If you decide to buy through a company, you need to consider who its shareholders will be. It is very easy to issue shares in a newly incorporated company; it has no value at the time of incorporation, and as a result, you can give shares to others without any tax implications. After the company completes the purchase, though, Canada Revenue Agency will take the position that the company has value and, therefore, issuing shares after the purchase will have tax consequences.

If there will be more than one shareholder, I strongly encourage you to enter into a shareholders' agreement. Many clients want to delay taking this step, to avoid either the time it takes to get its terms right or the expense associated with it. However, it's too late to enter into one if the relationship between the shareholders has deteriorated to the point where they no longer want to be in business together. Shareholders' agreements are like marriage contracts – if you can't agree going into the relationship, you'll be hard-pressed to agree when the relationship ends.

What should you buy: shares or assets?

One of the first questions I ask a client who is buying a business is whether they are buying shares or assets. This influences the nature of the agreement that must be drafted. Not knowing the answer to that question may put you at a disadvantage when you start negotiations.

If you are purchasing shares, you are acquiring the company that operates the existing business. That includes all of that company's assets and liabilities. Sellers often prefer a share deal because it may allow them to access the federal capital gains tax exemption. If they are eligible, that exemption allows the seller to receive upwards of $866,912[1] free of capital gains tax (this amount changes slightly each year).

A share transaction means that the assets stay inside the company. You become the owner of the shares in the company, and the company remains the owner of the assets. This may mean that there is no tax payable on the transfer of the asset. For example, if you were purchasing land in Nova Scotia you would have to pay deed transfer tax. If, however, you buy a company which owns land, you do not have to pay this tax. The company remains the owner of the property, and the purchaser becomes the owner of the shares in that company. However, the tax value of the assets inside the company would remain unchanged. That could mean increased capital gains if you later decide that the company's assets should be sold, rather than its shares.

In addition, because you are acquiring the company, you must consider any liabilities it may have. Not all liabilities may show on the financial statements. For example, consider what happens if a lawsuit is brought against the company after you have bought its shares. Usually, the lawsuit will not name you personally, but you will probably become involved in the litigation in order to protect your investment. Determining all liabilities that may exist is next to impossible. As a result, you will have to rely on a well-drafted agreement to protect your interests.

Should you worry about competition?

Another thing to consider is whether the seller might set up to compete with your business after the closing. You may wish to include a non-competition agreement as part of your transaction. Sometimes purchasers arrange for the seller to stay on as a consultant or an employee after the sale. That allows the buyer to take advantage of the seller's knowledge, and it can give the seller certain tax advantages as well.

[1] as of January 1, 2019