

Your Company Name

Corporate Redemption of Shares

November 16, 1999

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"Pay the cost of your Corporate Share Redemption Insurance from your company bank account and minimize the impact of capital gains taxation at death!"

Many shareholders of small, privately-held companies are unaware that:

- * Proceeds from a life insurance policy received by a private corporation result in a credit to the corporation's "Capital Dividend Account" and that when a corporation has a positive capital dividend account balance it may pay tax-free capital dividends to its shareholders.
- * An insurance funded corporate share redemption strategy using corporate owned life insurance can reduce capital gains taxes and that payments for the insurance are payable with corporate dollars which are often less expensive than after-tax individual dollars.
- * Life insurance can be issued on a less expensive "joint second-to-die" basis in situations where the proceeds are not needed until the death of the surviving spouse.

A life insurance policy that qualifies under Section 148 of the Income Tax Act is an excellent planning tool that can create a growing tax-advantaged account. This account is accessible and under your control while all of the shareholders are alive and is paid out to the company (as the designated beneficiary) at death. If you choose a Universal Life policy, any additional cash flow available, due to tax savings using your corporate tax rate, can accumulate in the "tax-exempt" policy; allowing you to stop paying premiums.

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The illustration compares the effectiveness of accumulating the cash to fund the buyout inside the company using traditional (non tax-deferred) methods with an exempt life insurance policy.

The redemption of shares from a shareholder by a corporation is usually carried out under the terms of a Buy-Sell Agreement that spells out the terms of the redemption and funding through a corporate-owned life insurance policy. The redemption is triggered by the death of the shareholder.

Upon the death of the shareholder, the proceeds from the corporate-owned policy are received tax-free by the corporation. Most, if not all of the proceeds are credited to the corporation's Capital Dividend Account.

On December 27, 1997 new provisions under section 112(3) of the Income Tax Act (ITA) were adopted that have impacted insured redemption of shares strategies.

Under the new "stop-loss" rules, the full amount of the capital gain can no longer be offset. It is still possible to carry-back the loss in the same manner as previously allowed to eliminate the gain occurring in the deceased shareholder's terminal taxation year due to the deemed disposition of the shares of the operating company. The maximum that can be received as capital dividend by the estate of the deceased on the purchase for cancellation of its shares, however, is now limited to 25% of the gain deemed realized by the deceased. This means any additional dividends resulting from the corporate repurchase for cancellation are classified as ordinary dividends. These dividends are now taxable to the estate.

As a result, many new buy-sell arrangements combine the Corporate Redemption of Shares approach with a criss-cross method of buying and selling shares between the spouse or the estate of the deceased shareholder and the surviving shareholder(s). Under the first approach, the shares are sold to the corporation and payment is usually in the form of a capital dividend to the shareholder's spouse or estate. The second approach usually involves promissory notes that are redeemed with tax-free capital dividends paid by the corporation to surviving shareholders.

This illustration focuses only on the "Corporate Redemption of Shares" part of any buy-sell arrangement. It shows that exempt life insurance can deliver the cash at the time it is needed for an investment known in advance. It does so in a considerably more cost-effective manner than accumulating the needed cash using the traditional Alternative Investment method.

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The illustrated values in the Alternative Investment take into account that earnings of the fund are considered investment income and are not subject to the small business deduction; they are taxed at the high corporate rate. The Income Tax Act requires that an extra refundable tax on investment income be collected. The extra rate is 6 2/3% on income from investments and taxable gains. Income from investments in the form of dividends is subject to 33 1/3% tax. The tax is credited to a notional tax account called the Refundable Dividend Tax On Hand (RDTOH) account. When the corporation pays taxable dividends to its shareholders, the tax is refunded at a 3:1 rate, regardless of what rate the RDTOH was collected.

The arrangement of a Corporate Redemption of Shares Buy-Sell Agreement is complex. There are many issues to consider that are beyond the scope of this illustration. The advice of an accountant and/or lawyer should be sought.

NOTE: The dividend tax rate is calculated as follows:

$$\text{Dividend Tax Rate} = 1.25 \times (\text{MarginalTaxRate} - 0.2)$$

Withdrawals from the policy may be subject to income tax, depending on the Adjusted Cost Basis (ACB) of the policy, at the time of withdrawal. However, the proceeds of a life insurance policy upon death of the insured are received tax free in the hands of the beneficiaries.

This is an illustration only and NOT a Contract. Rates of return and values contained within are projections only and are not guarantees or forecasts of future performance. It must be read in conjunction with a policy illustration from the Life Company.

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CONCEPT ASSUMPTIONS

Insureds

Joint Insured #1: Serge Client,
Male Age 57 Non-Smoker
Joint Insured #2: Mary Client,
Female Age 50 Non-Smoker

Prepared By:

Name: MR. AGENT

Product

Name: Universal Life
Policy Type: Joint Last-To-Die
Face Amount: \$300,000
Payment Method: Planned Deposits (20 Years)
Projected Annual Growth Rate: 7.000% (Years 1 - 20)
6.000% (Years 21 - 30)
5.000% (Years 31 - 69)

Alternative Investment

Growth Breakdown: 100% Interest
Effective Tax Rate On Interest: 54.67%
Projected Annual Growth Rate: 7.000% (Years 1 - 20)
6.000% (Years 21 - 30)
5.000% (Years 31 - 69)

Other Details

Corporate Tax Rate: 48.00%

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ACCUMULATING FUNDS WITHIN A COMPANY THROUGH PERIODIC DEPOSITS FOR CORPORATE REDEMPTION OF SHARES

Pol Yr	Age	Per. Deposit	Annual Growth	Tax				Total Dividend	Shareholder	
				Due on Growth	Unrealized Capital Gains (if any)	Due on Fund Available Corporate Redemption	Refund of RDTOH		Tax Payable	After-Tax Value to Shareholder
1	31	4,000	280	153	0	4,127	75	4,202	1,576	2,626
2	32	4,000	569	311		8,385	152	8,537	3,201	5,335
3	33	4,000	867	474		12,778	231	13,009	4,878	8,131
4	34	4,000	1,174	642		17,310	313	17,623	6,609	11,015
5	35	4,000	1,492	816		21,986	398	22,384	8,394	13,990
6	36	4,000	1,819	994		26,811	485	27,296	10,236	17,060
7	37	4,000	2,157	1,179		31,789	575	32,364	12,136	20,227
8	38	4,000	2,505	1,370		36,924	668	37,592	14,097	23,495
9	39	4,000	2,865	1,566		42,223	764	42,987	16,120	26,867
10	40	4,000	3,236	1,769		47,689	863	48,552	18,207	30,345
11	41	4,000	3,618	1,978		53,330	965	54,295	20,360	33,934
12	42	4,000	4,013	2,194		59,149	1,070	60,219	22,582	37,637
13	43	4,000	4,420	2,417		65,153	1,179	66,331	24,874	41,457
14	44	4,000	4,841	2,646		71,347	1,291	72,638	27,239	45,399
15	45	4,000	5,274	2,883		77,738	1,407	79,144	29,679	49,465
16	46	4,000	5,722	3,128		84,331	1,526	85,857	32,196	53,661
17	47	4,000	6,183	3,380		91,134	1,649	92,783	34,794	57,989
18	48	4,000	6,659	3,641		98,153	1,776	99,929	37,473	62,456
19	49	4,000	7,151	3,909		105,394	1,907	107,301	40,238	67,063
20	50	4,000	7,658	4,186		112,865	2,042	114,908	43,090	71,817
25	55		7,573	4,140		129,641	2,020	131,661	49,373	82,288
30	60		8,660	4,734		148,257	2,310	150,566	56,462	94,104
35	65		8,144	4,452		166,572	2,172	168,744	63,279	105,465
40	70		9,110	4,980		186,324	2,430	188,754	70,783	117,971
45	75		10,190	5,571		208,419	2,718	211,136	79,176	131,960
70	100		17,845	9,756		364,982	4,759	369,741	138,653	231,088

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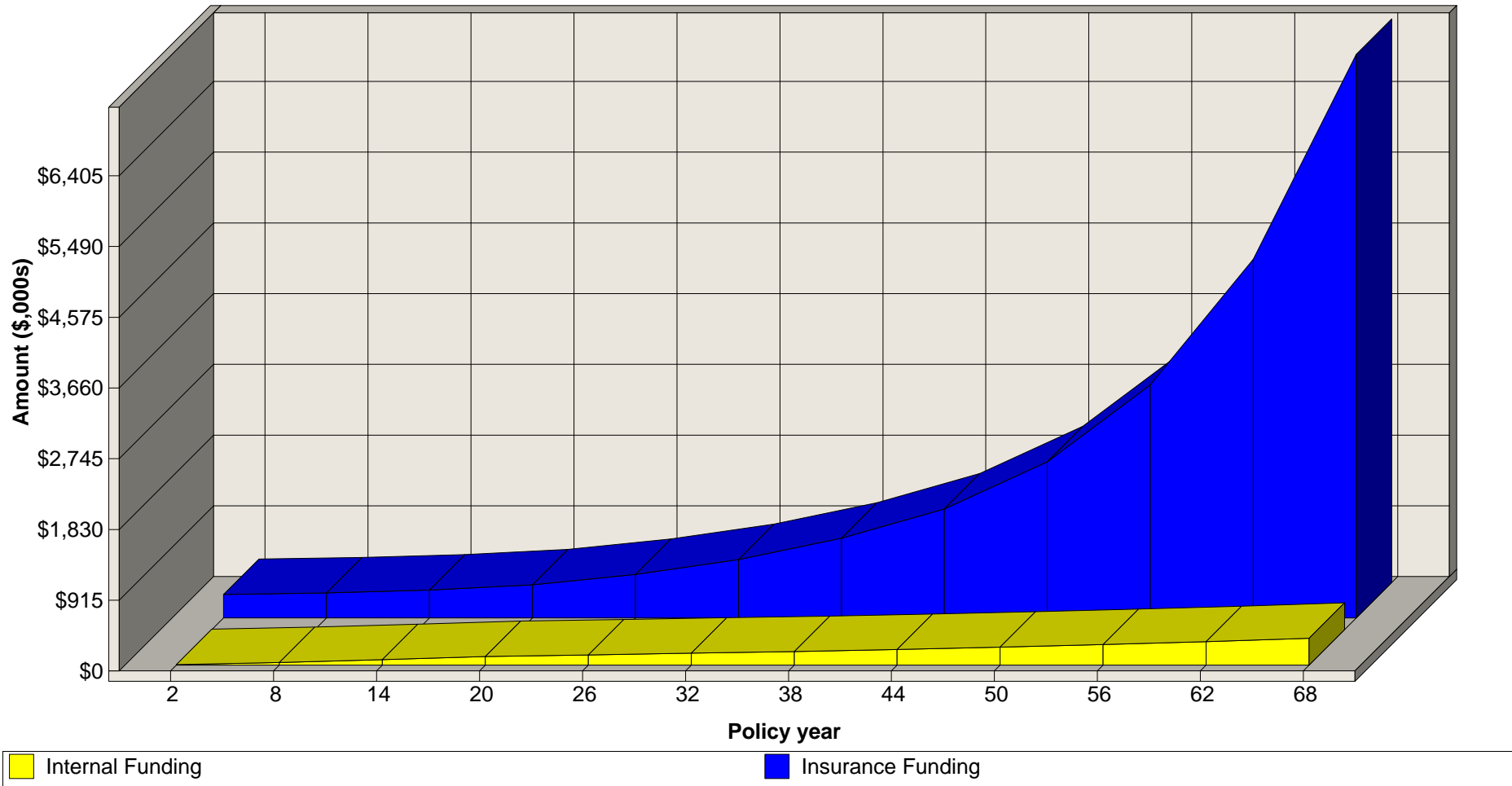
CREATING FUNDS THROUGH PERIODIC DEPOSITS IN A LIFE INSURANCE POLICY FOR CORPORATE REDEMPTION OF SHARES

Pol Yr	Age	Periodic Deposit	Life Insurance Corporate Asset Builder			Comparison		
			Insurance Proceeds	Credit to Capital Dividend Account	ACB	After Tax Value for Share Redemption	CAB Value less AI Value for Share Redemption	Percent Increase Using Corporate Asset Builder
1	31	4,000	303,335	299,458	3,877	301,881	299,255	11396%
2	32	4,000	306,904	299,162	7,742	304,001	298,665	5598%
3	33	4,000	310,723	299,128	11,595	306,375	298,244	3668%
4	34	4,000	314,809	299,376	15,433	309,022	298,007	2706%
5	35	4,000	319,368	300,112	19,256	312,147	298,157	2131%
6	36	4,000	324,293	301,232	23,061	315,645	298,585	1750%
7	37	4,000	329,612	302,764	26,848	319,544	299,317	1480%
8	38	4,000	335,356	304,739	30,617	323,875	300,379	1278%
9	39	4,000	341,561	307,199	34,362	328,675	301,809	1123%
10	40	4,000	348,376	310,296	38,080	334,096	303,751	1001%
11	41	4,000	355,755	313,981	41,774	340,090	306,156	902%
12	42	4,000	363,742	318,304	45,438	346,703	309,066	821%
13	43	4,000	372,389	323,320	49,069	353,988	312,531	754%
14	44	4,000	381,750	329,089	52,661	362,002	316,604	697%
15	45	4,000	392,099	335,891	56,208	371,021	321,556	650%
16	46	4,000	403,329	343,643	59,686	380,947	327,286	610%
17	47	4,000	415,514	352,416	63,098	391,852	333,863	576%
18	48	4,000	428,736	362,298	66,438	403,822	341,366	547%
19	49	4,000	443,083	373,383	69,700	416,946	349,882	522%
20	50	4,000	458,650	385,772	72,878	431,321	359,503	501%
25	55		563,023	496,153	66,870	537,947	455,659	554%
30	60		707,115	652,273	54,842	686,549	592,445	630%
35	65		894,548	863,024	31,524	882,727	777,261	737%
40	70		1,143,405	1,143,405		1,143,405	1,025,434	869%
45	75		1,494,037	1,494,037		1,494,037	1,362,077	1032%
70	100		8,504,070	8,504,070		8,504,070	8,272,982	3580%

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Proposal For: Mr. & Mrs. Client Prepared By: MR. AGENT

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Male 30 NS. PRODUCT: Universal Life. FACE AMOUNT: \$300,000. TAX RATE: 50.00%

AI RATE SPREAD: 0.00%.

NOTE: F.V. shown as portion of D.B. Must accompany a policy illustration. E.&O.E.