

# What does life insurance have to do with proposed intergenerational business transfers? - Lots

By: Florence Marino B.A., LL.B., TEP  
Vice President, Tax & Estate Planning

The business succession tsunami (See: [Succession Tsunami: Preparing for a decade of small business transitions in Canada \(cfib-fcei.ca\)](#)) expected in the next decade in Canada should not come as a surprise. Demographic factors, growth in business values, and yes, even positive changes to income tax rules contribute to this wave. After a private member's bill (Bill C-208) enacted June 29, 2021, forced the government's hand, the Department of Finance has after nearly two years, proposed a framework for genuine intergenerational business transfers.

This framework originally announced in the 2023 Federal Budget allows transfers that comply with the rules to occur on the same footing as arm's length sales – that is – the buyer is permitted to use a corporation they own to make the purchase so that after-tax corporate income can be used to fund the purchase. The vendor will have capital gains treatment on the sale of the shares, use of the capital gains reserve over 10 years and access to the lifetime capital gains exemption - not deemed dividend treatment imposed under subsection 84.1(1) of the Income Tax Act (the Act).

Here is a prior article on framework provided by the original proposals: [As a matter of tax - April 2023 | Manulife Advisors](#)

## Recent technical changes

August 4, 2023 draft legislation made some significant technical changes to the original proposals but the framework largely remains intact.

The revised proposals will allow the exclusion from section 84.1 to be used only once. Subsequent transactions are subject to deemed dividend treatment. Even transfers previously carried out pursuant to enacted Bill-C208 could be impacted by this change on a future transfer of shares. In September, the Conference for Advanced Life Underwriting (CALU) made a submission seeking that this measure be removed entirely as it fundamentally changes the flexibility that appeared to have been supported by the original proposals.

However, some welcome changes were made. These include: clarification that “management” refers to direction or supervision of business activities and not the provision of advice – enabling parents to still be a resource to children after the transfer; the addition of a relieving provision that enables certain subsequent transfers of shares between children; and, in addition to the relieving provision for death or disability of a child (where they are unable to satisfy the control, service, management or continuing active business conditions of the rules), relief is provided for distribution of business assets to satisfy creditors.

## **Use of life insurance**

Life insurance on the parent, in the short term, can be used to cover the debt outstanding to the parent and complete the buy-out in the event of their death. If there is existing insurance on the parent held by the corporation, unlike in a sale to an arm’s length third-party, there is no need to transfer the policy out of the corporation. Such transfers usually come with ugly tax consequences. Retention of existing insurance on a parent can accomplish estate equalization goals and fund remaining tax liabilities particularly in respect of preference shares that may be retained by a parent. Life insurance on the children can provide assurance to the parent that the buy-out will be completed in the event of premature death of a child. It also is important to the business, providing key person protection and, ultimately to the child and their family in funding the ultimate tax liability they will face for growing business values.

And, where a business transfer does not qualify under these specific intergenerational transfer rules, insurance should be considered in respect of any business transfer whether in the context of a freeze or a sale of business to an arm’s length third party to fund the deferred tax liabilities that result.

## **What’s next?**

This draft legislation has not yet been introduced but is expected to be introduced and enacted this fall. The rules will apply to business transfers on or after January 1, 2024.

## **FOOTNOTE:**

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