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Barristers and Solicitors

Estate Freezes and Other Corporate Restructuring During COVID-19

An estate freeze is a common planning mechanism that allows a deferral of tax on the capital gain in a corporation. The estate freeze allows for the interest held by the creator of the company in the corporation to be converted into voting preference shares with the common shares, expected to increase in value with the corporation, owned by the children. The preference shares will retain voting control.

In some situations, including the economic downturn resulting from the COVID-19 pandemic, an estate freeze may not function as intended. The value of the common shares, which had been expected to hold the increase in value, may even fall below the value of the preference shares retained by the original owner/parent.

In light of declining business values that we are seeing in many cases, it may be prudent to consider further planning options available where an estate freeze does not function as intended. Below is a brief summary of common strategies that may be available to amend or reverse an estate freeze:

- **Estate Refreezing:** Especially where the value of the common shares of the corporation unexpectedly decrease after the initial estate freeze, it may be appropriate to repeat the estate freeze process. This further alteration of the corporate structure can be accomplished by converting either the preferred voting shares held by the parent or the common shares held by the children (or in trust for them) into new fixed-value preferred shares.
- **Estate Thaw:** An estate thaw sees the parent reacquire the future growth in value of the corporation, in part or entirely. This reversal of the effect of an estate freeze can be accomplished by the return of the common shares from the children to the parent, the conversion of the parent's preferred shares into common shares, or, if a discretionary family trust is used to implement the initial freeze, the distribution of the growth shares to the parent (subject to the terms of the trust).
- **Estate Melt:** An estate melt can have the same effect as an estate thaw, without necessarily changing the structure of the corporation. The parent may reacquire growth in the corporation through his or her salary and/or bonuses, management fees, a share redemption, or another mechanism that does not require the return of common shares.

It is important that estate planning lawyers are aware of these options that might be available when the implementation of an estate freeze has gone awry. As with the initial estate freeze, tax and financial planning professionals should be consulted to assist clients in determining which option might be best for them.