Your Farm. Your Family. Your Future.

Tax and Succession Expertise for Generations

Volume 18

Succession or Retirement from your farm – Tax exit strategy concepts to consider

– Brian Krysowaty, B. Comm., CA, Consultant, Wealth Planning Group

Across the country, spouses, siblings and parents with children are discussing what should be done with their family farm. Should we sell it when the time is right, pass it down to the next generation or work alongside our children until they are ready to take over the family farm? Countless discussions, sleepless nights and likely the odd argument have taken place and with no real plan for the future in place. In looking at succession plans and/or retirement plans with the eventual sale of the family farm, one should consider various income tax considerations that could in the long run, limit the income tax exposure to you and your family.

Tax-free rollovers

As an owner of your family farm, you and perhaps your spouse have decided to allow your children to take over the family farm. If your farm is qualified farm property, as defined, under the Income Tax Act of Canada, you and your spouse can transfer the family farm assets to your children and do so on a tax-free basis. You and your spouse will not be subject to any tax on the asset transfer. It is important to note, any other property, other than qualified farm property, could be subject to tax in the hands of you and your spouse.

Estate freeze

A freeze or an estate freeze is a tax planning tool to "freeze" or "lock-in" the value of your family farm corporation. An estate freeze can be done at any point in time and you and/or your family members do not have to freeze all of the shares you would own respectively.

The basic premise of the estate freeze would be that you would exchange all or part of your common shares in your family farm corporation. For the common shares you do exchange, you would receive preferred shares of the family farm corporation.

With an estate freeze, new common shares can be issued to you, a spouse, family members, a family trust or an additional corporation. Future growth of the family farm corporation will be attributable to the newly issued common shares. The preferred shares you have received would be viewed as your return for all the work and effort in building your family farm. The preferred shares could be redeemed over time and provide a steady income in your retirement years for you and your spouse.

Holding Companies

A holding company can be used in several different ways. Holding companies can be used to freeze shares, as discussed above, for asset protection, and for purification issues.

With the payment of dividends, any excess cash and passive assets would be moved up to the holding company and provide a means of asset protection to you and your family, as the assets of the holding company are separate from the assets of the family farm corporation. At the same time and with careful planning, you would be keeping the family farm corporation pure for purposes of meeting the definition of qualified shares of a farm corporation in order to take advantage of the capital gains exemption on a potential sale of the family farm corporation.

The holding company could serve as an investment vehicle to you, as you may need to loan funds down to the family farm corporation and you can do so and securitize the inter-company loans to ensure creditor protection, or the funds in the holding company can be used for other investment alternatives or to pay you and your spouse a steady source of retirement income in the future.

Capital Gains Exemption

The capital gains exemption is indexed for 2015 at $813,600. Canadian resident farmers should take advantage of the most popular tax planning technique available to them. The capital gains exemption ("CGE") is available to every individual resident of Canada and only available up to $813,600 in their respective lifetimes on qualified farm shares or qualified farm property. The CGE is not available to corporations.

As mentioned above, with the use of holding companies, if a farm corporation has excess cash or passive assets that are not being used in the operations of the family farm, these particular assets may disqualify the family farm corporation from being eligible for the CGE. It is very prudent to monitor on a regular basis the family farm corporation's excess cash balances along with any other passive assets to ensure the family farm corporation meets the definition of a qualified farm corporation.

You should consider, in conjunction with an estate freeze, the ability to utilize more than just your own CGE. The option to introduce your spouse, children and possible grandchildren to being shareholders of the family farm corporation either directly or indirectly, could allow for a signification portion of capital gains to be sheltered from tax on a future disposition of the family farm corporation.

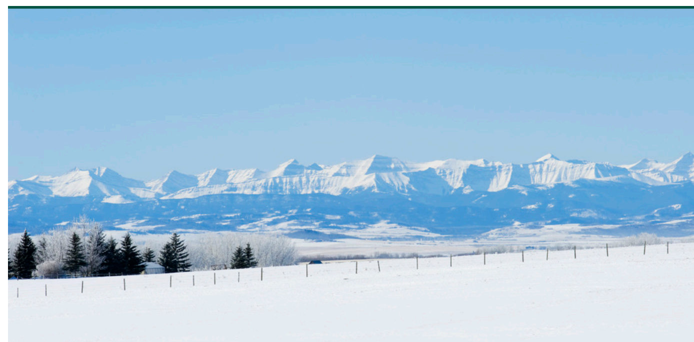
With proper planning, tax savings can be achieved with the CGE. Also, in the unlikely event of death, the CGE can also be utilized if the family farm corporation meets the definition of qualified farm corporation.

Life Insurance

You may consider the use of life insurance to offset significant tax liabilities on your death as opposed to having your family members make the hard decisions to sell some farm assets to pay the tax liability on your death.

The use of life insurance can be used as an equalization tool to provide for those family members who are not continuing on with the family farm, but for when you still want to leave some monetary consideration and/or assets. If the family farm corporation has a life insurance policy on you, the proceeds can be used very tax efficiently to redeem shares held by your surviving family members on a tax free basis.

This is a brief analysis of tax planning concepts. You and your family's situation is unique and has to be looked at independently. You should work with your advisors to implement and monitor one or more of the above tax planning concepts as you look to transition your family farm to the next generation or plan to sell and retire. Speak to your Assante Ag Group Advisor to determine which strategy is right for you. ■



Will the prescribed rate increase in 2015?

– Brian Krysowaty, B. Comm., CA, Consultant,
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Over the last five years taxpayers have enjoyed historically low prescribed interest rates.

The prescribed rate of interest is used by the CRA to calculate taxable benefits from interest-free and low-interest loans is currently at a historical low of 1% until the end of March 31, 2015. Are the prescribed rates expected to increase anytime soon? Nobody really knows for certain.

Prescribed Rate Loans

The income tax act contains attribution rules that prevent individuals from shifting taxable income to lower income family members using gifts of investable assets.

Income generated by a spouse or a minor child on funds subject to income attribution is taxed in the hands of the individual, thus defeating the income splitting purpose of the gift.

For example, Gary recently sold some farm land and now has $500,000 in cash to invest. Investment income earned by Gary would be taxed at 47% while investment income earned by his wife Sylvie would be taxed at 25%. If Gary simply gifted funds to Sylvie income attribution would apply and any investment income earned on those funds would be taxed in Gary's hands.

Gary could avoid income attribution using a prescribed rate loan.

Simply stated, Gary could loan funds to Sylvie charging interest at a rate no lower than the prescribed rate in effect at the time of the loan. The key to this strategy is that interest on the loan has to be paid to Gary before January 30th following the year it is earned. The interest must be paid every year. Failing to do so will cause income attribution to apply for the life of the loan.

Let's assume that the investments generate 5% in interest each year. Without the prescribed rate, Gary would pay approximately $11,750 in tax. Using a 1% prescribed rate loan, Gary and Sylvie's tax positions would be as follows:

	Gary	Sylvie
Income	$0	$25,000
Loan interest	$5,000	($5,000)
Net	$5,000	$20,000
Tax rate	47%	25%
Taxes paid	$2,350	$5,000

As you can see, total tax savings in this situation is $4,400 each year.

As the prescribed rate increases the tax savings decrease because more interest is taxed in Gary's hands.

We may never see interest rates this low again so if you lock in your loan before the prescribed rate increases you can take advantage of higher annual tax savings for an indefinite period of time. The prescribed rate in effect at the time of the loan will remain in effect for the life of the loan!

Opportunity to Consider

Corporate class investment structures are very tax efficient and in many cases are not suitable investments for this strategy. Often, annual tax savings with Corporate Class investments are higher when held by the higher income spouse. Speak to your Assante Ag Group Advisor to determine which strategy is right for you. ■

Call your Assante Ag Group Advisor to learn more about Corporate Class funds that largely defer taxable income well into the future, and can also result in future retirement income being taxed at preferential capital gains rates.

Financial Matters for Farmers – An invitation from the Assante Ag Group

Initial Introduction

We provide a free initial consultation to introduce our Wealth Management Program and to review your investment portfolio and financial situation for opportunities and income tax strategies.

What Our Clients Can Expect

- Comprehensive financial planning encompassing tax, insurance, estate, and succession planning based on your long-term goals while still providing for the short-term needs of you and your family
- A personal investment plan based on your goals, tax situation, income requirements, and risk tolerance
- Access to tax lawyers, accountants, and insurance, estate and investment specialists
- Identification, explanation and coordination of tax and estate planning strategies to be implemented by your professional advisors
- Ongoing monitoring of your investments and regular reviews of your financial, tax, and estate plans

Assante Ag Group

The Assante Ag Group is a national farm advisory group that assists Canadian farm families in the areas of tax planning, retirement planning, and wealth transfer. The Ag Group consists of highly experienced and trusted Wealth Advisors as well as lawyers and accountants with knowledge and experience in the tax and estate planning issues that affect farmers.

Taxation represents the single largest expense and loss of capital in the lives of many farm families, particularly in the retirement phase. Members of the Assante Ag Group work directly with the farm family to help them understand the complex tax and financial issues that need to be addressed in order to minimize loss of farm wealth when important transitions or transactions occur.

Tax, Financial and Estate Planning

The Ag Group's main focus and strengths are tax minimization, wealth planning and estate planning, including:

- Planning for the tax efficient transfer of the family farm to the next generation;
- Pre-retirement planning for the tax efficient sale of farm equipment, inventory and other assets;
- Planning tax efficient business structures for the family farm and other ventures;
- Personal tax and estate planning;
- Financial and retirement planning.

The Ag Group brings together not only tax, estate and financial planning, but also tax efficient managed wealth solutions and insurance strategies, all personalized to meet the unique needs and values of each client family.

Coordinating Professional Advice

The busy lives of farm families can seem further complicated by the necessary involvement of professionals from various disciplines, such as accountants and lawyers. The Ag Group provides a comprehensive plan that coordinates the services of these professionals. The Ag Group creates the plan, helps coordinate its implementation by the client family's accountant and lawyer, and continues to monitor the client family's tax and financial affairs thereafter and through the retirement years.

Our Commitment to Farm Families

The Assante Ag Group is committed to maintaining the high levels of proficiency and expertise required to provide professional advice throughout our long-term relationships with Canadian farm families. ■

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1502-0236_E (02/15)