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How Business Owners can create a "Gold Plated Pension"

Looming tax changes may negatively affect high net worth business owners owning significant passive investments earmarked for their future. This may leave some looking at other methods to maximize savings and investments in a tax effective fashion going forward. One avenue that has been available for a long time is a company-sponsored Personal Pension Plan or PPP. Think of this as a "supersized" RRSP with superior characteristics and benefits.

If you own a private incorporated business (or you are an incorporated professional), and are planning for your future retirement - this article is a must read for you.

What is a Personal Pension Plan?

In general, a personal pension plan is a corporate-sponsored retirement investment solution for the business owner or incorporated professional. It is designed to provide a reliable source of personal retirement income. The pension plan can also include key personnel and family members who work in the business. It also acts as a great estate planning tool, not just for yourself, but especially for your children if they will be taking over the business someday.

Considering that the pension plan is funded by the business, it is a tax-deductible expense against business income. Also, since it falls within the parameters of Canadian pension laws, it's also one of the most "bullet proof" creditor protected assets available.

Is it just like an RRSP?

While personal pension plans have many similarities to traditional RRSP's, there are several key material differences that make this a superior method to plan for retirement. For one, the annual contribution limits are greater, thus allowing for a larger pool of money over an RRSP. Here are some major highlights that differentiate it from a traditional RRSP:

	Pension Plan	RRSP
Maximum contribution limit	up to $43,532*	$26,230
Flexibility to choose contribution options (defined benefit/contribution)	yes	no
Fiduciary oversight	yes	no
Tax deductible admin and investment management fees	yes	no
HST 33% credit refund	yes	no
Deduction on interest of borrowing	yes	no
Ability to make additional tax deductible contributions during market volatility	yes	no

**enhanced contribution amounts are dependent on age.*
Source: INTEGRIS Pension Management Corp.

Additional Features:

"Business owners have a tendency to focus on taxes, profit margins, employees or other business related matters. Don't forget to take care of YOU too"

Income splitting - Tax crackdowns are putting the squeeze on business income splitting among spouses. While a pension plan doesn't solve that problem right now – it can in the future. Once you retire and start drawing an income from your pension, that money is defined as pension income under the tax act. This will not only qualify for the pension credit, but this income can be split with a spouse. As such, a spouse need not draw a salary from the company for this tax break to apply.

Estate Planning – The pension plan can be passed to a spouse on a tax deferred basis upon death. In addition, for a family business, the pension assets can be passed taxed-deferred to the adult children who are plan members and have taken over the business. By contrast, RRSP assets in the same situation are subjected to a 'deemed disposition' and become taxable to the estate. In this case, the pension can continue to grow and survivors use the assets left behind in the plan to fund their own retirement. Moreover, unlike a public sector-style pension plan, which ceases payments upon last-to-die, any named beneficiary can inherit the remaining assets in the pension after death through the more flexible surplus rules of the PPP. Just be aware that pension laws dictate spousal priority rights upon death or marriage breakdown unless he or she waives them.

Existing RRSP's - What should you do with your existing RRSP? A popular option is to roll it under the pension umbrella using a "sub account" called an "additional voluntary contribution (AVC)" account that is part and parcel of the PPP. Once transferred, it retains the same RRSP characteristics, however, an added benefit is that you'll now be allowed to deduct expenses associated with the RRSP such as commissions, admin, or investment management fees. Moreover, it will also enjoy the same creditor protection as the pension. As an extra bonus, these ex-RRSP assets can now be invested in new asset classes that are pension-eligible but unavailable to RRSP customers (such as some types of private equity, real estate, mortgages etc.)

Succession Planning – Whether you plan on selling your business or passing it down to the next generation, a pension plan can offer some additional flexibility and security. There can be many pitfalls when exiting a business, one of which might be the sale price of your business. After all, YOU might be the one providing a lot of the business value, and without you, the business may not be worth as much. The strategy of exiting using a family succession plan can be rewarding or filled with unforeseen conflict. The Canadian Federation of Independent Business says many businesses have an increased failure rate when passing to the next generation. That failure rate increases further after the third generational transfer. Considering these future unknowns, a pension plan not only offers great creditor protection against future business hurdles, it also protects YOU as it relates to your income needs during retirement. Upon retirement, one option could be to "port" the commuted value of your pension, and enjoy the next phase of your life.

Early Retirement & Perks – If you decide to retire early, an extra tax-deductible contribution can be made known as "terminal funding". This bridges the gap between what you would have received at age 65 and what is normally paid when you start receiving a pension early. Also, an additional top-up can be made to purchase "indexing", an inflation protection feature. Terminal funding amounts are fully tax-deductible to your business, do not create an 'income inclusion' and can often reach over $1,000,000 depending on the situation.

Conclusion

A professionally-managed personal pension plan could be the right solution for you to ensure your financial future, while tax efficiently removing money from your corporation over time. It can also form an important part of your strategy for succession planning. The summary above only captures a portion of the tax advantages that PPPs offer. To find out more information and to determine if this is right for you, please contact me directly. Alternatively, you can ask your accountant to contact me with any questions.

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