# Corporate Asset Transfer

Because you've made your business a success – pass it on.

## Meet Tom and Katie

They have left sizeable assets to accumulate inside their company to take advantage of the lower corporate tax rates. Now they face another tax dilemma.

Operating companies, professional corporations, holding companies and management companies often contain cash and investment assets not used in active business. These assets, locked within the corporation can usually only be paid out to the shareholders as taxable distributions unless there is a capital dividend account available with a credit balance.

Frequently, some assets are invested in GICs or other short-term investments. These vehicles provide guarantees and easy access to the cash, but usually have lower rates of return. While active business income may be taxed at the small business rate, generally substantially lower than the individual's marginal tax rate, income received by way of invested retained earnings and surplus are treated as passive income and are taxed at the top corporate tax rate.

There are two other levels of taxation to be considered as well. At the time of the shareholder's death, his/her estate may be subject to capital gains tax. For heirs who wish to extract value from the corporation, usually this can only be done by way of taxable dividends.

## The facts

- Tom is 55, Katie is 53. Both are in excellent physical health;
- They have accumulated $1,240,000 in retained earnings in their holding company;
- The funds are invested conservatively, and have been returning less than 5% annually, which is subject to the corporate passive income tax rate of 50.17%.*

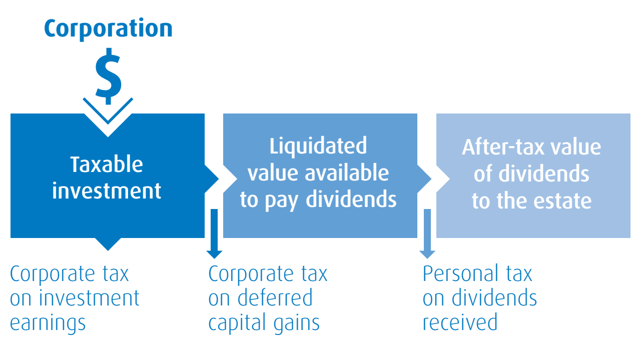
## The strategy

Tom and Katie's holding company purchases and is the beneficiary of a joint last-to-die permanent life insurance policy on them. The strategy involves a reallocation of corporate assets into the insurance plan over the next 10 years. Based on the assumed rate of return of 4% for their fixed-income corporate investments, this means an annual deposit into the plan of $135,299. When the death benefit is paid, it will be received by the corporation tax-free.**

## The challenge

Multiple layers of taxation prevent Tom and Katie from maximizing the value of their corporate assets.

- High tax rates on corporate investment income means much slower asset growth
- High tax rates on any capital gain that is realized by the corporation as investments are sold so dividends can be paid to the shareholders.
- Any remaining after-tax value can be paid out as a taxable dividend, further eroding the amount available for their heirs.



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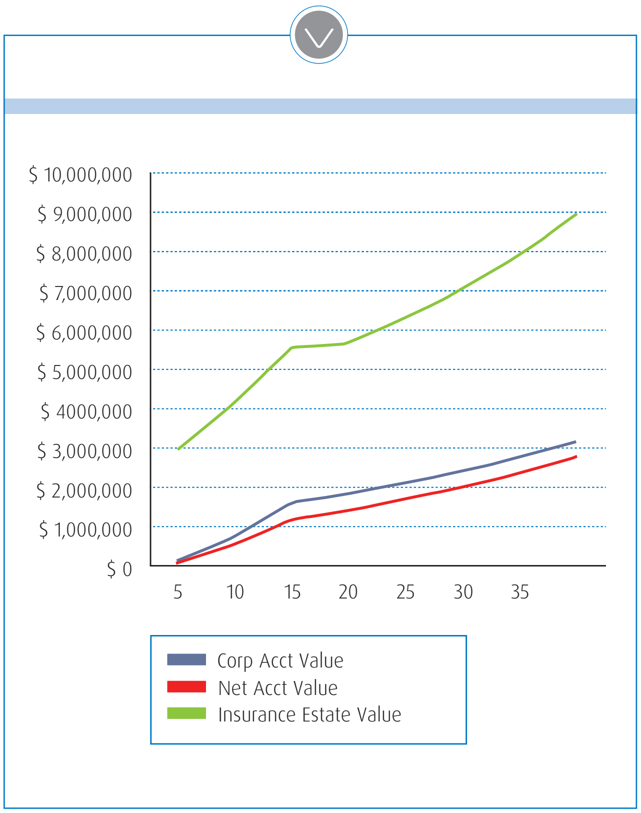
## The results

### Greater portfolio diversification over time

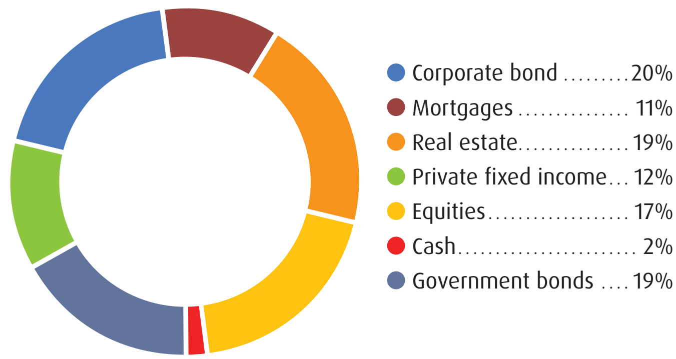
Tom and Katie have access to the insurance carrier's professionally managed investment or participating account.

### A stable pool of assets with low volatility

These accounts are managed to absorb the impact of short-term market fluctuations. Once a policy is credited, the amount credited cannot be taken away.




## Typical account composition




Even though the insurance carrier also invests primarily in fixed-income investments, the insurance policy's tax sheltering characteristics prevent the substantial erosion of value each year. In addition, the proceeds received tax-free by the corporation can flow to Tom and Katie's heirs through the Capital Dividend Account on a tax-free basis. The overall result is a substantially higher net value produced by the Corporate Asset Transfer strategy. ***

For more information, speak with your BMO financial professional who will refer you to an Estate & Insurance Advisor from BMO Estate Insurance Advisory Services.

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*Combined tax rate for Ontario corporations on interest income for 2015

**Amounts in excess of the adjusted cost basis are credited to the Capital Dividend Account

***Amounts credited to the CDA can be paid out as a tax-free dividend. Insurance proceeds beyond the CDA credit can be paid out as a taxable dividend account.

The asset allocation and crediting procedures for their whole life insurance contracts are very similar with the different insurance carriers. The actual numbers and values utilized in this example are taken from an illustration of a Canada Life Estate Achiever Joint Last To Die policy, with current rates as of January 1, 2017.

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