<u>Why Have the Holdco Own the Insurance for the Shareholders' Agreement?</u>

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There has been a lot of discussion lately about who should own the insurance contracts funding a shareholders' agreement.

Generally, where possible, we like to see a holding company own the contract; the opco is the revocable beneficiary and the holdco is reimbursed for the premium on a "market value" basis; for example, the cost of a competitive product that would provide similar benefits.

There are a number of good reasons to set up the insurance ownership this way including creditor proofing and, most importantly, maintaining control of the policy in the event of a change in ownership in the operating company.

It can be both awkward and expensive to transfer a life insurance policy out of an operating company back to a shareholder (executive) who has left or is changing his/her relationship. If there has been a change in health or other product changes (for example the dramatic increases in Universal Life costs recently), the policy may have become quite valuable and will need to be transferred at <u>fair market value</u>. This could result in tax payable on the "shareholder benefit".

Calculating the appropriate premium to be charged to the opco should be done with care and the shareholders' agreement should provide remedies, penalties, and adjustments in the event the insurance proceeds are not available to fund the share purchase/redemption arrangements. In order to minimize tax risks, planning should also take into account various statements that the CRA has made on the subject of corporate beneficiary designations. Consultation with tax advisors is a must. (For additional background, please refer to the CALU articles section, "July 2010 – CRA Roundtable", Question 2).