canada life™

Accessing cash value from your corporation's policy

The primary reason for corporately owned life insurance is to protect your business and your family.

With permanent life insurance, the policy can build up money that your corporation can use if needed.[1] This cash value[2] can grow tax-free within the policy, subject to legislative limits.

Your corporation can access cash value of its policy in several ways:[3]

1 | Withdraw cash value.

2 | Borrow from your policy.

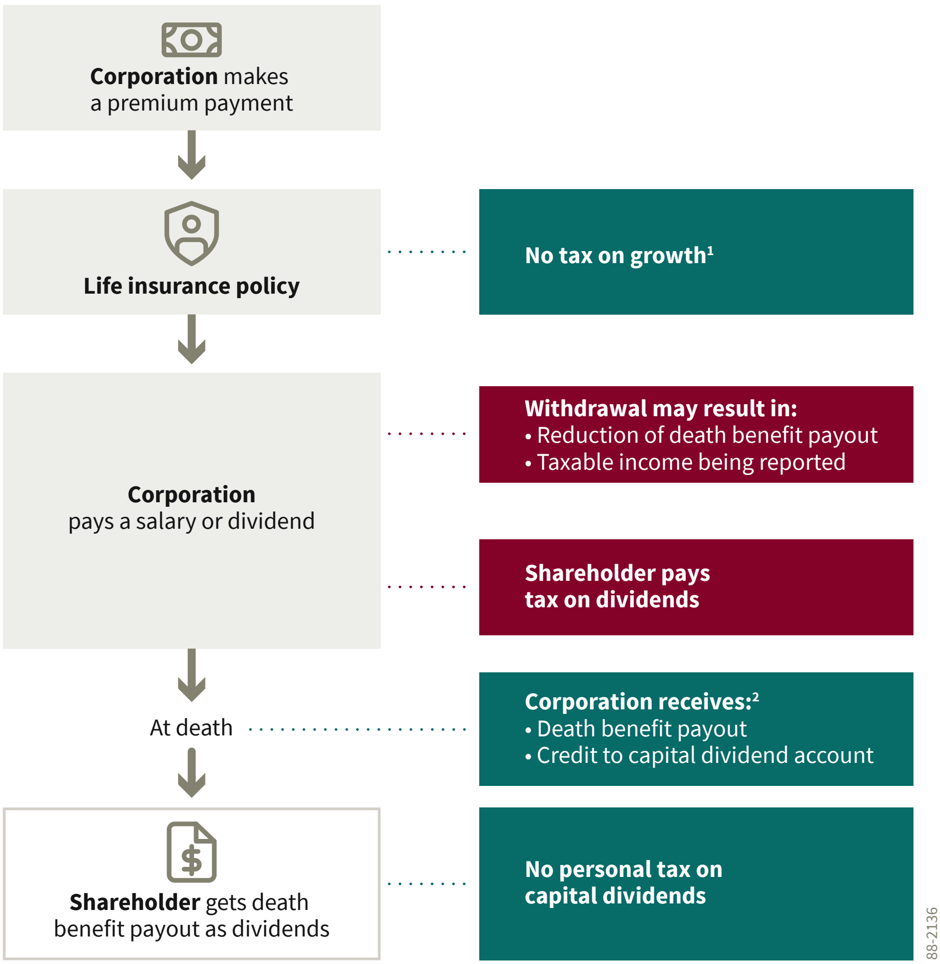
3 | Use it as collateral for a third-party loan (movable hypothec in Quebec).

Let's take a closer look at how each option works and how it can affect your coverage and taxes.

[1] Assuming you make the required premium payments and enough cash value has accumulated in the policy.
[2] Cash value also refers to account values.
[3] Accessing cash value may reduce the policy's cash value and insurance payout and may result in taxable income being reported to the corporation.

1 Withdraw your policy's cash value

Your corporation's policy guarantees that the owner (your corporation) can withdraw some or all the cash value, adjusted for any outstanding policy loans or fees. Known as the cash value, withdrawals will reduce your coverage and may result in taxable income being reported to the corporation. The policy ends if the corporation withdraws all the policy's cash value.

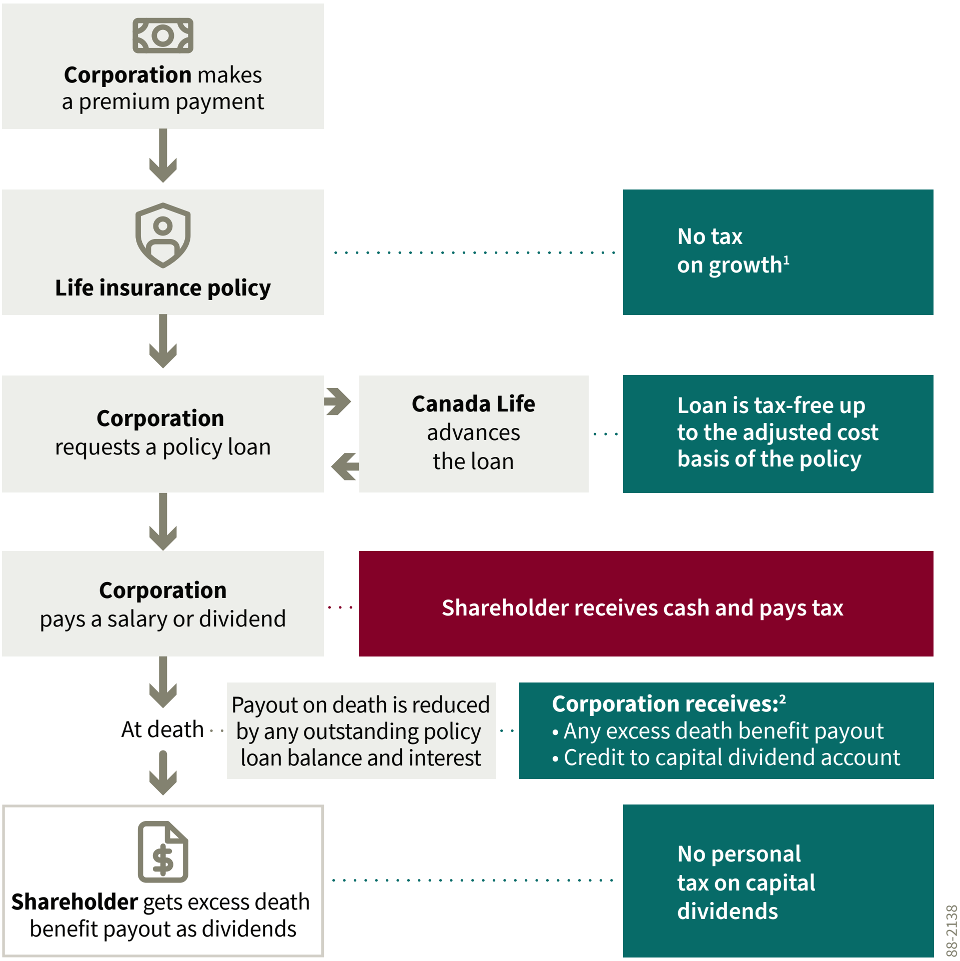


[1] The policy's cash value grows tax-free while inside the policy, subject to legislative limits.
[2] At death, the insurance proceeds are paid to the corporation on a tax-free basis. The capital dividend account of the private corporation typically receives a credit equal to the payout on death less the adjusted cost basis of the policy. The capital dividend account credit typically allows the corporation to pay a tax-free dividend to the Canadian resident shareholders.

2

Borrow from your policy

The policy guarantees that the owner (your corporation) can borrow money from Canada Life against the policy's cash value with interest. You can take advantage of the policy loan feature if the cash value in the policy is large enough and available. The policy loan is tax-free, up to the policy's adjusted cost basis.[*] The policy loan doesn't reduce the insurance coverage, or affect the cash value growth or any dividends the policy may receive. However, if the loan isn't repaid, any outstanding balance, including interest, will be deducted from the insurance payout on death or any cash value that is paid out.



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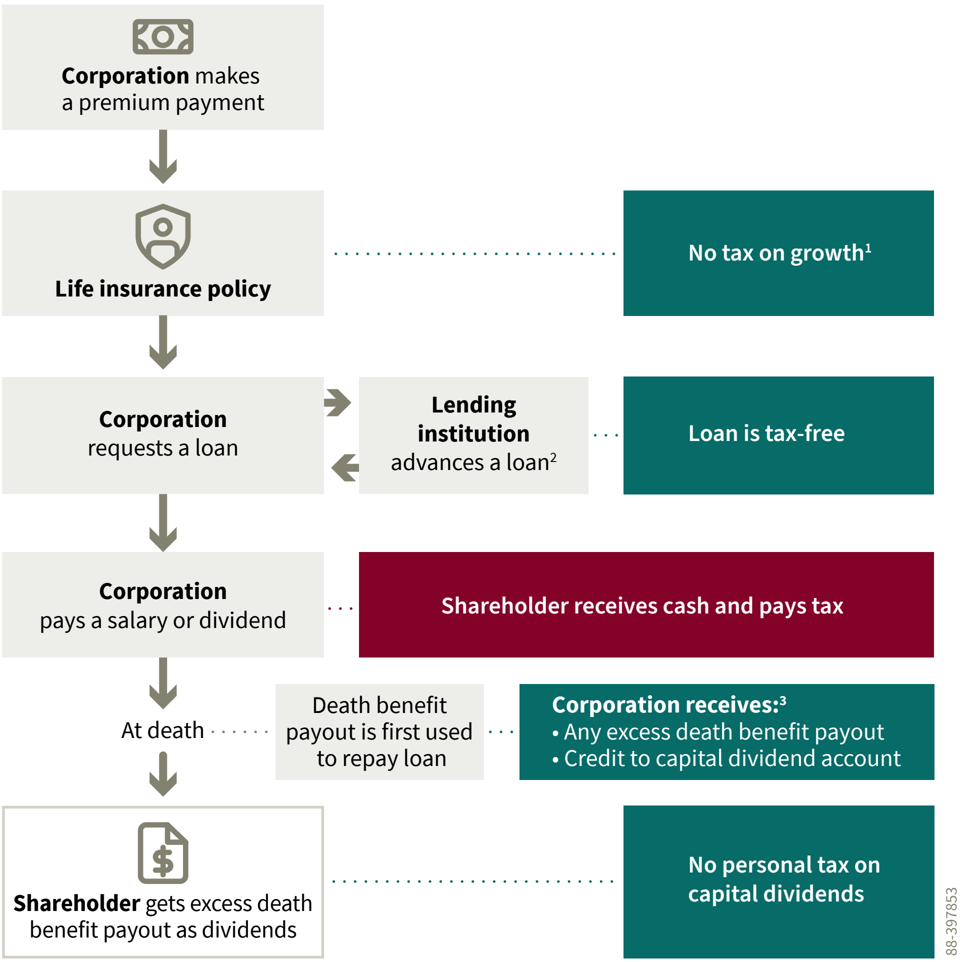
* Generally the adjusted cost basis is the premiums paid minus the net cost of pure insurance, assuming no dispositions. The adjusted cost basis is defined in 148(9) of the Income Tax Act.

3 Use your policy as collateral for a loan or line of credit

The corporation may be able to borrow from banks or other third-party lenders against the policy's cash value. Known as a collateral loan, it is not a disposition for tax purposes, but the corporation pays interest to the lender. A collateral loan doesn't reduce your insurance coverage, or affect the cash value growth or any dividends the policy may receive, or the capital dividend account credit. If the loan isn't repaid, the balance, including interest, is deducted from the amount paid out at death.

Depending on the lender, a collateral loan may be available at a lower interest rate. You should not purchase life insurance solely because of the future possibility of obtaining a collateral loan.



[1] The policy's cash value grows tax-free while inside the policy, subject to legislative limits.
[2] Need to be underwritten by the lender to qualify. Policyowner may need to make immediate repayment if lender calls in repayment of the loan.
[3] At death, the insurance proceeds are paid to the corporation on a tax-free basis. The capital dividend account of the private corporation typically receives a credit equal to the full death benefit less the adjusted cost basis of the policy. The capital dividend account credit typically allows the corporation to pay a tax-free dividend to the Canadian resident shareholders.

Collateral loan repayment

Once the loan is repaid, you may have a capital dividend account balance higher than your remaining insurance payout at death. This extra room can provide your business with the flexibility to release other assets to shareholders as a tax-free capital dividend. There's no guarantee a third-party lender will offer your corporation a loan. You'll have to negotiate that with the lender, subject to their financial underwriting and requirements. Because it involves greater risks, you shouldn't consider a collateral loan unless you have a high tolerance for risk. The corporation also needs enough income and capital to cover the interest and repay the loan, in addition to paying its required life insurance premium payments.

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This information is based on current tax legislation and interpretations for Canadian residents and is accurate to the best of our knowledge as of February 2022. Future changes to tax legislation and interpretations may affect this information. This information is general in nature and isn't legal or tax advice. For specific situations, you should consult an appropriate legal, accounting or tax advisor.

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