

INITIATIVE

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Corporate Owned Insurance: Do you have an insurable interest?

Many situations arise where the shareholder of a corporation wants to insure a relative (most often a parent or sometimes a spouse) who has no connection with the corporation.

The main issue is whether or not the proposed owner of the life insurance policy, the corporation, has an insurable interest in the life insured such as a parent with no involvement or financial interest in the corporation.

The tax consequences of having a corporation pay for insurance on a family member with no connection to the business give rise to a taxable benefit for the amount of the policy premium paid each year. The Canada Revenue Agency has access to several provisions of the Income Tax Act (Canada), to confer a benefit such as assess a shareholder benefit under Subsection 15(1), assess a benefit conferred on a person under Subsection 246(1), or assess a benefit under other subsections.

Let us look at an alternative. The following is a comparison of the amount of pre-tax corporate income required to pay an insurance premium of \$1,000 assuming all funds are derive from a corporation subject to the small business rate.

Assumptions (see table)

- Corporate small business tax rate:16%
- Personal taxable benefit tax rate:..... 35% and 45%
- Personal non-eligible dividend tax rate:22% and 33%

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The Initiative is a monthly case study and information brief for distribution partners of The Empire Life Insurance Company (Empire Life). Details are edited to illustrate relevant financial, tax & estate planning principles, generally using the Federal context. This material is current to the year and month of issue (Vol. yy, No. mm) but is not a tax or legal opinion. Retained professional advice should be engaged in relation to any actual Client matters.

The Sales, Tax, Estate Planning, Underwriting & Product (STEPUP) team provides broker support, including seminar education, advanced concept illustrations & Client case consultations.

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	Corporately Owned Mid Personal Tax Rate	Corporately Owned High Personal Tax Rate	Personally Owned Mid Personal Tax Rate	Personally Owned High Personal Tax Rate
Pre-tax Income required	1,190.48	1,190.48		
Corporate tax	-190.48	-190.48		
Insurance premium	1,000.00	1,000.00		
Taxable Benefit	1,000.00	1,000.00		
Personal tax on benefit	-350.00	-450.00		
Dividend required	448.72	671.64	1,282.05	1,492.54
Dividend required	-98.72	-221.64	-282.05	-492.54
Net to individual	350.00	450.00	1,000.00	1,000.00
Insurance premium	-	-	1,000.00	1,000.00
Pre-tax Income required	534.19	799.57	1,526.25	1,776.83
Corporate tax	-85.47	-127.93	-244.20	-284.29
Dividend to individual	448.72	671.64	1,282.05	1,492.54
Total pre-tax income	1,724.66	1,990.05	1,526.25	1,776.83

In this example, it requires less net income to fund a personally owned life insurance policy than a corporately owned policy if the corporate premium payment triggers a taxable benefit. Results will vary when applying different corporate (small business or investment) or personal (dividend or salary) tax rates. The principal behind tax integration is that income earned by a private corporation and distributed as a dividend or a salary to its shareholder should be subject to approximately the same amount of tax as if the income had been earned by the shareholder directly.

Integration is never perfect because so many variables come into play. For example: the source of income contemplated, the different tax rates, the Refundable Dividend Tax on Hand, the Capital Dividend Account, etc...

Though one may think at first that a corporate owned life insurance policy is more cost effective using corporate dollars versus a personally owned life insurance policy, it is important to review the alternative tax consequences and consider all the variables on a case-by-case basis. Your Tax & Estate Planning team can help you determine the most cost effective ownership structure to meet your needs.