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THE CANADIAN INSTITUTE *of*
CHARTERED BUSINESS VALUATORS™

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Dual Class Share Structures

by Aaron Atkinson[1] and Naizam Kanji[2]

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1.1 Overview of Dual Class Share Structures

In a DCS (Dual Class Share Structure), one class of equity shares has superior voting power (sometimes referred to as the "high-vote" shares) relative to the other class of equity shares (sometimes referred to as "low-vote shares"), but participates on the same basis economically. This permits one party (for example, the founder) to maintain control of the corporation without also holding a majority of total equity (or economic interest). This structure can be manageable, and profitable so long as the vision of the founder aligns with the views of the holders of the low-vote shares.

The Canadian securities regulatory regime with respect to dual class share structures is currently largely disclosure-based, with few substantive requirements. In this regard, issuers can organize their affairs as they wish, given that they provide adequate disclosure to investors. The system is driven to make sure that shareholders have the necessary information to make an informed investment decision

A DCS is generally structured in one of two ways: (i) multiple voting shares (e.g., 10 votes per share), and subordinate voting shares, (typically one vote per share), or (ii) one class of voting equity shares and one class of non-voting equity shares.

Market perceptions of dual class structures vary and it appears that the pendulum may be swinging back in their favour. For example, many recent IPOs in Canada have used a dual class share structure. With these structures seemingly regaining acceptance in the market, it is worth reviewing both their positives and negatives.

1.2 Canadian Landscape[3]

83	Number of DCS listed on the TSX and TSX-V (excluding SPACs and investment funds)
90	% of DCS issuers that trade on the TSX (as opposed to the TSX-V)
10	% of TSX issuers that have a DCS structure
50	% of DCS issuers whose MVS are listed
20	% of DCS issuers that operate within a "regulated industry" (e.g., telcos, air travel)
31	% of DCS that have "sunset" provisions (being the date by which, or trigger upon which the structure will collapse).

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3 Data complied from 2015

1.3 Key Advantages

The advantages of a DCS for the most part revolve around the controlling shareholder and the distribution of equity. If a founder wishes to seek capital from public sources, using a DCS allows the founder to raise outside capital without necessarily diluting voting control. Furthermore, in our era of increased shareholder activism, a DCS can insulate the board and management from short-term investors allowing them to more freely implement the founder's vision. In this way, a DCS can promote "long-termism".

Additionally, a DCS might entice a business that would perhaps otherwise stay private to go public, thereby allowing outside retail investors an opportunity to invest.

As we note below, while a DCS structure can lead to problems of misalignment of interest, the structure itself does not, per se, result in misalignment of interest.

1.4 Key Disadvantages

A DCS separates legal control from economic exposure. Where there is a wide disparity between the number of votes the founder holds and the founder's economic interest (the so called "skin" in the game), friction can arise between the founder and the minority shareholders, particularly as a result of differing risk appetites and the increased potential of value extraction mechanisms outside of the equity structure.

While a DCS can insulate management from "short-termism", the same structure can be criticized if management is viewed as underperforming, at least in the eyes of minority shareholders. The structure itself impedes investors from seeking to make changes to the board and management because they simply do not have the votes to do so. This entrenchment can then result in a non-assertive board of directors. In that regard, an independent director of a dual class company may feel saddled with the seemingly impossible task of advocating for the public minority while at the same time knowing that they could be replaced by the controlling shareholder.

In this sort of environment, a DCS can facilitate nepotism, wealth extraction, and insulation from accountability, which increases agency costs.

2.1 Policy Issues – Regulatory Perspective

One of the principal roles of securities regulators regarding a DCS is in managing the potential conflicts between the controlling shareholder and the minority. One of the main advantages of accessing the public capital markets is the ability to raise money from many individuals. The downside is that those individuals cannot collectively address problems with the company. This is a common issue in any public company. However, it becomes even more difficult in a dual class company because the typical external governance mechanisms are not possible. For example, there is no possibility of a hostile bid, or the launch of a proxy contest, and majority voting for directors does not work. Managing conflicts is therefore largely left to the independent directors who are essentially the gatekeepers.

One area of potential conflict arises when the high-vote shareholder has a very high voting to equity ratio. There are no requirements that specifically regulate the ratio of voting rights to equity stake. In circumstances of a wide disparity between voting and equity stake, since dividend payments on the equity may be relatively modest, the structure could lead to various value extraction mechanisms outside of the equity structure. Accordingly, tension may arise between the independent directors and the high-vote shareholder over matters such as executive compensation and related party transactions.

In some circumstances, the transaction may be subject to Multilateral Instrument 61-101[4]. For material transactions, this rule requires that public shareholders have the opportunity to vote on the transaction (with a "majority of the minority" vote) and the company may be required to obtain a formal valuation of the subject matter of the transaction.

Outside of issues relating to voting and disclosure, another policy issue arises when the structure does not have a termination date (or "sunset" clause). In these cases, over time it may become mutually beneficial for the founder and the public shareholders for the structure to be unwound; however, it can be very challenging to arrive at an appropriate price for the founder ceding control.

On the flip side, there may be circumstances where the DCS has a sunset clause and the founder seeks to extend the structure beyond the termination date, which can raise contentious issues of its own.

2.2 Policy Issues – Investor Perspective

In evaluating the issues raised by dual class issuers, regulators tend to apply a risk-based approach. Regulators tend to focus on the potential harms to investors that may arise from the structure. However, from an investor perspective, there is the competing idea that a DCS allows founders to implement their "idiosyncratic vision" which may be compelling to certain investors. Particularly with IPOs in the tech industry, public shareholders may be willing to forgo certain rights in exchange for the opportunity to invest in a cutting-edge technology to which they might not otherwise have access.

A DCS may also be a method to entice more entrepreneurs to take their companies public. A founder may view the compliance costs and increased scrutiny of public company status as outweighing the benefit of accessing public capital. As noted earlier, a DCS ameliorates some of these issues for the founder.

3.1 Oversight: Investors

There are mixed feelings among investors about dual class issuers. Some institutional investors refuse to invest in them and have published policies in this regard.

At the same time, investors may feel pressure (notwithstanding their theoretical objections and principles-based objections) to invest in dual class structures because of the scarcity of IPOs. In addition, index investors may have no choice but to invest in some of these issuers.

Other investors may accept dual class issuers in concept, but the more disproportionate the gap between voting and economic interest, the more challenging it may be for them to invest.

3.2 Oversight: TSX

The TSX (Toronto Stock Exchange) and TSX-V (TSX Venture Exchange) have special listing rules for "restricted securities", including a requirement that dual class issuers who implement the structure after 1987 must have "coattail" provisions, which allow holders of the low vote shares to participate

4 Multilateral Instrument 61-101 Protection of Minority Security Holders in Special Transactions. *Securities Law & Instruments*.
5 TSX Company Manual. *H Restricted Securities*. Sec. 624. 2013. Web.

in and enjoy the benefits of a take-over bid[5]. Coattail provisions also effectively restrict the high vote shareholders from selling control without allowing the low vote shareholders an opportunity to participate.

3.3 Oversight: CCGG

The Canadian Coalition for Good Governance (CCGG) is an organization whose members include the majority of the large institutional investors in Canada. CCGG has published a DCS policy that sets out certain "best practices"[6].

Some of the CCGG's suggestions include:

1. The number of directors nominated by high vote shareholders should be limited.
2. The founders should adopt meaningful equity ownership: a 4:1 is suggested as a reasonable limit.
3. High vote shareholders should not be able to monetize their interest unless others have the same opportunity.
4. No premium should be paid to high vote shareholders if they collapse the DCS. If the DCS is collapsed as part of an acquisition by a third party, then a premium may be permissible if there is coattail protection.
5. A sunset clause should be included.

3.4 Oversight: OSC

As noted earlier, the OSC's rules are largely disclosure based.

1. OSC Rule 56-501 Restricted Securities, which imposes disclosure and minority approval requirements for the creation of dual class structures[7].
2. NI 51-102 Continuous Disclosure Requirements, which mandates specific disclosure obligations for dual class issuers, including details of coattail provisions[8].
3. MI 61-101 Protection of Minority Security Holders in Special Transactions, which mandates formal valuation and minority approval rights in certain transactions involving related parties, in addition to enhanced disclosure.

3.5 Oversight: Proxy Advisors

Proxy advisory firms are organizations that provide voting recommendations to their institutional shareholder clients. Many of these institutional clients also take advantage of the vote execution services offered by the proxy advisory firms. The view of proxy advisory firms (ISS[9] and Glass Lewis) can carry considerable weight on any vote to convert or collapse a DCS.

ISS generally recommends voting against proposals to create a new class of low vote shares. ISS will support a DCS only in exceptional circumstances, including all of the following[10]:

6 *CCGG Publication of Dual Class Share Policy.* Canadian Coalition for Good Governance. 28 Aug 2013. Web.
7 Ontario Securities Commission Rule 56-501 Restricted Shares. *Securities Law & Instruments*. Ontario Securities Commission. 29 Oct 1999. Web.
8 IFRS-Related Amendments to National Instrument 52-107 Acceptable Accounting Principals and Auditing Standards and Certain other Instruments. Securities Law & instruments. Ontario Securities Commission. 10 Dec 2010. Web.
9 Institutional Shareholder Services
10 Canada Proxy Voting Guidelines for TSX-Listed Companies 2017 Benchmark Policy Recommendations. *ISS Governance.* 28. 12 Jan 2017. Web.

1. The low vote holders may elect some board nominees.
2. Coattails and a sunset provision are included.
3. The structure is required due to foreign ownership restrictions, and financing is required to be done out of country.
4. The structure is not designed to preserve the voting power of an insider or significant shareholder.

4.1 Concluding Remarks

Dual class structures appear to be experiencing a renaissance as witnessed by numerous recent IPOs that have used the structure. As a result, in future we can expect to see proposals to collapse or extend dual class structures, which will once again raise challenging issues for boards, advisors, and regulators.

CBVs As Experts In Litigation

by Ron Petersen[1], Ron Martindale[2], Judith Snider[3], and Mike Carnegie[4].

2

1.1 Objectives

The objective of this article is to provide useful information for Chartered Business Valuators (CBVs) who are, or aspire to be, involved in litigation matters as potential expert witnesses for matters including: shareholder disputes, family law, transaction controversies, and damage quantification.

The article will cover various topics pertaining to CBV's serving as experts including independence and objectivity, factual assumptions, retainer agreements, hot tubbing, and electronic trials.

1.2 Independence and Objectivity – Role of the CBV

What is the role and responsibility of a CBV serving as an expert?

A judge does not know everything; they require experts to fill in the knowledge gaps they may have. Experts are the exception to the rule that only judges can form opinions, and that a witness can only testify as to facts within their knowledge. *The role of the expert is to assist the judge so that they may form a reasonable opinion.* An expert is, first and foremost, there to serve the court regardless of whether they have been hired by the court, the defendant, or the plaintiff.

1.3 Independence and Objectivity – Experts in Court

Three recent cases frame how experts operate in the court setting: White Burgess Langille Inman v Abbott and Haliburton Co, 2015 SCC 23; *Westerhof v. Gee Estate*, 2015 ONCA 206; and *Moore v. Getahun*, 2015 ONCA 55. The focus of this article will be less on the specifics of the cases, and more on their practical functions for experts.

Regarding allegations of bias, White Burgess[5] offers a good roadmap to consider. In *White Burgess*, the plaintiff shareholders brought a professional negligence action against the former auditors of their company after retaining a new accounting firm as auditors. The new auditors revealed problems with the previous auditors' work, which had caused financial losses. In response to the defendants' summary judgment motion, the plaintiffs filed an affidavit from a forensic accounting expert who also happened to be a partner in a different office of the same accounting firm as the new auditors. The defendants argued that the expert was not impartial and ought to be disqualified due to this connection. The case was eventually brought to the Supreme Court where it was ruled that a connection alone was not enough to disqualify evidence or prove bias. The extent and type of connection had to be taken into consideration when arguing for bias.

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4 Mike Carnegie is a partner at Taylor Leibow LLP and the moderator for the panel from which this article began.
5 White Burgess Langille Inman v Abbott and Haliburton Co. S.C.R.189. Supreme Court of Canada. 2015. Supreme Court of Canada. Web.

On a more practical basis, there are four thresholds requirements that need to be met for an expert to serve in court: relevance, necessity, absence of any exclusionary rule, and a properly qualified expert. The Supreme Court has now meshed in the notions of objectivity and non-partisanship to these four prior thresholds. Once the four are met, the next step is to determine notice if there is a strong degree of independence and impartiality. If the answer is no, that the expert is too embedded in one of the parties, then that evidence will be discarded no matter how relevant. There is however, a grey zone as shown in *White Burgess*. For example, let us say that in past the firm a CBV works for worked with one of the parties. Does that disqualify the evidence provided by that CBV? The answer is, probably not, but the court has to weigh the importance of the evidence against a potential for bias.

Westerhof v. Gee Estate[6], defined the types of experts permitted to give opinions as opposed to their independence. Generally, only expert witnesses are permitted to provide opinion evidence. However, treating physicians are often asked to testify in legal proceedings regarding their assessment, diagnosis, and prognosis of a given patient, all of which represents the physician's opinion. This raises the question whether treating practitioners should be included as experts and subject to the requirements set out in rule 53.03 of the Ontario Rules of Civil Procedure. What the Westerhof case did was propose that there can be "litigation experts", "participant experts", and "non-party experts". Furthermore, depending on the circumstances, a participant expert or a non-party expert can give their opinion without going through the process of a litigation expert, essentially without complying with rule 53.03.

When an expert is retained for a litigation case, it is obvious that the expert is a litigation expert. However, a CBV, at times, may work outside of litigation context. Let us say that there is a question of a business valuation, long before the parties to a transaction contemplate litigation. A few years after the successful valuation by the CBV, everything implodes. The circumstances are such that there are charges of bad faith and pleadings filed. The CBV has done the work and they appear at the trial, how do they appear? They do appear as a fact witness, but according to the *Westerhof* case, they have an opportunity to present the opinions that they formed at the time. Furthermore, they do not have to swear an affidavit as they would if they were a litigation expert. They are classified as a "participant expert". Depending on circumstances, *Westerhof* can be a useful case to consider.

Lastly there is *Moore v. Getahun*[7]. This case explored the relationship between the counsel who, in almost all cases retains the expert, and the expert. In Moore, there was much conversation on how much influence the lawyer has on the report of the expert and whether that creates bias. It is one of many cases that are popping up in the current landscape regarding the relationship between lawyers and experts and it is something to consider for the future. A CBV can converse with the lawyer and they can have communication that is not required to become public in litigation. The discussions between the lawyer and the CBV are, in most cases, protected under litigation privilege. The CBV does not have to produce records of these interactions; the Ontario Court of Appeal was clear on that. However, there may be occasions where the other side tries to expose some earlier drafts to prove that the CBV was inconsistent. Keep in mind, of course, that the draft does not always look like final copy and that if a CBV can explain why changes were made there is nothing improper in correcting earlier mistakes. The idea is that the opposing party wants to show that the lawyer unduly influenced the CBV. The burden is on the side that is alleging that this bias occurred to prove it and the evidence has to be fairly strong for a conclusion of bias.

That is not the say that there is no difficulty or potential for influence between expert and lawyer. There is an inherent conflict between the duties of the expert to be totally impartial and independent to the

6 Westerhof v. Gee Estate. ONCA 206. Ontario Court of Appeal 2015. Ontario Court of Appeal. Web.
7 Moore v Getahun. ONCA 55. Ontario Court of Appeal 2015. Ontario Court of Appeal. Web.

court while the person who is paying them is the lawyer or the client. However, the bottom line is that the CBV must serve the court. If a CBV is not considered independent and objective, their evidence will not be admitted by the court. It is up to the CBV to maintain their objectivity, both perceived and otherwise.

1.4 Independence and Objectivity – Perception

Once the qualifications have been established, and a client is interested in working with a CBV, the next step is to determine if the expert has an issue of conflict of interest or lack of independence. The question of independence should also be addressed as soon as possible, by proceeding with a conflict check within the firm. This should be done by the expert upon the initial considerations of working on a case.

The expert should also take care to consider the matter of perception. If it is a family member, or friend that wants to hire the CBV the immediate decision should be to pass the case on. If it is a grey zone, such as a client an expert may have worked with a decade ago, the expert can ask the counsel their opinion. As a rule of thumb, however, if a CBV has any doubts towards serving as an expert, be that due to actual biased or potential perceived bias, they should pass on the assignment.

2.1 Factual Assumptions

The lawyer presents the case, the CBV presents the opinion, and at some point before then, the CBV needs to have an understanding of background and factual assumptions. It may be somewhere between the time a CBV is engaged and the time they issue a draft report that the counsel might give or ask them to make assumptions.

The assumptions should be set out clearly in the report and they should be reasonable. An expert does not want to be caught at a mediation or a trial where they have been asked to make an assumption, and that assumption turns out to be unreasonable, most likely because some of the facts were unaccounted for or unknown. This leads to the conclusion that the report is of little value and the CBV will be criticized.

An expert cannot take a request for a factual assumption at face value; they have to put some thought into it. In many cases where an expert runs into difficulty with the court, the expert has accepted facts or assertions without any verification. This reliance on such facts, without independent examination, may lead to unfortunate, or skewed results. It can be as simple as doing a valuation where there are six family members in the business and the owner of the family states that the family members are all paid at fair market value. It might be pertinent to know that two of those family members are teenagers and two are seniors, lest the valuation consider all six to be contributing members to the company.

As soon as the CBV receives the first call or email, the valuator should reach out to counsel and obtain the key facts. If it is a marriage, what is the date of separation? If it is a breach of contract what is the date of the breach? The scope of information and the limitations should be known to the valuator in order to be able to successfully proceed with a valuation. A CBV expert should fact check as much as possible, within reason.

2.2 Retainer Agreements

In the business of business valuation, after a CBV has been hired they must send out an engagement letter. An engagement letter should, ideally, limit the professional liability of the expert. It is a way to manage the client's and counsel's expectations as to what the CBV is going to do, and how they going to do it. It should also include how and when the CBV will get paid as well as the services they will be providing in exchange. The question of privilege becomes crucial when considering whether to engage with the lawyer or the client. If the CBV engages with the lawyer, they retain privilege, which means that all communications between the expert and counsel are treated as "protected" or private. If they engage with the client then there is a loss of privilege, which means that all conversations between the expert and the council will be subject to scrutiny in court.

In regards to the differences in an engagement letter between a one-sided versus a joint retainer, the key focus should be on communication. When one side retains a CBV it can be more straightforward because the expert is aware of who needs to know what information. This becomes more difficult with joint retainers because there are two people to inform, and who needs to know what information becomes a question. Due to this uncertainty, it is important to establish a communication protocol. This should include: how is the expert going to communicate and to whom? If an email goes out does it go to just the lawyers or the lawyers and clients? Problems can also arise when an expert asks for the representation letters and one side comes up with new facts – specifically, facts that the expert has not been advised of, but that they must now account for. The engagement letter should clearly delineate which side will pay for changes in anticipation of this potential problem.

Outside of the engagement letter, a joint retainer can mean that there can be opposing facts. A common example would be between a former employee and an employer. The employee may say that they worked all the time, while the employer may say that the employee was never at work, or worked poorly. It is not the job of the CBV to determine facts. An expert is to do some testing as to their reasonability of the facts but otherwise the facts are what they have been presented as. If two people or parties cannot decide on what those facts are, an expert can either send it down for the court decide or they can offer to create two scenarios for the two sets of facts.

The last scenario to cover briefly is the self-represented litigant. While they are not to be underestimated, they come with their own complications. The argument for self-litigation would be one of expense. However, it is up to the CBV whether or not they have any interest in cases that involve self-representation. There is no solicitor client privilege between a non-lawyer and a CBV.

3.1 Hot Tubbing

The term "hot tubbing" is used to describe a voluntary or mandated situation where experts share their opinions, and/or discuss issues. The idea is that allowing the experts to meet to share their opinions, analyses, methodologies, and assumptions will result in a narrowing of issues and, consequently, a reduction in litigation and trial. Even if the experts cannot agree on every point, the differences in their evidence can be narrowed. Hot tubbing can be done with the experts alone, or with the clients and/or lawyers present.

When hot tubbing occurs outside the trial as part of pre-trial attempts to settle, it is normally considered to be without prejudice, which is something all of the parties must agree on and understand before the meeting proceeds. This means that the contents of these meetings cannot be brought up in trial unless agreed upon by all the parties. So if one party implies that they are liable for an action in any way, shape or form, that implication cannot be used as evidence for their liability in trial.

Hot tubbing can also take place during a trial, where a judge requests that experts retained by both sides appear together. In this situation, both experts will be cross-examined and then asked questions by the judge. For a judge, the expert is there to educate the judge. If at any point, the judge wishes to ask for clarification they can, have, and will. This is something that an expert should be prepared for. With both experts testifying at the same time, the judge can more easily compare the two opinions and select those portions of the experts' reports which they prefer. With the judge able to see and assess both experts at the same time, there is a risk that the performance of the expert will begin to outweigh the contents of their report. It can become a test of advocacy skills and the report can hinge on how well it has been presented.

While hot tubbing is, in fact, permitted under Federal Court Rules of Practice and Procedure, historically it has not been used frequently. However, it has recently become more popular. It can be a useful tool for clarification, agreement, and implication of the expert evidence whether it occurs pre-trial or during.

4.2 Expert Qualification

As stated above, one of the four factors for acceptance of an expert opinion is that the expert is qualified to give such opinions. Most of the time the qualification of the expert is not an issue. When it is, the side opposing the expert's qualifications will cross-examine the expert. Then the lawyers will make their respective arguments to the trial judge, usually with the expert out of the room. The judge will then make a decision. The decision could be to accept the expertise or the judge could decide that the expert is only qualified in A B or C but not D. If it were the latter, relevant parts of the report would be excised.

5.1 Electronic Files and Demonstrative Aids

Although the way of the future is electronic, both CBVs and lawyers have to appreciate that the administration of most courts is quite lean. For example, the clients might have to provide the server for the documents if the documents are too large depending on the court. It is important to keep cognizant of the limitations of the court, and the preferences of the particular judge when considering the use of electronic evidence and demonstrative aids.

In this new electronic context, the word "file" has become expanded; a "file" can now be a laptop, or an electronic record. What it comes down to is that electronic files are efficient and reasonable. They are easier to search, easier to compile, and contain the same content as paper files. The CBV should have access to draft reports, the engagement letter and representation letter, all aspects that created the expert's scope of review, and, depending on who the client was, all of the email interactions.

In terms of demonstrative aids, be that exhibits or slides, while they can be criticized they are useful. A demonstrative aid used by an expert during their oral testimony should present no new evidence beyond the contents of the written report. Rather, it should be a way of clearly and concisely explaining the evidence to the court. There may be discussion on whether or not the aid is admissible because it can be seen as new evidence. A way to combat this accusation is to reference the report in the aid, whatever that aid may be, and to provide the aid to other parties as early as possible. The perception of new evidence can cause much excitement. However, for the most part, demonstrative aids are a good way to summarize reports into smaller pieces of digestible information for the court. An expert may even be asked to prepare an aid for court, or to replicate the aid of another expert with contrasting conclusions.

6.1 Concluding Remarks

The role of a CBV as an expert in litigation is, for the most part, one that hinges on accurate communication and an understanding of the role. A CBV must be able to communicate what they can and cannot do with the client, what their facts are to the other expert, and what their conclusions are to the court. The CBV, when acting as an expert witness, must understand that their role is to work for the court and not for the party who hired them. Regardless of pressure from the client, as an expert, any information given, any conclusions reached, and any methodologies used should be ones that the CBV is comfortable standing by. If a CBV wishes to work as expert in litigation, they must understand that they are the ones responsible for maintaining their perception as fair and independent.

With every opinion, the CBV expert witness represents their profession. If the CBV does a poor job on the assignment it will reflect badly on all CBVs.

Business Valuations vs. Transfer Pricing

by Dr. Muris Dujsic, CBV[1] and Samer Wani, CPA, CA[2]

3

Abstract

Transfer pricing for tax purposes is defined by domestic law and international tax treaties. This paper first establishes the transfer pricing framework by focusing on its constituent elements. This is followed by a comparative analysis aimed at exploring overlaps, dichotomies, and other interactions between business valuations and transfer pricing through the standards of value, pricing methods, documentation requirements, and penalty provisions of each. Some questions that are considered are: are these value standards directly comparable? Do they lead to the same valuation conclusion? Would valuation reports spontaneously meet the legislative transfer pricing documentation requirements? The paper closes by offering concrete suggestions as to how to bridge the gaps and develop effective risk mitigation strategies.

TRANSFER PRICING FRAMEWORK

1.1 Overview

Generally, transfer prices are the prices at which services, tangible property, and intangible property are "traded" across international borders between a Canadian taxpayer and a non-resident person (i.e., corporation, partnership, trust or individual) with whom the taxpayer does not deal with at arm's length.[3]

The transfer prices adopted by a group of non-arm's length parties directly affect the profits reported by each of those parties in their respective countries. This is why transfer pricing in Canada is defined and governed by both domestic law and international tax conventions as entered into between Canada and its treaty partners. The domestic law defining Canada's transfer pricing rules is in section 247 of the Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.) ("ITA"), while Article 9 of the Organisation of Economic Co-Operation and Development's ("OECD") Model Tax Convention defines the international standard of value for transfer pricing which Canada and its treaty partners generally adopt in their bilateral tax conventions. The Canada Revenue Agency ("CRA") and OECD have also issued numerous publications providing relevant administrative guidance for transfer pricing in Canada.[4]

The transfer pricing questions concerning how, and at what price, are technically and pragmatically complex as there are various aspects and opposing interests to consider. Technical complexity arises from the fact that the transfer pricing analysis needs to find the answer to a hypothetical question, that is, what the parties to the transaction would negotiate if they were unrelated. This often leads to the necessity of expressing the pricing conclusion in the form of a range. At the same time, the taxpayer and each of the tax authorities involved may have their own views on what the transfer price should be.

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3 Section 251 of the ITA defines the meaning of "arm's length" as well as the meaning of the "related persons".
4 The OECD's publications can be found at http://www.oecd.org/ctp/transfer-pricing/. The CRA's publications can be found at https://www.canada.ca/en/revenue-agency/services/tax/international-non-residents/information-been-moved/transfer-pricing.html

When there are conflicting views the price actually used by the taxpayer for tax filing purposes might be adjusted, upon audit conducted after the fact by either of the relevant tax authorities. The taxpayer usually challenges this audit adjustment and that leads to a long and complicated dispute resolution journey. It also often leads to double taxation since the same income is subject to tax twice.[5]

Effective transfer pricing is always about finding a compromise and performing a balancing act that takes into consideration the partially divergent interest of the multiple stakeholders.

1.2 Domestic Law: Section 247 of the ITA

Transfer pricing rules in Canada are contained within in Part XVI.1 / section 247 of the ITA, which is comprised of 15 subsections covering the subjects summarized in the list below:[6]

- **Subsection (1):** Definitions
- **Subsection (10):** No adjustment unless appropriate
- **Subsection (11):** Provisions applicable to Part XVI.1
- **Subsection (12):** Deemed dividends to non-residents
- **Subsection (15):** Non-application of provisions
- **Subsection (2):** Transfer pricing adjustments
- **Subsection (3):** Transfer pricing penalties
- **Subsection (4):** Documentation requirements to avoid penalties
- **Subsection (8):** Other provisions of the ITA not applicable
- **Subsection (9):** Anti-avoidance
- **Subsections (13), (14):** Repatriation, repatriation interest
- **Subsections (5), (6):** Partner's gross revenue, deemed member of a partnership
- **Subsections (7), (7.1):** Exclusions for loans, guarantees to CFAs

Amongst a number of additional terms, subsection 247(1) notably defines both "transfer price" and "arm's length transfer price" as presented in the section below:[6]

> ***Key definitions from subsection 247(1) of the ITA***
>
> *"transfer price" means, in respect of a transaction, an amount paid or payable or an amount received or receivable, as the case may be, by a participant in the transaction as a price, a rental, a royalty, a premium or other payment for, or for the use, production or reproduction of, property or as consideration for services (including services provided as an employee and the insurance or reinsurance of risks) as part of the transaction.*
>
> *"arm's length transfer price" means, in respect of a transaction, an amount that would have been a transfer price in respect of the transaction if the participants in the transaction had been dealing at arm's length with each other.*

The actual standard of value employed in transfer pricing in Canada is the "arm's length principle" ("ALP"), which is defined in subsection 247(2) of the ITA. The section below presents this using a relevant excerpt

5 Hence, the network of bilateral international tax conventions that assists taxpayers to obtain relief from double taxation.
6 This paper does not cover all of these subsections directly; rather, it focuses on those highlighted in blue.

from subsection 247(2):[7]

Arm's length principle (emphases added) in subsection 247(2) of the ITA

*(2) Where a taxpayer or a partnership and a non-resident person with whom the taxpayer or the partnership, or a member of the partnership, does not deal at arm's length (or a partnership of which the non-resident person is a member) are participants in a **transaction** or a **series of transactions** and*

*(a) the **terms or conditions** made or imposed, in respect of the transaction or series, between any of the participants in the transaction or series **differ from** those that would have been made between persons dealing at **arm's length**, ...*

*...**any amounts** that, but for this section and section 245, would be determined for the purposes of this Act in respect of the taxpayer or the partnership for a taxation year or fiscal period **shall be adjusted** (in this section referred to as an "adjustment") to the quantum or nature of the amounts that would have been determined if,*

*(c) where only paragraph 247(2)(a) applies, the terms and conditions made or imposed, in respect of the transaction or series, between the participants in the transaction or series had been those that would have been made **between persons dealing at arm's length**, or...*

1.3 International Tax Conventions: Article 9 of the OECD Model Tax Convention

Article 9 of the OECD Model Tax Convention defines the standard of value for transfer pricing internationally; Canada and its treaty partners generally adopt it in their tax conventions. It is presented in the section below:[8]

Arm's length principle (emphases added) in Article 9 of the OECD Model Tax Convention

*Where an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State, and **in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.***

*Where a Contracting State includes in the profits of an enterprise of that State — and taxes accordingly — profits on which an enterprise of the other Contracting State has been charged to tax in that other State and the profits so included are profits which would have accrued to the enterprise of the first-mentioned State if the conditions made between the two enterprises had been those which would have been made between independent enterprises, then that **other State shall make an appropriate adjustment to the amount of the tax charged therein** on those profits. In determining such adjustment, due regard*

7 Emphases are added by the authors of the paper.
8 Emphases are added by the authors of the paper.

shall be had to the other provisions of this Convention and the competent authorities of the Contracting States shall if necessary consult each other.

Article 9 of the OECD Model Tax Convention and subsection 247(2) of the ITA are clearly very similar. Most notably, both reference the conditions of the transaction instead of only the price.

2.1 Transfer Pricing Penalties and Contemporaneous Documentation

In addition to imposing the ALP, subsection 247(2) of the ITA enables the CRA to make transfer pricing adjustments. If substantial enough, these transfer pricing adjustments may result in substantial transfer pricing penalties, which are equal to 10% of the net adjustment made by the CRA.

Whether transfer pricing penalties are applicable is governed by subsection 247(3) of the ITA. The relevant excerpt is presented below:

> ***Transfer pricing penalties in subsection 247(3) of the ITA***
>
> *"A taxpayer... is liable to a penalty for a taxation year equal to 10% of the amount determined under paragraph (a) in respect of the taxpayer for the year, where...*
>
> *(a) the amount, if any, by which (i) the total of (A) the taxpayer's transfer pricing capital adjustment for the year, and (B) the taxpayer's transfer pricing income adjustment for the year* exceeds the total of...
>
> *... is greater than...*
>
> *(b) the lesser of (i) 10% of the amount that would be the taxpayer's gross revenue for the year if this Act were read without reference to subsection (2), subsections 69(1) and (1.2) and section 245, and (ii) $5,000,000."*

The risk of transfer pricing penalties applying can be mitigated through the timely preparation and provision of contemporaneous documentation, as prescribed by subsection 247(4) of the ITA. The section below presents subsection 247(4).

> ***Contemporaneous documentation in subsection 247(4) of the ITA***
>
> *...a taxpayer or a partnership is deemed not to have made reasonable efforts to determine and use arm's length transfer prices or arm's length allocations in respect of a transaction or not to have participated in a transaction that is a qualifying cost contribution arrangement, unless the taxpayer or the partnership, as the case may be,*
>
> *(a) makes or obtains, on or before the taxpayer's or partnership's documentation-due date for the taxation year or fiscal period, as the case may be, in which the transaction is entered into, records or documents that provide a description that is complete and accurate in all material respects of*
>
> > *(i) the property or services to which the transaction relates,*
> >
> > *(ii) the terms and conditions of the transaction and their relationship, if any, to the terms and conditions of each other transaction entered into between the participants in the transaction,*
> >
> > *(iii) the identity of the participants in the transaction and their relationship to each other at the time the transaction was entered into,*

(iv) the functions performed, the property used or contributed and the risks assumed, in respect of the transaction, by the participants in the transaction,

(v) the data and methods considered and the analysis performed to determine the transfer prices or the allocations of profits or losses or contributions to costs, as the case may be, in respect of the transaction, and

(vi) the assumptions, strategies and policies, if any, that influenced the determination of the transfer prices or the allocations of profits or losses or contributions to costs, as the case may be, in respect of the transaction;

(b) for each subsequent taxation year or fiscal period, if any, in which the transaction continues, makes or obtains, on or before the taxpayer's or partnership's documentation-due date for that year or period, as the case may be, records or documents that completely and accurately describe each material change in the year or period to the matters referred to in any of subparagraphs (a)(i) to (vi) in respect of the transaction; and

(c) provides the records or documents described in paragraphs (a) and (b) to the Minister within 3 months after service, made personally or by registered or certified mail, of a written request therefor.

As presented in paragraphs 247(4)(b) and (c), absent of the timely preparation and provision of the adequate documentation there are no means for a taxpayer to qualify for the "reasonable efforts" exception from the transfer pricing penalties.

Although the dispute resolution journey involved in resolving the double taxation resulting from a transfer pricing adjustment made by the CRA is outside of the scope of this paper, the exhibit below presents a potential early sequence of events in a Canadian transfer pricing audit and that may lead to the application of transfer pricing penalties pursuant to subsection 247(3).[9]

CRA	TAXPAYER
	Preparation of transfer pricing documentation
Letter requesting contemporaneous documentation	
	Provide contemporaneous documentation within three months
Queries and consultations with HQ TP Economist on technical matters	Responding to CRA queries
TP adjustment is issued	
Make representations to TP Review Committee on applicability of TP penalties	Make representations to TP Review Committee on applicability of TP penalties
TP Review Committee evaluates applicability of TP penalties	

9 This exhibit was prepared by the authors of this paper.

COMPARING BUSINESS VALUATIONS TO TRANSFER PRICING

3.1 Purpose and Scope

BUSINESS VALUATIONS

Business valuations are performed for a variety of purposes, including financial reporting, litigation, matrimonial, tax, and other commercial purposes. Depending on the purpose, the valuations may be governed by accounting standards, commercial law, family law or the ITA.

Valuations of business interests may cover domestic or cross-border boundaries and they may also cover arm's length or non-arm's length transactions. Typically, businesses, tangible and intangible property, and financial instruments are valued.

TRANSFER PRICING

Transfer pricing is only performed for tax purposes and it is domestically governed by section 247 of the ITA and internationally through bilateral tax conventions.

The scope of transfer pricing covers all cross-border, non-arm's length transactions. Transfer pricing generally involves the determination of arm's length transfer prices for tangible and intangible property, services and financial instruments.

COMPARISON

Both the purpose and scope of business valuations are notably broader than those of transfer pricing analyses, which focus solely on cross-border, non-arm's length transactions and is performed only for tax purposes. However, based on this comparison, there is also a distinct overlap – the pricing of cross-border intercompany transactions for tax purposes. This raises a fundamental question for taxpayers, that is to say, how are these transactions valued/priced?

3.2 Pricing of Intercompany Transactions for Tax Purposes

In this context, the pricing of intercompany transactions for tax purposes is governed by two sections of the ITA - subsection 69(1) and section 247.

BUSINESS VALUATIONS FOR TAX PURPOSES

> ***Fair market value in paragraph 69(1)(a) of the ITA***
>
> *"Except as expressly otherwise provided in this Act, where a taxpayer has acquired anything from a person with whom the taxpayer was not dealing at arm's length at an amount in excess of the fair market value thereof at the time the taxpayer so acquired it, the taxpayer shall be deemed to have acquired it at that fair market value"*

Unlike subsection 247(2), paragraph 69(1)(a) of the ITA imposes the fair market value ("FMV") as a standard of value. Notably, subsection 69(1) of the ITA also does not contain any specific penalties, nor does it impose any contemporaneous documentation requirements for taxpayers to mitigate those penalties.

TRANSFER PRICING FOR TAX PURPOSES – SECTION 247 OF THE ITA

As described earlier in this paper, subsection 247(2) of the ITA imposes the ALP as a standard of value and allows the CRA to make transfer pricing adjustments. In addition, it is important to notice that paragraph 69(1)(a) is a deeming provision whereas subsection 247(2) effectively adjusts any amounts and therefore has significantly broader tax implications.

If substantial enough, a transfer pricing adjustment may result in substantial transfer pricing penalties, which are equal to 10% of the net adjustment made by the CRA. Transfer pricing penalty risk can be mitigated, but not fully eliminated, through the timely preparation and provision of contemporaneous documentation as prescribed by subsection 247(4). An additional condition (introduced in subparagraph 247(3)(a)(ii)) contributing to the mitigation of transfer pricing penalty risk is the actual implementation and use of the arm's length transfer prices determined by the taxpayer. Ultimately, in Canada, the standard that the ITA holds to taxpayers is that they must both determine (completely, accurately, and on a timely basis) and use arm's length transfer prices.

COMPARISON

These two sections of the ITA impose differently defined standards of value.

Section 247 also imposes transfer pricing penalties and contemporaneous documentation requirements to mitigate them. By comparison, section 69 does not impose any specific penalties or documentation requirements.

As noted above, the scope of both section 247 and section 69 may cover cross-border intercompany transactions. However, subsection 247(8) (presented below[10]) of the ITA leaves little to interpretation, as it plainly indicates that if subsection 247(2) is applicable in adjusting an amount then subsection 69(1), amongst others, will not apply.

> ***Subsection 247(8) of the ITA (emphasis added)***
>
> *"Where subsection (2) would, if this Act were read without reference to sections 67 and 68 and subsections 69(1) and (1.2), apply to adjust an amount under this Act, sections 67 and 68 and subsections 69(1) and (1.2)* ***shall not apply*** *to determine the amount if subsection (2) is applied to adjust the amount."*

Given this, it is apparent that, to the extent that the CRA raises a transfer pricing adjustment, there is a very real risk that punitive transfer pricing penalties may apply. As previously stated, these penalties may be mitigated through the preparation of contemporaneous documentation supporting the taxpayer's determination and use of arm's length prices, using the ALP as the standard of value.

This integral observation leads to the questions explored in subsequent sections of this paper:

- How do the FMV standard and ALP compare?
- How do valuation approaches compare to transfer pricing methods?
- Can a valuation report spontaneously meet transfer pricing documentation requirements?

3.3 Standards of Value

BUSINESS VALUATIONS – FAIR MARKET VALUE

The standard of value employed in performing business valuations is the FMV standard. As identified above, the FMV standard is also imposed in paragraph 69(1)(a) of the ITA as the standard of value when performing certain business valuations for tax purposes. The relevant definition of FMV was established

10 Emphases are added by the authors of the paper.

in *Henderson Estate v. M.N.R. 73 D.T.C. 5471*. The CRA's Information Circular 89-3 also defines FMV as presented below.[11]

Fair market value standard (colour coding added)

"the highest price, expressed in terms of money or money's worth, obtainable in an open and unrestricted market between knowledgeable, informed and prudent parties acting at arm's length, neither party being under any compulsion to transact"

TRANSFER PRICING – ALP

As stated previously in this paper, the ALP is the standard of value employed for transfer pricing purposes and it is imposed in subsection 247(2) of the ITA, which is presented below.[12]

COMPARISON

As illustrated by the colour coding added in the two exhibits above, the key elements of the FMV standard can broadly be identified within the definition of the ALP.

Arm's length principle from subsection 247(2) of the ITA (colour coding added)

"Where a taxpayer or a partnership and a non-resident person with whom the taxpayer or the partnership, or a member of the partnership, does not deal at arm's length (or a partnership of which the non-resident person is a member) are participants in a transaction or a series of transactions

...the terms or conditions made or imposed, in respect of the transaction or series, between any of the participants in the transaction or series differ from those that would have been made between persons dealing at arm's length ...

...any amounts that, but for this section and section 245, would be determined for the purposes of this Act in respect of the taxpayer or the partnership for a taxation year or fiscal period shall be adjusted to the quantum or nature of the amounts that would have been determined if,

... the terms and conditions made or imposed, in respect of the transaction or series, between the participants in the transaction or series had been those that would have been made between persons dealing at arm's length..."

In addition to the ALP language from subsection 247(2) of the ITA, one should also consider the definition of the "arm's length transfer price" (presented below) as part of reconciling the definitions of the two standards of value.

Key definitions from subsection 247(1) of the ITA

"transfer price" means, in respect of a transaction, an amount paid or payable or an amount received or receivable, as the case may be, by a participant in the transaction as a price, a rental, a royalty, a premium or other payment for, or for the use, production or reproduction of, property or as consideration for services (including services provided as an employee and the insurance or reinsurance of risks) as part of the transaction.

"arm's length transfer price" means, in respect of a transaction, an amount that would have been a transfer price in respect of the transaction if the participants in the transaction had been dealing at arm's length with each other.

11 The authors of this paper have colour coded this definition for illustrative purposes.
12 The authors of this paper have colour coded this definition for illustrative purposes.

As illustrated above, the definition "arm's length transfer price", in fact, introduces a direct reference to the price, but not necessarily "the highest price obtainable". The views of the authors are that it is logical to assume that if the "participants" were "dealing at arm's length with each other" they would be driven by the economic imperatives to the "highest price obtainable" outcome.

The authors of this paper have also identified two additional key items that may have to be addressed in an in-depth reconciliation exercise of the two standards of value:

- First, under the ALP, the terms and conditions rather than only the price itself are subject to arm's length verification, and this verification requirement is not only applicable to a single transaction, but also to a series of transactions.
- Second, when defining the "persons" under the ALP, one needs to consider the special interest purchaser issue (i.e., to what extent any synergistic benefits are to be factored into a valuation conclusion), while at the same time being cognizant of the fact that this consideration is taking place in the intercompany context when all of the benefits of the actual transaction are apparent to the transacting parties, and are legislatively required to be described in the pertinent documentation.
- Finally, and most importantly, it is noted that both standards of value clearly impose the pricing of the transaction under notional circumstances.

Once having, hopefully, dealt with the FMV/ALP reconciliation issue one can move to the next step of the comparative analysis, this being the comparison of the approaches actually undertaken to effect these standards of value.

3.4 Valuation Approaches and Transfer Pricing Methods

BUSINESS VALUATIONS – VALUATION APPROACHES TO APPLY THE FAIR MARKET VALUE STANDARD

The selection of a valuation approach depends on what is being valued (shares, **assets** or an interest in a business). The first step is to determine whether the valuation is to be conducted on a going concern or liquidation basis. The generally accepted approaches to determining value include the following:

- **Income/cash flow approach:** ascribes value based on valued assets ability to generate future discretionary cash flows and earn a reasonable return on investment.
- **Market approach:** ascribes value based on value relationships and/or activity ratios derived from the analysis of other market transactions.
- **Asset/cost approach:** uses the current value of a company's tangible net assets as the prime determinant of value.

TRANSFER PRICING – TRANSFER PRICING METHODS TO APPLY THE ARM'S LENGTH PRINCIPLE

The selection of a transfer pricing method always aims at finding the most appropriate method for a particular case. The evaluation of the appropriateness of a particular method depends on a functional analysis (functions, assets, and risks), delineation of the transaction to determine the terms and conditions, the availability of information, and the degree of comparability between controlled and uncontrolled transactions.

Transfer pricing methods include the following:

- Traditional transaction methods (comparable uncontrolled price method, resale price method, cost plus method).

- Transactional profit methods (profit split method, transactional net margin method).
- Other methods (such as cash-flow-based valuation methodologies) may also be employed in the appropriate circumstances.

COMPARISON

Fundamentally, determining whether an application of a particular valuation approach will lead to the same value conclusion as an application of a particular transfer pricing method given the same facts and circumstances is entirely dependent on those facts and circumstances.

A notable dichotomy that may lead to differing value conclusions, again entirely dependent on the facts and circumstances, is that valuation approaches are driven by the underlying assets being valued; whereas, transfer pricing methods are driven by a functional analysis of the transaction (i.e., the functions performed, risks borne, and assets employed by the participants to the transaction).

3.5 Base Erosion and Profit Shifting

This dichotomy is further complicated through significant and transformational recent changes in the revised transfer pricing guidance issued by the OECD as a result of its Base Erosion and Profit Shifting ("BEPS") project. Some of these fundamental changes and the rational in support of them are presented in the exhibit below.[13]

> ***OECD/G20 Base Erosion and Profit Shifting Project - Aligning Transfer Pricing Outcomes with Value Creation - Actions 8-10: 2015 Final Reports (emphasis added)***
>
> *"The arm's length principle has proven useful as a **practical and balanced standard** for tax administrations and taxpayers to evaluate transfer prices between associated enterprises, and to prevent double taxation. However, with its perceived emphasis on **contractual allocations** of functions, assets and risks, the existing guidance on the application of the principle has also proven **vulnerable to manipulation**. This manipulation can lead to outcomes which do not correspond to **the value created through the underlying economic activity** carried out by the members of an MNE group." (p.9)*
>
> *"For intangibles, the guidance clarifies that **legal ownership alone does not necessarily generate a right** to all (or indeed any) of the return that is generated by the exploitation of the intangible." (p.10)*
>
> *"If this associated enterprise does **not in fact control the financial risks** associated with its funding...then it will not be allocated the profits associated with the financial risks." (p.11)*
>
> *"The guidance...will ensure that **capital-rich entities without any other relevant economic activities** ("cash boxes") will not be entitled to any excess profits. The profits the cash box is entitled to retain will be equivalent to **no more than a risk-free return**." (p.11)*
>
> *"...the goals set by the BEPS Action Plan in relation to the development of transfer pricing rules have been achieved **without the need to develop special measures outside the arm's length principle**."(p.12)*

These changes are so transformational that they are calling into question the status quo interpretation of the ALP. The authors of this paper are aware of numerous instances wherein the CRA is employing this new guidance to make very significant transfer pricing adjustments, which often results in extremely complex and long dispute resolution journeys.

3.6 Valuation Reports and Transfer Pricing Documentation

BUSINESS VALUATIONS – VALUATION REPORTS:

According to CICBV Practice Standard no. 110, at a minimum, valuation reports include:

- Introduction
- Report definitions
- Report scope of review and limitations
- Report disclosure (i.e., basis of valuation and key assumptions)
- Report restrictions and qualifications
- Conclusion

Comprehensive and estimate valuation reports also include a description of valuation calculations, summary of relevant financial information, business description, earnings/cash flow risk factors, description of shares and their prices and volumes (if applicable). In addition to these items, comprehensive valuations reports also include the economic context and industry outlook bearing on the shares, assets or interest in a business being valued.

TRANSFER PRICING - TRANSFER PRICING DOCUMENTATION

According to paragraph 247(4)(a) of the ITA, transfer pricing documentation should include a complete and accurate description (in all material aspects) of the following:

1. The property or services to which the transaction relates;
2. The terms and conditions of the transaction and their relationship, if any, to the terms and conditions of each other transaction entered into between the participants in the transactions;
3. The identity of the participants in the transaction and their relationship to each other at the time the transaction was entered into;
4. The functions performed, the property used or contributed and the risks assumed, in respect of the transaction, by the participants in the transaction;
5. The data and methods considered and the analysis performed to determine the transfer prices or allocations of profits or losses or contributions to costs, as the case may be, in respect of the transaction; and,
6. The assumptions, strategies and policies, if any, that influenced the determination of the transfer prices or the allocations of profits or losses or contributions to costs, as the case may be, in respect of the transaction.

COMPARISON

In general, depending on the type of valuation report prepared and the specific report itself, the CRA's transfer pricing review committee may recommend the application of penalties if, amongst other things, it identifies deficiencies in any of the six elements indicated above. Although it is difficult to generalize this, given the contents of CICBV Practice Standard no. 110, the following aspects may be viewed as potentially deficient from the transfer pricing perspective:

- the terms and conditions of the transaction and their relationship, if any, to the terms and conditions of each other transaction entered into between the participants in the transactions;
- the relationship of the participants to the transaction to each other at the time the transaction was entered into;
- the functions performed, the property used or contributed and the risks assumed, in respect of the

transaction, by the participants in the transaction;

- the data and methods considered; and,
- the strategies and policies, if any, that influenced the determination of the transfer prices.

4.1 Bridging the Gaps and Effective Risk Mitigation Strategies

Based on the comparative analysis of business valuations and transfer pricing above, the application of the FMV standard and ALP may lead to diverging value conclusions. Furthermore, a valuation report prepared in accordance with CICBV Practice Standard no. 110 may not be viewed by the CRA's transfer pricing review committee as satisfactory in the context of qualifying for the "reasonable efforts" exception from the transfer pricing penalty as prescribed by section 247 of the ITA.

In order to mitigate the fundamental risks associated with these dichotomies, there are practical, both proactive and reactive measures that Canadian taxpayers can undertake.

Certain proactive risk mitigation measures that taxpayers should consider include the following:

- Making sure the valuation/pricing analysis is a team effort by bringing in both the business valuators and the transfer pricing specialists when dealing with the section 247 transactions;
- taking inventory of your cross-border intercompany transactions in the past seven years, and performing a risk assessment regarding their terms and conditions from a Canadian perspective;
- reviewing and, if required, supplementing existing valuation reports to confirm subsection 247(2) compliance and meet contemporaneous documentation requirements with the assistance of a transfer pricing specialists; and,
- coordinating with the tax preparers to ensure that the slips to the T106 information return reflect that contemporaneous documentation has been prepared (only if it has actually been prepared).

Certain reactive risk mitigation measures that taxpayers should consider include the following:

- involving transfer pricing specialists upon the commencement of a CRA transfer pricing audit, which is typically initiated with a request for contemporaneous documentation;
- compiling and providing contemporaneous documentation to CRA within three months of it being requested; and,
- responding to CRA queries on a timely basis and working through the tax administration process related to transfer pricing.

The Valuation Profession, IVSC (International Valuations Standards Council) and its Role in the Global Financial System

4

by Sir David Tweedie[1] and Nick Talbot[2]

1.1 IVSC Structure

The IVSC is the international standard setter for valuation. It is formally recognized by the United Nations, and can claim the World Bank as a member and a sponsor through the IFC (International Finance Corporation). The IVSC is roughly comprised of: a council of members, a Standards Review Board, three specialist boards, and a Membership and Standards Recognition Board.

The IVSC has over a hundred members and sponsors from around the world. The CICBV, for example, is a leading member and sponsor; it participates in the council of members which is the ultimate decision making mechanism for how the organization, as well as other boards, are operated. There is an independent board of trustees, who have responsibilities in regards to the governance of the organization, fundraising, and representation. Additionally, there is a Standards Review board, which oversees three specialist standards boards that cover Tangible Assets, Business Valuation, and Financial Instruments respectively (the latter is just now being put in place). This structure is quite new and has the aim of both establishing a more in depth expertise for each asset class, and increasing global representation. The Standards Review Board is essentially responsible for the generic parts of standards, which include correlating information from the three specialist boards in order to ensure that all of the trajectories are aligned and fit together. The Standards Review Board reviews the market needs with the specialist standards boards, to establish priorities.

The IVSC welcomes and encourages new views, particularly in consultations, in order to establish the highest quality of standards. The IVSC actively engages with all stakeholders, whether that is professional bodies, regulators, institutions or corporates, in order to continuously improve our outputs and what we do. This engagement is important to ensure that the standards are used effectively.

The Membership & Standards Recognition Board takes action to achieve the adoption of IVS (international valuations standards) globally. The board reviews the requirements needed to join the IVSC, and explores what is needed to further professionalism around the world, particularly in developing markets.

This supports the aim of the IVSC to promote professionalism globally. To clarify, what does it mean to be professional in this context? It means that valuators should have an ethical stance; they should put the interest of the general good of society first. They should apply the right standards and submit to monitoring and oversight if needed. As to a professional body, it should have an effective qualification process, ongoing learning, monitoring, and investigation. It should additionally have fundamentals that hold it together, such as a code of ethics and a competence framework.

1 David Tweedie was the first chair of the International Accounting Board for over ten years, starting in 2001. He was knighted in 1994 for his service to the accounting profession. He is currently the Chair of the Board of Trustees of the International Valuations Standards Council, and has been since 2012.

2 Nick Talbot has been the Chief Executive Officer of the IVSC since 2016. Prior to his role as CEO he served as a global director for a VPO. Nick has also worked in a number of global senior consulting roles. In 2016 he received a Point of Light Award from the British Prime Minister for his charity work.

An independent structure operating in the public interest is of great assistance when the IVSC is approaching regulators or governments in terms of the credibility needed for an organization to promote effective valuation approaches, as well as excellent professionalism.

2.1 International Valuations

Historically the IVSC began to operate in the 1980s. At this point, it mainly dealt with real estate. This changed in 2008, partially due to the financial crisis, when a decision was made to expand the IVSC horizons to cover all asset classes.

The objectives were, and remain, simple:

1. Set global valuation standards across all asset classes
2. Protect the public interest
3. Improve the credibility of the valuation profession

The IVSC strived for one set of high quality valuation standards in order to narrow the gap between national and institutional valuations. The idea was and is, that it does not matter if a CBV performs a valuation in Quebec or Qatar or Queenstown, they should be able complete it in the same manner in order to provide valuations that are consistent, comparable, and confident to the end user.

The notion of high quality is one aspect where globalization plays a role. If one country has discovered a better approach to a problem, then that approach is taken into the standards as opposed to any others. The cream, or good standards in this case, rise to the top. The goal of the IVSC is to make the international valuation standards not only the gold standard, but also the global standard, with excellent professionalism in place globally throughout the VPOs (Valuation Professional Organizations).

Why global? Why choose to be global at all? Valuation is so ingrained in the international economy that perhaps even valuators do not understand the importance of what they do to help ensure financial stability.

When the International Accounting Standards Board (IASB) started, only five countries used the international financial reporting standards (IFRS), 10 years later over a 120 chose to partake, currently 140 countries do. One notable exception is the US, however it may only be a matter of time until they too use the IFRS due to its growing spread. The idea was and is to provide the world market with an integrated accounting market. We wanted to remove the accounting risk of not understanding a nations accounting, particularly as more interactions necessitate global collaborations. For example, 20 percent of the companies listed in London are foreign[3].

There is, of course, resistance to moving to one set of standards. Change can be a great fear for some, while for others it is the potential cost that causes unease. Perhaps most profoundly, it is the perceived loss of control that causes the most resistance. However, corporations are global, they consolidate, and they want to use the same methods. Change is already here, globalization is becoming increasingly prevalent, and so the standards should reflect the needs of the people. Organizations can either lead the discussion or ultimately be pushed to accept it.

The IASB had quite a concern considering those needs and how to meet them on such an expansive scale. One direction that helped was brevity. The IFRS is about two and a half thousand words while its US coun-

11 Emid Al, Grahman Gavin. Investing on Frontier Markets. Mississauga: John Wiley & Sons, 2013. Print.

terpart is seventeen and a half thousand words. The IASB chose to be concise because professionalism and principle based standards seemed to be the most effective for the largest group of people. Similarly, the international valuations standards (IVS) are not there to tell valuators what to do, as each situation has its own complexities, but to set up the principles that determine how a situation should be approached. We aim to create standards that would allow valuators to extrapolate what they need from said standards in order to deal with their own individual issues. It is more prudent and manageable for all parties involved to cover 80 percent of the issues concisely in 30 pages rather than 95 percent in 300 pages.

What then is to be done about the remaining 20 percent of the issues? It is the responsibility of national valuation standard setters to deal with national concerns. There are some issues that are not of concern to the international community that are of great concern to a particular country. It is up to that country to regulate what should be done. If the standards are to be global, then the IVSC cannot deal with every country-specific issue. Global standards deal with the main issues for the reasons discussed above. National standards address the unique and individual issues of a nation. The two should work in tandem for the greatest effect. One dealing with the large picture, the other the small.

2.2 Why are Valuations Important?

Valuations are vital to almost all aspects of our financial system. For example, financial stability and financial reporting depend heavily on valuations. Consequentially, financial reporting helps financial regulators determine how to control stability. Financial regulators, do not however, trust valuations quite yet.

In the financial crisis of 2008, valuation was at the heart of the arguments. One of the problems during the crisis was the level of equity held in banks. In the mid-19th century 33 percent of major banks balance sheets was equity. By the end of the 19th century it was 20 percent and one hundred years later it was 5 percent. At the time of the crisis it was 2 percent. It is not difficult to get valuations wrong enough to lose two percent, and it was lost. At one point in the world crisis one quarter of the world's GDP was propping up the global banks.

To put the importance of valuation further in perspective, when the G7 held an emergency meeting in Brussels after the crisis hit, Mario Draghi who was the chairman of the financial stability board at that time, turned to me and asked a question along the lines of: "David what are your accountants doing about valuation"? I replied, "nothing - that's not our expertise, we take values not create them". He then asked me "who's doing it" and I said, rather nonchalantly, "there are people out there". It turns out there was a deficit of people focusing solely on the creation of values, and that was part of the problem. The valuation differences in different banks for the same instruments were inconceivable. There was great confusion during the crisis as to where the numbers given came from.

Cost is easier to control than value. Things can be sold as needed, and people can manipulate profit. When using value it becomes more difficult to do so. For that reason value was used during the crisis and as values fell it was not appreciated. It was, however, necessary. There were huge pressures to stop valuing and return to cost, which was more familiar; however, it was simply impractical to do so.

There are certain things cost simply cannot cover such as derivatives or homegrown intangibles to name a few. In the IFRS you cannot show an internally generated intangible unless you can measure it reliably. That is a fault of accounting; assets cannot be called as such, in some cases, as the reliability of their value, is at present, not accepted. People are nervous about value, but what can be done in situations dealing with agriculture and the like without valuation? Consider, for example, what the cost of a calf might be – could it be half of a cow, a quarter? It is more sensible to simply value the cow than to determine cost. There are many such examples where cost simply does not cut it.

3.1 Conclusion

In short, we believe that globalization and valuation are the trajectory of the future. One set of global standards is a key component to make valuation an international profession. We want valuation to be international and recognized as such. We want the fact that value is trusted to spread across the markets. The end goal of these aims is ideally, the increase of financial stability across the world benefitting all countries.

5

Write Less. Say More.

by Susan H. Glass[1]

A. INTRODUCTION

This paper addresses successful report writing, focusing on valuation reports. We will cover the report-writing process, the style and structure of a valuation report, and tips on how to write less and say more.

Why should you focus on writing clearly and concisely?

1) To get to the point in a way that the reader will easily understand
2) To capture and retain the reader's interest
3) To persuade the reader
4) To enhance your insight
5) To impress clients and others

What is involved?

Well-written reports require attention to at least eight key issues:

1) Organization and planning
2) Grammar and spelling
3) Word choice
4) Word count
5) Sentence construction
6) Sentence and paragraph length
7) Transitions
8) Detailed editing

Should you always write clearly and concisely?

Benjamin Franklin once said: "I have already made this paper too long, for which I must crave pardon, not having now time to make it shorter"[2].

Writing clearly and concisely takes time, and you should assess whether the benefits outweigh the costs in each situation. In making that decision, ask yourself a few questions: Who is my audience and will they appreciate a well-written report? Will the report be public or private? What is the purpose of the report? Am I trying to convince the reader or merely inform the reader?

Chances are that formal opinions, reports for public disclosure, and reports that must be persuasive will deserve the extra time, whereas internal reports, reduced-scope reports, brief memos and emails will not. Reports that will be publicly disclosed or otherwise viewed as critical should undergo a formal process, which involves preparation, an initial draft, editing, copyediting, and proofing – each as discussed below.

1 Susan Glass leads KPMG's Canadian valuation and litigation services practice. She specializes in valuations, damage quantifications and financial modeling.
2 Franklin, Benjamin. Letter to Peter Collinson. 29 July. 1750.

Preparation, Initial Draft, Copyedit, and Proof

PREPARATION: BEFORE YOU WRITE

Before you put pen to paper, decide what type of report you need. Will it be a formal written report or a presentation? Who are your readers? Are they financial experts or novices? Will you need to explain basic financial concepts or will the reader readily understand the basics?

With these issues in mind, you should prepare a report schematic – an outline of the report that includes the relevant sections and a brief summary of the intended content of each section. Decide what is crucial to the valuation and include those issues in the main body. More detailed analyses and information that is required, but not directly relevant, can be placed in appendices. Information that is irrelevant and is not required should not find its way into your report.

Before writing, consider reviewing the report schematic with relevant individuals – such as a partner or the client.

PREPARE AN INITIAL DRAFT

The process begins with an initial draft – and your focus at this stage should be on content and organization, together with key structural issues. Minor wording issues can be addressed later.

At all times, keep it simple. The more you can simplify things the better, particularly if your reader has limited valuation experience. Experts and novices see things differently. An expert will see the whole, while a novice will see only individual parts. For example, when learning to read, a child will read each individual letter, while an adult will see whole words and full sentences. Valuators will see the whole, whereas lawyers, judges, and many clients will see only the individual parts. Make it easy for them to connect the dots. Use charts or pictures when doing so to simplify the discussion.

Avoid jargon as much as possible. If you are using a term for the first time, define it. Additionally, include a glossary of terms for further reference.

Aim for simplicity – minimalism – in report organization and sentence structure. Split long, complex sentences into two. Upon occasion use very short sentences for emphasis. Consider analogies where helpful.

As we will later discuss, be specific, definite and concrete, particularly when discussing key valuation concepts, such as your choice of methodology and assumptions underlying free cash flow, discount rates, and terminal growth rates. Explain why you selected the approach or assumption and, where relevant, explain why you did not consider other approaches or assumptions.

As you're writing, remember to include signposts to tell the reader what you're going to cover. Use phrases like: "as will be discussed below", or "in the following section". Being on a journey and not knowing what's coming next can be frustrating. Don't frustrate your reader. If you provide a roadmap, and update the reader from time to time, he or she will be more interested in your report.

In most cases, your report will benefit from an executive summary, which might be the only part of the report that is read. In my experience, the executive summary is best written after the rest of the report has been prepared, at which point you will be in a better position to know which items are key.

EDIT STEP 1: CONTENT EDITING

Content editing addresses ***what you say***. Is the analysis well supported? Have you properly explained the valuation approach selected? Have you provided support for all key assumptions? Is the report well organized?

EDIT STEP 2: COPY EDITING

Copy editing focuses on ***how you say it***. This step involves correcting punctuation and grammar, as well as sentence structure and length. Ensure the report is understandable. If you find yourself rereading a sentence, that likely means the sentence is confusing, and needs to be rewritten. Make sure your writing is clear and concise, by considering many of the tips we will soon discuss.

EDIT STEP 3: PROOFING

The proof is the final edit – a last check to remove any mistakes. Consider printing the report and reading it aloud. When we read silently, we tend to read entire sentences at once. When we read aloud, we slow down and catch more detail, because we comprehend each word separately.

B. COMMON ERRORS

We will begin by reviewing a few common errors: misplaced modifiers, word choice, and parallelism.

1. Misplaced (or Dangling) Modifiers

A modifier is a word or phrase that adds description to a sentence. When a modifier is misplaced it leads to incorrect or confusing sentences. Let us first look at a few obvious problems:

Example Set 1:

Hanging on the wall, Mary Jane studied the painting.
Covered in mustard and relish, Benjie ate the hot dog.
Flying overheard, Monika saw the geese pass by in a V formation.

In these three examples, the modifiers are misplaced, or separated from that which they are supposed to be describing. The sentences imply that Benjie is covered in mustard; Mary Jane is hanging from the wall; and Monika is flying overhead with the geese. Misplaced modifiers are easy to identify in simple examples such as these, but are often more difficult to spot in your own valuation reports.

Example Set 2:

By using the incorrect capital structure, KPMG's enterprise value for the company is understated.
Turning to the income statement, revenue increased significantly.
After applying the criteria outlined above, our search yielded seven comparable transactions.
In providing our conclusion, you have asked us…"

In these examples, KPMG's enterprise value is apparently capable of using an incorrect capital structure, revenue has turned to the income statement as if they are sitting beside each other, the search itself applied the outlined criteria, and the client evidently provided the conclusion they hired you t o derive.

Beware of phrases that end in "ing", such as "by using", "turning to", "in providing", etc., which are referred to as participle phrases. If your sentences begins with a participle phrase, then the first word after the phrase must be whomever is using, turning to, providing, etc.

Corrected Examples:

Turning to the income statement, we see that revenue increased significantly.
After applying the criteria outlined above, we found seven comparable transactions.
In providing our conclusion, we have..."

2. Word Choice

Ensure you use the appropriate word. Common mistakes include mixing up the words listed below:

- There, their, they're
- To, too, two
- Its, it's
- Between, among
- Imply, infer
- Affect, effect

More subtle problems arise with several other word choices:

1) *Utilize vs. Use:* Utilize is overused. Consider the word "use" if you want to avoid sounding pompous. Reserve "utilize" for situations involving science or income taxes – such as "loss utilization".

2) *Fewer vs. Less:* Use "fewer" when the items can be counted, such as "fewer apples", "fewer people". You can count apples and people. Use "less" when the item cannot be counted (or counting would not be practicable), such as "the jug contains less water". Advise your local grocery store that the express lane should be reserved for "Fewer than 12 items", not "Less than 12 items".

3) *Percent vs. Percentage Points:* Avoid writing "percent" when you really mean "percentage point". For example, a fall in growth from 30% to 20% is not a 10% fall in growth – it is a 10 percentage-point fall in growth. A 10% fall would mean that growth declined from 30% to 27%.

4) *It vs They.* Corporations should be referred to as "it" not "they". Do not write: ABC-Co plans to sell **their** investment. Instead, write: ABC-Co plans to sell **its** investment.

5) *i.e. vs. e.g.:* Some use these two acronyms interchangeably, which is imprecise. The acronym "i.e." is Latin for "id est", which means "in essence". In contrast, "e.g." stands for exempli gratia, which means "for example". That is / for example:
   - Our analysis was based on gross debt (i.e., cash was not deducted)
   - Ex-Co sells sporting goods (e.g., baseballs, hockey sticks, and football helmets)

6) *Which vs. That.* “Which” is non-restrictive. The word “which”, along with all that accompanies the word “which”, can be removed from a sentence without changing the meaning of the sentence. In contrast, the word “that” is restrictive. It cannot be removed from a sentence without changing the meaning. For example, compare “Dogs, which bark, annoy me” to “Dogs that bark annoy me”. The first example implies that all dogs annoy me, and dogs happen to bark. The second example implies that I have no problem with dogs, except for those that bark.

3. Parallelism

Items in a series should have the same grammatical structure. A series includes lists and bullet points, along with items connected by either/or, neither/nor, but also/not only, etc.

Example 1:

INCORRECT	CORRECT
“Susan is professional, courteous, and she always comes to work on time”.	“Susan is professional, courteous, and punctual”.

This sentence contains two adjectives (professional, courteous) and an independent clause (always comes to work on time). The sentence would be improved if an adjective, such as “punctual”, were used instead of “always comes to work on time”, because the sentence would then consist of three adjectives in a row.

Example 2:

INCORRECT	CORRECT	CORRECT (AND PREFERRED)
“Although based in Norway the company also operates internationally, not only in the rest of Europe, but it also operates in North America and Asia.”	“Although based in Norway the company also operates internationally, not only in the rest of Europe, but also in North America and Asia.”	“Although based in Norway, the company also operates in Europe, North America, and Asia.”

Whenever you use “not only”, it should be following by “but also” – and whatever follows “not only” should be structured identically to whatever follows “but also”. In the above example “not only in..” must be followed by “but also in...”. Alternatively, the sentence could be rewritten entirely:

Example 3:

INCORRECT	CORRECT
“CBV Co. estimated the fair value of the company, the fair value of the tangible fixed assets associated with the company, and the estimation of the fair value of the intangible assets associated with the company”.	“CBV Co. estimated the fair value of the company’s business, tangible fixed assets, and intangible assets”.

Proper use of parallelism would turn this incorrect sentence from one that is vague and verbose into one that is clear and concise.

C. STYLE & STRUCTURE

We will now turn from grammar to style. In doing so, we will consider the words of William Shrunk Jr.[3], who wrote: "Vigorous writing is concise. A sentence should contain no unnecessary words, a paragraph no unnecessary sentences, for the same reason that a drawing should have no unnecessary lines and a machine no unnecessary parts. This requires not that the writer make all sentences short, or avoid all detail and treat subjects only in outline, but that every word tell"[4].

We will begin with what I view as the key to a well-written report: Be specific!

1. Be Specific, Definite & Concrete

In the words of Professor Strunk: "Prefer the specific to the general, the definite to the vague, the concrete to the abstract. If those who have studied the art of writing are in accord on any one point, it is this: the surest way to arouse and hold the readers attention is by being specific, definite, and concrete"[5]

Professor Strunk then provided a few examples to distinguish the abstract from the concrete, one of which was:

ABSTRACT	CONCRETE
"A period of unfavorable weather set in"	"It rained every day for a week".

In the first sentence we only know the weather was unfavorable, but we do not know if it was too hot, too cold, snowing or raining. We also do not know how long the weather was poor. The second sentence provides the reader full information and paints a much clearer picture.

Let us turn to examples involving valuations.

Example 1:

ABSTRACT	CONCRETE
"As shown on table seven, there were a number of companies that experienced strong sales growth".	"As shown on table seven, four companies experienced double digit sales growth, ranging from 23% to 73%".

The reader is likely to gloss over the first sentence, which is broad and abstract. The second sentence is specific and concrete. It invites the reader to look at the table more closely, if only to see which company grew by 73%.

3 Shrunk authored The Elements of Style, a respected and recommended text that will be used as a reference throughout this paper. All references to Professor Strunk are taken from this text.
4 Shrunk, William and White, E.B. The Elements of Style. Boston: Allyn & Bacon, 1999.
5 *Elements of Style*

Example 2:

ABSTRACT	CONCRETE
"Although somewhat smaller than the comparables, Port Co. operates in the same industry and is similar in terms of nature of operations".	"In comparing Port Co. to the public companies, potential purchasers would focus on four key factors, three of which are negative, and one of which is positive: • *PortCo is smaller than the public companies. The median revenue for the public companies in 2013 was $914 million, almost 20 times PortCo's revenue. PortCo's smaller size would mean that fewer investors would be interested in the investment, which would limit the potential purchaser pool, which in turn would limit value.* • *The majority of the public ports are seaports, whereas PortCo is an inland port. Thus, …* • *Discuss the remaining differences. In each case, be specific and explain why the difference matters.*

In this "abstract" example, the valuator uses subjective terms (smaller and similar) that mean different things to different people. What does small mean, and how are the companies similar? Equally important, why are size and similarity important? The report would be improved if the valuator were specific and concrete.

In this second example, readers better understand how small Port Co. is, relative to the public companies and why size matters. Remaining bullets would need to display the same characteristics.

All valuation reports contain a few key elements. You should be specific, definite, and concrete when discussing the following issues, in particular:

- *Projected revenues, margins, and capital spending:* How do the projection assumptions compare to history, market data, and other reference points? Do they seem overly conservative, overly ambitious?
- *Selection of the discount rate and underlying risks:* What is the rationale underlying each assumption? Why did you select a 20-year risk-free rate rather than a 10-year rate (or vice versa)? Why did you use a five-year monthly beta rather than a two-year weekly beta? Be specific.
- *Rationale for terminal growth rates or terminal multiples:* Why did you use a perpetual growth model as opposed to a terminal EBITDA multiple (or vice versa)? How did you select the perpetual growth rate (or EBITDA multiple)?
- *Differences between the subject company and the public companies (or transactions)* that drive the selection of the multiple – both general (public vs. private, etc.) and company specific: How do the companies compare in terms of size, growth, risks, margins, nature of operations? Again, be specific.

2. Avoid Expletive Constructions

Expletive constructions are phrases or sentences that begin with: it is, it was, there is, there are, there were (the verb "to be"), when the reference is generic. Expletive constructions are grammatically correct, but they drain your writing of energy.

Example 1:

WEAK	STRONG
There are a number of risks that impact the forecasts, as discussed below: x, y, z	Three key risks impact the forecasts: x, y, z

Example 2:

WEAK	STRONG
There was an increase in competition that resulted in the Company's sales decline in 2016.	In 2016, sales declined due to increased competition.

Other phrases include: It is recommended that…It is inevitable that…It is thought that…There is reason to believe that…It is necessary for… These verbose phrases have no place in your well-written reports.

In addition to expletive constructions, you should avoid "to be" verbs tucked into dependent clauses, such as: "that is", "who is", "that were". These added words serve no purpose.

Example 3:

WEAK	STRONG
The Board approved the forecasts that were prepared by Management	The Board approved the forecasts prepared by Management.

Example 4:

WEAK	STRONG
Another valuation method used by us in determining the fair value of Y-Co was to apply the acquisition EV/EBITDA multiple of 6.1x to the 2016 EBITDA of Y-Co.	We also estimated fair value by applying the 6.1x acquisition EV/EBITDA multiple to Y-Co's 2016 EBITDA.

3. Redundancies

Redundant refers to something that is not needed. In writing, a redundancy refers to two or more words with the same meaning. Your writing will be stronger if you do not repeat yourself.

Common redundancies involve the words "and" or "but":

- We reviewed the income statement and we also reviewed the balance sheet.
- Furthermore, we also considered…
- In addition, we also…
- but instead
- but nevertheless
- but rather

Another common redundancy involves sentences that start with **"The reason why"** and later include **"is because…"**. "The reason why" has the same meaning as "because". You don't need both.

VERBOSE	CONCISE
The reason why sales declined is because…	Sales declined because…
The reason why fair value is higher than last year is because…	Fair value increased relative to last year because…

Other redundancies arise when you state the obvious – by modifying a word using other words that mean the same thing. Some of these redundancies can be amusing. For example:

- Postpone until later: Do you really need "later"? Have you ever postponed until earlier?
- Merge together: Could we merge apart?
- Exactly identical: Are you unsure as to the meaning of the word "identical"?
- Past history; surrounded on all sides; eliminate altogether; future plans; desirable benefit; final outcome; absolutely essential; could possibly… The list goes on…

4. Omit Needless Words: Concise vs. Verbose

Professor Strunk is famed for advising his students to "omit needless words". Thus far, we have reviewed a few words that should be omitted, such as the verb "to be" and redundancies. Other words that cry out for omission include: cases, in terms of, in the process of, for purposes of…:

POOR	BETTER
"Cases"	
In many cases, the comparable companies reported EBITDA losses.	Many comparable companies reported EBITDA losses.
"In terms of"	
X-Co is smaller than the public companies in terms of average revenue.	X-Co's revenue is below the average revenue of the public companies.
"In the process of"	
Z-Co is in the process of upgrading its reporting systems.	Z-Co is upgrading its reporting systems.

The word "that" often begs for omission, especially when combined with "the fact".

POOR	BETTER
"The fact that & that"	
Despite the fact that profits had recently declined, management came to the conclusion that they should proceed with the expansion	Despite the recent profit decline, management decided to proceed with the expansion

POOR	BETTER	BETTER STILL
"The fact that & that"		
Profits increased due to the fact that productivity improved as a result of new technology that was recently introduced	Profits increased because of improved productivity arising from recently-introduced new technology	The Company recently introduced new technology, resulting in improved productivity and higher profits

5. Avoid Verb/Noun Pairs and Wordy Expressions

As was said by Thomas Jefferson: "The most valuable of all talents is that of never using two words when one will do."

Your writing will improve if you use verbs rather than verb/noun pairs. For example, you needn't "come to a conclusion". You can simply "conclude". Don't bother "providing a summary". Just "summarize". And don't travel far and wide to "arrive at a decision". Simply "decide". Other examples of verb/noun pairs and wordy expressions appear below on the left, with the preferable alternate on the right.

Make it clearer	Clarify
Make an acquisition	Acquire
Carry out an improvement	Improve
Put forward the suggestion	Suggest
Regarded as being	Regarded
Submit the recommendation	Recommend
Take into consideration	Consider
Basis (on a daily basis, weekly basis, etc.)	Daily, weekly, etc.

6. Write in the Positive, not the Negative

Your writing will be stronger if you say what happened or what is the case – rather than what did not happen or what is not the case. Reserve the negative for situations when you need to emphasize what did not happen, or when you need to be polite or show restraint.

Compare the examples on the left to those on the right. The examples on the right are stronger, but more severe:

Did not consider	Ignored
Did not	Failed to (or neglected to)
Does not have	Lacks
Did not approve	Rejected
Did not allow	Prevented
Not unreasonable	Reasonable
Not able	Unable
Not different	Alike (or similar)
Not sufficient	Insufficient
Is not the same as	Differs from
Did not perform well	Performed poorly

7. Weasel Words, Overstatements and Qualifiers

If you doubt yourself, others will follow suit. So, do what you can to reduce weasel words, such as may, might, can, could, would, possibly, maybe, perhaps, conceivably, seems, appears, etc.

At the same time, avoid overstating. As Professor Strunk warns: "A single overstatement can diminish the whole". Thus, avoid words and phrases like clearly, obviously, without a doubt, it goes without saying, exceedingly, extraordinarily, amazingly, exceptionally, undisputedly, etc.

Finally, avoid unnecessary qualifiers, such as rather, somewhat, little, pretty, fairly, virtually, very, and really. If you believe the sentence calls for a qualifier, then either consider a stronger word or be specific using data or analysis. For example, instead of saying the company's growth was "very strong", refer to robust growth or solid growth. Alternatively, be specific: "The company's growth was double that of the industry". Instead of saying margins are "really poor", refer to inferior, meagre or deficient margins. Alternatively, be specific: "The company's margins are 60% lower than industry norms".

8. Active vs. Passive Voice

An active voice tells the reader who did what, whereas the passive voice does not specify the actor.

PASSIVE	ACTIVE
An adjusted asset approach was used.	KPMG used an adjusted asset approach.

The active voice generally leads to more dynamic writing. However, the passive is voice is preferred in three cases:

- *To be tactful.* For example, you might say “The report was poorly written”. You avoid mentioning who wrote the report, which is more tactful.
- *To emphasize the action rather than actor.* For example, you might say “The acquisition was approved”. In this case, you want to focus on what was approved, not who gave the approval.
- *When the subject (actor) is irrelevant.* You might say “X Co. was founded in 1996”. In making this statement, you are focused on the founding date. The identity of the founder is irrelevant.

9. Transitions

Transitions bridge concepts and paragraphs. They unify your writing and help the reader understand relationships between ideas or move from one idea to the next. Below are some helpful transitions, organized by category:

1) Add:	In addition, furthermore, moreover, also, and, besides, likewise, further
2) Illustrate:	To illustrate, specifically, in particular, for instance, e.g., for example, indeed
3) Compare:	Similarly, likewise, equally, also, correspondingly, just as
4) Contrast:	Yet, nevertheless, nonetheless, but, however, although, on the other hand, otherwise, on the contrary, in contrast
5) Explain:	In other words, to explain, to clarify, i.e., that is, put simply
6) Conclude:	In conclusion, to conclude, finally, lastly
7) Cause:	Because, since, as a result, due to, attributable to
8) Effect:	Therefore, consequently, so, accordingly, thus, hence, as a result, for that reason
9) Summarize:	To summarize, in short, in summary, finally

10. Source Referencing

Source references should cover when, what, and how. Reference items only when the source matters. For example, if multiple sources have the same information, and that information is common knowledge, there is no need to reference.

Direct quotes should be placed in quotation marks, and cited in the footnotes. The footnotes are also a good place to expand on information given in the document that is not in quotations but could use more detail.

D. CONCLUSION

Writing clearly and concisely takes time, but will lead to a stronger report. You, your client and others will be happier with a short report that covers all pertinent information clearly, than with a long report that includes irrelevant information, unsupported assertions, and confusing explanations.

The time you devote to writing a report clearly and concisely will minimize the time the reader needs to spend to understand the report. In most cases, a well-written report is worth the extra effort.

When the Whole is Greater than the Sum of its Parts

6

An Analysis of Trends in the Application and Quantum of Minority Discounts in Canadian Court Judgments, 1986-2015

by Prem M. Lobo[1] and Stephanie Dexter

Prepared for the 2016 Ian R. Campbell Research Initiative of The Canadian Institute of Chartered Business Valuators

"Every time you go away you take a piece of me with you"
Paul Young, Every Time You Go Away (1985)

"I want to be the minority I don't need your authority"
Green Day, Minority (2000)

"There's such a difference between us and a million miles"
Adele, Hello (2015)

1.0 Introduction

The term "minority discount" in business valuations refers to a reduction of the pro-rata en bloc (i.e. 100%) value of a business' equity to reflect that a less-than-controlling equity interest has a comparative lack of ability to direct business operations. The quantum of a minority discount is a function of various factors including the size of the shareholding in question and the operational context of a business.

Minority discounts are a quintessential topic in the canon of valuation literature. With respect to the theory behind minority discounts, virtually every valuation text book and course addresses, in some fashion, if and when a minority discount may be appropriate when valuing a less-than-controlling interest in a business, and the qualitative factors that should be considered to arrive at the appropriate quantum of discount.

With respect to **empirical data** on the quantum of minority discounts, most such data is US-focused and is derived from premiums paid to acquire controlling interests in public market merger and acquisition transactions. That is, most such data is derived from publicly traded companies and comparatively "larger" companies.

There is, unfortunately, no similar empirically derived Canadian data on the quantum of minority discounts which focuses on the shares of private companies and comparatively "smaller" companies.

1 This paper is dedicated to Tami, Tricia and Tyler, who prove every day that the whole is indeed greater than the sum of its parts.

The purpose of this research paper is to address, to some degree, this dearth of relevant Canadian-based data. Specifically, this research paper analyzes Canadian legal judgments over the 30-year period from 1986 to 2015 in order to summarize the quantum of minority discounts over time, to identify any trends in the application and quantum of minority discounts over this period, and to understand how courts have interpreted and applied the concept of minority discounts.

Part I of this paper sets out the research questions, methodology and summary of findings. **Part II** sets out a brief overview of the valuation literature and theory with respect to minority discounts. **Part III** sets out details of the empirical analysis and findings.

PART I: RESEARCH QUESTIONS, METHODOLOGY, SUMMARY OF FINDINGS

2.0 Research Questions & Relevance

This research paper analyzes Canadian legal judgments for the overall period 1986 to 2015, and for each of the ten-year blocks 1986-1995, 1996-2005 and 2006-2015 respectively, in order to:

1) Summarize, from a specific analysis of relevant legal judgements, the quantums of minority discounts determined by Canadian lower and appeals courts ("Courts") over time for specific sizes of business interests, and the factors considered by the Courts in arriving at such quantums.
2) Identify if there have been any trends in the application and quantum of minority discounts over time. In particular, have minority discounts for specific sizes of business interests been increasing or decreasing over time?
3) Summarize, in an overall manner, how courts have understood and applied the concept of minority discounts. For instance, what is the current "state of the art" with respect to Canadian case law on minority discounts? In which contexts do Courts apply discounts for minority business interests and in which contexts do they not? What overall criteria do Courts consider in deciding on a particular quantum of discount?
4) Identify if there are any opportunities for the valuation community to better educate the legal community and the court with respect to minority discounts.

2.1 Relevance

Research findings in respect of the above-noted areas of inquiry will be useful for Canadian Chartered Business Valuators ("CBVs") who, during the course of their practice, may need to determine the appropriate quantum of minority discount for a less-than-controlling business interest. Moreover, an appreciation of any trends in the quantum of discounts applied by the Courts will provide for a more holistic appreciation of the context in which minority discounts are determined, and, hopefully, a more thoughtfully considered determination of the quantum of minority discounts by CBVs. In addition, the identification of opportunities to educate the legal community and judiciary with respect to minority discounts will hopefully enhance the robustness of legal decision making and adjudication in this area.

3.0 Research Methodology

In order to address the above-noted research questions, Canadian case law for the period 1986 to 2015 was analyzed to identify legal judgments dealing with minority discounts. Specifically:

1) A key word search using different permutations of the words "minority discount" was run against the legal judgments archived online at the Canadian Legal Information Institute ("CanLII") website.This resulted in the identification of **204** legal judgments over this time period which had some mention of the term.
2) Each of these judgments was then reviewed in order to exclude those legal judgments where minority discounts were only mentioned peripherally or where the legal judgments did not address issues associated with the application and quantum of minority discounts in a substantive manner. **122** legal judgments were identified for detailed analysis in this manner (the "relevant judgments"). These represented **7,023** pages of text.
3) The relevant judgments were analyzed in detail to identify the type of case (matrimonial, commercial litigation etc.), the description of the business interest being valued, the size of the business interest being valued, whether a minority discount was deemed relevant by the judge in question, the quantum of such minority discount and the factors considered by the judge in arriving at the quantum. Some judgments dealt with the valuation of multiple minority interests, and therefore provided additional data points. These details were summarized into schedules. Overall, the **122** relevant legal judgments provided **133** data points (the "relevant data points").
4) Some of the relevant judgments dealt with situations of alleged shareholder oppression. Where oppression was proven, the judge usually did not apply a minority discount to value the respective minority interests. While these shareholder oppression cases did not provide conclusive data with respect to the quantum of minority discounts, the judgments in question still provided useful information. For example, various such judgments set out the possible minority discounts that would have applied if a finding of oppression had not been proven and the criteria for doing so, insights into the judge's overall acceptance of the concept of minority discounts and the underlying case law upon which such acceptance was founded, criteria for proving or disproving oppression, and the criteria (i.e. exceptions) that would allow for a minority discount to be applied even in a situation of shareholder oppression. In short, oppression cases were helpful, were analyzed, and were summarized.
5) Where judgments did conclude on the quantum of minority discounts, the summarized data was then input into various matrices and charts, and observations were formulated as set out further herein.

Based on the nature of the relevant cases identified, legal judgments were categorized as matrimonial, commercial litigation (primarily shareholder and post-purchase price disputes), other litigation cases (including income tax and insolvency matters) and oppression cases (including minority oppression and shareholder dissent matters).

A 30-year period was chosen in order to focus on more recent (and, therefore, more relevant judgments) and provide a long-enough time period from which to identify a sufficient number of relevant judgments, while limiting the total number of judgments to a number that was manageable for analysis.

In a few instances, the judgment of the court of first instance was subsequently appealed, and the appeal dealt with minority discounts. As we were interested in the rationale and thought process of both the initial court and appeal court, we have considered, included and summarized data with respect to both the initial judgment and the subsequent appeal.

The number and types of relevant data points that were analyzed were as follows:

Table 1

NUMBER AND TYPE OF RELEVANT DATA POINTS					
	Matrimonial Cases	Commercial Litigation Cases	Oppression Cases	Other Litigation Cases	Total Relevant Data Points
	a	b	c	d	a +b=c+d
1986 to 1995	8	2	10	1	21
1996 to 2005	15	14	25	1	54
2006 to 2015	25	14	16	3	58
Total	**48**	**29**	**51**	**5**	**133**

3.1 Caveats

The research methodology set out above has several inherent limitations.

Although every attempt was made, through word searches, to identify relevant judgments, this is not a perfect exercise, and there is no guarantee that every relevant judgment was identified. Moreover, we referred to one legal database, CanLII. Other legal databases exist, and, as such, may have provided additional/different relevant judgments in response to our word searches.

Some judgments were rather voluminous and discussed a number of complex legal and factual issues in addition to minority discounts. While a good faith attempt was made to accurately summarize the salient data points as they related to minority discounts (as detailed below), there is no guarantee that every nuance was perfectly captured.

The probative value of the judgments themselves varied. Some judgments were shorter while others were longer, and some judgments discussed minority discounts in more detail while others in less detail. The data, in short, varied in consistency.

Finally, this research focuses on legal judgments. While the results of the research, in the author's view, are relevant and useful, this research does not replace the need for a broader study of minority discounts using Canadian public or private market merger and acquisition transactions or other sources.

4.0 Scope Of Review

The documents and information reviewed and relied upon in preparing this paper are set out in Appendix A.

5.0 SUMMARY OF SIGNIFICANT FINDINGS

Pursuant to the research methodology, scope of review, caveats and limitations as set out herein, significant research findings were as follows:

1) With respect to the average size of minority discounts between 1986 and 2015, matrimonial and commercial cases provided numerous relevant data points for analysis, while oppression and other litigation cases provided fewer. When all cases were considered as a whole, out of the data points

analyzed, the average size of minority interest valued was 27%, and the corresponding average size of minority discount percentage applied was 24% as set out in Table 2a below.

The average size of minority discount applied in matrimonial cases was lower than in commercial litigation cases. Overall, in many matrimonial situations, the companies being valued were closely held family companies or companies with a two or so owners who had worked together for many years as compared to commercial litigation contexts which tended not to be closely held family companies, and in which a larger number of shareholders were involved.

Table 2a

SIZE OF MINORITY DISCOUNT OVER TIME - ALL CASES					
	Total Relevant Data Points	Minority Discount Not Applied	Minority Discount Applied	Average Size of Minority Interest	Average Size of Minority Discount
	a = b + c	b	c	Subset of c	Subset of c
1986 to 1995	21	12	9	20%	33%
1996 to 2005	54	46	8	41%	20%
2006 to 2015	58	24	34	29%	20%
Total	**133**	**82**	**51**	**27%**	**24%**

2) With respect to the size of minority discounts in relation to the size of business interests, between 1986 and 2015, the sizes of minority discounts did not increase as the sizes of business interests decreased.

A review of the comments made by judges in the relevant cases suggests that while the size of a particular business interest does influence the quantum of minority discount, there are various other contextual factors that are also considered.

A summary of the average size of minority discount for different sizes of business interests between 1986 and 2015, without segregation by type of case or decade, is as follows:

Table 2b

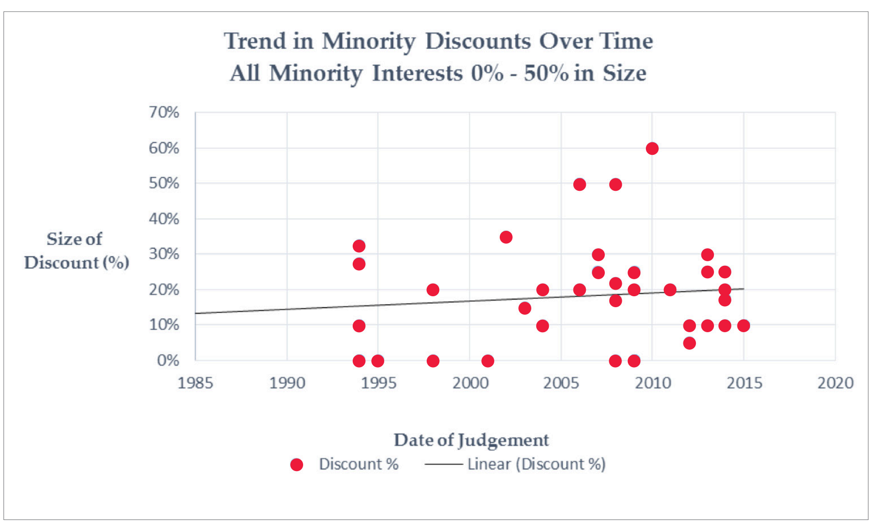
ALL YEARS, ALL TYPES OF CASES			
	Total Relevant Data Points	Minority Discount Applied	Average Size of Minority Discount
Size of Interest			
0-10%	13	4	20%
11-20%	19	7	18%
21-30%	32	18	21%
31-40%	16	9	25%
41-50%	36	13	9%
50% +	2	0	n/a
Various	3	0	n/a
Not specified	12	0	n/a
Total	**133**	**51**	**19%**

3) With respect to the trend in the quantum of minority discounts over time, the trend line for all size categories demonstrates a gradual increasing trend over time.

   Individual relevant judgments suggest that some part of this apparent increase is certainly due to the specific contextual facts of each case.

   A summary of the average size of minority discount for different sizes of business interests between 1986 and 2015, without segregation by type of case or decade, is as follows:

Table 2c



4) Overall, during the period 1986 to 2015, Canadian courts have accepted the concept of minority discounts and have applied these in circumstances where they have deemed these relevant.

   It is interesting to note that, based on fact circumstances, judges may make exceptions and apply minority discounts even in oppression cases, particularly when the plaintiff/applicant's own "misconduct" led to their exclusion from the company in question.

5) Many court judgments aggregate minority and marketability discounts together. There is an opportunity for the valuation community to better educate the legal community and the court with respect to the differences between minority discounts and marketability discounts, particularly where marketability discounts should be separate and apart from minority discounts.

PART II: LITERATURE AND THEORY

6.0 Minority Discounts – The Literature And Theory

The primary purpose of this paper is to carry out empirical research with respect to Canadian judgments for the period 1986 to 2015 as described above. Therefore, the paper does not delve into a detailed discussion of theory as set out in valuation literature. As such, the below represents a **brief** overview of the theory, to establish context.

6.1 Minority Shareholders and Minority Discounts

A minority interest is defined as an ownership interest that is less than 50% of the voting interest in a business enterprise.[2] Relative to a controlling shareholder, among other things, a minority shareholder cannot usually (i.e. unilaterally):

1) Control the operations and strategic direction of a business;
2) Sell, liquidate, dissolve or recapitalize the business;
3) Declare dividends;
4) Change the articles of incorporation or by laws;
5) Hire or fire management and establish management compensation; and,
6) Have the business purchase or divest assets.

A minority shareholder is not generally able to control his or her own destiny.[3] Given the lack of control, an arm's length purchaser will usually require a reduction to the pro-rata en bloc value of a company's equity in order to purchase a minority interest.

The size of a minority discount generally varies with the ability of minority shareholders to be able to defend against majority oppression or exert influence on the company and with the extent to which minority shareholders are economically disadvantaged.[4]

2 Practice Bulletin No. 2: International Glossary of Business Valuation Terms. Canadian Institute of Chartered Business Valuators, 2001.
3 Control Premiums, Minority Discounts and Marketability Discounts. Philip Saunders. 2006. Pg. 3.
4 Control Premiums, Minority Discounts and Marketability Discounts. Philip Saunders. 2006. Pg. 3.

The size of a minority discount may be impacted by one or more of the following, among others:

1) The size of the minority shareholding, and the number and relative sizes of the other shareholdings in a company;
2) The existence of a shareholders' agreement;
3) The relationship of shareholders with each other;
4) Whether group or family control exists;
5) The ability of a minority shareholder to influence management policy;
6) Dividend history of the company; and,
7) The "nuisance ability" of the minority shareholding to block, alter or delay corporate actions initiated by the controlling shareholder.

6.2 Existing Data on the Quantum of Minority Discounts

Most data available to quantify minority discounts is US-based and is derived from "the premiums for control" paid to acquire controlling interests in public market merger and acquisition transactions. Publicly traded shares tend to be minority interests and, therefore, are inherently priced as such. Control premiums are observed in the public securities markets with regularity as publicly traded companies are acquired by or merge with other (generally public) companies.[5] Historical studies have suggested that when takeovers of companies whose shares are publicly traded occur, average takeover prices are often in the order of 30% greater than the trading prices prior to a takeover announcement (although the range of premiums varies significantly).[6] The percentage difference between the takeover price and the previous market trading price may be viewed as a proxy for minority discounts.[7] That is, the quantum of a minority discount is the inverse of the "premium for control". [8] [9]

For example, if an average control premium of 40% is observed, then the implied minority discount is [1 – 1 / [1 + 40%]], which is 28.6%.

The Factset Mergerstat/BVR Control Premium Study ("the Mergerstat Study"), a database/publication which is updated quarterly, is widely regarded as one of the most comprehensive sources of empirical data with respect to control premiums.[10] The Mergerstat Study captures transactions whereby 50.01 percent or more of a company was acquired, and where the target company was publicly traded.[11] Acquisition data and the calculated control premiums are provided for each transaction included in the data set, and are summarized by industry. For example, for the 12-months ended December 31, 2014, the median control premium for all transactions was 27.2%, and for the 12-months ended December 31, 2015, the median control premium for all transactions was 31.8%.[12] These imply minority discount percentages of approximately 21.4% for 2014 and 24.1% for 2015.

5 A Brief Review of Control Premiums and Minority Interest Discounts. Z. Christopher Mercer. Pg. 368.
6 The Valuation of Business Interests. Ian R. Campbell and Howard E. Johnson. Canadian Institute of Chartered Accountants. 2001. Pg. 488.
7 The Lawyer's Business Valuation Handbook. Shannon Pratt. American Bar Association. Pg. 201.
8 See for example, A Brief Review of Control Premiums and Minority Interest Discounts. Z. Christopher Mercer. Pg. 368; Business Valuation: A Primer for the Legal Profession. Jeffrey M. Risius. American Bar Association. 2007. Pg. 155; and, The Value of Control: Control Premiums, Minority Interest Discounts, and the Fair Market Value Standard. Kevin Kreitzman. April 15, 2008. Pg. 3.
9 The minority discount is usually calculated as follows:
Minority Discount Percentage = [1 – 1 / [1 + Control Premium Percentage]].
10 For example, see Business Valuation Discounts and Premiums Second Edition, Chapter 3. Shannon Pratt. John Wiley & Sons. 2009. Pg. 41.
11 Factset Mergerstat/BVR Control Premium Study, 3rd Quarter 2016. About the Control Premium Study.
12 Factset Mergerstat/BVR Control Premium Study, 3rd Quarter 2016. Page 3.

Other sources of empirical data exist with respect to historical control premiums and implied minority discounts. However, given that the empirical findings of such studies are not the primary focus of this paper, they will not be further discussed henceforth.

Overall, the empirical data on control premiums and the calculations of minority discounts derived from such sources is primarily US-focused and tends to focus on larger, publicly traded companies. Moreover, the data thus obtained has inherent challenges such as:[13]

1) Where the shares of the acquired public company were actively traded with widely disseminated corporate information prior to the bid, the control premium may relate to purchaser perceived synergies, not exclusively to a premium for control.
2) It is not always the case that the daily trading prices of publicly traded shares incorporate a minority discount, and are freely traded. Where shares are not widely traded, the premium may reflect an elimination of illiquidity. Moreover, sometimes, news of an acquisition may have already been incorporated into share prices even before an official announcement.
3) Takeover premiums reflect completed transactions. The data does not reflect transactions that were considered but not pursued.

Notwithstanding the existence of the above data, there is a considerable degree of professional judgment that is required when determining the quantum of minority discounts, depending on the context of each particular situation.[14][15]

Moreover, there is no Canadian empirical data on the quantum of minority discounts which focuses on the shares of private companies and comparatively smaller companies.

6.3 Minority Discounts and Marketability Discounts

Marketability discounts relate to the inability of a shareholder to deliver to a purchaser an investment that is immediately liquid. A marketability discount relates to an amount or percentage deducted from the value of an ownership interest to reflect the relative absence of marketability.[16]

Although the concepts of a minority discount and a marketability discount are distinct, the line between them is blurred and the factors giving rise to each are frequently common to both.[17]

The focus of this paper is on minority discounts. The relevant judgments were specifically identified because they deal with minority discounts. In some cases, where the judgments separately identify marketability discounts, these have been identified and noted.

6.4 FAIR MARKET VALUE AND FAIR VALUE

In a valuation, the term fair market value refers to the price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arms-length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts.[18]

13 The Valuation of Business Interests. Ian R. Campbell and Howard E. Johnson. Canadian Institute of Chartered Accountants. 2001. Pg. 488-489.
14 The Lawyer's Business Valuation Handbook. Shannon Pratt. American Bar Association. Pg. 201
15 The Valuation of Business Interests. Ian R. Campbell and Howard E. Johnson. Canadian Institute of Chartered Accountants. 2001. Pg. 479-480.
16 Practice Bulletin No. 2: International Glossary of Business Valuation Terms. Canadian Institute of Chartered Business Valuators, 2001.
17 The Valuation of Business Interests. Ian R. Campbell and Howard E. Johnson. Canadian Institute of Chartered Accountants. 2001. Pg. 476.
18 Practice Bulletin No. 2: International Glossary of Business Valuation Terms. Canadian Institute of Chartered Business Valuators, 2001.

Meanwhile, fair value has generally been interpreted by Canadian Courts to mean fair market value without the application of a minority discount.[18] As discussed subsequently, in oppression cases Canadian Courts usually employ the concept of fair value.[19]

PART III: EMPIRICAL ANALYSIS

7.0 OVERALL SUMMARY OF LEGAL JUDGMENTS REVIEWED, 1986 TO 2015

7.1 SUMMARY

Based on the methodology outlined above, the following represents a summary of the average size of minority discount and the average size of business interest valued, by the type of case (matrimonial, commercial litigation etc.).[20]

Table 3a

I: MATRIMONIAL CASES					
	Total Relevant Data Points	Minority Discount Not Applied	Minority Discount Applied	Average Size of Minority Interest	Average Size of Minority Discount
	a = b + c	b	c	Subset of c	Subset of c
1986 to 1995	8	1	7	27%	7%
1996 to 2005	15	11	4	37%	10%
2006 to 2015	25	5	20	32%	19%
Total	**48**	**17**	**31**	**32%**	**12%**

Table 3b

II: COMMERCIAL LITIGATION CASES					
	Total Relevant Data Points	Minority Discount Not Applied	Minority Discount Applied	Average Size of Minority Interest	Average Size of Minority Discount
	a = b + c	b	c	Subset of c	Subset of c
1986 to 1995	2	1	1	13.50%	Not specified
1996 to 2005	13	9	4	45%	23%
2006 to 2015	14	6	8	21.84%	25%
Total	**29**	**16**	**13**	**27%**	**24%**

19 Canada Valuation Service, 2012 Student Edition. Carswell. 4-13.
20 Note that the "average" figures presented in the tables are for summary purposes only. The determination of a minority discount in any case requires a consideration of the specific contextual facts of that case and the exercise of prudent professional judgment.

Table 3c

III: OPPRESSION CASES					
	Total Relevant Data Points	Minority Discount Not Applied	Minority Discount Applied	Average Size of Minority Interest	Average Size of Minority Discount
	a = b + c	b	c	Subset of c	Subset of c
1986 to 1995	10	10	0	n/a	n/a
1996 to 2005	25	25	0	n/a	n/a
2006 to 2015	16	12	4	20%	31.67%
Total	**51**	**47**	**4**	**20%**	**32%**

Table 3d

IV: OTHER LITIGATION CASES					
	Total Relevant Data Points	Minority Discount Not Applied	Minority Discount Applied	Average Size of Minority Interest	Average Size of Minority Discount
	a = b + c	b	c	Subset of c	Subset of c
1986 to 1995	1	0	1	18%	33%
1996 to 2005	1	1	0	n/a	n/a
2006 to 2015	3	1	2	42%	20%
Total	**5**	**2**	**3**	**30%**	**27%**

Table 3e

V: TOTAL - ALL CASES					
	Total Relevant Data Points	Minority Discount Not Applied	Minority Discount Applied	Average Size of Minority Interest	Average Size of Minority Discount
	a = b + c	b	c	Subset of c	Subset of c
1986 to 1995	21	12	9	20%	33%
1996 to 2005	54	46	8	41%	20%
2006 to 2015	58	24	34	29%	20%
Total	**133**	**82**	**51**	**27%**	**24%**

7.2 Commentary

Matrimonial and Commercial Litigation Cases

Matrimonial cases provided the largest number of relevant data points with respect to minority discounts. Out of the 31 data points analyzed, the average size of minority interest valued was 32%, and the average size of minority discount percentage applied was 12% between 1986 and 2015.

Commercial litigation cases provided the second largest number of relevant data points. Out of the 13 data points analyzed, the average size of minority interest valued was 27%, and the average size of minority discount percentage applied was 24% between 1986 and 2015.

The average size of minority discount applied in matrimonial cases was lower than in commercial litigation cases. Overall, in many matrimonial situations, the companies being valued were closely held family companies or companies with two or so owners who had worked together for many years. Therefore, lower minority discounts were deemed appropriate (or no minority discounts in the case of some closely held family companies) relative to commercial litigation cases, which tended not to be closely held family companies, and in which a larger number of shareholders were involved.

For example, in a matrimonial case, A.A. v. Z.G.[21], one of the issues was the valuation of a 24% interest in a family-owned business, 808276 Ontario Inc. ("808"), which was involved in the real estate/construction industry. The valuator for the husband applied a 30% reduction for the minority interest 808 had in several joint real estate ventures. He applied a further 10% discount to the husband's minority shareholdings in 808. The valuator for the wife "accepted that it is a generally customary practice to discount minority interests in the public market. [She] opined that 808 was closely held and there was no evidence of any disagreement within the family members, who together owned 100% of 808, to warrant a minority discount. While the percentage interests of the shareholders are different, there was no evidence that the shares of the various family members were treated differently."[22] The judge accepted that a minority discount was not appropriate in this privately held "family" corporation.

Similarly in another matrimonial case, *Blatherwick v Blatherwick*[23] a number of minority business interests needed to be valued including shares of Seasons Capital Limited, shares of Blatherwick Holdings Inc., shares of Capitalrich Group Limited, and shares of Seasons Limited – Macao Commercial Offshore, all directly or indirectly involved in the Halloween costumes and related products business. The judge noted that the husband's valuator "applied a minority and illiquidity discount of 5% to 35% depending on the particular company. For Seasons HK she applied a discount of 27.45% to 31.80% and for Seasons Macao of 30.27% to 35.16%."[24] Meanwhile, the wife's valuator applied "a minority and illiquidity discount of 0% to 20% depending on what he considered to be the "unique factors in each corporation."[25] The judge concluded that due to the closely held nature of the various ownership interests, "a minority discount is appropriate and I accept the lower minority discounts calculated by [the wife's valuator] in his reports.[26]

Meanwhile in commercial litigation cases, interests tended not to be closely held or family owned, and other criteria were examined in arriving at a decision as to the quantum of minority discount.

21 2015 ONSC 4397.
22 2015 ONSC 4397 at Par. 234.
23 2015 ONSC 2606.
24 2015 ONSC 2606 at Par. 376.
25 2015 ONSC 2606 at Par. 377.
26 2015 ONSC 2606 at Par. 380.

For example, in *Farwell v. Integrated Management & Investments Inc.*[27], one of the issues was the valuation of a number of minority interests of a group of plaintiffs, ranging in size from 0.69% to 17.97%, or an average of 2.6%, owning interests in Ol'Grandad's Snacks Inc., distributor of potato chips. An expert testified that "a typical minority/marketability discount was in the range of 10 to 40%".[28] The judge concluded on a 25% "minority/marketability discount".[29]

In addition, in *Ishani v. Kulasingham*[30], the issue was the valuation of a partnership interest in Joint Therapy, a medical/physiotherapy services company. In arriving at a 20% to 30% minority discount, the judge cited that the lack of a partnership agreement made it hard to get money out of the business and that there was no evidence that the other two partners would bid for the remaining third partner's interest.

Oppression and Other Litigation Cases

It is interesting that minority discounts were applied in some oppression cases. Normally, in most oppression cases no minority discounts are applied.

For example, in an oppression case involving the "squeeze out" of dissenting minority shareholders, *Ford Motor Company of Canada, Ltd. v. Ontario Municipal Employees Retirement Board*[30], the judge noted that "although the jurisdiction may be broad and flexible, the section does not confer on the court an unfettered discretion to do whatever the judge feels would be fair. The determination of fair value must be anchored in the principle that gives rise to the jurisdiction. Here, where the triggering event is a squeeze out of minority shareholders, the notion of fair value involves an exercise in appraisal of the present market value of the shares but taking into account that this is a forced sale that deprives the shareholders of the opportunity to share in the fortunes of the corporation. Thus, as was conceded in this case, the fair value should not be reduced for a minority discount."[32]

Similarly, in *Brant Investments Ltd. v. KeepRite Inc.*[33] the judge noted that "it has been accepted by counsel for both parties, correctly I think, that there should be no minority discount in the determination of "fair value". To do so would be unfair to the minority. By parity of reasoning it seems to me that the majority, forced against its inclination to acquire the shares of the minority, ought not to be obliged to pay a premium for those shares. It seems to me therefore that the determination of "fair value" by a court under s. 184(3) should seek to avoid both and to give to the minority the value of its investment without either discount or premium."

However, based on fact circumstances, judges may make exceptions and apply minority discounts in oppression cases. In these cases, the judge in question saw fit to include a minority discount when valuing the shares because the plaintiff/applicant's own "misconduct" let to their exclusion from the company in question. In many of these cases, the judge cited the criteria in *Re Bird Precision Bellows Ltd.*[34], affirmed by the Court of Appeal, in which the judge held that there might be circumstances where a minority shareholder whose interests had been unfairly prejudiced by the conduct of the majority but who had nevertheless so acted as to deserve his exclusion from the company, would be entitled to relief. However, he would be not entitled to have the majority purchase the shares at their full fair value but at a minority discount.

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27 2007 ONSC 13512.
28 2007 ONSC 13512 at Par. 70.
29 2007 ONSC 13512 at Par. 71.
30 2014 ONSC 6957.
31 2006 ONCA 15.
32 2006 ONCA 15 at Par. 132.
33 1991 ONCA 2705.
34 1984 3 All E.R. 444.

For example, in *Derdall Irrigation Farms Ltd. v. Derdall*[35], the issue was the valuation of a 33.3% interest in Derdall Irrigation Farms Ltd. The court of first instance applied a minority discount of 20%. Upon appeal, the court called for a significantly deeper 60% discount, citing four factors that justified such a discount. These were:

1) Boyd, the minority shareholder was seeking to share in the increase in the value of the business assets, without having fulfilled his part of the bargain towards the company.[36]

2) Boyd's reasonable expectations when he left the company were adjudged to be "nothing more than minimal".[37]

3) Boyd left to work for his brother and ultimately to establish his own business, which was a competitor.[38]

4) Boyd delayed for many years before he brought an action for redress.[39]

Overall

Matrimonial and commercial cases provided numerous relevant data points, while oppression and other litigation cases provided fewer.

When all cases were considered as a whole, out of the 51 data points analyzed, the average size of minority interest valued was 27%, and the corresponding average size of minority discount percentage applied was 24% between 1986 and 2015 as set out in Table 3e above.

8.0 Minority Discounts By Size Of Business Interest

8.1 Summary

A further analysis was made of the minority discounts ascribed to different sizes of business interests. Business interests were segregated into size categories 0-10%, 11-20%, 21-30%, 31-40% and 41-50%. Using the relevant data points, a summary was made of the average size of minority discount for different sizes of business interests between 1986 and 2015, without segregation by type of case or decade, as follows:[40]

35 2010 SKCA 104.
36 2010 SKCA 104 at Par. 42.
37 2010 SKCA 104 at Par. 43 and 44.
38 2010 SKCA 104 at Par. 45.
39 2010 SKCA 104 at Par. 46.
40 Note that the "average" figures presented in the tables are for summary purposes only. The determination of a minority discount in any case requires a consideration of the specific contextual facts of that case and the exercise of prudent professional judgment.

Table 4

ALL YEARS, ALL TYPES OF CASES			
	Total Relevant Data Points	Minority Discount Applied	Average Size of Minority Discount
Size of Interest			
0-10%	13	4	20%
11-20%	19	7	18%
21-30%	32	18	21%
31-40%	16	9	25%
41-50%	36	13	9%
50% +	2	0	n/a
Various	3	0	n/a
Not specified	12	0	n/a
Total	**133**	**51**	**19%**

8.2 Commentary

It is interesting to note from the above that the sizes of minority discounts did not increase as the sizes of business interests decreased.

A review of the comments made by judges in the relevant cases suggests that while the size of a particular business interest does influence the quantum of minority discount, there are various other contextual factors that are also considered.

For example, in *Matthews v. Accent Lines (1988) Ltd.*[41], a 50% interest in a bus transportation company received a 20% minority discount to reflect lack of control. Counsel for the Defendant argued that a minority discount of 35% should be applied, which the judge believed was too high. The judge noted that "because Counsel for Matthews [the plaintiff] did not argue against [the application of a minority discount], and presumably Counsel for the Defendants relied on this concession, I have nevertheless, left the minority discount in the calculations."

Meanwhile, in *Grant v. Grant*[42], a 12.5% interest in C.W. Farms Limited Partnership, a farming business, received a 0% minority discount. The judge noted that "it is true that Mr. Grant owns a minority interest in C.W. Farms, but in addition to controlling 12.5% of the shares, Mr. Grant is one of three members of the management team. Mr. Grant is also the spokesman for a group of other partners, which gives him an additional element of control."[43] The judge also noted that the history of the partnership and the provisions of the partnership agreement also demonstrate that if Mr. Grant sold his partnership units, the likely buyers were the other partners. The judge noted that "taking all of these factors into account, I

41 1998 ABQB 180.
42 1994 CanLII 974.
43 1994 CanLII 974.

cannot accept that a minority discount of the magnitude suggested by Mr. B is warranted"[44] and ascribed a 0% minority discount.

In short, the specific contextual facts of each case determined the quantum of minority discount that was applied.

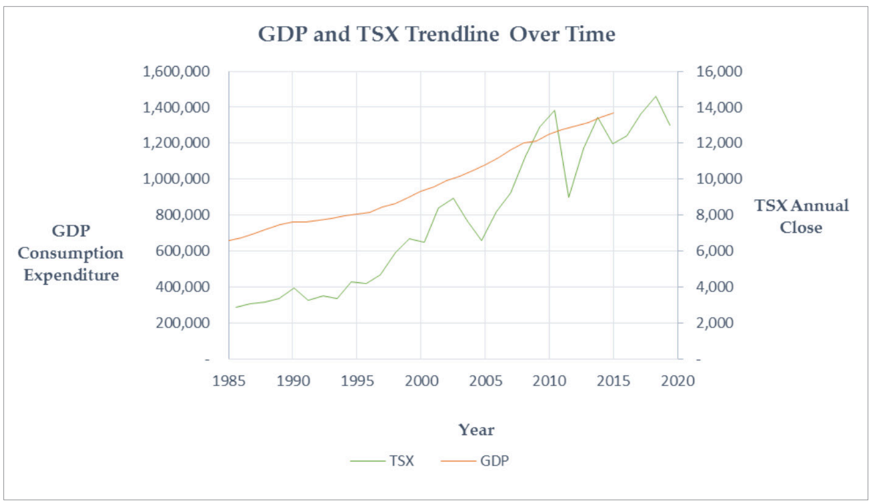
9.0 Trends In Minority Discounts 1986 To 2015

The focus of this paper now turns to trends in minority discounts over time, if any. The paper attempts to identify if minority discounts for specific sizes of business interests have demonstrated any perceptible increasing or decreasing trend over time.

9.1 Economic Context, 1986 to 2015

By way of a broad economic context, between 1986 and 2015, the S&P/TSX Composite Index (formerly the TSE 300) and the Canadian gross domestic product (as measured based on consumption expenditure) ("GDP") trended as follows:[45]

Table 5



The S&P/TSX Composite Index and the Canadian GDP both demonstrate an increasing trend over time, albeit the S&P/TSX Composite Index in rather more exciting fashion.

9.2 Trend in Minority Discounts

With the larger economic context having been examined, the question that arises is whether minority discounts demonstrated any discernable trend during the time period 1986 to 2015.

44 1994 CanLII 974.
45 For context only. We do not suggest that any of the trends in Canadian GDP, the S&P/TSX Composite Index or the overall economy may have impacted the quantum of minority discounts at particular points in time.

Using the relevant data points, a summary of minority discounts over time based on size categories 0-10%, 11-20%, 21-30%, 31-40%, 41-50% and all categories 0-50% is set out in the charts below. A trend line based on the available relevant data points has been plotted on each chart.

Table 6a

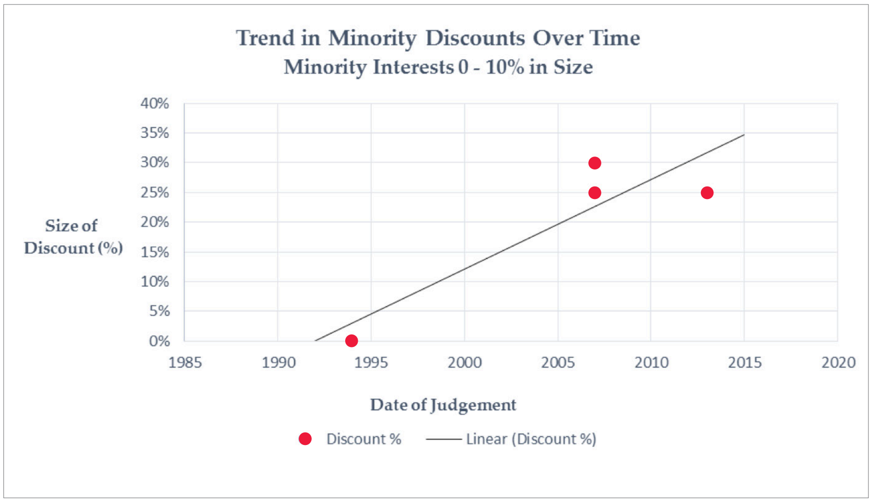


Table 6b

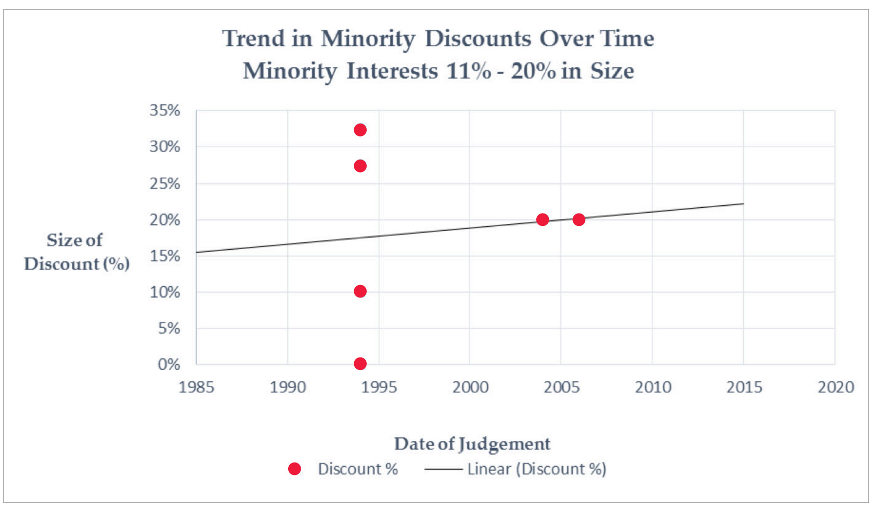


Table 6c

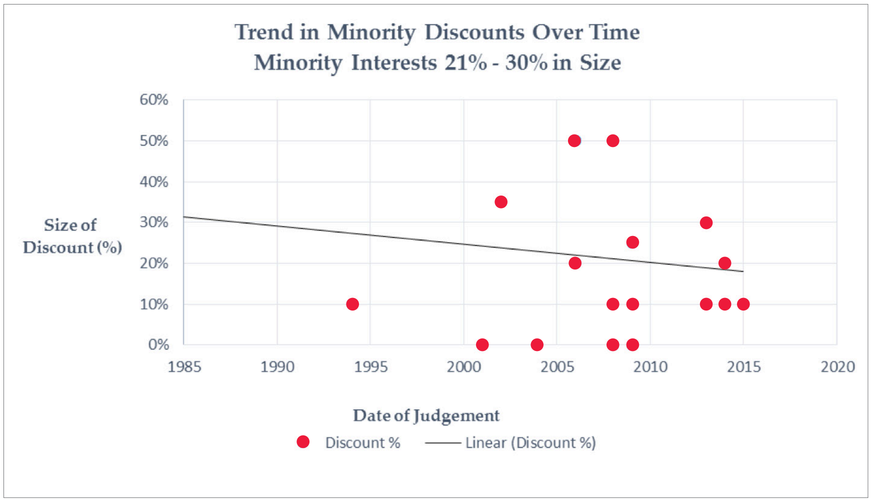


Table 6d

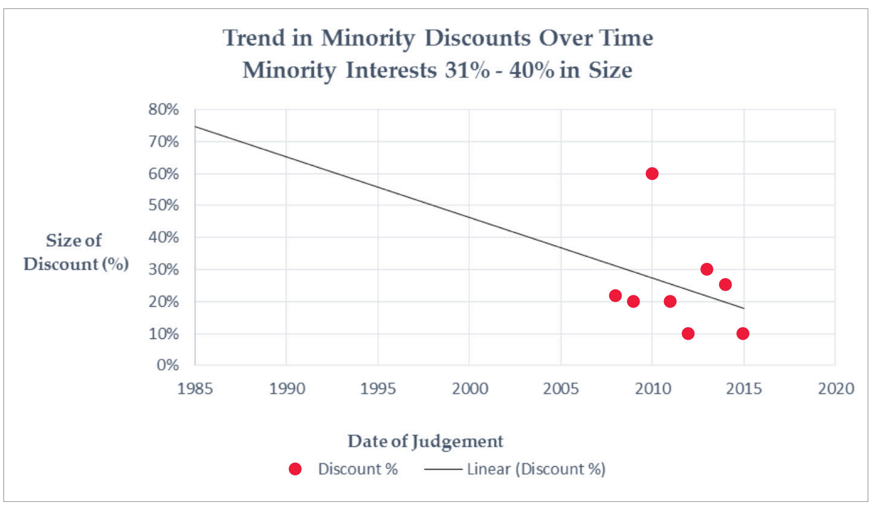


Table 6e

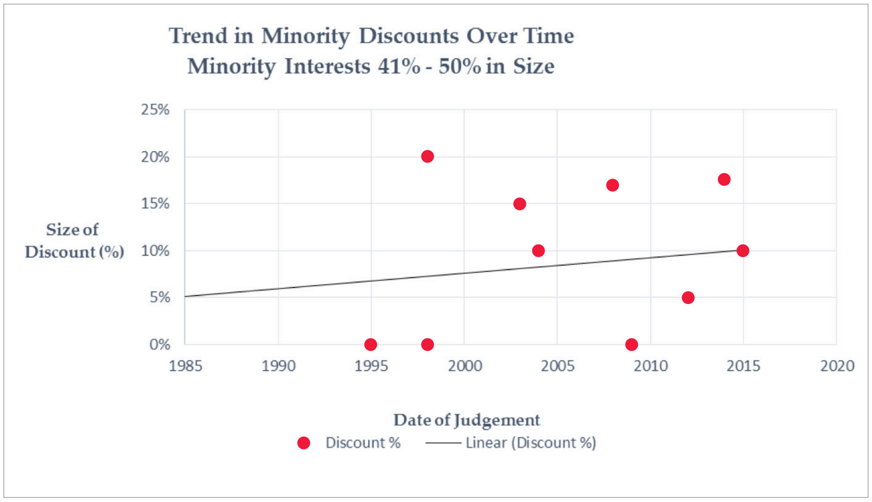
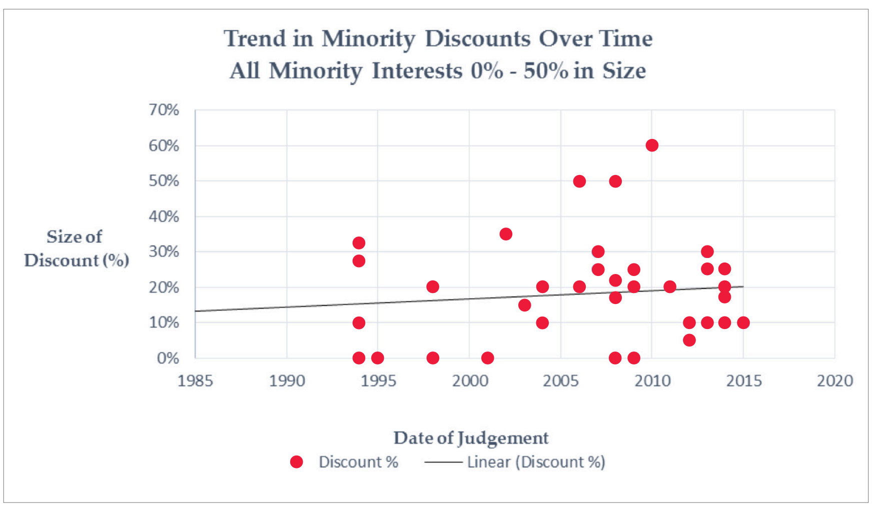


Table 6f



9.3 Commentary

0-10% and 11-20% Size Categories

The trend lines for the 0-10% and 11-20% size categories demonstrate an increasing trend over time. However, given the relatively more limited number of data points, it is difficult to establish a firm trend for these size categories.

21-30% and 31-40% Size Categories

The trend lines for the 21-30% and 31-40% size categories demonstrate a decreasing trend over time. While the data points for the 21-30% size category are spread over a larger time period, the data points for the 31-40% size category are concentrated in the 2006 to 2015 time period, making it relatively more difficult to infer a trend over a longer time period for this latter size category.

41-50% Size Category

The trend line for the 41-50% size category demonstrates an increasing trend over time.

All Size Categories

Given the rather differing trends in minority discounts noted for the various size categories, perhaps it is helpful to look at the overall trend in minority discounts for all size categories over time.

Overall, the trend line for all size categories demonstrates a gradual increasing trend over time.

A review of the individual relevant judgments suggests that some part of this apparent increase is certainly due to the specific contextual facts of each case. However, the data nevertheless does demonstrate that there is an overall increasing trend in the quantum of minority discounts over time.

10.0 How Canadian Courts Have Understood And Applied The Concept Of Minority Discounts Over Time

All things considered, during the period 1986 to 2015, Canadian courts have accepted the concept of minority discounts and have applied these in circumstances where they have deemed relevant.

Matrimonial, Commercial Litigation and Other Litigation (Other than Oppression) Contexts

In matrimonial, commercial litigation and other litigation contexts, courts have referred to the specific contextual facts of each case to establish the quantum of applicable minority discount.

The case of *Blatherwick v Blatherwick*[46] summarizes the overall approach to specific contextual facts, wherein the court indicated that the setting of a minority discount "is a very subjective area relying upon the valuators understanding of the nature of the business, the industry and other specific factors associated with the particular shareholder's circumstances and then, exercising judgment in a variety

46 2015 ONSC 2606.

of areas to build up or calculate a minority discount."[47] Similarly, in *A.A. v Z.G.*[48], the court noted that "Discounting for a minority shareholder interest is a subjective exercise".[49]

Various judgments made reference to various contextual factors such as whether:

1) The minority interest was in a closely held family company and whether the family members had worked together for many years, and were likely to continue to do so in the future.[50]
2) The minority shareholder had the largest shareholding relative to other shareholders in in a particular business.[51]
3) Any potential buyer of a minority interest would need the assistance of the minority shareholder to transition customers which he or she had dealt with directly for many years [52]
4) A minority shareholder was part of a group of shareholders who had historically acted in concert to their mutual benefit, and would likely continue to do so, including eventually selling their collective interests together.[53]
5) A minority shareholder was in a leadership role in a company.[54]
6) Whether a potential buyer would be available and whether a sale was imminent.[55]
7) The financial position of a particular company was robust so as to facilitate a purchase.[56]
8) There would have been an "inside" purchaser (i.e. another shareholder of the company) of the minority interest.[57]
9) Relative to a controlling or 50% interest, a minority interest would have an ability to deadlock corporate decisions.[58]
10) A shareholders' agreement exists to offer some protection to a minority shareholder,[59] and the specific terms of such shareholders' agreement.
11) Prior purchases of minority interests were acquired at a premium as opposed to a discount.[60]
12) There was historically evidence of a distribution of any excess cash to its shareholders.[61]
13) Any prospective purchaser of a minority interest would achieve control, and consequently could compel a company to make any distributions of earnings.[62]
14) There were any special purchasers for the minority interest in question.[63]
15) The size of a specific minority holding relative to other shareholder holdings.[64]
16) The actual prices that were paid to acquire minority shareholding interests between shareholders.[65]

47 2015 ONSC 2606 at Par. 375.
48 2015 ONSC 4397
49 2015 ONSC 4397 at Par. 236.
50 A.A. v Z.G., 2015 ONSC 4397 at Par. 234.
51 Blatherwick v Blatherwick, 2015 ONSC 2606 at Par. 379.
52 Blatherwick v Blatherwick, 2015 ONSC 2606 at Par. 379.
53 JAC v VRC, 2015 YKSC 15 at Par. 167 and 168.
54 JAC v VRC, 2015 YKSC 15 at Par. 167, 168 and 198.
55 Reid v. Reid, 2014 BCSC 1691 at Par. 195.
56 Reid v. Reid, 2014 BCSC 1691 at Par. 195.
57 Linn v Frank, 2014 SKCA 87 at Par. 44, 48 and 49.
58 Boreta Estate v McRory, 2014 ABQB 498 at Par. 102.
59 Brown v. Silvera, 2009 ABQB 523 at Par. 548.
60 McKinney v. McKinney, 2008 BCSC 709 at Par. 99.
61 McKinney v. McKinney, 2008 BCSC 709 at Par. 99.
63 McKinney v. McKinney, 2008 BCSC 709 at Par. 99.
64 Rendle v. Stanhope Dairy Farm Ltd. et al., 2003 BCSC 1894 at Par. 75.
65 Black v. Black (H.C.J.), 1988 ON SC 4756.

What is interesting from the various relevant judgments is that while Canadian courts are generally accepting of the concept of minority discounts, many times courts do not distinguish between minority discounts and marketability discounts, and instead tend to aggregate minority and marketability discounts together.

For example in *Farwell v. Integrated Management & Investments Inc*. the court did not distinguish between a minority and marketability discount.[66]

In many cases, minority interests are inherently less marketable as well. However, the valuation literature suggests that minority and marketability discounts are generally separate and distinct concepts.[67] While in some minority valuation contexts both may apply, in others it may be necessary to separate the two.

This does suggest an opportunity for the valuation community to better educate the legal community and the court with respect to the differences between minority discounts and marketability discounts, particularly where marketability discounts should be separate and apart from minority discounts.

Oppression Contexts

In oppression contexts, Canadian courts generally do not apply a minority discount. In such circumstances, courts cite *Diligenti v. RWMD Operations Kelowna Ltd*.[68]

For instance, in *1043325 Ontario Ltd. v. CSA Building Sciences Western Ltd*.,[69] the court noted that "In determining the price to be paid for the shares in circumstances where oppression or unfairly prejudicial conduct has been found, the question is not necessarily what is the market value of the shares but rather what is a fair price or value in the circumstances".[70] The court noted that "with regard to whether a minority discount should be applied to the valuation, the authorities I was referred to tend not to take a minority discount into account in oppression proceedings. That seems to accord with the fact that the majority shareholder or the company is acquiring the shares, and as such the question is not what the shares would have fetched in the marketplace on a sale to a third party who would receive only a minority stake in the company."[71]

However, it is interesting to note that, based on fact circumstances, judges may make exceptions and apply minority discounts even in oppression cases, particularly when the plaintiff/applicant's own "misconduct" let to their exclusion from the company in question.

In many of these cases, the judge cited the criteria in *Re Bird Precision Bellows Ltd*.[72], in which the judge held that there might be circumstances where a minority shareholder whose interests had been unfairly prejudiced by the conduct of the majority but who had nevertheless so acted as to deserve his exclusion from the company, would be entitled to relief. However, he would be not entitled to have the majority purchase the shares at their full fair value but at a minority discount.

66 2007 ON SC 13512 at Par. 70 and 71.
67 The Lawyers Business Valuation Handbook. Shannon Pratt. 2000. Pg. 197.
68 1977 B.C.J. No. 1331 (S.C.).
69 2015 BCSC 1160.
70 2015 BCSC 1160 at Par. 14.
71 2015 BCSC 1160 at Par. 18.

As previously noted, in the oppression case *Derdall Irrigation Farms Ltd. v. Derdall*[73], the court called for a 60% minority discount for a 33.3% minority interest, citing four factors that justified such a discount, all dealing with the behavior of the minority shareholder in question.

It is also interesting to note that even in oppression contexts, it is the positon of the majority party or parties that a minority discount inevitably *should* apply, and evidence is led with respect to the quantum of discount that is appropriate.

11.0 Significant Findings And Conclusion

Pursuant to the research methodology, scope of review, caveats and limitations as set out herein, significant research findings were as follows:

1) With respect to the average size of minority discounts between 1986 and 2015, matrimonial and commercial cases provided numerous relevant data points for analysis, while oppression and other litigation cases provided fewer. When all cases were considered as a whole, out of the data points analyzed, the average size of minority interest valued was 27%, and the corresponding average size of minority discount percentage applied was 24% as set out in Table 2a below.

   The average size of minority discount applied in matrimonial cases was lower than in commercial litigation cases. Overall, in many matrimonial situations, the companies being valued were closely held family companies or companies with a two or so owners who had worked together for many years as compared to commercial litigation contexts which tended not to be closely held family companies, and in which a larger number of shareholders were involved.

Table 7a

SIZE OF MINORITY DISCOUNT OVER TIME - ALL CASES					
	Total Relevant Data Points	Minority Discount Not Applied	Minority Discount Applied	Average Size of Minority Interest	Average Size of Minority Discount
	a = b + c	b	c	Subset of c	Subset of c
1986 to 1995	21	12	9	20%	33%
1996 to 2005	54	46	8	41%	20%
2006 to 2015	58	24	34	29%	20%
Total	**133**	**82**	**51**	**27%**	**24%**

72 1984 3 All E.R. 444.
73 2010 SKCA 104.

2) With respect to the size of minority discounts in relation to the size of business interests, between 1986 and 2015, the sizes of minority discounts did not increase as the sizes of business interests decreased.

A review of the comments made by judges in the relevant cases suggests that while the size of a particular business interest does influence the quantum of minority discount, there are various other contextual factors that are also considered.

A summary of the average size of minority discount for different sizes of business interests between 1986 and 2015, without segregation by type of case or decade, is as follows:

Table 7b

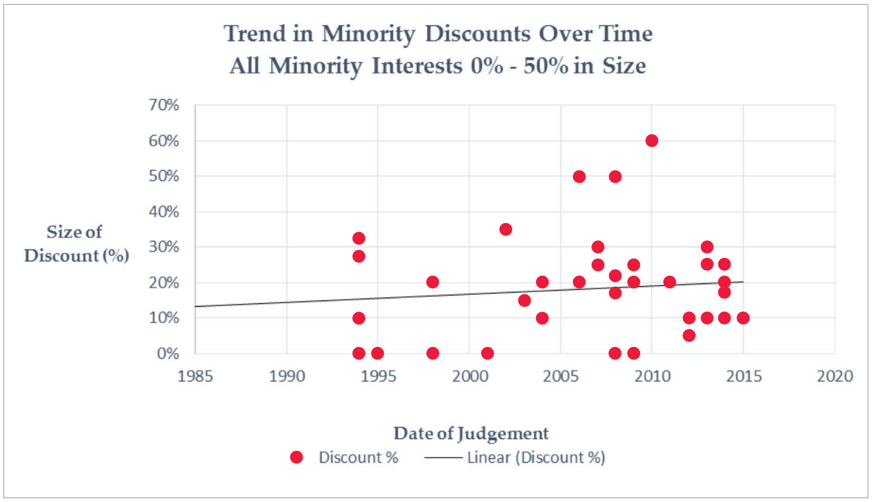
ALL YEARS, ALL TYPES OF CASES			
	Total Relevant Data Points	Minority Discount Applied	Average Size of Minority Discount
Size of Interest			
0-10%	13	4	20%
11-20%	19	7	18%
21-30%	32	18	21%
31-40%	16	9	25%
41-50%	36	13	9%
50% +	2	0	n/a
Various	3	0	n/a
Not specified	12	0	n/a
Total	**133**	**51**	**19%**

4) With respect to the trend in the quantum of minority discounts over time, the trend line for all size categories demonstrates a gradual increasing trend over time.

Individual relevant judgments suggest that some part of this apparent increase is certainly due to the specific contextual facts of each case.

A summary of the average size of minority discount for different sizes of business interests between 1986 and 2015, without segregation by type of case or decade, is as follows:

Table 7c



4) Overall, during the period 1986 to 2015, Canadian courts have accepted the concept of minority discounts and have applied these in circumstances where they have deemed these relevant.

   It is interesting to note that, based on fact circumstances, judges may make exceptions and apply minority discounts even in oppression cases, particularly when the plaintiff/applicant's own "misconduct" let to their exclusion from the company in question.

5) Many court judgments aggregate minority and marketability discounts together. There certainly is an opportunity for the valuation community to better educate the legal community and the court with respect to the differences between minority discounts and marketability discounts, particularly where marketability discounts should be separate and apart from minority discounts.

12.0 Conclusion

The purpose of this research paper was to address, to some degree, the dearth of relevant Canadian-based data on minority discounts. It is the intention of the paper that the information obtained from the empirical analysis will be found relevant, useful, and contribute in some fashion to filling in the lack of Canadian data in this important area of valuations.

This paper is by no means the "be all and end all" of Canadian empirical research on minority discounts. The focus was on legal judgments as one source of empirical data. There are certainly other areas to obtain additional Canadian empirical data, and this paper does not replace the need for a broader study of minority discounts using Canadian public or private market merger and acquisition transactions or other such sources.

The great Detroit rock artist and philosopher, Kid Rock, once said "you get what you put in and people get what they deserve".[74] Minority shareholders, too, ought to "get what they deserve"in a valuation of their shares. Following on from the findings of this research paper, valuators can better accomplish this by ensuring that minority discounts are reflective of the specific contextual facts of each case.

WHEN THE WHOLE IS GREATER THAN THE SUM OF ITS PARTS - SCOPE OF REVIEW

In preparing this research paper we have reviewed and relied upon the following information:

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74 Only God Knows Why. 1998 Lava/Atlantic Records at Stanza 25.

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