INVESTMENT
SOLUTIONS

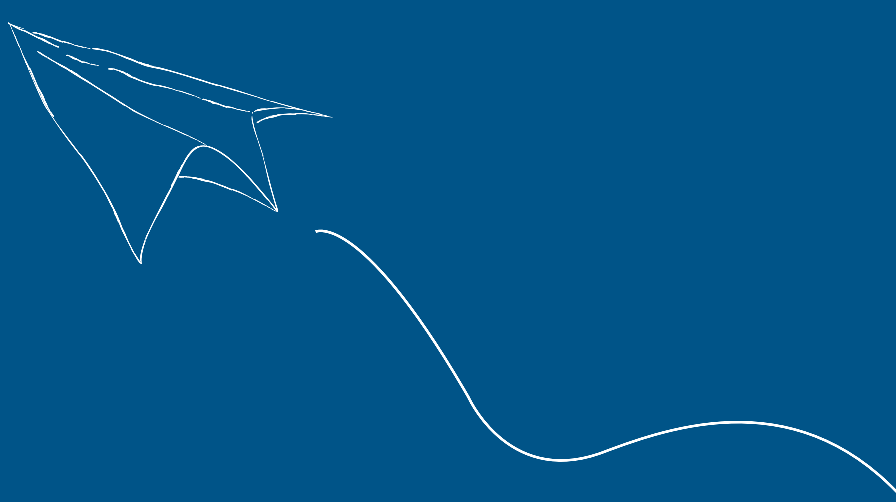
Life isn't static, neither is your business

GROW WEALTH AND FUTURE INCOME

BUSINESS OWNER
WEALTH TRANSFER STRATEGY

A tax-effective strategy to move assets from a corporation with the *Business owner wealth transfer*

For business owners, it can be challenging to tax-effectively get the value of assets or excess cash flow out of the business. Properly structured, the *Business owner wealth transfer* strategy is an effective way to move the value of a corporation's assets to personally benefit from the growth of the business, while offsetting the tax effect of doing so.



Meet David and Karen

Married, both age 35; experienced investors

David inherited ABC Inc. from his parents 10 years ago; it has grown into a successful, established business

David and Karen's current state

- David and Karen have been putting the majority of their earnings back into the company versus building assets outside of the company
- Karen has begun to contribute to registered retirement saving plan (RRSPs)
- David has been keeping his earnings in the business to avoid paying tax personally

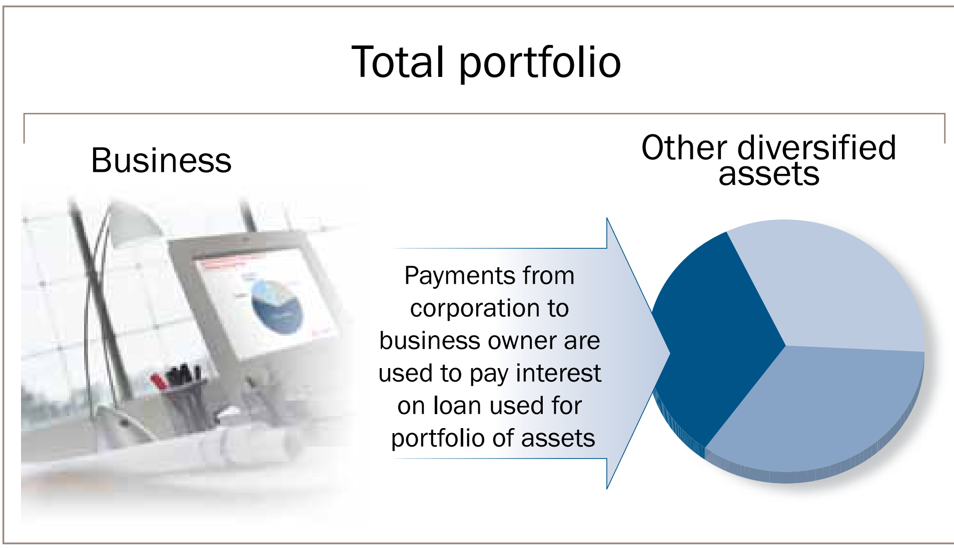
The situation

Income planning needs

- Reduce overall dependence on the corporation by using some of its assets to grow personal wealth
- Find tax-effective strategies to move assets from the company for personal use
- Create savings that can be used to protect against unforeseen events and for future income planning

The solution

After discussing risks associated with leveraging, David and Karen’s advisor suggests David consider the Canada Life’s *Business owner wealth transfer* strategy.



With this strategy, David secures a personal investment loan and purchases non-registered investments to diversify and grow wealth outside of the corporation. The business then pays a salary, or bonus that will be taxable to David, but may be deducted by ABC Inc., or alternatively pays David a taxable dividend from the business’ after-tax surplus. David uses the payments to pay the interest on the investment loan. The interest deduction from the investment loan offsets the tax arising from the income David receives.

Implementing the strategy

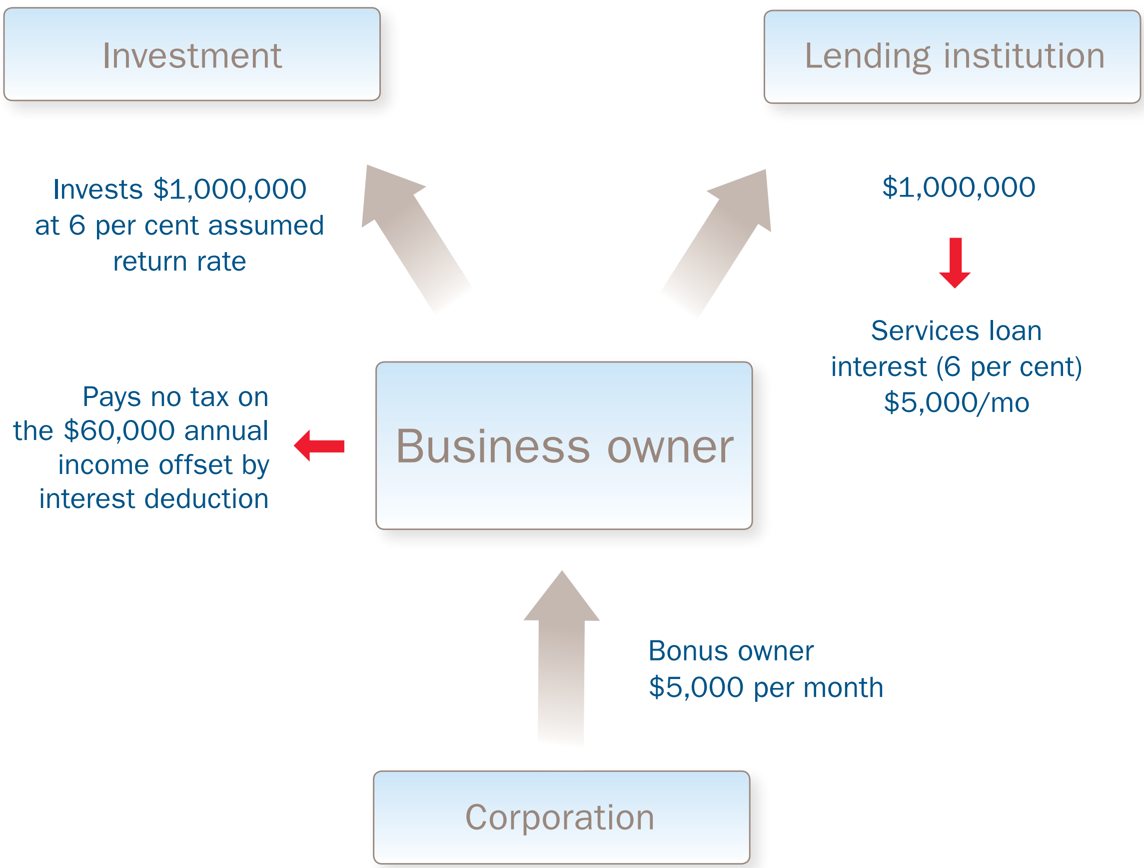
David secures a personal leveraged loan and invests it in a portfolio of non-registered funds with a 15-year time horizon for borrowing.

- David secures a $1 million[1] qualified interest-only investment loan – $5,000 monthly interest payments[2] and David invests in Canada Life non-registered segregated funds; these funds are collateral for the loan
- ABC Inc. pays David monthly income payments (i.e. salary, bonuses, or dividends) equal to $5,000
  - After 15 years, David receives income totalling $900,000 ($60,000 X 15) with little to no net-personal tax payable each year
  - He owns the investments outside the corporation
- David declares $60,000 annual income and $60,000 interest as a tax deduction
  - The salary he receives would be a deductible expense for the corporation and the corporation's tax would have been reduced as a result
- After repaying the bank loan and taxes on part of the investment, the final investment balance is **$1,300,776**

[1] Loans over $250,000 are approved on a case-by-case basis.

[2] Assuming the interest rate remains at six per cent during the loan period.

How it works



- After 15 years, capital is repaid to bank
- Owner retains $1,300,776 investment balance
- Corporation has paid owner $900,000 and obtained $135,000 tax deduction (assumed 15 per cent corporate tax rate)

The above example is for illustrative purposes only.
Situations may vary according to specific circumstances

Loan repayment calculations: 15 years later

After fifteen years, David would sell part of the segregated fund policy so after-tax proceeds can be used to repay the investment loan.

Business owner wealth transfer loan repayment calculations

Opening investment balance	$2,396,558
Segregated fund redemption amount needed to repay investment loan and capital gains tax	$1,095,782
Ending investment balance	$1,300,776

Summary of segregated fund redemption amount

Prorated ACB	$670,082
Capital gain	$425,700
Inclusion rate	50 per cent
Taxable capital gain	$212,850
Personal tax rate	45 per cent
Tax payable	$95,782
Net proceeds to pay investment loan	$1,000,000
Amount	$1,095,782

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Assumptions

- Six per cent investment rate of return
- Six per cent borrowing
- 15 per cent corporate tax rate
- 45 per cent personal tax rate
- Income earned consists of interest, dividends and potential capital gains; therefore, personal investment income assumes a 60 per cent tax inclusion mix
- 45 per cent personal tax rate

Investment loan option

Year	Beginning of year segregated fund investment balance	Annual growth 6%	Allocation (2%)	Tax out of pocket on allocation (60% inclusion mix, 45% personal tax rate)	Adjusted cost basis	End of year investment balance
1	1,000,000	60,000	20,000	5,400	1,020,000	1,060,000
2	1,060,000	63,600	21,200	5,724	1,041,200	1,123,600
3	1,123,600	67,416	22,472	6,067	1,063,672	1,191,016
4	1,191,016	71,461	23,820	6,431	1,087,492	1,262,477
5	1,262,477	75,749	25,250	6,817	1,112,742	1,338,226
6	1,338,226	80,294	26,765	7,226	1,139,506	1,418,519
7	1,418,519	85,111	28,370	7,660	1,167,877	1,503,630
8	1,503,630	90,218	30,073	8,120	1,197,949	1,593,848
9	1,593,848	95,631	31,877	8,607	1,229,826	1,689,479
10	1,689,479	101,369	33,790	9,123	1,263,616	1,790,848
11	1,790,848	107,451	35,817	9,671	1,299,433	1,898,299
12	1,898,299	113,898	37,966	10,251	1,337,399	2,012,196
13	2,012,196	120,732	40,244	10,866	1,377,643	2,132,928
14	2,132,928	127,976	42,659	11,518	1,420,301	2,260,904
15	2,260,904	135,654	45,218	12,209	1,465,519	2,396,558

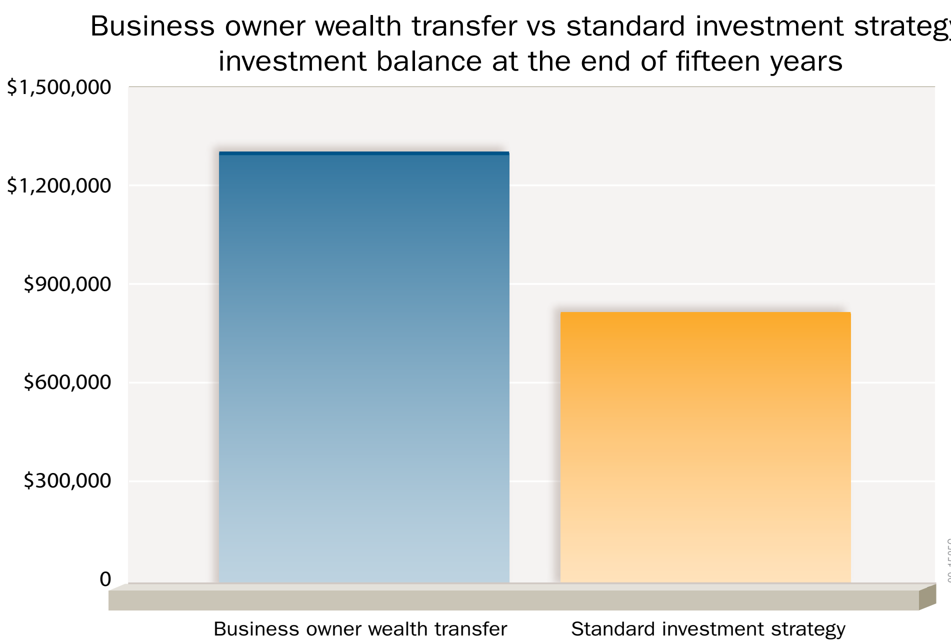
Standard investment loan option

Alternatively, David could simply invest a $5,000 monthly income, which he would draw from the corporation. If he chooses a monthly contribution plan instead of an investment loan, his investments into the segregated fund portfolio would be made with after-tax dollars. The final investment balance after 15 years is **$814,193**.

Year	Salary	Personal tax	After-tax investment deposit	Annual growth 6%	Tax on growth (60% inclusion, 45% personal tax rate)	End of year investment balance
1	60,000	27,000	33,000	1,980	535	34,980
2	60,000	27,000	33,000	4,079	1,101	72,059
3	60,000	27,000	33,000	6,304	1,702	111,362
4	60,000	27,000	33,000	8,662	2,339	153,024
5	60,000	27,000	33,000	11,161	3,014	197,186
6	60,000	27,000	33,000	13,811	3,729	243,997
7	60,000	27,000	33,000	16,620	4,487	293,616
8	60,000	27,000	33,000	19,597	5,291	346,213
9	60,000	27,000	33,000	22,753	6,143	401,966
10	60,000	27,000	33,000	26,098	7,046	461,064
11	60,000	27,000	33,000	29,644	8,004	523,708
12	60,000	27,000	33,000	33,402	9,019	590,111
13	60,000	27,000	33,000	37,387	10,094	660,497
14	60,000	27,000	33,000	41,610	11,235	735,107
15	60,000	27,000	33,000	46,086	12,443	814,193

Investment loan – 59 % advantage in growth

If David uses a standard investment strategy and invests his $60,000 yearly salary, after tax, the investment balance at the end of fifteen years would be less than with a *Business owner wealth transfer* strategy.



- Traditional strategy: $814,193
- *Business owner wealth transfer* strategy: $1,300,776 or **59 per cent advantage in growth**

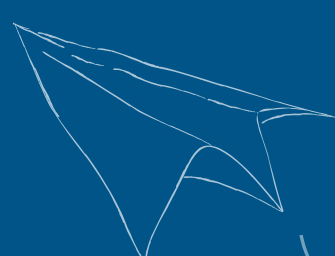
Tax considerations

- It's recommended business owners talk to their tax advisor to understand the conditions necessary to deduct personal loan interest for tax purposes and understand how their investment may be considered eligible for an interest deduction.

Protection with 100/100 guarantee segregated fund policy

The 100/100 guarantee segregated fund policy is appealing for business owners who want to guarantee their investment loan is covered on their death and/or at maturity.

Segregated funds offer many protection features, including the potential for creditor protection; also, after 15 years a 100 per cent maturity guarantee may benefit business owners looking to protect their personal savings prior to retirement. The 100 per cent death benefit guarantee is also valuable for those planning to leave something for beneficiaries outside of the business.



Traditional investments assumes fixed-income investments.

In Quebec, advisor refers to a financial security advisor for individual insurance and segregated fund policies; and to an advisor in group insurance/annuity plans for group products.

Canada Life™

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For individual circumstances, consult with your accountant, lawyer and tax advisor.

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