

# Your Farm. Your Family. Your Future.

## Tax and Succession Expertise for Generations



Volume 21



## Preparing your farm corporation for the intergenerational rollover

Thomas Holmes, CPA, CA Regional Vice-President,  
– Wealth Planning Group

### Meeting our family

Pat and Linda incorporated P&L Farms Ltd. several years ago when their farming operation began producing significantly more income than they require to live on. By incorporating, they were able to take advantage of the tax deferral accomplished by retaining income within the corporation.

After several extremely profitable years they had accumulated significant cash and resources and approached their accountant to discuss their plans to take advantage of the tax-free intergenerational rollover and transfer the shares of their corporation to their son Nick in the next 5 years.

### The Problem

Pat and Linda had previously rolled farmland to Nick, so assumed that the shares of P&L Farms Ltd. would also qualify. Pat and Linda did not realize however that the tests that are required to be met for the rollover of farmland held personally and the tests to be met for the rollover of farm corporation shares are quite different.

In order for the shares of a farm corporation to be eligible to roll to the next generation tax free, it is necessary that 90% or more of the value of the assets in the corporation be used principally in the business of farming immediately before the transfer. The excess cash and investments held in P&L Farms Ltd. would not qualify as farming assets, therefore the shares would be offside and not eligible for the rollover.

### Potential Solution

The primary issue with withdrawing excess cash and investments out of the corporation is that generally this is done by paying taxable dividends or salaries to the shareholders which are taxable at their marginal tax rates. Pat and Linda do not need additional cash from the corporation to fund their lifestyle so they would prefer to withdraw the excess cash as tax-efficiently as possible.

One plan to address this issue involves transferring the excess cash and investments (“passive assets”) to a separate corporation (“Holdco”). This can be done on a tax-deferred basis but needs to be carefully planned and reviewed by tax specialists to ensure complex anti-avoidance rules aren’t applied by the CRA.



*Be well-advised.*

The goal for the family would be to continue to operate a successful farm corporation, meaning it's likely that P&L Farms Ltd. will continue to accumulate excess cash. Because of this, the goal of the planning is to implement a structure to ensure that the excess cash can be flowed to Holdco on a tax-deferred basis going forward through tax-free intercorporate dividends.

As always, it is recommended that this sort of planning is done proactively to ensure that planning opportunities are not missed.

### Potential Trap

One trap that some farmers fall into is rolling the farm assets to their child so that their child can turn around and sell the property to access their own capital gains exemption.

As a refresher, every Canadian resident may realize up to \$1,000,000 in capital gains tax-free over the course of their lifetime on sale of qualified farm property.

For example, let's assume in this scenario that instead of transferring the shares to Nick, Pat and Linda wanted to sell the shares of their corporation but they had already utilized their capital gains exemptions. If they decided to roll the shares of the corporation to Nick at cost, so that he could then sell the shares and utilize his capital gains exemption, the planning would be caught. The CRA has a rule in place designed to catch this sort of planning.

If Nick were to sell the shares within 3 years of receiving them, the tax rules in place would deem the rollover from Pat and Linda to have taken place at fair market value and Pat and Linda would have to go back and claim the full capital gain on the transfer to Nick on their personal tax returns.



The result is that Nick would receive the shares with an increased cost base but the gain on transfer would be fully taxable in Pat and Linda's hands.

If you are involved in a succession plan where parents are rolling farm property to their children with the plan to utilize their children's capital gains exemption, these rules should be carefully considered. ■

## Buy-sell Agreements – An Important Part of Your Business Planning

– Sandra Tabori, Lawyer, M. Fisc,  
Wealth Planning Group, and Assante Estate and Insurance Services Inc.

If you own a business with one or more other shareholders, what would happen if you, or another shareholder, were to die, retire or become disabled?

Having a shareholders' agreement that includes a properly structured buy-sell arrangement to address these events would help to provide a smooth transition plan, avoiding uncertainty and potential conflict and ensuring that the interests of deceased, departing and continuing shareholders are taken into account.

### What is a buy-sell agreement and what are the advantages of having one?

A buy-sell agreement is generally part of a comprehensive written, legal shareholders' agreement between the key shareholders of a company. As the name implies, it addresses the buyout of a shareholder's shares when a specified event occurs, such as when a shareholder dies, retires or becomes permanently disabled. A buy-sell agreement typically includes 3 key elements:

1. The method of structuring a buy out when a triggering event occurs;
2. A mechanism for valuing the business, to facilitate setting the price for the shares; and
3. How the purchase will be funded.

A properly drafted buy-sell agreement provides valuable advantages:

- provides a market for the shares of the business
- helps to ensure the business doesn't fall into the hands of a stranger or spouse
- provides stability to the business by setting out a transition plan and reducing potential conflict

### Funding a share purchase on the death of a shareholder

Some of the most effective methods to fund a buy-sell agreement when a shareholder dies involve the use of life insurance. For example:

*Criss-cross purchase using personally owned life insurance*

The terms of the buy-sell agreement require the surviving shareholder to purchase the deceased shareholder's shares at the price determined under the agreement. To fund the purchase, each shareholder purchases insurance on the life of the other and names himself or



herself as beneficiary. The surviving shareholder would then use the insurance proceeds to purchase the shares from the deceased shareholder's estate.

This provides guaranteed funding for the buyout and may allow the deceased shareholder to benefit from the capital gains exemption. However:

- the premiums would be paid with personal after-tax dollars
- there could be possible inequity in the premiums payable depending on the health of each shareholder

### *Promissory note with corporate owned insurance*

The terms of the buy-sell agreement require the surviving shareholder to purchase the deceased shareholder's shares in exchange for a promissory note payable to the estate. The operating company is the owner and beneficiary of insurance on the life of each shareholder. When a shareholder dies, the buy-sell agreement requires the company to use the insurance proceeds to pay the surviving shareholder a tax-free dividend from the capital dividend account (to the extent possible or desired) and the surviving shareholder pays out the promissory note.

With this method, the company pays the insurance premiums and the deceased shareholder may benefit from the capital gains exemption.

### *Share redemption with corporate owned insurance*

The terms of the buy-sell agreement require the company to purchase the deceased shareholder's shares at the price determined under the agreement. The operating company is the owner and beneficiary of insurance on the life of each shareholder. When a shareholder dies, the company uses the insurance proceeds to redeem the deceased shareholder's shares, resulting in a deemed dividend, which is either partially or wholly tax free utilizing the capital dividend account.

This method also involves the payment of the insurance premiums by the company.

If you own a business with one or more other shareholders, consult with your legal advisors to ensure that you have a properly structured buy-sell agreement in place. ■



Call your Assante Ag Group Advisor to learn more about Corporate Class funds that help defer and minimize tax on investment income, and can also result in retirement income being taxed at preferential dividend and 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. ■

This newsletter is paid for in part by Assante Private Client. Assante Private Client is a registered trademark and business name of CI Investments Inc. The Assante Ag Group is comprised of Assante Financial Management Ltd. ("AFM") advisors and Assante Capital Management Ltd. ("ACM") advisors. This material is provided for general information and should not be construed as investment recommendations and is subject to change without notice. Every effort has been made to compile this material from reliable sources however no warranty can be made as to its accuracy or completeness. Commissions, trailing commissions, management fees and expenses, may all be associated with pooled investments and the use of the Asset Management Service. The pools used in Private Client Managed Portfolios are not guaranteed, their values change frequently and past performance may not be repeated. Before acting on any of the above, please make sure to read the prospectus and consult your Assante Advisor for individual financial advice based on your personal circumstances. Insurance products and services are provided through Assante Estate and Insurance Services Inc. unless otherwise indicated by your advisor. Services and products may be provided by your Assante Advisor or through affiliated or non-affiliated third parties. The opinions expressed are those of the authors and not necessarily those of ACM/AFM. Private Client Managed Portfolios are made available through Assante Private Client, a division of CI Private Counsel LP ("Assante Private Client"). The pools used in the Private Client Managed Portfolios are managed by CI Investments Inc., an affiliate of CI Private Counsel LP. AFM and ACM are indirect, wholly-owned subsidiaries of CI Financial Corp. ("CI"). Assante Wealth Management is a registered trademark of CI Investments Inc. Please also see Legal section at our website, [www.assante.com](http://www.assante.com). \*indicates AFM advisor; \*\*indicates ACM advisor

#### Western Canada

**Adrian Spitters\*\***, CFP, FMA, FCSI  
Abbotsford, British Columbia  
604-855-6846

**Bruce McQueen\***, BA (Econ)  
Brandon, Manitoba  
204-725-2300

**Donavon K. Tofin\***, B.Comm, CA, CFP  
Saskatoon, Saskatchewan  
306-867-8696 1-877-996-8696

**Dustin M. Regehr\***, CFP  
Edmonton, Alberta  
780-450-3311

**Gerrit VandeWal\***  
Lethbridge, Alberta  
403-320-7777  
877-416-2237

**James Reimer\***, CFP  
Winnipeg, Manitoba  
204-982-1906

**Mark Driediger\***, CFP  
Abbotsford, British Columbia  
604-859-4890

**Michele Yergens\*\***, B.Admin, CFP  
Estevan, Saskatchewan  
306-634-9008

**Robert Bouchard\*\***, CFP  
Dauphin, Manitoba  
204-622-4766

**Shannon Briske\***, B.Comm, CFP  
**Byron T. Briske**, B.Comm.\*  
Saskatoon, Saskatchewan  
306-665-3244

#### Ontario

**Mike Andrews\*\***, CFP, RFP, FCSI, CIM  
London, Ontario  
519-438-0338 1-800-547-9669

**Patrick Gilmour\***, BA (Econ), CFP  
Kingston, Ontario  
613-549-8602 1-800-990-7893

**Ted Vanos\*\***, CFP, CAFA  
Sarnia, Ontario  
519-332-4100

#### Eastern Canada

**Chris Ball\*\***, CFP, FCSI, CIM  
Halifax, Nova Scotia  
902-431-3850 1-888-305-7526

**Peter Pomponio\*\***, CFP, RFP, C.Adm.  
St. Laurent, Québec  
514-832-5210

**Suzanne Mignault\*\***, CPA, CA, F.PI., FMA  
Ottawa, Ontario (Eastern Ontario and Quebec)  
613-567-8266 1-800-567-5504