

**RSM! Richter Chamberland**



## **2009 Professional Development Seminar**

**Tax-planning opportunities in today's economy**

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Montreal, Quebec  
June 10, 2009

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### Capital Dividend Account (CDA) Planning

- CDA includes the non-taxable portion of capital gains [currently 50%]
  - Also includes life insurance proceeds, non-taxable goodwill gains, CDA from other corps
- Can be paid out tax-free to individual
  - Election must be filed
- CDA may be reduced by “non-taxable” portion of capital losses [currently 50%]
  - Also includes non-deductible portion of allowable business investment losses
  - Planning – pay out CDA before losses triggered and CDA reduced

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### Dividend Payments

- Retained earnings could be at risk to creditors
  - If business downturn shareholder ranks after both secured and unsecured creditors
- Payment of dividend followed by loan covered by security
  - Allows secured creditor to rank in advance of ordinary creditors
  - Beware legal restrictions, solvency tests

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#### Refundable Dividend Tax on Hand (RDTOH)

- Refundable to corporation at \$1 for every \$3 of taxable dividends paid
- If dividend supported by RDTOH, it is an inexpensive way for shareholder to access cash
  - Highest personal marginal rate for dividends in Quebec in 2009 of 36.4% vs. 33.3% refund to corporation, resulting in a net cost of 3.1%.
  - For eligible dividends, highest personal marginal rate for dividends in Quebec in 2009 of 29.7% vs. 33.3% refund to corporation, resulting in a net saving of 3.6%.
- Eligible dividend tax rates to be increased in coming years

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#### Example

- RDTOH of \$1,000
- Dividend paid of \$3,000

	Eligible	Non-Eligible
Dividend paid	\$ 3,000	\$ 3,000
Refund to corp	1,000	1,000
Tax to shareholder	<u>(890)</u>	<u>(1,090)</u>
Net funds available	\$ 3,110	\$ 2,910

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### Freeze/Refreeze

- Individuals taxed on deemed disposition at FMV on death
  - Excludes transfers to spouses
  - Excludes transfers to qualifying spousal trusts
  
- Freezing values
  - To limit tax on death
  - Tax-deferred exchange of common shares for fixed value preferred shares
  - Redeemable, retractable
  - Subscription for common shares by next generation/trust

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#### Freeze/Refreeze

- Value of fixed preferred shares may have dropped below original value
  - Consider exchanging for new preferred shares reflecting current value
  - CRA – permits this provided no benefit conferred on others
- Exposure
  - Attribution rules – potential deemed interest charge
  - Valuation issues

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#### Back-to-Back

- Life insurance (other than CSV) not included in value of shares on death
  - Life insurance (net of ACB) added to CDA account
  - Tax-free to estate
  
- Annuity included in value of shares on death but is replaced on liquidation by life insurance
  - Loss may be triggered on dissolution to offset gain on death
  - Beware of stop-loss rules

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#### Example

Assume shares have value of \$10MM (including \$5MM annuity) at time of death

Additional \$5MM of life insurance (no CSV)

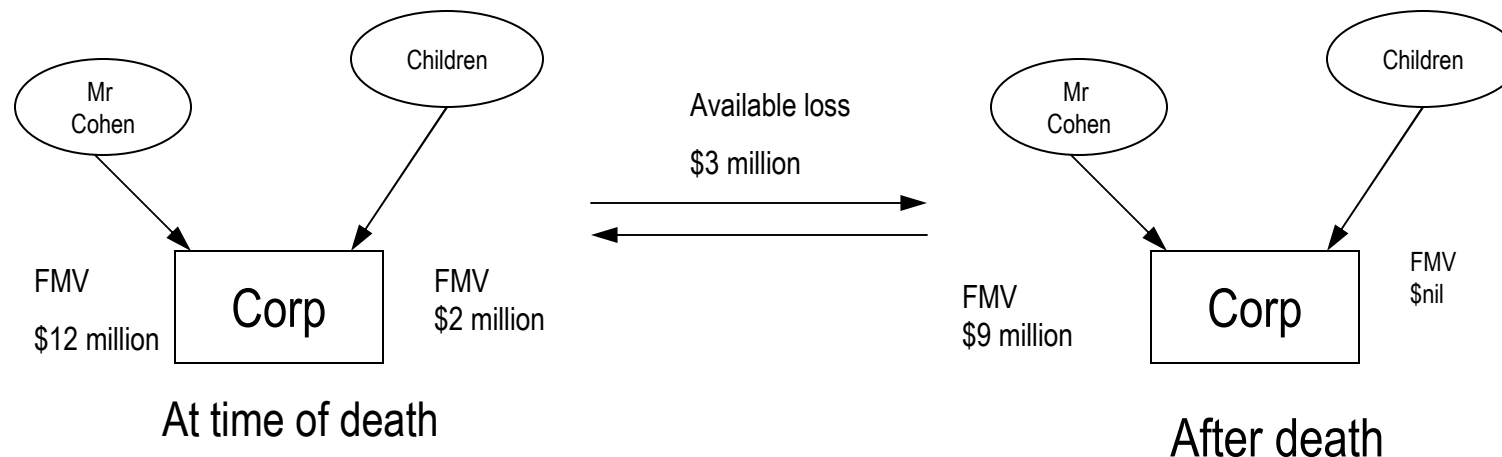
Value of shares on death	\$ 10MM
Termination of annuity	(5MM)
Life insurance proceeds	5MM
CDA paid from life ins.	<u>(5MM)</u>
Value of share on wind-up	<u>\$ 5MM</u> [potential capital loss]

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Back-to-back

- Might be less effective in freeze scenario
  - If loss created not effective if it reduces common share values to next generation
  - Consider use of separate corporation
- Assume \$5 million loss created to Cohen family



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Example with separate Holdco

