

Managing and Planning for Retiring Founders: Transactional and Employment Implications

Presented to CBV Institute

Alex Kagan

Partner
Workplace Law Group
Aird & Berlis

Jackson Phillips

Partner
Capital Markets Group
Aird & Berlis

June 12, 2025

AIRD BERLIS

This presentation may contain general comments on legal issues of concern to organizations and individuals. These comments are not intended to be, nor should they be construed as, legal advice. Please consult a legal professional on the particular issues that concern you.



Agenda


- Introduction
- Asset vs. Share Purchase
- The Founder's Post-Transaction Role-Restrictive Covenants: Non-Solicit vs. Non-Compete
- Retention Incentives: Change of Control, Stock Options; RSUs
- Structuring the Deal: Asset Purchase vs. Share Purchase
- Structuring the Deal: Form of Consideration
- Earn-Out Considerations
- Indemnities: Market Standards
- Representation & Warranty Insurance

Polling Question # 1 - Prior to a business sale, how much time do founders invest in planning?

- a. Less than six (6) months
- b. Approximately a year
- c. 18 months
- d. More than 18 months

Business Owners and Retirement

- Baby boomers – who were born between 1946 and 1965 and were between the ages of 56 and 75 in 2021, represent 24.9% of the Canadian population ([Statistic Canada – 2021 Census](#))
 - By 2031, the youngest Baby Boomers will reach the age of 65
 - The median age of self-employed individuals in Canada is 66.7 ([Statistics Canada](#))
- In 2022, the Canadian Federation of Independent Business ("**CFIB**") conducted an updated study called "[Succession Tsunami: Preparing for a decade of small business transitions in Canada](#)" – the study found that:
 - 76% of Canada's business owners plan to exit their business in the next decade
 - Only one in 10 business owners (9%) have a formal business succession plan



The Business Sale – Share Purchase vs. Asset Purchase

Wrongful Dismissal 101

- Three sources of financial compensation in a without cause dismissal:
 1. Employment Standards Legislation
 2. Common Law Reasonable Notice
 3. Contract ("**EA**" or "**K**")

Enforceable Employment Agreements

- To be enforceable, a contract must have:
 1. Offer
 2. Acceptance
 3. **Fresh Consideration**

Employment Standards Legislation – Ontario

- In Ontario, the *Employment Standards Act, 2000* (the “**ESA**”) governs all provincially regulated employers.
- Ontario is the only province which provides both:
 - a) **termination notice (or pay in lieu)** – approx. one (1) week per year of service – maximum eight (8) weeks; and
 - b) **statutory severance** – one (1) week per year of service to a maximum of twenty-six (26) weeks.

*ESA severance pay is only triggered if the employee also has (a) five (5) or more years of service and (b)(i) the business has an annual payroll of \$2.5 million or (ii) there is a permanent closure which results in fifty (50) or more dismissals in a six (6)-month period.

Wrongful Dismissal 101 – The Common Law

- Common law reasonable notice – the most important *implied contractual* term in employment law
- The *Bardal Factors* in assessing the reasonable notice period:
 - i. Age
 - ii. Length of Service
 - iii. Position
 - iv. Availability of Similar Employment and Extenuating Circumstances
- Performance is not a factor (absent incentive compensation)
- The one-month “rule of thumb”? The 24-month ceiling?
- What is included? *Everything!* Commissions? Incentives? Stock options? LTD coverage?

Share Purchase vs. Asset Purchase

- **Share purchase** is the simpler analysis – there is no break in employment and the Purchaser assumes all termination liabilities of the workforce.
 - The Purchaser is “adopting” the workforce – good and bad. This includes all prior service and terms of employment under employment standards and the common law.
 - The Purchaser and the Founder can agree to a new and evolved post-Transaction employment relationship. The transaction proceeds are good and valuable “**fresh consideration.**”

*Less flexibility for the general workforce and executives. New contracts offered by Purchaser will not be enforceable unless there is “fresh consideration.”

Share Purchase vs. Asset Purchase

- **Asset purchase** is more complex from an employment law perspective. There is a termination of employment at common law upon the asset transfer involving a “going concern.”
 - Any employee, including a Founder, will have their prior service recognized as a matter of law under employment standards legislation, which in Ontario is the *Employment Standards Act, 2000*.
 - Under the common law, past service does not automatically transfer to the Purchaser. However, courts will take the skills and expertise that retained employees – especially Founders – provide the Purchaser employer in determining severance obligations.

*The Purchaser can negotiate new contracts with both the Founder and each member of the workforce. For the Founder, the transaction proceeds represent “fresh consideration.” For everyone else, the post-employment itself is “**fresh consideration**,” which is NOT the case in a share purchase.

**Founders are motivated to sign a new employment agreement with the Purchaser. *What about the rest of the workforce?*

The Duty to Mitigate – “Substantially Similar Terms”

- Transaction agreements, especially in an Asset Purchaser, often expressly require the Purchaser to offer all (or just some) non-unionized employees employment on substantially similar terms.
- Why? In order to claim wrongful dismissal damages, a dismissed employee must satisfy their duty to mitigate.
- The duty to mitigate means the employee must make **reasonable efforts** to find a **comparable job**.
 - If a Vendor employee refused a job offer from the Purchaser, their claim to common law damages might be in jeopardy if the offer represented a comparable role and their refusal is deemed unreasonable.



The Founder's Post-Transaction Role

The Founder's Post-Transaction Role

- Founders have some leverage in negotiating a post-transaction employment agreement.
- Considerations?
 - Time horizon for the transition?
 - Full-time or part-time?
 - Title and responsibilities?
 - Employee vs. independent contractor vs. "consultant"
 - Incentives?
 - Golden parachute?

Polling Question # 2 - Following a business sale, how long do Purchasers want to retain the Founder?

- a. Not at all
- b. Less than six (6) months
- c. Approximately a year
- d. More than a year



Restrictive Covenants: Confidentiality, Non-Solicitation, Non-Competition

Restrictive Covenants: Employment Sphere vs. Commercial Sphere

Canadian courts will not enforce a restrictive covenant if it is an unwarranted “restraint of trade.”

- Courts will not “read down” or “blue pencil” a restrictive covenant that is deemed too broad or aggressive.
- However, the exact same provision will have a very different legal justification if it is within an employment agreement vs. a Restrictive Covenant Agreement connected to a transaction.

Restrictive Covenants: Non-Solicitation

- The non-solicitation applies globally, unlike a non-competition provision.
- Scope must still be limited to a specific time horizon and prohibited conduct.
- Legal in every jurisdiction, including Ontario.
- Less difficult to enforce than a non-competition clause. But the moving party has the burden to marshal the evidence and successful injunctions are rare.

Restrictive Covenants: Non-Competition

- Statutorily prohibited in Ontario unless it involves a business sale or applies to a “C”- Suite executive or President.
- Scope must still be limited to a specific time horizon and prohibited conduct and geographic area.
- More difficult to enforce than a non-competition clause. Again, the moving party has the burden to marshal the evidence and successful injunctions are rare.

Restrictive Covenants: Practical Advice

- Employment sphere vs. commercial sphere
- Demanding 80% vs. 100%
- Develop levels of influence so you have other than the restrictive covenant
- *"A good defence is a good offence"*



Retention Incentives: Change of Control, Stock Options; RSUs

Retention Incentives: Change of Control, Stock Options, RSUs

A key consideration is motivating the retention of key employees during the business sale and subsequent post-transaction transition period

- **Change of Control** – highly flexible and typically involves a “trigger” that provides a non-equity incentive.
- **Stock Options/RSUs** – equity-based incentive that aligns key personnel to the interests of the business.
- **Phantom Shares/Share Appreciation Rights** – a non-equity that is designed to increase in value in parallel to the pending transaction proceeds.



Structuring the Deal: Asset Purchase vs. Share Purchase

Structuring the Deal: Asset Purchase vs. Share Purchase

Share Purchase

- Acquiring the whole company, all assets and liabilities
- Potential for tax advantages (e.g., retained loss carryforwards, CCPC or QSBC tax treatment)
- Continuity of employment relationship and business operations under the same corporate name

Asset Purchase

- Acquiring specified assets and liabilities
- Possible tax costs on asset disposition, also consider transfer taxes
- May require extensive negotiations over asset valuation

In Canada from 2020 to 2022, approximately 74% of private M&A transactions were share purchases, 8% of private M&A transactions were asset purchases, 18% were hybrid deals*

*Source: American Bar Association: Business Law Section. "2025 Canadian Private Target M&A Deal Point Study" ("**2025 Canadian Deal Point Study**")



Structuring the Deal: Form of Consideration

Structuring the Deal: Form of Consideration

- Cash
 - ... is king
 - 28% of Canadian private M&A transactions in 2020-2022 were all cash*
- Shares or other securities of the Purchaser
 - Vendor will want to conduct a certain level of diligence on Purchaser
 - Consider how long-term relationship will play out between Vendor and Purchaser
 - Consider path to liquidity, are shares freely tradable?
 - Equity consideration has possibility for Canadian tax deferral for vendor
 - 36% of Canadian private M&A transactions in 2020-2022*
- Vendor Take-Back or other Deferred Consideration
 - Portion of the consideration payment is effectively delayed
 - Consider whether this is secured or unsecured, and what happens in a bankruptcy event of the Purchaser
 - Need to negotiate terms and timing of repayment, interest, etc.

Polling Question # 3 - What form of deferred compensation do Purchasers and Founders typically agree upon?

- a. “Classic” Earn-Out – Holdback of portion of purchase price, paid out on hitting specific target by target corporation
- b. “Staggered” Earn-Out – Holdback of portion of purchase price, paid out over different points over a specified post-closing period by target corporation
- c. “Reverse” Earn-Out – Reduction of purchase price to the extent target corporation does not achieve certain specified target(s)
- d. Vendor Take Back – Portion of purchase price is paid by way of promissory note to vendors, with the purchaser as lender, usually not tied to specific target



Earn-Out Considerations

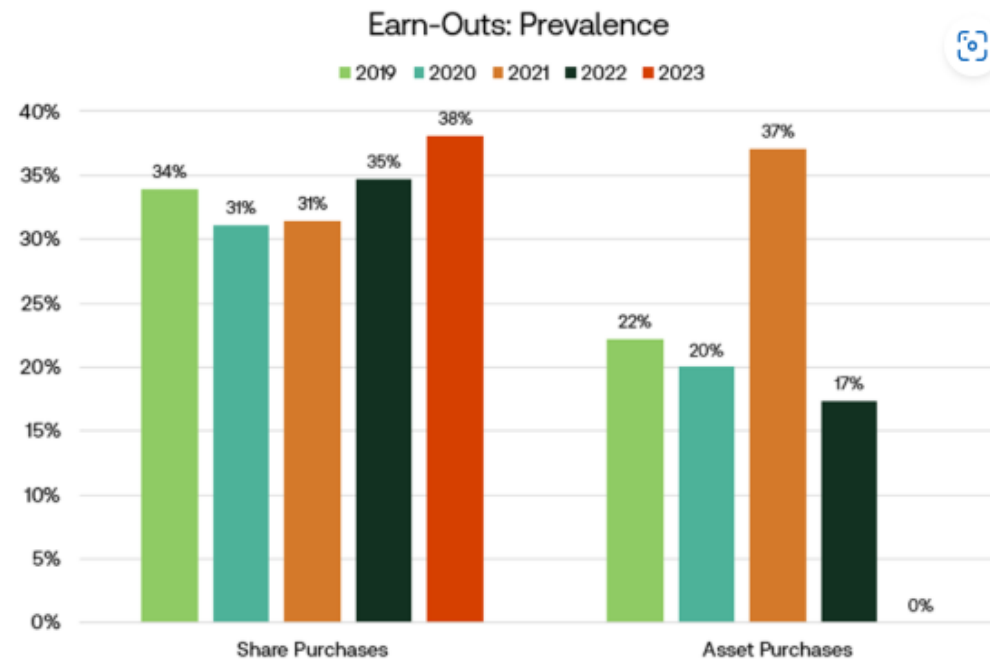
Earn-Out Considerations

- Advantages of an Earn-Out
 - Help bridge the valuation gap and value the target more effectively
 - Motivate the vendors post-closing
 - Help apportion risk
- Disadvantages of an Earn-Out
 - Complicated to draft and often lead to disputes
 - Profitability of a target may be difficult to forecast post-closing
 - May be negative tax consequences (i.e., earn-out payments taxed as income rather than capital gains)
 - Can be avoided using a reverse earn-out
 - Earn-out payments are vulnerable to Purchaser's action post-closing

Earn-Out Considerations: Prevalence

In Canadian private M&A transactions in 2023:

- Approximately 28% of transactions included an earn-out
- More common in share acquisitions and smaller transactions, about 40% in deals <\$25m



Earn-Out Consideration: Aspects of the Earn-Out

- Most common metrics*:
 - Revenue (29%), EBITDA/profit (12%), development milestones (35%), regulatory approvals (6%)
- Earn-Out Percentages*:
 - 29% of the base purchase price (2022: 48%; 2021: 56%; 2020: 20%; 2019: 35%)
- Earn-Out Term*:
 - Over 36 months (46%), 24 months to 36 months (8%), 12 months to 24 months (31%), 12 months or less (15%)
- Operating Covenants*:
 - Present in 53% of the transactions with earn-outs in 2023, can be pro-purchaser (18%), neutral (29%) or pro-seller (6%)



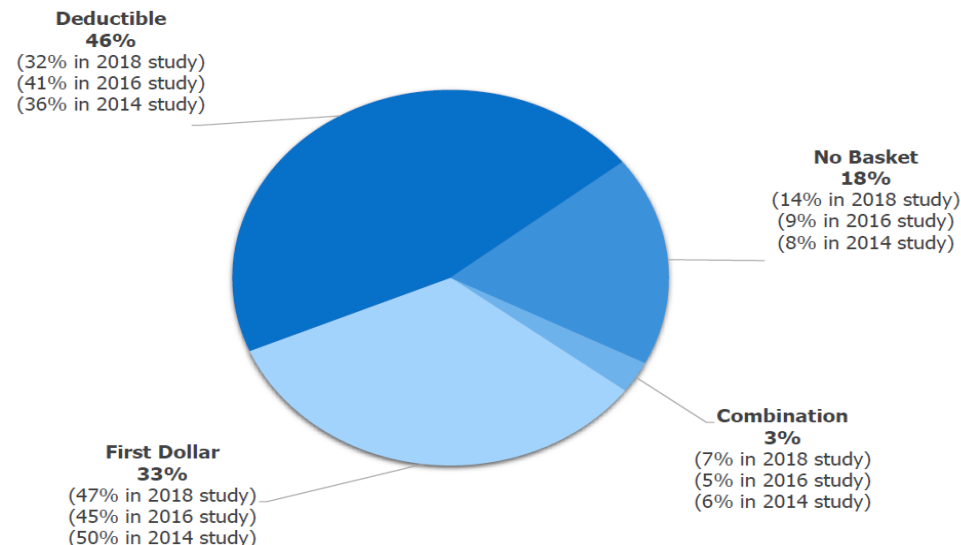
Indemnities: Market Standards

Indemnities: Market Standards

Main components of an indemnification provision:

- Length of indemnity*
 - 12 months (23%), 18 months (19%), 24 months (16%), tied to expiry of statute of limitations (1%)
- Basket*
 - Deductible (46%), first dollar (33%), combination (3%)

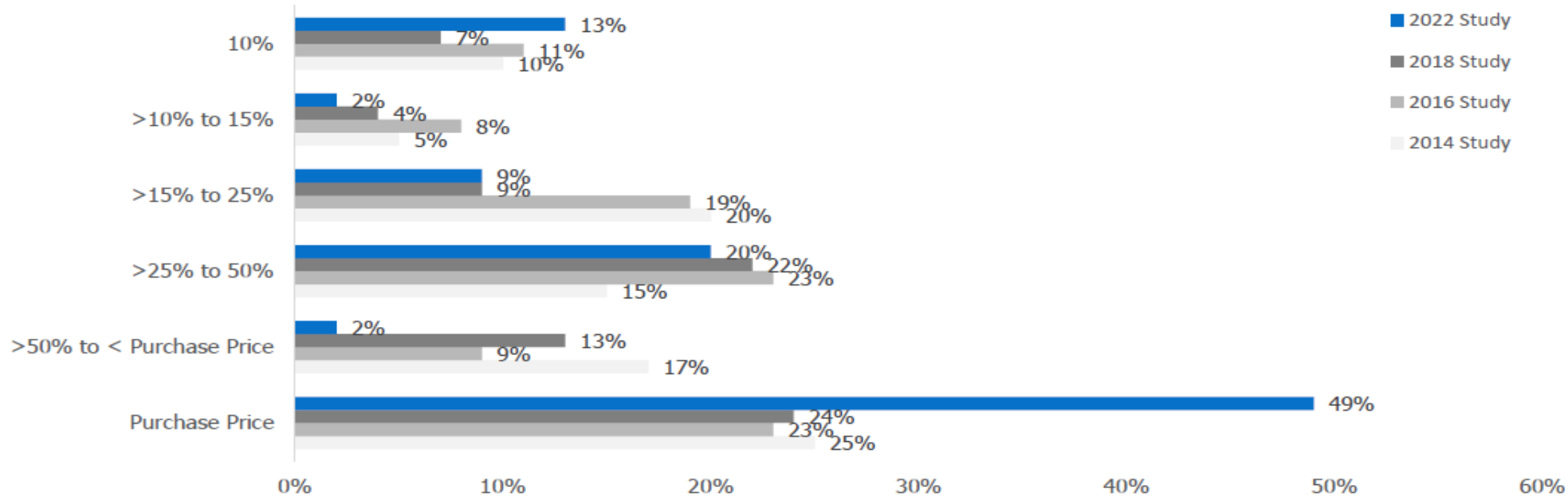
*Source: 2025 Canadian Deal Point Study



Indemnities: Market Standards (cont'd)

Main components of an indemnification provision:

- Caps*
 - 94% of Canadian M&A transactions have indemnity caps, applicable percentages of purchase price



*Source: 2025 Canadian Deal Point Study



Representation & Warranty (R&W) Insurance

Representation & Warranty (R&W) Insurance

- What is R&W Insurance?
- Advantages and disadvantages of R&W Insurance
- Main components of R&W Insurance
 - Coverage, exclusions, policy limits, deductible, survival period
- Prevalence of R&W Insurance
 - Present in approximately 13% of Canadian private M&A transactions*
 - Usually placed by purchaser (92% of transactions), premiums often paid for by both parties (62%), or purchaser only (23%)



Questions?

Contacts



Alex Kagan

Partner, Workplace Law Group

akagan@airdberlis.com

T 647.426.2293



Jackson Phillips

Partner, Capital Markets Group

jphillips@airdberlis.com

T 416.637.7550

Aird & Berlis LLP | Lawyers

Brookfield Place, 181 Bay Street, Suite 1800, Toronto, ON M5J 2T9 T 416.863.1500 F 416.863.1515

701 West Georgia Street, Suite 1420, Vancouver, BC V7Y 1E4 T 778.371.2241 F 778.371.2270

airdberlis.com

Aird & Berlis LLP operates as a multi-disciplinary practice.

Presented by



Aird & Berlis LLP | Lawyers

Brookfield Place, 181 Bay Street, Suite 1800, Toronto, ON M5J 2T9 T 416.863.1500 F 416.863.1515
701 West Georgia Street, Suite 1420, Vancouver, BC V7Y 1E4 T 778.371.2241 F 778.371.2270
airdberlis.com

Aird & Berlis LLP operates as a multi-disciplinary practice.