Life's brighter under the sun

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Estate Freezes – A Practical Guide

Estate Freeze for Business Owners

WHY SUN LIFE CREATED THIS GUIDE

We prepared this guide to outline the estate freeze planning strategies that can be employed for shareholders owning private company shares. Tax legislation provides that taxpayers are deemed to dispose of all of their property at fair market value (FMV) immediately prior to death. This can produce a significant income tax liability in the year of death, thereby eroding the estate that is passed on to the beneficiaries.

While this deemed disposition[1] can be deferred when assets are left to a spouse or a spousal trust, this is only a temporary solution to the problem and does not solve the issue of tax due on the transfer of the shares to the children. The purpose of an estate freeze is to transfer to other persons (children, grandchildren, key employees) the future increase in value of the assets (generally shares of a small business corporation) that an initiator of a freeze (the transferor) owns. The transferor retains the current value of his/her shares and defers the income taxes on the capital gain to the time of their actual or deemed disposition.

Challenges in family business succession

There are many challenges that business owners face when the time comes to pass their business on to family members: the successors' lack of interest or ability, concerns about equity between heirs, and even outright refusal by the directors to transfer ownership of the business. Every family succession plan involves human, financial, legal and tax considerations that are unique to each business. In the sections below, we discuss the tax aspects of family business succession.

[1] When a person dies, the CRA considers that the person has disposed of all capital property right before death. The CRA calls this a deemed disposition. Also, right before death, the CRA considers that the person has received the deemed proceeds of disposition

Reasons for transferring ownership of a family business

Owners have various reasons for transferring ownership of the family business. The main motivations are usually to:

Lock in a purchase price for the business: By locking in the value of the business (through an estate freeze, for instance), the owner also sets the price that the successors will have to pay for the business.

Secure a commitment to the business: Transferring ownership to the successors will secure their commitment to the business since they will profit from the future increase in value that the business generates. As the value of the business grows, so does their incentive to remain in the business.

Ensure a smooth transition: Through an estate freeze, the original owner can retain control of the company for a period of time. The owner is then able to ensure a smooth transition of the business to the successors.

Provide retirement income: For most business owners, the bulk of their estate comes from the value of their company's shares.

When it comes time to transfer ownership, the business is often the owner's sole source of retirement income. Through an estate freeze, the owner can gradually transfer preferred shares to the successors. This strategy allows the successors to buy out the owner over time while generating retirement income for the owner.

Common considerations when transferring a family business

- ❖ Share valuation
- ❖ Financing the transfer
- ❖ Estate equity between siblings

Share valuation

When business ownership is transferred to family members, determining the value of the business is very important. If the owner has other children who do not buy shares in the company, those children will tend to overestimate the company's value. This can lead to discord between family members who are involved in the business and those who are not.

For this reason, it’s very important to thoroughly explain how the valuation was done and explain the impact that the siblings involved in the business have already had on its value.

In planning any family business succession, determining share value is a crucial step. If the share valuation is too high, the successors may become discouraged by having to wait longer for their involvement in the business to generate a profit. By contrast, a valuation that is too low could draw the attention of the tax authorities.

FMV can be defined as *“the highest dollar price obtainable under prevailing market conditions in a sale of property between knowledgeable, informed and prudent parties acting at arm's length, neither party being under any compulsion to transact.”* This is similar to the concept used by the Canada Revenue Agency ("CRA") in Information Circular IC89-3.[2]

In the case of a non-arm's length sale of shares, a price adjustment clause is recommended. It is based on the assumption that the parties have made a reasonable effort to determine the price of the disposed asset.

Ideally, a realistic share value should be determined by an independent valuator using one of the common valuation methods (discounted cash flow, asset valuation, capitalization of earnings, etc.) to ensure that the valuation is completely objective.

Financing the transfer

The other major challenge in transferring a family business is access to financing. It is often difficult for children to access sufficient funds to pay the selling parent up front. If the business is the parent’s only source of retirement income, this will be an issue at the time ownership is transferred. For this reason, financing the transaction is of paramount importance.

If the selling parent decides to self-finance, a written agreement should be drawn up that specifies the terms of repayment. There may also be tax consequences to anticipate from either a capital gain or a deemed dividend when preferred shares are redeemed. Some form of security for the seller and the other members of the family should also be in place. An example would be certain guarantees that are applied to the balance of the sale price (chattel and real estate mortgages). Ideally, a life insurance policy should be taken out on the life of the seller, as well as on the life of the buyer. Payments based on a minimum annual amount and a percentage of the annual profits can also be put in place.

[2] Canada Revenue Agency, Information Circular IC 89-3, "Policy Statement on Business Equity Valuations”, August 25, 1989.

Deemed disposition of shares at death

Immediately before the shareholder's death,[3] there is a deemed disposition of his/her shares at their FMV.[4] With a deemed disposition, it is assumed that the deceased shareholder's estate will receive the shares at a price equal to the shares' FMV immediately prior to death.[5] In most cases, the deemed disposition will trigger a capital gain, half of which will be included on the shareholder's terminal tax return. Deemed dispositions can be avoided if the shares are rolled over to a spouse or spousal trust.

Let's look at the case of Paul Smith, 55 years old and owner of SMT Inc. The business is valued at $3.5M. Paul is single and has two children who are involved in the business. If Paul died this year, there would be a deemed disposition of his company's shares at an FMV of $3.5M.[6] The tax impact would be the following:

Proceeds of disposition		$3,500,000
Less:	ACB	100
	Capital gain	3,499,900
Less:	Eligible deduction[7]	913,630
Net capital gain		$2,586,270
Taxable capital gain (50%)		$1,293,135
Income tax payable (53.53%)[8]		**$692,215**

[3] As a taxpayer resident in Canada.

[4] Paragraph 70(5)(a) of the *Income Tax Act*, R.S.C., 1985, c. 1 (5th Supp.) (hereinafter the "ITA"). Unless otherwise noted, all statutory references will be the ITA.

[5] Paragraph 70(5)(b).

[6] FMV on date of death.

[7] Paul hasn't used any of his capital gains deduction. This deduction is $913,630 in 2022.

[8] Combined Federal / Ontario marginal tax rates

Paul Smith’s situation

Paul anticipates that his business will double in value over the next ten years because of strong demand for his products. His current wealth is not enough to fund a comfortable retirement without access to at least a portion of his company’s value.

Because his two children are involved in the business, he would like to find the best solution for transferring ownership of the business to his family. After much reflection, he decides to transfer the future growth in the value of his shares to his two children in equal portions. This decision is based on the fact that they are already involved in the business. Paul would like to proceed quickly before the value of the shares increases even more. In a nutshell, he wants to know how to reconcile all his goals and avoid putting his children in a tough financial situation or creating family conflict.

Obviously, Mr. Smith does not want to be taxed immediately on the unrealized capital gain of his shares, because the transaction will not generate any immediate cash that would allow him to pay the taxes owing. Accordingly, it is important to structure the transaction to generate little or no tax, if any.

CHANGES IN SMT INC.’S VALUE OVER TIME

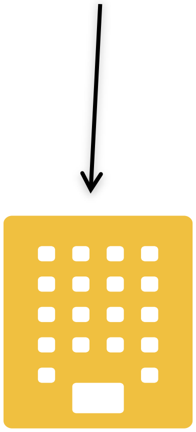
Today	In 5 years	In 10 years
FMV **$3.5M**	**FMV** **$5M**	**FMV** **$6M**

Current corporate structure

Paul Smith

100% common shares

$100 ACB / $100 PUC



SMT Inc.[9]

(FMV = $3,500,000)

The estate freeze

Setting up an estate freeze will essentially reduce or freeze any future growth in the succession value of Paul's business. The company's current value is capped such that any growth beyond this value will flow to his two children. The estate freeze is therefore set up for the benefit of his children.

[9] SMT Inc. is an SBC within the meaning of subsection 248(1) ITA whose shares are qualified small business corporation shares.

Tax rollover

For an estate freeze to be taxed deferred at death, it is critical that the initial freeze operation be carried out on a tax rollover basis. This goal is easily achieved when the initiator of the freeze transfers his or her participating common shares to non-participating preferred shares and utilizes the many rollover mechanisms that are allowed under the *Income Tax Act*.[10]

Tax deferral

The other key element of an estate freeze is the tax deferral it provides the freezer. The first key element we looked at (rollover) refers to the "freeze" part of the transaction. The "estate" part of an estate freeze refers to the taxes that the transaction gives rise to on the death of the freezor.

Tax savings to the family

An estate freeze allows for taxes to be deferred. In addition to tax deferral, an estate freeze can also be used to multiply the capital gains exemption. Keep in mind that the capital gains exemption[11] only applies to an individual person, not to a couple, a family, or a business. In this case, there are potentially four opportunities for Paul Smith and his two children to use the capital gains exemption.[12] For this to happen, the family members must own qualified small business corporation (QSBC) shares.

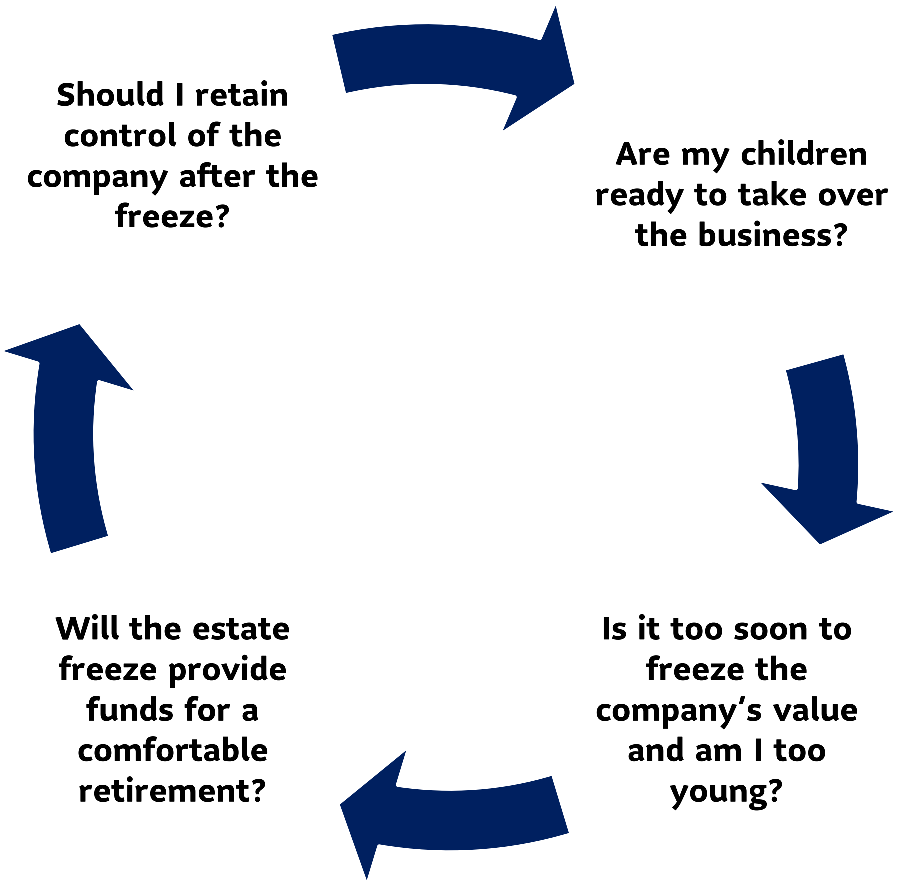
[10] Specifically, sections 51, 85 and 86 of the ITA.

[11] The lifetime capital gains exemption (LCGE) for qualifying shares is $913,630 in 2022. This amount is indexed annually.

[12] The tax savings realized using 3 exemptions is $730 584 (3 × $913,630 × 50% × 53.3%)

Fundamentals to verify before the freeze

Generally speaking, managing shareholders are not usually concerned with the technical aspects of an estate freeze. In all likelihood, it won't matter to Paul which method is used to implement the freeze. Instead, Paul's actual concerns about the freeze would revolve around the following:



Should I retain control of the company after the freeze?

Are my children ready to take over the business?

Is it too soon to freeze the company's value and am I too young?

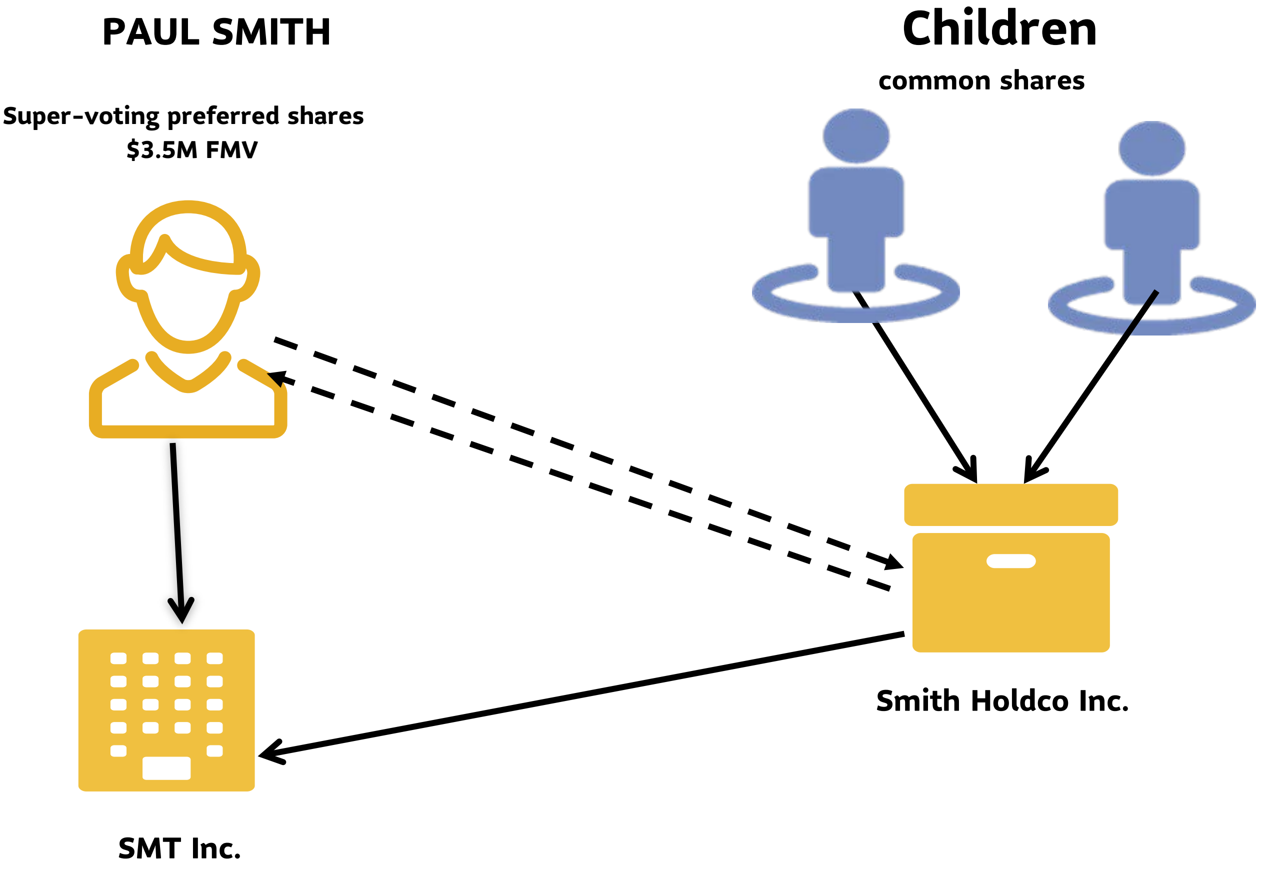
Will the estate freeze provide funds for a comfortable retirement?

Structuring the estate freeze

An estate freeze is a fairly complex tax planning procedure. There are several methods that can be used to structure the freeze.[13] Depending on the method, the business owner can retain total or partial control of the property involved in the freeze. Two commonly used methods are:

- Using a holding company, or
- Using a trust.

1. Using a holding company


PAUL SMITH
Super-voting preferred shares
$3.5M FMV
Children
common shares
Smith Holdco Inc.
SMT Inc.

[13] Specifically, sections 51, 85 and 86 of the ITA.

Explanations

A classic estate freeze can be structured using a corporation (Smith Holdco Inc.), as per subsection 85(1) of the ITA. This type of estate freeze is normally done as follows:

1. Paul's children will incorporate a new chartered company, Smith Holdco Inc. The siblings purchase the common shares of Smith Holdco Inc. By doing so, they will be involved in the future increase in the corporation's value. To avoid potential problems with the tax authorities, his children should subscribe for the common shares of Smith Holdco Inc. before Paul transfers SMT Inc.'s shares so that the tax authorities won't dispute the common shares' FMV at their date of issue.

2. Paul, as initiator of the freeze, transfers the common shares of SMT Inc. to Smith Holdco Inc. Under the provisions of subsection 85(1) ITA, the transfer takes place without immediate tax consequences. In exchange, Paul receives preferred shares at a fixed value. These shares are non-participating so that their value does not increase over time.

The preferred shares received for consideration should have the following attributes:

- sufficient voting rights to retain control of Smith Holdco Inc. This is important because Paul wants to retain control of SMT Inc. for at least another ten years;
- the right to fixed, non-cumulative dividends at a reasonable rate;
- the right of share redemption, at his option, at the value for which they were issued, i.e. the FMV of the transferred property on the date of issue.

By freezing SMT Inc.'s shares, the value of all future growth of the transferred property will accrue to the common shares held by Paul's children. The post-freeze growth will not be taxed at Paul's death since the common shares shares are owned by Paul's children.

Tax implications of the classic freeze

First, the current value will be frozen at $3,500,000 comprising 3,500 preferred shares of Smith Holdco Inc. The shares will be redeemable at the option of the holder. The shares will be voting and not participating. At rollover, the agreed amount will be set at $913,730 to realize a capital gain of $913,630 which will be exempted by the capital gains deduction on the shares of SMT Inc. The rollover will not result in any adverse tax consequences from the application of subsection 84(1) ITA (deemed dividend)[14] because the transaction consists entirely of shares.

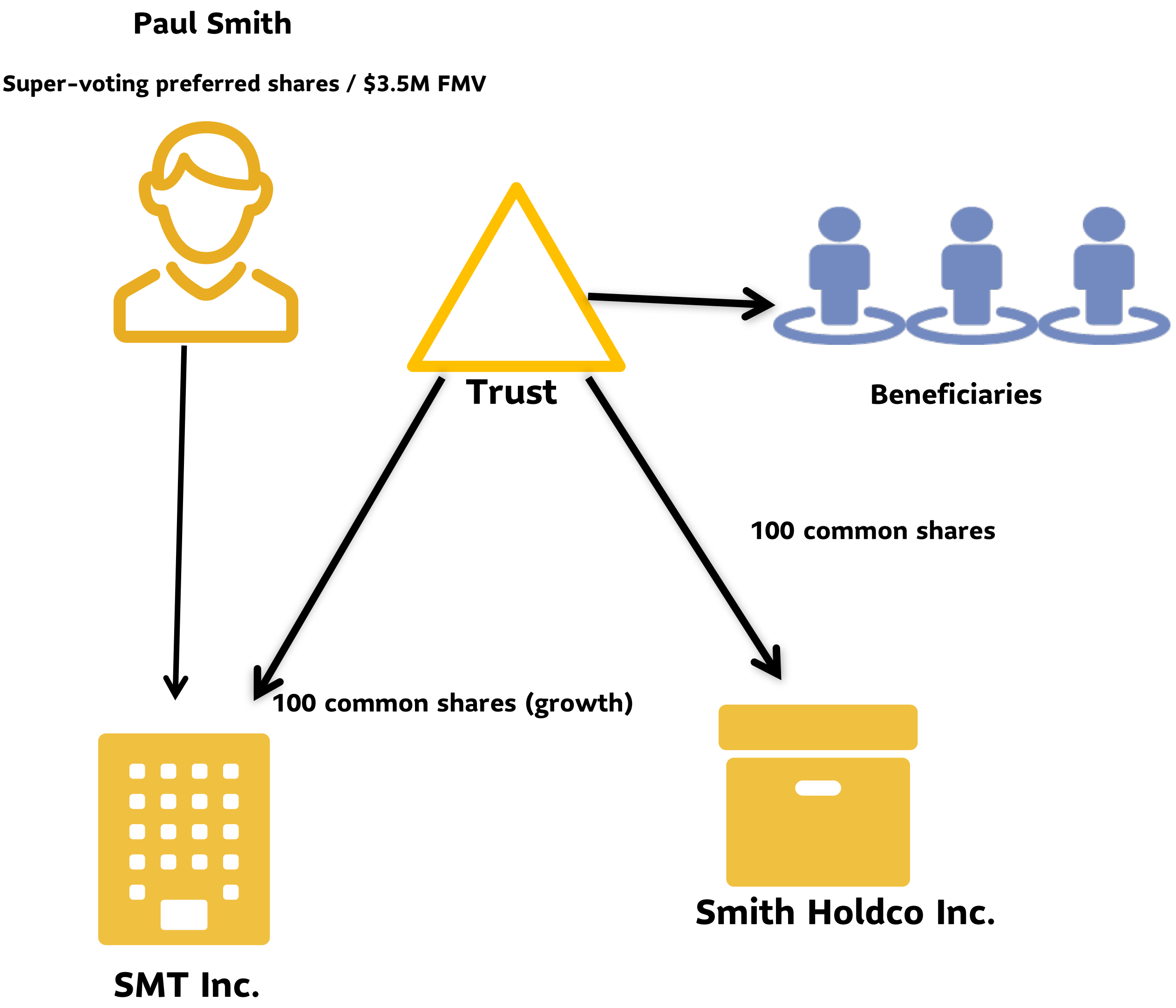
Disposition of shares by Mr. Smith:	
Proceeds of disposition (agreed amount)	$913,730
Less: ACB	$100
Capital gain	$913,630
Less: Capital gain deduction	$913,630
Tax payable[15]	$ 0
ACB of Smith Holdco Inc.'s preferred shares:	
The ACB equals the agreed amount in this case	$913,730
Paid-up capital of Smith Holdco Inc.'s preferred shares	$100
Redemption value of Smith Holdco Inc.'s preferred shares	$3,500,000

The value of Paul's shares has been frozen. These shares are valued at $3,500,000 and will not increase over time. If Paul dies a few years from now, the capital gain on his preferred shares would be $2,586,270 instead of $3,499,000. The capital gain reduction is not tied to the freeze. Instead, the reduction is the result of crystallization. Paul receives no money from this transaction. He will have to redeem his preferred shares if he wants access to cash.

[14] Under paragraph 84(1)(b) of the ITA.

[15] Subject to AMT, if applicable.

2. Using a discretionary trust


Paul Smith
Super-voting preferred shares / $3.5M FMV
Trust
Beneficiaries
100 common shares
100 common shares (growth)
Smith Holdco Inc.
SMT Inc.

Explanations

The trust will subscribe to the participating and non-voting shares of SMT inc. Although there is a deemed disposition of all assets following the 21st year of existence of the trust, experience has shown that many events can occur during these 21 years. For this reason, it was planned, as an additional precaution, to create the holding company (Smith Holdco inc.) during the freeze.

Ultimately, this estate freeze structure will defer capital gains tax on new common shares issued in the name of the family discretionary trust by allocating them to designated beneficiaries at the appropriate time.

The family trust strategy has the following advantages:

- More flexible structure than the classic freeze;
- Income splitting among beneficiaries, subject to certain TOSI conditions[16];
- Ongoing purification of SMT Inc.;
- Since the family trust will be a shareholder, any capital gain on the disposition of the trust shares will be realized in the family trust. However, the taxable portion (i.e. 50%) of the capital gain can be made payable to one or more beneficiaries and taxable in their hands, allowing multiplication of the LCGE;
- Protection of the estate from creditors;
- The "freeze value" depletes over time, reducing the tax payable on the frozen shares at Paul's death;
- Facilitates "thawing", if ownership transfer to his children becomes problematic.

The main disadvantages of this structure are:

- Higher cost to set up and maintain;
- More administration;
- Deemed disposition rule for the trust every 21 years.

[16] Subsection 120.4(1) ITA. Under the current income tax rules, the TOSI applies the highest marginal tax rate to "split income" of an individual under the age of 18. In general, an individual's split income includes certain taxable dividends, taxable capital gains and income from partnerships or trusts. Starting with the 2018 tax year, these updated rules apply for adults aged 18 or older. Individuals may be excluded from TOSI if the income they receive in the year comes from excluded shares, provided they reached the age of 25 before the end of the year in which the income was received.

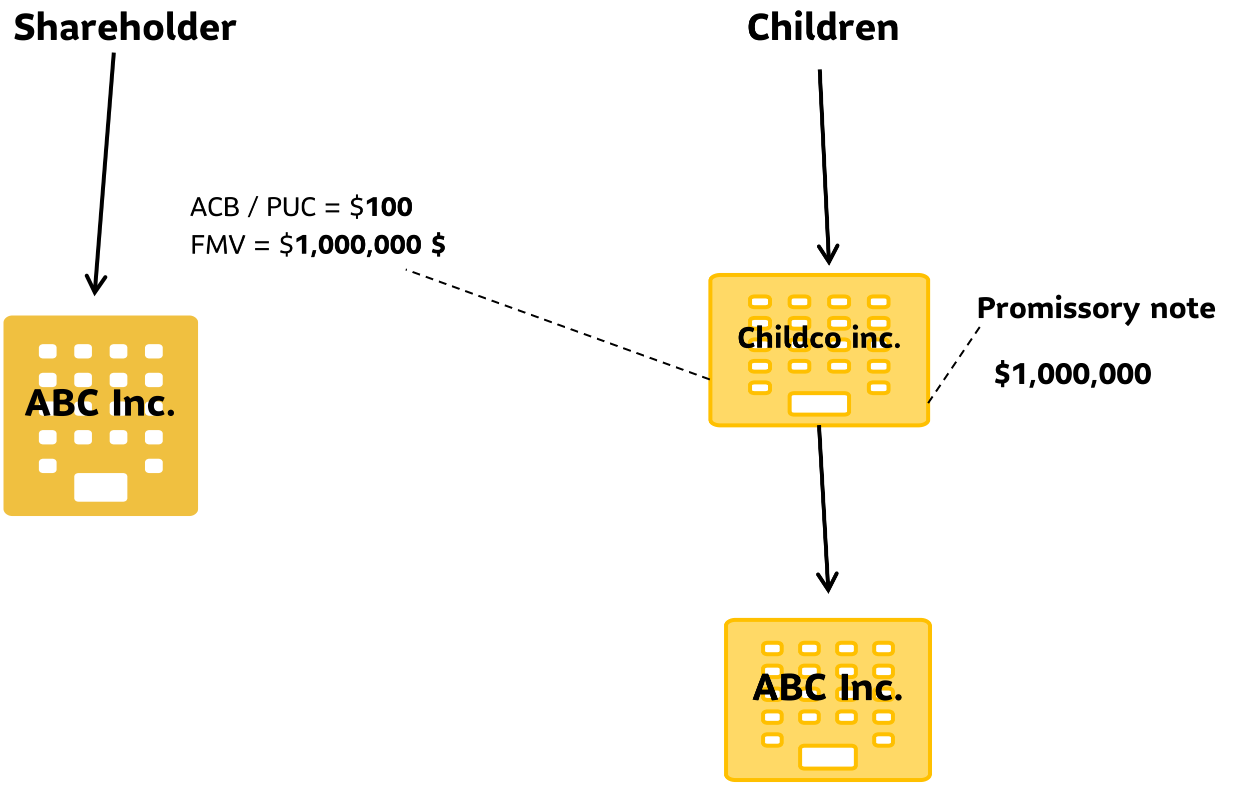
Tax pitfalls of an estate freeze

Surplus stripping and section 84.1 of the ITA

The provisions of section 84.1 of the ITA are really an **anti-avoidance rule** to prevent the withdrawal of taxable surplus from a company by converting it into a tax-free return of capital on a non-arm's length transfer of shares by an individual.[17]

In other words, section 84.1 of the ITA is really intended to prevent shareholders from making tax-free withdrawals of cash or consideration other than shares. Section 84.1 therefore prevents a person from "cashing in" his or her capital gains deduction when dealing with a related company.

Illustration of section 84.1 ITA


Shareholder
Children
ACB / PUC = $100
FMV = $1,000,000 $
ABC Inc.
Childco inc.
Promissory note
$1,000,000
ABC Inc.

[17] Since March 18, 2016, the rules in Quebec differ regarding this anti-avoidance rule.

Illustration of section 84.1 ITA

The chart below summarizes the tax saved with a section 84.1 estate freeze.

	Without LCGE	With LCGE	Sec. 84.1 ITA
Sale price	$1,000,000	$1,000,000	$1,000,000
ACB	($100)	($100)	($100)
Initial capital gain	$999,900	$999,900	-
Deemed dividend	-	-	$999,900
2022 LCGE	-	($913,630)	-
Final capital gain	$999,900	$ 86,270	-
Tax payable[18]	$267,573	$ 23,085	$477,352
Amount available	**$732,327**	**$976,815**	**$522,548**

Main consequences:

- The realized capital gain becomes a deemed dividend of $999,900 for the shareholder.
- The shareholder won't be able to claim the LCGE.

When a dividend is deemed received, there is an additional tax cost of $209,779 compared to the first scenario (without LCGE) and an additional $454,267 compared to the second scenario (with LCGE).

[18] Ontario marginal tax rate: 26.76% (capital gains) / 47.74% (non-eligible dividends)

Six conditions for section 84.1 of the ITA to trigger a deemed dividend

There are six conditions that must all be met for section 84.1 of the ITA to apply and trigger a deemed dividend. The conditions are as follows:

1) the seller is a taxpayer resident in Canada (trusts included);

2) the purchaser is a corporation;

3) the property disposed is the capital stock of a corporation resident in Canada;

4) the seller and purchaser do not deal at arm’s length;

5) the purchaser corporation and selling corporation are “connected corporations”[19] after the transaction;

6) consideration other than shares received by the seller does not exceed the greater of:

a) the tax paid-up capital of the shares transferred by the seller to the purchaser;

b) the “modified" ACB of the shares transferred by the seller to the purchaser.

Thoughts on section 84.1 of the ITA

The main issue with section 84.1 of the ITA is that, unlike an arm’s length sale of shares, it becomes nearly impossible for a “bona fide” family transaction to avoid the negative impacts of a share sale.

If a shareholder were to sell his business to an arm's length third party, that third party would be able to use its LCGE, any capital losses from stock market investments and ultimately benefit from a favourable capital gains tax rate.

Furthermore, an arm's length buyer could use a corporation to acquire the shares of the company, so that the purchase price would be supported with after-tax corporate dollars which are normally taxed at a lower rate.

On the other hand, if the shareholder were to sell the business to his children through a company without careful tax planning, he would be taxed on a "deemed dividend" at a tax rate that could reach 47.74%.

However, if the shareholder were to sell directly to his children (and not to a holding company owned by his children), he would come out the winner. However, his children who

[19] Within the meaning of subsection 186(4) ITA

acquired the shares personally would "lose out" because they would have to pay the purchase price of the shares using personal after-tax dollars. Finally, there would be an impact on the ACB of the shares, which would normally equal the price paid for the shares less the exemption amount claimed by the shareholder as part of the transaction.

CONCLUSION: To avoid all consequences from the application of section 84.1, the transaction must be planned so that the sum of the paid-up capital of the shares plus the fair market value of the non-share consideration received by the seller does not exceed the greater of:

- the paid-up capital of the transferred shares
- the arm's length adjusted cost base[20] of the transferred shares.

Bill C-208

Bill C-208 received Royal Assent on June 29, 2021. In order to facilitate intergenerational transfers of businesses, this bill introduced an exception to the anti-avoidance rule in section 84.1 ITA

The 2022 federal budget set up a consultation process to allow interested people to share their views on how the current rules could be changed to protect the integrity of the tax system while continuing to facilitate real intergenerational business transfers. The government is committed to proceeding with legislation to address these issues. A bill is expected to be tabled in the fall of 2022 following the conclusion of the consultation process.

[20] The concept of "arm's length ACB" prevents two related persons from planning a transaction to take advantage of the LCGE by withdrawing funds from a company owned by them. For example, an individual could sell his or her shares to his or her spouse at their FMV and claim the LCGE. The spouse would then sell the shares to a related company and receive the proceeds tax-free since the ACB of the shares would equal the FMV. Paragraph 84.1(2)(a.1) prevents this strategy because, for purposes of section 84.1, the ACB of the spouse's shares is reduced by the exemption taken by the individual on those shares.

Conditions for claiming the lifetime capital gains exemption (LCGE) for qualified small business corporation (QSBC) shares during an estate freeze

When a business is sold, it’s very common for the seller to want to claim the LCGE. This operation is commonly called “crystallization” of the capital gains. The LCGE applies to capital gains realized by an individual who is resident in Canada on the disposition of qualified small business corporation (QSBC) shares or qualified farm or fishing property (QFFP).[21]

Keep in mind that if an individual elects to claim the federal capital gains exemption, this election will be binding on the individual with respect to the applicable Quebec exemption.

To verify if an individual can claim the LCGE, they must first verify that the shares they own are QSBC shares. First, the shares must have been held for a period of at least 24 months by the individual or a non-arm’s length person. Second, at the time of sale, the shares must be shares of a small business corporation (SBC) with more than 90% of the FMV of its assets being qualifying assets.

Qualifying assets are defined as assets that are principally used in an active business carried on primarily in Canada.

Finally, during the 24-month period preceding the disposition, more than 50% of the FMV of the company's assets must be assets used primarily in an active business carried on primarily in Canada.

In some cases, a company can lose its SBC status temporarily through the accumulation of investments or assets unrelated to its operations.[22]

[21] The LCGE limit in 2022 is $913,630 for QSBC dispositions.

[22] For example: stock market investments, surplus cash or a life insurance policy with cash surrender value.

This usually isn't an issue when there is no disposition of the company's shares. To dispose of corporate shares that do not satisfy the 90% qualifying asset test, there are purification techniques[23] that can be used to ensure that the company's shares will qualify for the LCGE.

LCGE illustration

	Individual claims LCGE	Individual does not claim LCGE
Realized capital gain	$800,000	$800,000
Taxable capital gains (50%)	$400,000	$400,000
Capital gains deduction	$400,000	$0
Taxable income	$0	$400,000
Tax	$0	$176,280 *

**Not including AMT payable*

In certain situations, a company will reach a point where its accumulated profits will no longer be fully distributed or reinvested in the company's qualifying assets. In this situation, the profits will be invested in investments or other assets that are not actively used to earn income. As a result, these assets will eventually make the 90% test difficult and even impossible to satisfy unless a continuous purification strategy is put in place.

[23] Various transactions can be performed to purify a company's assets. For example, the company could repay debts, acquire qualifying assets or pay dividends to shareholders.

Summary of the LCGE rules

Below is a summary of the rules for businesses wanting to take advantage of LCGE.

Rule	Detail
Resident status	At least 50% of the shareholders must be Canadian residents.
Personal share ownership	The operating company's shares must be owned personally and not by another corporation such as a holding company.
Use of assets	At the time of sale, 90% or more of the FMV of the company's assets must be mainly used in an active business in Canada. No more than 10% of the fair market value of your company's assets can be in passive assets, including: • cash in the bank; • non-registered investments; • real estate not actively used in the business; or • certain types of life insurance policies with cash surrender values.
Active business assets, 24 months before sale	Throughout the 24 months before the sale, at least 50% of the fair market value of the company's assets must have been mainly used in an active business in Canada.
Owning shares, 24 months before sale	Throughout the 24 months before the sale, shareholders must generally have owned any shares they want to claim the LCGE for when they sell.

Decrease in the value of the business

If an estate freeze has already been executed and the value of the business has dropped, the preferred shares will also decrease in value. In a situation like this, another freeze can be done to lock in the shares at a lower value. This approach can help reduce tax liability at death.

In addition, if a family trust was set up to own the common shares in the original estate freeze, these shares could be frozen at the lower value and a new trust created. This has the added benefit of resetting the 21-year time limit for the new trust (a trust is deemed to dispose of its assets at fair market value every 21 years).

There may be other opportunities when market conditions are weak. For example, assets can be sold to family members to have the losses offset the capital gains realized in the current or prior year(s) (careful consideration should be given to the superficial loss rules and the impact on the corporation's capital dividend account). Another option is to purify the company's balance sheet so that it can claim the qualified small business capital gains exemption.

Other aspects to consider

Life insurance

Life insurance is an excellent product to consider when planning an estate freeze. First of all, life insurance can be used to pay the tax resulting from deemed disposition upon the death of the owner or spouse, whichever is later. On the owner’s death, the tax-free insurance proceeds will be paid to the estate and can be used to pay the tax liability. To do this, it may be preferable to have the company own the insurance policy since corporate tax rates are generally lower than individual tax rates. On the business owner’s death, the death benefit is paid to the company and any proceeds in excess of the adjusted cost basis (ACB) can be credited to the company’s capital dividend account (CDA). The company can then pay a tax-free capital dividend to the estate to pay any taxes owing. Remember that in this scenario and if the company is the policyholder, the shares must not be given to the successor before the capital dividend is paid since it would then be impossible to ensure that the money will be paid to the estate to pay the taxes.

Life insurance can also be used to provide money to family members who are not involved in the business. This is one way to establish equity between family members. Accordingly, the parent initiating the freeze can purchase a life insurance policy and name his or her inactive children as beneficiaries. Estate equalization can also be achieved using life insurance shares.[24]

Finally, a third option is to name the company as the owner and beneficiary of the life insurance policy so that the successor(s) can redeem the shares of the company owned by the inactive children. In this scenario, the author of the freeze bequeaths his or her shares to all the children.

The successor(s) redeem(s) the shares of the children not involved in the business at their FMV. Regardless of the life insurance strategy, the owner initiating the freeze must thoroughly document his or her intentions and discuss them with all concerned to avoid potential conflicts.

Shareholders' agreement

A shareholder's agreement is crucial for an estate freeze involving family. The agreement essentially governs the relationships between the shareholders and ensures a smooth transition between all parties involved. Just like a will, there is no "one-size-fits-all" shareholders' agreement. Each agreement must be "customized" to suit the shareholders' specific needs.

A shareholders' agreement will normally contain the following provisions:

- How directors are appointed;
- How profits are used;
- The rules for buying back shares held by the owner-director and paying out dividends;
- Restrictions on the transfer of shares (right of first refusal, tagalong right, drag-along right, compulsory withdrawal);
- Mechanisms at death (purchase/redemption, life insurance).

[24] See Sun Life's guide on "Life Insurance Shares", December 2021.

Wills

Once the estate freeze is in place, all parties involved should update their will or have one drawn up. A will makes it possible to defer the taxes normally payable at death, to ensure continuity of the business, and to ensure all heirs are treated fairly, among other things. It is important for a will to include items such as:

1. Setting up post-mortem strategies[25] to avoid double taxation on certain assets passed on to the heirs.
2. Setting up a tax rollover to a spouse or a spousal trust, if applicable.
3. Where the freezor still owns preferred shares of the operating company, provisions for the freezor's estate to redeem these shares as soon as possible after the freezor's death.
4. Provisions for siblings who are not involved in the business to receive the cash value of the shares promptly.

Conclusion

An estate freeze is a very effective tool for transferring ownership of a family business to the next generation. But executing an estate freeze is a complex undertaking. It is important to obtain advice from qualified tax professionals. The freezor will also need to address personal and organizational concerns with successors to the corporation. Finally, determining the corporation's proper value and the timing of the estate freeze are crucial to this strategy's success.

[25] See Sun Life's "Post-mortem strategies for business owners – Practical guide," December 2021 for more information.

Any examples presented in this article are for illustration purposes only. No one should act upon these examples or information without a thorough examination of their tax and legal situation with their own professional advisors after the facts of the specific case are considered.

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