The Estate Freeze: Tax Planning for the Future

The topic of estate freezes is probably not on every business owner's radar. Entrepreneurs typically spend their time growing their businesses and managing cashflow. It's rare to find business owners laser-focused on exiting their businesses or even thinking about death.

The reality is that there are two certainties in life: death and taxes. Death and taxes. Given that tax is a significant matter up there with death, business owners should take it seriously.

In the infancy stages, business owners typically rush to incorporate their businesses with minimal attention to ownership and succession. A typical entrepreneur will most likely incorporate a basic off-the-shelf corporation with him or herself as the sole shareholder and director. Fast-forward 10 years, that business has now taken on a life of its own and has grown significantly. You may even find that family members are now working in the business too. Its value is increasing with each passing day. As the value increases, so does the tax on the deemed disposition at death or on a transfer or sale.

Estate freezes can minimise the impact of these events and it is almost never too late to take advantage of these structures.

As a result, the direct comparison approach has become the preferred land valuation method. Even so, its correct application has become more challenging due to a lack of comparable sales, a rapidly changing planning environment, and increasingly complex deal terms.

By definition, an estate freeze is a mechanism that allows an individual to freeze the value of their business and assets, either to pass them on to their heirs, or to reorganize a corporate structure in preparation for selling those assets. The purpose of the freeze is to cap the taxable value of a person's net worth in certain circumstances. Given the importance, estate freezes have evolved to encompass family trust planning, life insurance planning, and wealth preservation strategies at large.

Our tax system affords Canadians the opportunity to sell shares of a Canadian Controlled Private Corporation and earn up to $1,250,000 tax-free. Furthermore, the 2024 Budget also proposed certain new incentives to entrepreneurs that will allow for tax-free proceeds. Canadians are encouraged to capitalize on those programs and plan effectively to maximize their net-worth.

Once a business has matured beyond its infancy, owners should strongly consider an estate freeze to effectively manage future growth within the family. For example, the business owner can freeze the value of his/her business utilizing preferred or special shares in favour of having new common shares held by a family trust. This will effectively allow the value of the business to grow in the Trust or other chosen vehicle, facilitating future planning and opportunities for all involved parties.

To give you an example of the way this can work, planning strategies are contained in Sections 85 and 86 of *The Income Tax Act* ("the Act"). These sections permit a deferral of income tax in a freeze transaction by effecting transfer and redemption of that value over time. This strategy reduces capital gains tax payable on death or sale. Once a freeze has been completed, new common shares can be issued at a nominal value to the taxpayer's children, a holding corporation, or a family trust, etc. This allows future growth to accrue to them, rather than the original taxpayer. Voilà—succession planning.

To recap, whether you have grown your business to a size that requires it to be in a corporation, or you have an established business and wish to prepare for succession, sale, or simply efficient tax planning, an estate freeze may be the right process for you to investigate. In order to do that, you need the right professional advisors and a solid plan to take into account your goals and objectives.

When done correctly, this provides a method to drive change and promote growth in a fashion that can only benefit both the business and the businessman. Good Luck! **IR**

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