

How to prepare for intergenerational business transfers before key tax-related changes kick in

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With pending changes to Bill C-208 and the alternative minimum tax (AMT) in the new year, accountants and advisors are in a time crunch helping clients who are selling their business to a family member while it's still advantageous to do so from a tax perspective.

[Bill C-208](#) provided families with more flexibility with intergenerational business transfers by giving the seller the ability to utilize the current \$971,000 in lifetime capital gains exemption (LCGE). But as of Jan. 1, 2024, more stringent conditions will be required to prove that a business transfer between family members is a genuine transaction, says Kevin Burkett, partner at Burkett & Co. Chartered Professional Accountants in Victoria.

Requirements include the child working in the business for a longer period and retaining legal control. But Mr. Burkett says the main difference effective next year involves the company's voting and growth shares.

“Parents must transfer the majority of voting shares and at least 50 per cent of growth shares at the time of transfer and the remaining voting and growth shares 36 months afterward,” Mr. Burkett explains.

Michelle Connolly, senior vice president, advanced tax and estate planning, at Wellington-Altus Private Wealth Inc. in Toronto, notes that most advisors have been reaching out to business owner clients over the past few years about business succession, whether it be next-generation family members or arm’s length third parties.

“Throughout 2023, we have been looking at specific situations in which the intention is to structure an intergenerational transfer,” she says. “If the successor isn’t going to be a family member, the announced Bill C-208 measures are not a concern.”

How the AMT changes factor in

Meanwhile, the revised AMT will likely [impact business succession planning](#), particularly in cases in which it’s structured as a sale of shares. Ms. Connolly notes that as of Jan. 1, the AMT capital gains inclusion rate will increase to 100 per cent, up from 80 per cent now, and the AMT tax rate will be rise to 20.5 per cent from 15 per cent.

Ms. Connolly says the AMT is a numbers and proportion game. If a business owner is selling their shares and makes \$15-million in capital gains, or a business owner reports a \$2-million capital gain, and \$1-million is sheltered from taxes by using the LCGE, it “will likely trigger [the] AMT.”

Scott Plaskett, certified financial planner and chief executive officer at Ironshield Financial Planning in Toronto, notes that even though capital gains have a 50 per cent inclusion rate after the LCGE is used up, the AMT calculation will likely push the amount of taxes business owners pay much higher.

He is using these upcoming tax changes as an opportunity to examine whether his applicable clients have structured their businesses efficiently, from a tax perspective, so they qualify for the LCGE in the first place. He notes that a lot of owners are so focused on the business, they fail to consider that issue.

To qualify for the LCGE, Mr. Plaskett says the business must be incorporated at the time of a sale when the shares are sold. Also, more than 50 per cent of the business’s assets must have been used in an active business in Canada for 24 months prior to the sale.

He adds that incorporation likely makes sense for businesses that make more money than is paid out to the owner and employees.

“There’s no sense in paying personal taxes on all that money when you can retain it in the company at a lower tax rate,” he explains.

Creating a holding company to avoid liabilities

The next step is for the retained money to be moved and protected in a holding company.

“We move the surplus wealth away from the operating company into the holding company, protecting it from the liabilities of the operating company,” he explains. “Doing so also allows it to maintain its lower tax rate.”

Business owners may also incorporate to avoid exposing their personal assets to the liabilities of the corporation.

Mr. Plaskett also likes to discuss clients’ future plans to sell the business to get a handle on their thinking. While many may not have a succession plan, the discussion gets them thinking about the possibilities.

“I ask, ‘[Is your business] a personal services corporation once you’re gone, so the business isn’t worth anything? Or, could the business be worth something to someone else in the future?’” he says.

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