consider an outside buyer.

## GETTING STARTED

Most advisors recommend at least a five-year plan to sell a business. This amount of time provides plenty of opportunity to attend to all the details a sale requires. Meeting with a team of trusted advisors is a good first step. Include a lawyer and CA for legal and financial input, and consider an organizational psychologist if there are management, family shareholder or other transition issues to be addressed.

Because your advisors work with a broad range of clients, they can be an excellent source of ideas, especially in terms of potential buyers. A strong competitor or supplier can also be a good candidate to purchase the company. Spread the word and lay the groundwork early so that the best strategic deal can be pursued. A business broker can also be helpful, especially in specialized industries.

## CLEANING UP

Selling the company will likely require a fair amount of work. In order to maximize value, it's important to get the company in great shape. Now's the time to firm up crucial supplier or employment contracts, negotiate new leases, take care of nagging personnel problems, and get systems and other operational details in order.

It's also important to clean up financial statements. Personal expenses, cars and real estate should be off the books so that potential

buyers can get a realistic picture of the company's position.

Taking care of these things early will set the company on an efficient course and make it most attractive to potential buyers.

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You'll probably sell a business only once in your lifetime, so be sure you make the most of it.

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## DOING THE DEAL

Unfortunately, many business owners have an inflated idea of the value of their companies. A professional business valuation will provide a sound idea of what the company is really worth. When it comes time to do the deal, be sure to work with advisors who have a big picture view, who can help with due diligence and structure the deal to your advantage, especially in terms of financing, taxes and timing.

## PLANNING THE FUTURE

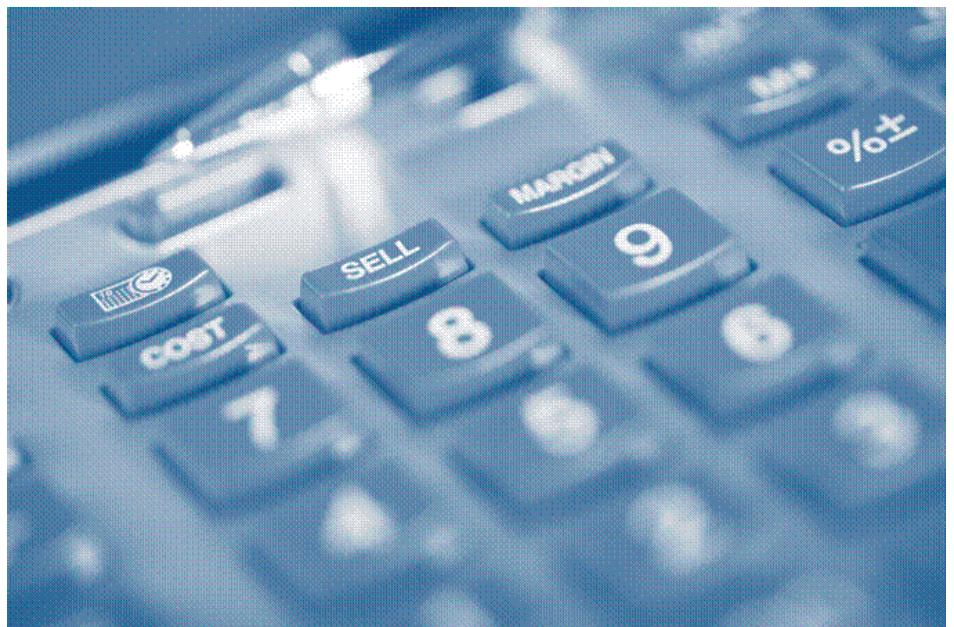
What will you do on the first day you don't have to go to the office? What will you do after that? While some owners have a contractual obligation to help manage the

company for a period of time, many are not welcome on the premises once the deal is done. Spend some time planning for what's next, whether it's a long vacation, a move, a new hobby or a new job. If feeling productive is important, consider board memberships or volunteer opportunities. Or lend your seasoned business expertise to a charitable organization. Make sure you have a plan.

And don't forget the emotional aspects of the sale. Selling a business can be a difficult time for an owner. In fact, some have described it as a sort of "death in the family." Be prepared to deal with the soft side of this transaction as well.

While it may be difficult to see "strangers" running your business, it may be the best option. You'll probably only sell a business once in your lifetime, so be sure you make the most of it.

*If you would like to discuss the sale of your business, please contact Young Parkyn McNab LLP.*



## PIPEDA Compliance:

# Keeping Customer Information Secure

The Personal Information Protection and Electronic Documents Act (PIPEDA) has been in effect for five years. Enforced by the Office of the Privacy Commissioner (OPC), the law protects citizens by regulating how companies collect, use and disclose “personal information” in the course of doing business.

While most companies have been appropriately complying with PIPEDA, a few have been caught off-guard by unusual privacy protection issues:

**Captured on Camera:** Many businesses collect images of people in public places, and it is a common misperception that a company doesn’t need permission to do so. In fact, “personal information” includes a person’s image that is recognizable to others. While there are a

few exceptions for journalistic, artistic or literary purposes, most companies must take steps to ensure the privacy of individuals captured by street-level imaging technology.

**Lost Laptops & E-mails:** Data security breaches happen with alarming frequency, but many are not obvious. For example, a lost laptop may contain customer or employee personal information. Misdirected e-mail, letters or faxes can also put data at risk. Pay close attention when these events occur and notify individuals immediately if personal information has been — or may be — inadvertently released.

**Cross-Border Concerns:** While Canadians enjoy PIPEDA protection at home, it’s different outside the country. Canadian

companies have a legal obligation to have appropriate security measures in place to prevent a US-based subsidiary, affiliate, supplier or government entity from secretly obtaining access to Canadian personal information. PIPEDA also includes a “whistle blowing” provision to protect employees who notify the OPC that a company intends to transfer information abroad in violation of PIPEDA.

Compliance with PIPEDA requires vigilance. To be safe, gather only the personal information you need to do business, and keep it secure.



**Young Parkyn McNab is a unique and innovative team pursuing excellence in a fun environment. We truly care about our clients, our people and our communities.**

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