



*Managing Partner Miles Feltmate congratulates James Tuck on his recent admission to the partnership. "James is an excellent lawyer, community leader and a vital part of our team" remarked Miles. "We're absolutely delighted to have him as a partner now, as we prepare to celebrate our 15th year in 2012".*

## December 2011

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- InProfile - Continental Ingredients Canada Inc.



## From the Editor's Desk...

By Brian Heagle



*Tim Hogarth(left) of Pioneer Energy, and Kevin Brady of Brady Benefits.*

This is a story worth telling, and sharing.

Through its Strong Kids Program, the YMCA of Hamilton/Burlington/Brantford opens its doors wider to children and youth from families with financial difficulties.

A decade ago, Brady Benefits established a charity golf tournament to support Strong Kids. FDH has proudly been a lead sponsor each year. Another business with a philanthropic heart, Pioneer Energy, joined forces with Brady Benefits to co-host.

This year, an astonishing new record was set – over \$125,000 was raised!

The Fine Print focuses on the business acumen and financial success of our clients. However, we should also recognize and applaud their giving nature, including each company's vital role to play as a community leader.

What's your story?



Feltmate Delibato Heagle

L A W Y E R S

## Rent-to-Own Properties: Perils and Benefits

by Vince Rinaldi



### Rent-to-Own Model

Recently “rent-to-own” real estate has become trendy among the real estate community in Ontario. The rent-to-own model essentially involves a tenant/buyer agreeing to pay a lump sum to the landlord/seller up front as an “option price” in order to secure the right in the future to purchase the property at an agreed price. In the meantime, they are a tenant and must pay monthly rent which is higher than the market rent. The portion above market rent is then credited against the eventual purchase price of the property. The agreement states that the tenant/buyer is only a tenant with an option to purchase the property. Typically, the length of the term ranges anywhere from one to five years.

### Agreement for Sale vs. Option to Purchase

Unfortunately some tenants/buyers enter into these agreements with the notion that they have purchased the property and are paying the purchase price over time, which is not the case. There is an important distinction at law between an “agreement for sale” and an “option to purchase”. In an agreement for sale, which is generally used in the western provinces and not Ontario, the buyer makes monthly payments to the seller. Title to the property remains in the seller’s name until the entire purchase price is paid. Title is then transferred.

An option to purchase is quite different. Under an option, the “buyer” is not really a buyer, rather only a tenant of the property. Some rent-to-own agreements stipulate that the tenant’s option is terminated immediately upon any default of the tenant. Furthermore, virtually all rent-to-own agreements state if the full purchase price is not provided by the closing date, tenants/buyers forfeit the ability to purchase the property, all the money which they have paid towards the equity in the home and the rights to any improvement they have made to the property.

### Profitable Planning

The following benefits and risks should be considered prior to entering into a rent-to-own agreement:

- It appeals to tenants with a poor credit, yet with enough money to pay for the option.
- Real estate investment firms advertise annual returns of 20-26% to investors who purchase the properties and rent them to tenants.
- The purchase price is fixed, which is beneficial for the tenant/buyer in a rising market.
- Since the downpayment is spread out over time, home ownership

is easier to achieve for tenants/buyers on fixed budgets, while benefitting from occupying the home of their choice immediately.

- There are no standardized rent-to-own agreement forms accepted by the real estate industry, and the commonly-used forms are poorly drafted.
- Determining the purchase price for a transaction taking place anywhere from one to five years in the future is problematic. If the price is too low, the landlord/seller will try to walk away for potential additional profit and if the purchase price is too high the tenant/buyer will attempt to back out of the transaction.
- Tenants/buyers generally pay “above market rent” in order that each month some money will be credited against the purchase price. However if the tenant/buyer backs out of the transaction at the end of the option period, they will lose the option fee, any monies credited against the purchase price, and the rights to any improvements made to the property.
- Tenants/buyers may encounter dishonest sellers or unlicensed real estate agents. There have been instances of rent-to-own operators who rented homes from desperate sellers, subleased them to tenants, pocketed the rents without making mortgage payments, and left the tenant/buyer to be evicted by the mortgage lender.
- It may be difficult for the tenant/buyer to obtain financing with a conventional lender when they are trying to obtain mortgage financing to pay out the landlord/seller. Some banks will not recognize the past payments as part of the down payment. If the tenant/buyer cannot satisfy the bank’s requirement with respect to a further downpayment, he or she will not be able to obtain a mortgage, which in turn means they cannot exercise the option and they lose their investment.
- The Landlord and Tenant Board has ruled that if a tenant/buyer defaults under the agreement it does not have jurisdiction to evict a defaulting tenant/buyer who has an option to purchase.
- Power of Sale or foreclosure proceedings cannot be used against a defaulting tenant/buyer. Landlords/sellers must commence a lawsuit against defaulting tenants/buyers to evict them and terminate the option agreement.

### Final Thoughts

Rent-to-own transactions involve a significant amount of risk for both the landlord/seller and tenant/buyer. It is not for everyone. Persons wishing to participate in these transactions must fully understand the legal implications involved, the associated risks, and only deal with licensed real estate agents and real estate lawyers familiar with this concept.

## Shareholders Agreements Can Be Taxing

By David Boxen and David Rickards



Like most entrepreneurs you probably appreciate the importance of having a will to deal with the tax consequences of your death. But are you aware of the role that your shareholders' agreement can play in your estate planning?



Normally a shareholders' agreement is negotiated at a time when all of the parties are getting along and are healthy. The primary purpose of such an agreement is to define the relationships among the parties and to deal with the possibility that these relationships may sour or that the parties may change due to disability or death. If not structured properly, survivorship arrangements in shareholders' agreements can have unintended and significant tax consequences.

In general, Canada's *Income Tax Act* deems an individual to have, immediately before death, disposed of all of his or her capital property, including shares of a private corporation, at fair market value (FMV). The deceased individual will realize a capital gain on the deemed disposition to the extent the FMV of the capital property exceeds the tax cost, and 50% of such gain might be subject to tax depending on the availability of a capital gain exemption for qualifying small business shares. The deceased's estate is deemed to acquire the shares at FMV, which becomes the new adjusted cost base of the shares.

Commonly, shareholders' agreements are structured so that the corporation is required to purchase the deceased's shares, and the estate is then deemed to receive a dividend. Without getting bogged down in the details, it may be possible for the estate to realize a capital loss with such an arrangement, and for that capital

loss to be carried back to the terminal year of the deceased to offset capital gains realized by the deceased in the terminal year. Before April 27, 1995 it was possible to wipe out any tax being paid by the deceased and the estate with respect to the shares in this way.

Today, dividend stop loss rules will result in the denial of part of the capital loss that an individual or an estate would otherwise realize on a disposition of shares by a portion of the capital dividends received on the shares. There are a few exceptions to the newer rules, as well as grandfathering provisions that can apply in certain circumstances.

***If not structured properly, survivorship arrangements in shareholders' agreements can have unintended and significant tax consequences.***

Where exceptions and grandfathering do not apply it may be more beneficial for the estate to sell the shares to the surviving shareholder(s), rather than for the corporation to purchase the deceased shares for cancellation. Drafting flexibility into the shareholders' agreement in order to allow for either a purchase for cancellation or a purchase by the surviving shareholder(s) is helpful since at the time the agreement is drafted, it would be impossible to foresee which course of action would be most beneficial at the time the purchase is exercised.

The preceding touches on only a small fraction of the tax considerations for shareholders' agreements. Give us a call to see how these planning techniques as well as put/call options or estate rollover provisions in your shareholders' agreement can be used to further reduce the taxes payable by your estate.



*Feltmate Delibato Heagle was a table sponsor at the Oakville Chamber of Commerce 57th Annual Chair's Dinner on November 22, 2011.*

*Cam Neil of Feltmate Delibato Heagle and also a Director of Oakville Chamber of Commerce is shown here with Bruce Croxon, co-founder of Lavalife and the newest dragon on the popular television program, Dragon's Den.*

**FDH News**

- FDH congratulates **Thomson-Gordon (TG) Group** who is celebrating its 100th anniversary in 2011.
- Over the summer and fall 2011, FDH sponsored many charity events, including the Tony Clark Legacy Charity Golf Tournament benefitting **Kidney Cancer Canada** and were hole sponsors at the Scotiabank Key Partners golf tournament benefitting **Ronald McDonald House**.



The Parkinson SuperWalk for Oakville and Burlington had its 10th anniversary, and once again FDH was a proud sponsor.

- As part of his ongoing duties as a director **Brian Heagle** was recently elected as the Governance Chair of the Joseph Brant Memorial Hospital Foundation Board.



**F E E D B A C K**

We are always interested in hearing what you think about our Newsletter. If you have any comments or suggestions, or a topic that you would like to see covered, please contact our Editor, Brian Heagle at [bheagle@fdhlawyers.com](mailto:bheagle@fdhlawyers.com).

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