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January 2022

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Employee Benefit Plans – *A Hidden Intangible in the Sale of a Company*

By: Chuck Zima

Employee benefits can play a very important role in the transition of a business from one owner (seller) to another (buyer). The traditional reasons for having employee benefits other than a tax effective form of compensation, hold true in the transitioning of a business; they are to attract and retain the very best quality employees. When a business is sold, a good quality employee benefit plan can solidify the companies' culture, and thus add a hidden "value added" component on the Income Statement at the time of the sale that is sometimes overlooked.

But, just as a high-quality employee benefit program can do wonders in the sale of a company, there are potential liabilities as well. An unfunded liability within a defined benefit pension plan, for example, can have devastating consequences on the valuation, and therefore the sale of a company.

Most employee benefit programs are viewed as a cost of doing business by business owners – however on the sale of a company, they should be viewed as an intangible benefit, similar to goodwill, that can add true value to the company. The importance of a well communicated, tax effective form of additional compensation should be highlighted before, during and after the sale of a company. However, in the hype of transition, many business owners fail to take advantage of this gift horse that is a diamond in the rough.

The reasons for this are simple – transitioning a business is complicated, and time consuming. Most of the time and upfront effort is dedicated to a) finding an appropriate buyer, b) ensuring the right deal is obtained, c) a meeting of the minds on the valuation of the company, d) due diligence and e) implementing the transition plan. It is easy to see how something that affects the corporate culture of both organizations could be missed in the above. In fact, when polling employees (after completion of the transition) to find areas of optimization, most employees concerns are first and foremost, "am I going to be able to maintain my job into the future". Very closely thereafter is the consideration (in the minds of the employees) of their benefit program. Will it stay the same – as most employee have budgeted for these health or dental expenditures – or might it be enhanced. This is where the hidden value can really shine for not too much cost. In fact, in some cases, the total relative cost to the employee and the employer may decrease due to the increase in insurance volumes because of more employees now on one program.

Likewise, a buyer must perform due diligence if a multi-employer pension plan is in place – say for example in the case of unionized employees, or other programs like ASO (Administration Services Only), cost plus or Health and Welfare Trusts are used to cover eligible healthcare expenses.

Of the upmost importance is the perception of the benefit program in the eyes of the company's employees and dependents. On this point, communication is the key. Good quality employee benefit programs will regularly communicate the total value of the renumeration package to employees, so that they understand their total compensation & rewards program. If the total renumeration has not been communicated recently to the employee population, the sale of a company could be the perfect time to begin a communication strategy.

As an example, should the company that is for sale not have a benefit package in place currently, but is bought by a company that does have one – this increase in the total

compensation package must be communicated to employees as a distinct increase in total compensation – and a tax effective one at that!

Aside from the advantages that can be derived from fully utilizing your current employee benefits program on the sale of a company (or transition to a new owner), the current owner should also take advantage of all benefit programs that are available to them. One example is the purchase of past service if they have not contributed the max to an RRSP. Although rare, there are instances where a company owner has simply re-invested in the company, and his/her own private investment portfolio, without investing in a tax deferred compensation program, similar to an RRSP. In this case the Tax Act allows an owner, through an actuarial valuation, to purchase a type of RRSP as if they had been contributing to one all these years. The vehicle for this is called an Individual Pension Plan (IPP), and the amount of "past service" that can be transferred tax free into an IPP can sometimes be in the hundreds of thousands of dollars. An owner that falls into this category should consult with their accountant, and their financial advisor.

Another benefit that an owner should consider upon the sale of their company is the set up of a Health and Welfare Trust to cover potential future health/dental concerns once the company has fully transitioned to the new ownership.

Bottom Line

It is important to maximize the inherent value in both the sellers and the buyer's employee benefit program. Simple programs to implement, can yield a long-term muti-year increase in return on investment (ROI).

Prior to the time of sale, owners should review their employee benefits programs with their financial advisor, or insurance provider to ensure that it meets the needs of its employees once the company has been fully transitioned.

About the Author

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Chuck joined the Robbinex team in 2021 and works closely with business owners, assisting them with growth initiatives and transition alternatives.

Chuck graduated from Ryerson University with a Bachelor of Commerce. He began his career with a Bay Street consulting company. After moving to a financial services company where he progressed with increasing responsibility and a progressively larger book of business, he transitioned to a private healthcare organization where he developed and marketed innovative and highly profitable products and services for major Canadian corporations. He then became the Vice President of Sales & Marketing for an international medical manufacturer, where he led a team that tripled sales in two years.

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