

# *Freezing your estate*

***Let's talk series***

*An estate freeze defers taxes by transferring growing wealth from the current generation to a future generation.*



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*It doesn't matter if your business is on solid financial footing or not—this economic crisis is hitting everyone. Bottom line: if you were to sell your business today, the value will have dropped. And that is precisely why this might just be the perfect time for an estate freeze. “There is opportunity here,” says Angela Ross, associate partner in PwC’s High Net Worth Tax Services practice.*

“The whole point of doing an estate freeze is to defer taxes by transferring growing wealth in private company shares from the current generation to a future generation. In order to do that, you cap or freeze the value of your interest in the company at the current value and allow all future growth to accrue for the benefit of future generations.”

To be dramatic, let's say your business has dropped 50% in value, but you have every expectation that it will rebound in the next two to five years. If you freeze today, what otherwise would have been value taxed in your hands upon your death can now be deferred and moved to the next generation who will stand to benefit once the company recaptures lost value and resumes its growth trajectory. This planning may also make it possible to use your family's lifetime capital gains exemptions to shelter significant capital gains from future tax.

**When it comes to tax, deferral is the next best thing to tax savings.**

In Canada, when you die, you are deemed to have disposed of all of your assets (business, investments, anything you own) and your estate will be left with the tax bill. If you can freeze the value of your interest in the company, you will have capped the amount that will be subject to tax in your hands. If you do nothing, and your investments and business continue to grow, the amount of tax you pay on your death also continues to grow. And your estate is left paying. Ouch.

“Even if you take the economic crisis out of the equation, freezing in and of itself is a great idea, particularly if your wealth is already such that you will live comfortably for the rest of your life and you plan to give anything else you might accumulate to the next generation on your death,” says Ross. “Planned properly, the taxes on that growth will only be triggered if and when your children die or sell the business.”

**Be proactive and make an estate freeze part of your succession plan.** “An estate freeze makes a lot of sense for business owners who have accumulated enough wealth to keep them happy for the rest of their lives and who have children in their teens or older who will likely succeed them in the business.”

Why? Because the growing wealth captured in an estate freeze can be put into a trust and that trust structure doesn’t have to be wound down for 21 years. You have all that time to work out exactly what you want to do before the wealth has to be transferred to the next generation. “Consider it 21 years of cushion time,” says Ross. “This gives you plenty of time to best decide who you are going to leave the company to; who will rise to the challenge.”

**The flexible freeze.** An estate freeze does not have to be an all or nothing proposition. A flexible freeze allows you to include yourself as a beneficiary of the freeze through a discretionary trust, not just your children. “The beauty of it is, if you are in a position where you aren’t sure you have enough wealth yet, or your succession plans change, you can take the wealth back so long as

the trustees agree,” says Ross. “In other words, you can put it in place and if you decide to use it, fine—if not, that’s also fine. The trustees have 21 years to make that decision.”

**Proper planning is key.** “There are a lot of technical pitfalls that could trip you up,” says Ross. “A good tax advisor can help you steer clear of them.”

Take the corporate attribution rules, for example. If an estate freeze and trust deed are not planned and drafted properly, the Income Tax Act may deem taxable income in your hands through the corporate attribution rules—regardless of whether or not you actually had the income.

**Word to the wise.** Tax planning should not stop with an estate freeze. In fact, once you’ve done the freeze, you can start reducing tax even further. “Done properly and at the right time, you can take what otherwise would have been a big tax hit on death and significantly reduce or possibly eliminate it,” says Ross. “But you need the freeze in place first. There is a real magic to it.”

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