SALE OF ASSETS OF A CORPORATION VS. SALE OF SHARES OF THE CORPORATION

When the shareholder is interested in selling the business, he or she can has two options:

1. Sell the individual assets, pay off the liabilities and taxes and distribute the remainder as dividends
2. Sell the shares of the corporation

Sale of Assets of a Corporation

Why would corporations sell assets rather than the shares?

- The business may not be profitable, and therefore may not be attractive to investors
- The business may be too specialized and cannot be carried on by a new shareholder

Step 1: Sale of Assets by the corporation and pay taxes on income generates by sale

The corporation will sell the assets of the corporation:

Asset	
Accounts Receivable	▪ The sale of accounts receivable is treated as a capital transaction. ▪ Businesses often sell accounts receivable at a capital loss. ▪ Therefore only **one-half of the capital loss will be deductible**. ▪ Since purchaser never included the income from the A/R, they will not be able to claim a reserve for bad-debts There is a joint election under **section 22** ▪ This will treat the sale as a non-capital transaction ▪ **Section 22** can only be used when **at least 90%** of the business assets are being sold ▪ 100% of the losses will be deductible by the seller as **business loss** ▪ The purchaser can claim a reserve for bad-debts
Inventories	▪ Gain/loss will be treated as **active business income**
Prepaid Assets	▪ Gain/loss will be treated as **active business income**
Non-depreciable capital assets	▪ There will be a **capital gain or loss** ▪ The taxable capital gains/loss are considered **aggregate investment income** ▪ Non-taxable Capital gains will increase the **capital dividend account (CDA)**
Depreciable capital assets	▪ CCA Recapture is considered active business income ▪ The taxable capital gains/loss are considered **aggregate investment income** ▪ Non-taxable Capital gains will increase the **capital dividend account (CDA)**
Eligible Capital Property	▪ 50% of economic gains are considered **active business income** ▪ The recapture is also considered **active business income** ▪ 50% of the economic gains increase the **CDA** ▪ Sale of **goodwill** is an eligible capital property; usually goodwill will not have a tax value in the CEC pool; the disposal will still generate recapture and/or economic gains

Calculating the Taxes on Income generated by Disposal:

Type of Income	Combined Tax Rate
Active Business Income ≤500,000	15%
Active Business Income >500,000	28%
Aggregate Investment Income	46%
Refundable Portion of Part I Tax	26.67%

Step 2: Residual amount after taxes and liabilities are paid off gets distributed to shareholder

Amount available to distribute to shareholder = Proceeds of Disposition – Liabilities – Taxes + RDTOH

Step 3: Determine taxable dividends and type of dividends

Amount available to distribute (step 2)	$xxx
less: Paid-up Capital (PUC)	(xxx)
Deemed Dividends	**$xxx**
less: Capital Dividend Account (CDA)	(xxx)
Taxable Dividends	**$xxx**
less: GRIP = Eligible Dividends	**(xxx)**
Non-Eligible Dividends	**$xxx**

Step 4: After Tax money in the hands of the shareholder

Amount available to distribute (step 2)	$xxx
less: tax on eligible dividends (30% @ top bracket)	(xxx)
less: tax on non-eligible dividends (33% @ top bracket)	(xxx)
After tax money	**$xxx**

Sale of Shares

- Sale of shares is the easiest way to sell a business
- There will be a taxable capital gain (or an allowable capital loss) on the sale of shares
- Note that if the shares are QSBC shares, it will be eligible for the $750,000 life time capital gains deduction
- **After tax money = Proceeds – tax paid on the capital gain**

Sale of Assets vs. Sale of Shares

- The shareholder should choose the method that yields the highest after tax money (assuming all else equal)
- Here are some factors to consider:

Asset Sale	Share Sale
Pros • Higher **UCC** balance for buyer; since assets purchased with after tax money; higher UCC = higher CCA deduction • No **liabilities** assumed by the buyer • Capital Gains generate **CDA** balance to distribute dividends tax free **Cons** • More work; need to sell assets	**Pros** • QSBC shares are eligible for the $750,000 lifetime capital gains deduction • AOC rules apply so buyer can carry fwd. non-capital losses (w/ streaming rules) • Easier to implement **Cons** • Liabilities assumed by new buyer • No asset cost bump up