Broadcasting Public Notice CRTC 2008-57

Ottawa, 30 June 2008

Information bulletin

Allocation of the transaction value in changes in the effective control of broadcasting undertakings

In this notice, the Commission sets out its practice with respect to the determination of the transaction value in changes in the effective control of broadcasting undertakings.

The Commission also issues its determination on the approaches proposed in Broadcasting Public Notice 2007-139 to simplify the allocation of this value between different types of regulated broadcasting undertakings the change in effective control of which requires commitments to varying levels of tangible benefits or between such undertakings and broadcast distribution undertakings and/or unregulated undertakings the change in effective control of which does not require benefit commitments.

Given the consensus among interveners that an allocation of the value of transactions based on the simplified methods set out in Broadcasting Public Notice 2007-139 would not ensure a proper reflection of the actual value of assets and that the Commission's current discounted cash flow (DCF) methodology is the preferred methodology, the Commission has determined that it will continue to apply the DCF approach as the preferred methodology for those transactions where a valuation report is requested.

Although DCF is the preferred methodology, the Commission realizes that there may be circumstances where the preparation of a DCF valuation report may cause an undue financial hardship on the applicant. In these cases, an applicant may use a different methodology where it can convince the Commission that using the DCF method will cause an undue financial hardship and that the method chosen by the applicant stands the test of reasonableness, is consistent and is the most appropriate under the circumstances, as set out in Broadcasting Public Notice 2007-139.

Introduction

1. In *Call for comments on ways to streamline the determination of the allocation of the value of the transaction in changes in the effective control of a broadcasting undertaking*, Broadcasting Public Notice CRTC 2007-139, 14 December 2007, the Commission

- outlined the methodology that it currently uses to calculate the value of transactions requiring its approval; and

- set out its concerns regarding the subsequent allocation of this value between different types of regulated broadcasting undertakings the change in effective control of which requires commitments to varying levels of tangible benefits (e.g. radio and television undertakings) and between such undertakings and broadcasting distribution and/or non-regulated undertakings the change in effective control of which does not require benefit commitments.

2. To simplify the allocation of the transaction value in such cases, the Commission proposed two approaches based on each undertaking subgroup's past earnings before interest, taxes, depreciation and amortization (EBITDA). The Commission received five interventions in response.

Calculation of the value of transactions

3. As set out in Broadcasting Public Notice 2007-139, the Commission determines the value of transactions on a case-by-case basis. It first bases its calculations on the provisions of the purchase and sale agreement, including the negotiated purchase price, as well as on those of any other ancillary agreement. It considers all elements related to the purchaser, the vendor and any party related to them.

4. The Commission's approach to determining the transaction value in changes in effective control is consistent with the International Business Brokers Association's definition of transaction value, which reads as follows:

> The total of all considerations passed at any time between the buyer and seller for an ownership interest in a business enterprise, and may include, but is not limited to, all remuneration for tangible and intangible assets such as furniture, equipment, supplies, inventory, working capital, non-competition agreements, employment and/or consultation agreements, licences, customer lists, franchise fees, assumed liabilities, stock options, stock or stock redemption, real estate, leases, royalties, earn-outs and future considerations.

5. Under this approach, the value of the transaction is to include, among other items, the negotiated purchase price plus the value of certain liabilities and financial commitments. In cases where there are additional considerations or contractual obligations that must also be undertaken by the purchaser as part of the acquisition, such as payments for non-competition or employment agreements, their value is to be included in the value of the transaction as well.

6. In this regard, in addition to the negotiated purchase price, the Commission generally includes the following liabilities and commitments in the value of the transaction:

- assumed long-term liabilities (e.g., long-term debt, including debt related to capital leases);
- assumed commitments disclosed in the notes to financial statements (e.g., operating leases, other commitments);

- break-up fees paid;
- payments or commitments that are entered into by the purchaser, directly or indirectly, as a result of the purchase (e.g., employment/consulting agreements, non-competition agreements); and
- any purchase or control premiums.

7. The Commission does not include in the value of the transaction liabilities such as deferred income taxes and minority interests where, as of the date of the transaction, the payment date of the liability is unknown.

8. In share transactions, the Commission determines the value of the transaction based on the economic interest of the number of shares acquired and adds elements such as assumed debt to this value in the same proportion as the economic interest. On the other hand, elements that are solely to the benefit of the purchaser, such as purchase or control premiums and break-up fees, are allocated in their entirety to the value of the transaction.

9. The amounts for the elements added generally reflect their value either at the date of the transaction or as disclosed in financial statements prepared at a date that is close to the date of the transaction.

Allocation of the value of transactions

10. There was a consensus among interveners that an allocation of the value of transactions based on the simplified methods set out in Broadcasting Public Notice 2007-139 would not ensure a proper reflection of the actual value of assets. For example, the EBITDA methods proposed in the public notice would not take into account the growth rate and the risk specific to an undertaking. The discounted cash flow (DCF) method is preferred because it applies to most circumstances (including start-ups and undertakings operating at a loss) and is the one that generally better assesses the value of assets.

11. Given the consensus of the interveners that the DCF methodology is the preferred methodology and that transactions requiring an allocation will for the most part be only the more complex transactions involving larger undertakings, the Commission has determined that it will continue to apply its current DCF approach as the preferred methodology for those transactions where a valuation report is requested.

12. The valuation report will be required to be prepared along the following lines:

    - The report will determine the value of all of the assets involved in the change of effective control.

    - The value will be determined at the date of the transaction.

    - The report will follow the requirements of Appendix A of the Canadian Institute of Chartered Business Valuators (CICBV) Standard 110.

- The report will include a main valuation method (generally the DCF method since it is appropriate for most circumstances) and at least one secondary method to support the value determined with the main method.

13. The value to be allocated will generally be the value of the transaction determined as at the date of the transaction. To reflect the value at the date of the transaction, the applicant and/or the Commission may use values disclosed in financial statements that are prepared at a date that is close to the date of the transaction and that can be considered as a reasonable proxy for determining the values at the date of the transaction.

14. Although DCF is the preferred methodology, the Commission realizes that there may be circumstances where the preparation of a DCF valuation report may cause an undue financial hardship on the applicant. In these cases, an applicant may use a different methodology where it can convince the Commission that using the DCF method will cause an undue financial hardship and that the method chosen by the applicant stands the test of reasonableness, is consistent and is the most appropriate under the circumstances, as set out in Broadcasting Public Notice 2007-139.

Secretary General