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Succession Planning: Consider an Estate Freeze

As a business owner developing your succession plan, you must consider your personal goals, the objectives of the business, and the role that future generations of your family will play in the business. A potential strategy may be to implement an estate freeze.

What is an Estate Freeze?

An estate freeze "freezes" your interest in the business at a particular time by exchanging your shares on a tax-free basis for fixed value "freeze shares". The business then issues new "growth shares" to your children or other heirs so they can participate in the future increase in value of your business. Growth shares may be acquired by your heirs directly and/or indirectly (i.e., by way of a discretionary trust).

When implementing a freeze, many owners maintain control of their businesses by ensuring that the freeze shares received have all, or a majority of, the voting rights of the company.

Benefits of an Estate Freeze

Since the value of the shares that you own is fixed, you will have limited your tax liability on death and deferred the tax on any future growth until such time that your heirs pass away or sell their growth shares. Also, the locked-in value of the freeze shares should allow you to estimate the amount of taxes owed upon death so that appropriate planning measures can be made to fund that liability. Furthermore, since the value of frozen assets owned at death will be lower than the value of assets without a freeze, the amount of probate fees or estate administration taxes, if applicable, may be minimized.

In certain situations, you may be able to use your lifetime capital gains exemption (LCGE) limit to shelter capital gains when freezing your shares. For 2015, the LCGE is $813,600 (and the amount is indexed to inflation for future years). Additionally, an estate freeze may allow you to multiply the use of the capital gains exemption limit as your heirs may be able to use their exemption limits when they, or the discretionary trust, dispose of the growth shares in the future.

An estate freeze may also provide an effective means of splitting income with your heirs.

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Is an Estate Freeze Right for Me?

A variety of factors should be considered when deciding if an estate freeze is right for you:

- **Current value of your business** — As an estate freeze locks the current value of the business into freeze shares, it is generally preferable to freeze when the value of the business is low, which may be the case in a slower economic environment.
- **Forecasted growth** — One of the benefits of the estate freeze is tax deferral resulting from transferring the future growth of the business to your heirs. If future growth prospects are not substantial, other potential strategies may be more appropriate.
- **Your age and financial position** — Before proceeding with a freeze, you must be satisfied that the fixed value of the freeze shares, along with any other assets that you own, will be sufficient to provide financial security for the remainder of your lifetime. If you are not comfortable transferring all of the future growth of the business to your heirs, you may consider a partial freeze of the business (i.e., you acquire a portion of the new growth shares) or implement a flexible freeze (i.e., you become a beneficiary of the discretionary trust).
- **Age and interest of your heirs** — You should be sure that your heirs are ready and willing to participate in the equity of the business. If your heirs are minors, a discretionary trust may be a viable alternative.

If you are considering an estate freeze, consult a professional to determine the most appropriate path given your circumstances.