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Retirement Planning for an Entrepreneur

A multi-faceted challenge.

May 15, 2019

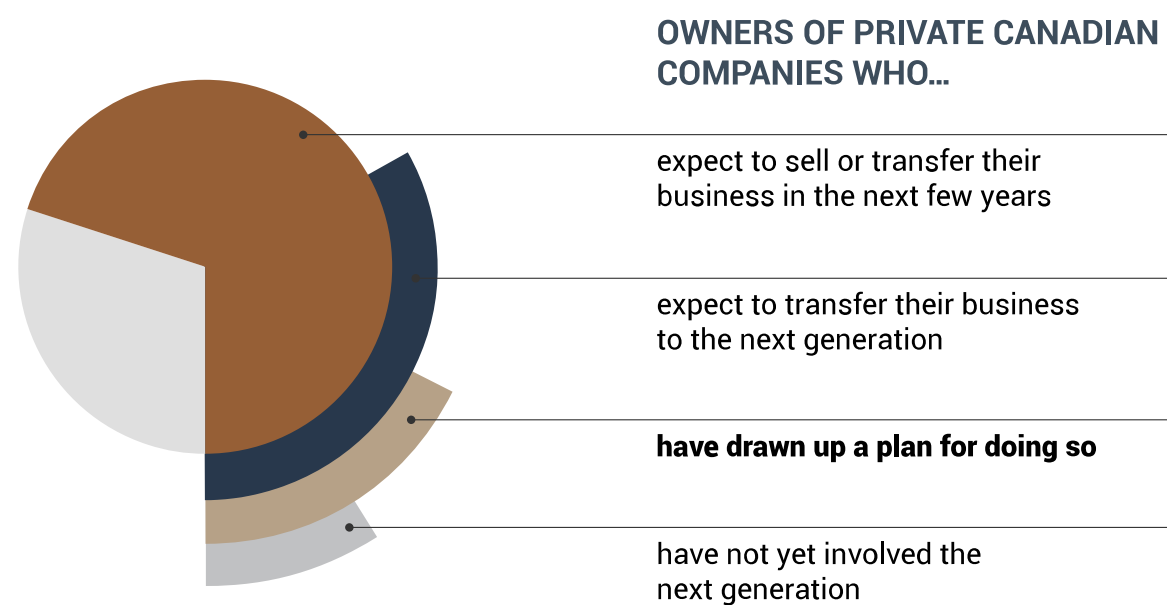
Retirement planning demands rigor and discipline. For people who own their own company, the challenge can be that much greater, since it often includes a desire to transfer ownership of the business.

In the next few years, many owners of private Canadian companies are planning to pass the torch. However, as illustrated below, it seems as though only a minority of them have come up with a plan for doing so.



Are entrepreneurs ready to pass the torch?

Maybe not, if we can trust the numbers



Source: PWC / Graphics: Actualis

The business takes priority

Why is this the case? It would seem that business owners, especially those with small or medium-sized companies, have a tendency to prioritize day-to-day management and business growth, and simply don't have time to plan for the next phase. Consequently, like someone who has invested everything in a house, the entrepreneur ends up with a potentially large value – that of the business – which is very concentrated and not necessarily liquid: there is no guarantee of getting the desired price at the desired terms, nor of finding a buyer. For instance, consider the case of a record store owner who had planned to finance his or her retirement by selling the business... around the end of the last decade.

Challenges and solutions

In this context, business owners face a number of specific challenges, and it might be advisable to find solutions well before the time comes to retire.

Convert the market value of the business into retirement capital

Surveys show that entrepreneurs have a tendency to underestimate the time and effort required to successfully sell or transfer their business. While, on average, they allow about three years for this, in reality it can take up to seven or eight years to complete such a transaction. This gap between perception and reality can make the difference between a comfortable retirement and one that is plagued by worries.

Manage the tax shock

Unlike individuals who expect to draw years and years of retirement income from an employer's pension fund or an RRSP, entrepreneurs who sell their business could end up with substantial capital, but part of it might be immediately subject to capital gains tax. Various strategies can help to ease, spread or delay the tax shock, as long as these are implemented ahead of time, with the advice of professionals.

Have a Plan B

In the eventuality that the business doesn't find a buyer, or finds a buyer, but not at the expected price, it could be important for the owner to further diversify his or her assets so that the whole retirement plan does not rest on a single source of value. One tool that might be worth considering is an Individual Pension Plan (IPP), which is roughly equivalent to a registered pension plan that the entrepreneur sets up for him- or herself.

Consider catch-up strategies

For entrepreneurs, an IPP can be one way of implementing a retirement income catch-up strategy. However, this can be complicated to administer. If preferred, another option would be to simply set up an accelerated savings strategy that could, in particular, take advantage of any unused RRSP contribution



room. Entrepreneurs could also sit down with their mutual fund representative to decide whether it might be appropriate to review their portfolio risk level in order to spur the growth of the part of their wealth that is not tied up in the business.

Structure the business to protect accumulated capital

Finally, it might be of benefit for entrepreneurs to structure their businesses in a way that could protect their retirement capital from the company's operating risk. One frequently used way of doing this is to set up a holding company. Other approaches could also be discussed with tax professionals, particularly in the context of estate planning.

As we can see from this brief overview, retirement planning for entrepreneurs can involve a number of components that present a large degree of complexity. So getting some advice could be the first step to setting up an effective retirement plan.

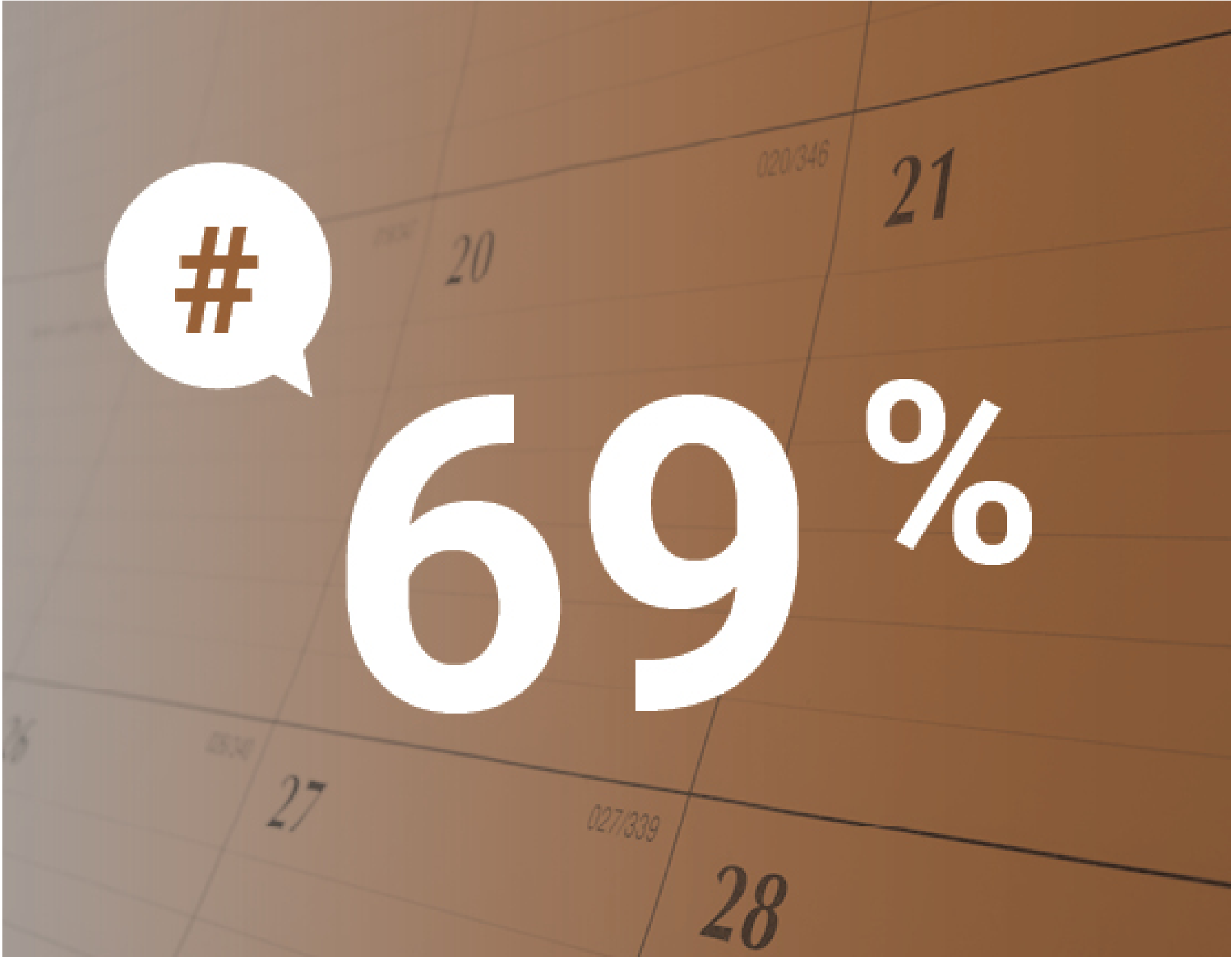
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