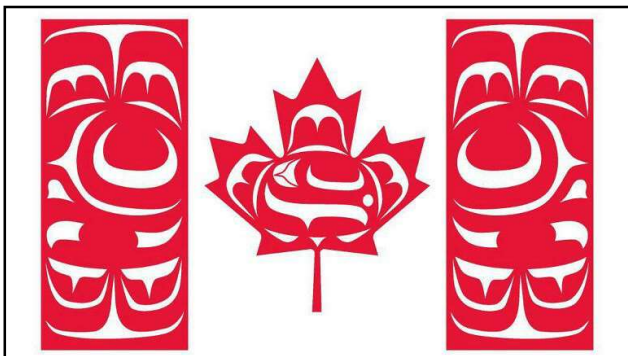


Transferring an Interest in a Life Insurance Policy

Peter A. Wouters
Director, Tax Retirement & Estate Planning Services

For dealer use only | 1





Transferring an Interest in a Life Insurance Policy

Peter A. Wouters
Director, Tax Retirement & Estate Planning Services

For dealer use only | 3



Disclaimer



A description of the key features of the individual variable insurance contract is contained in the Information Folder for the product being considered. Any amount that is allocated to a Segregated Fund is invested at the risk of the contract owner and may increase or decrease in value.

This document reflects the views of Empire Life as of the date published. The information in this document is for general information purposes only and is not to be construed as providing legal, tax, financial or professional advice. The Empire Life Insurance Company assumes no responsibility for any reliance on or misuse or omissions of the information contained in this document.

Policies are issued by The Empire Life Insurance Company.

The Empire Life Insurance Company
259 King Street East
Kingston ON
1-877-548-1881
info@empire.ca

Agenda



- What is a policy disposition
- Tax implications
- Transfers of a policy
- Case studies



FOR ADVISOR USE ONLY 1.5

“Disposition” of a policy



- Ss 148(9) of the Income Tax Act (ITA)
- A disposition, in relation to an interest in a life insurance policy, includes:
 - a surrender of the interest (including a partial surrender of the interest)
 - a disposition of the interest by operation of law
 - a policy loan
- But does not include
 - An assignment of an interest in the policy for the purpose of securing a debt or a loan other than a policy loan

FOR ADVISOR USE ONLY 1.6

“Disposition” of a policy

- Ss 148(10) of the Income Tax Act (ITA)
- Policyholder who exercises any provision of the policy deemed
 - Not to have disposed of an interest in a life insurance policy
 - Nor to have acquired an interest in a life insurance policy
- Exception :
 - Other than a conversion into an annuity contract



“Disposition” of a policy

- **Situation:**
 - Policyholder-insured of life insurance policy in terminal phase of life (<6 months to live) changes beneficiary of policy to benefit of third party
 - In consideration for:
 - New beneficiary pays premiums of policy until death of insured AND
 - Pays an amount in cash to owner of policy
- **Question:**
 - Is there a disposition of the life insurance policy?

“Disposition” of a policy

- **CRA's position:**
 - To determine if there is a disposition of an interest in a life insurance policy by operation of law only
 - Paragraph d) of definition of “disposition” at ss148(9) ITA
 - It must be determined if change to existing contract results because of applicable legislation
- **Generally:**
 - Change in beneficiary not a modification that leads to disposition of interest in policy

“Disposition” of a policy



- However:
 - New beneficiary may have acquired an interest in the policy because:
 - Policyholder receives an amount as consideration for the change of beneficiary
 - Premiums are paid directly by the new beneficiary
- Result:
 - Application of ss148(1) ITA
 - Policy gain to be calculated by policyholder

BENEFICIARY



General Rules



- Para. 56(1)(j) ITA
 - Inclusion of income from the disposition of an interest in an exempt life insurance policy
- Income inclusion or “policy gain”
 - Proceeds of disposition - adjusted cost basis
 - No loss possible



FOR ADVISOR USE ONLY 11

General Rules



“Proceeds of disposition” – ss148(9) ITA

- If disposition of interest – proceeds policyholder entitled to receive
- If surrender of the interest – CSV of the interest
- If policy loan – amount of the loan

“Adjusted Cost Basis” (ACB) – ss148(9) ITA

- Some factors that increase the ACB:
 - Cost of an interest in the policy acquired by the policyholder
 - Premiums paid by the policyholder
- Some factors that decrease the ACB:
 - Total of “net cost of pure insurance” (NCPI)
 - Proceeds of disposition of an interest in the policy (policy loans)



FOR ADVISOR USE ONLY 12

General Rules



- Are policy gains capital gain or income for tax purposes?
 - A policy gain is not a capital gain
 - 100% taxable income
 - Income from property
- Consequences from taxation of policy gains:
 - Attribution rules under ss 74.1 ITA
 - Investment income earned by a corporation with respect to calculating the corporation's Refundable Dividend Tax on Hand (RDTOH)



FOR ADVISOR USE ONLY | 13

Policy Transfers – General Rules



- Taxable policy gain to transferor = excess of proceeds of disposition less adjusted cost basis (ACB)
- Policy loss?
 - No loss can be realized upon disposition of policy
- Proceeds of disposition
 - Proceeds that the policyholder is entitled to receive
- Exceptions?



FOR ADVISOR USE ONLY | 14

Policy Transfers – Specific Rules



- Specific rules – ss148(7) ITA
- One of four circumstances:
 - Transfer by way of gift or bequest;
 - Distribution from a corporation;
 - Disposition by way of operation of law only; or
 - Disposition to any non-arm's length person.



FOR ADVISOR USE ONLY | 15

Policy Transfers – Specific Rules



Consequences for policyholder:

- Proceeds of disposition deemed greatest of:
 - Value of the interest
 - Fair market value of the consideration given for the interest
 - Adjusted cost basis (ACB) of the interest

Consequences for person that acquires the interest

- New ACB =
Deemed proceeds of disposition



Policy Transfers – Value of interest



Value– defined at ss148(9) ITA:

- When the interest includes an interest in the cash surrender value (CSV) of the policy,
 - The amount in respect thereof that the holder of the interest would be entitled to receive if the policy were surrendered at that time
- In any other case
 - Nil

What if:

- Surrender charges are in effect at the time of transfer?
- A policy loan has been issued prior to the transfer?



Policy Transfers – Value of interest



- Life insurance policy with surrender charges applicable
- Ownership of policy transferred in non-arm's length transaction (ss 148(7) ITA applies to transfer)
- Question to CRA
 - Does the CRA agree that the value of the policy is the amount the holder is entitled to receive, net of surrender charges?
- CRA's response
 - Depends upon all terms and conditions of a particular policy and the law applicable to the policy.

Policy Transfers – Corporation to Shareholder or Employee



- Taxable benefit to shareholder/employee
 - Shareholder benefit – ss 15(1) ITA vs
 - Employee benefit – para 6(1)(a) ITA
- What if the person is both a shareholder and employee?



FOR ADVISOR USE ONLY | 18

Policy Transfers – Corporation to Shareholder or Employee



Benefit as shareholder or employee?

- **Question of fact**
- CRA:
 - Employee-shareholder receives benefit as shareholder if can significantly influence business policy unless:
 - Benefit available to all employees of corporation
 - Benefits comparable to benefits offered to non-shareholder employees of similar business with similar responsibilities
 - Ensure taxes are withheld (ss 153(1) ITA)



• Ref. Folio S2-F3-C2

FOR ADVISOR USE ONLY | 20

Policy Transfers – Example of Transfer to Shareholder or Employee



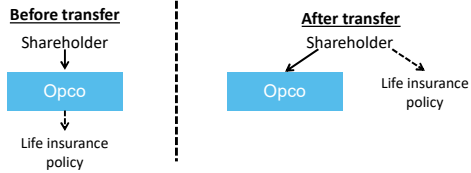
- Characteristics of the policy:
 - CSV: \$150,000
 - ACB: \$ 50,000
 - FMV: \$250,000
- No consideration paid by shareholder or employee

	For Operating Company (Opco)				For Shareholder / Employee	
Capacity of transferee	Deemed proceeds (148(7) ITA)	ACB	Policy Gain	Deduction	Consideration given	Taxable Benefit
Shareholder	\$150,000	\$50,000	\$100,000	\$0	\$0	\$250,000 (ss 15(1) ITA)
Employee	\$150,000	\$50,000	\$100,000	\$250,000	\$0	\$250,000 (para 6(1)(a) ITA)

FOR ADVISOR USE ONLY | 21

Policy Transfers – Consideration given

- Transferor: Operating Company (Opco) (corporation)
- Acquirer: shareholder of Opco (individual)
- Life insured: shareholder of Opco



Policy Transfers – Consideration given

- 2 possibilities for transfer from Opco to shareholder:
 1. Shareholder pays sum to Opco for policy
 2. Opco declares dividend to shareholder

Characteristics of life insurance policy

- CSV: \$150,000
- ACB: \$ 50,000
- FMV: \$250,000



Policy Transfers – Consideration given

Fair market value of a life insurance policy

- CRA Information Circular IC 89-3
- Cash surrender value (CSV) of policy
 - Policy's loan value
 - Face value of policy
 - State of health of the insured and his/her life expectancy
 - Conversion privileges under the policy
 - Replacement value of policy
 - other policy terms



Policy Transfers – Consideration given

1. Shareholder pays sum to Opco for policy

	Consideration given by shareholder	Operating Company (Opco)			New ACB for shareholder	Taxable benefit ss15(1) ITA
		Deemed proceeds ss148(7) ITA	ACB	Policy gain		
#1	\$0	\$150,000	\$50,000	\$100,000	\$150,000	\$250,000
#2	\$50,000	\$150,000	\$50,000	\$100,000	\$150,000	\$200,000
#3	\$150,000	\$150,000	\$50,000	\$100,000	\$150,000	\$100,000
#4	\$250,000	\$250,000	\$50,000	\$200,000	\$250,000	\$0

Policy Transfers – Consideration given

2. Opco declares dividend to shareholder

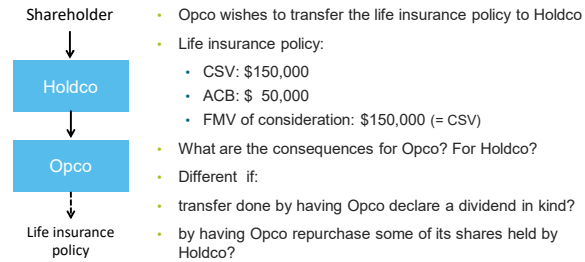
- Question:
 - What is the consideration given by the shareholder when Opco declares a dividend?
 - No consideration given by the shareholder to Opco

	Amount of dividend	Operating Company (Opco)			New ACB for shareholder	Taxable benefit ss15(1) ITA
		Deemed proceeds ss148(7) ITA	ACB	Policy gain		
Dividend	\$250,000	\$150,000	\$50,000	\$100,000	\$150,000	\$0

Policy Transfers – Consideration given

	Consideration given by shareholder	Opco			New ACB for shareholder	Taxable benefit ss 15(1) ITA
		Deemed proceeds ss 148(7) ITA	ACB	Policy gain		
#1	\$0	\$150,000	\$50,000	\$100,000	\$150,000	\$250,000
#2	\$50,000	\$150,000	\$50,000	\$100,000	\$150,000	\$200,000
#3	\$150,000	\$150,000	\$50,000	\$100,000	\$150,000	\$100,000
#4	\$250,000	\$250,000	\$50,000	\$200,000	\$250,000	\$0
Dividend	\$250,000	\$150,000	\$50,000	\$100,000	\$150,000	\$0

Policy Transfers – Transfer from Opco to Holdco



FOR ADVISOR USE ONLY! 28

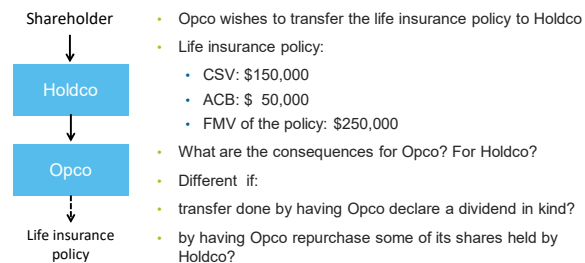
Policy Transfer– Consequences



- Holdco pays sum to Opco for policy

	Consideration given by Holdco	Opco			New ACB for Holdco	Taxable benefit ss15(1) ITA
		Deemed proceeds ss148(7) ITA	ACB	Policy gain		
#1	\$0	\$150,000	\$50,000	\$100,000	\$150,000	\$150,000
#2	\$50,000	\$150,000	\$50,000	\$100,000	\$150,000	\$100,000
#3	\$150,000	\$150,000	\$50,000	\$100,000	\$150,000	\$0

Policy Transfers – Transfer from Opco to Holdco



FOR ADVISOR USE ONLY! 30

Policy Transfer– Consequences



1. Holdco pays sum to Opco for policy

	Consideration given by Holdco	Opco			New ACB for Holdco	Taxable benefit ss15(1) ITA
		Deemed proceeds ss148(7) ITA	ACB	Policy gain		
#1	\$0	\$150,000	\$50,000	\$100,000	\$250,000	\$250,000
#2	\$50,000	\$150,000	\$50,000	\$100,000	\$250,000	\$200,000
#3	\$150,000	\$150,000	\$50,000	\$100,000	\$250,000	\$100,000
#4	\$250,000	\$250,000	\$50,000	\$200,000	\$250,000	\$0

Policy Transfers – Transfer from Opco to Holdco

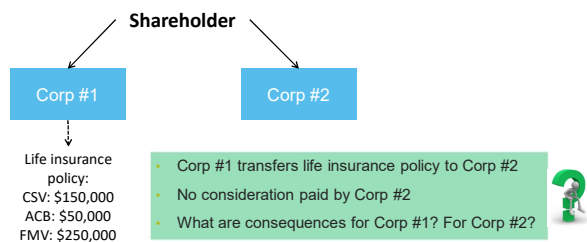


	For Opco			For Holdco		
	Deemed proceeds (148(7) ITA)	ACB	Policy Gain	Consideration given	Taxable Benefit	Taxable dividend
Transfer of policy	\$150,000	\$50,000	\$100,000	\$0	\$250,000	N/A
Dividend in kind	\$150,000	\$50,000	\$100,000	\$0	N/A	\$250,000
Repurchase of shares	\$250,000	\$50,000	\$200,000	\$250,000	N/A	≈\$250,000

FOR ADVISOR USE ONLY | 32

Assume FMV of policy=\$250,000

Policy Transfers – Transfer between sister corporations



FOR ADVISOR USE ONLY | 33

Policy Transfers – Transfer between sister corporations



- Life insurance policy:
 - CSV: \$150,000
 - ACB: \$ 50,000
 - FMV: \$250,000
- No consideration given by Corp #2
- ACB for Corp #2 = Deemed proceeds for Corp #1

	For Corp #1			For Corp #2		
	Deemed proceeds ss148(7) ITA	ACB	Policy Gain	Consideration given	Taxable Benefit	Taxable dividend
Transfer of policy	\$150,000	\$50,000	\$100,000	\$0	(?)	N/A

FOR ADVISOR USE ONLY | 34

Policy Transfers – Transfer between sister corporations



- CRA's position:
 - Transfer between sister corporations could result in shareholder benefit for shareholder of Corp #1 & Corp #2
 - Reasoning implies:
 - Impoverishment of transferor corporation (Corp #1)
 - Shareholder is enriched
- Transfer between sister corporations could also be deemed indirect payment
 - ss 56(2) or s 246 ITA
 - Shareholder assessed taxable benefit = FMV of policy – consideration paid

FOR ADVISOR USE ONLY | 35

Policy Transfers – Shared Ownership



- Corporation owns death benefit, shareholder / employee owns cash value
- Plan is at some point to have corporation transfer ownership of interest in death benefit to shareholder / employee
- Shareholder / employee benefit based on:
 - Fair market value of the policy at time of transfer
 - Not the CSV of the policy at time of transfer
- Personally owned policy with corporation an irrevocable beneficiary on death benefit portion

FOR ADVISOR USE ONLY | 36

Policy Transfers – Intergeneration Transfers



Conditions at ss148(8) ITA

- Transfer to policyholder's child **for no consideration**
- Life insured under the policy is:
 - **Result:**
 - A child of the policyholder; or
 - A child of the transferee
 - May transfer to guardian
 - Do not transfer via will or trust
- Proceeds of disposition equal to the ACB to the policyholder
- Acquired by transferee at a cost equal to those proceeds



FOR ADVISOR USE ONLY | 37

Policy Transfers – Intergeneration Transfers



- **"Child"** – ss148(9), ss 252(1), ss70(10) ITA
 - Children, Grandchildren, Great-grandchildren
 - Wholly dependent < age 19
 - Step children, step grandchildren; spouses of children
- **No time limit for transfer**
 - Parent can maintain control of policy
- **Recipient child need not be life insured child**

FOR ADVISOR USE ONLY | 38

Policy Transfers – Intergeneration Transfers



Structure of life insurance policy at issuance :

- Owner: Robert
- Contingent Owner: Emily
- Life insured: Emily

Structure of life insurance policy after Robert's death :

- Owner: Emily
- Life insured: Emily
- Beneficiary: at Emily's discretion

Benefits for Robert:

- Income tax-sheltered
- Tax-free transfer
- Maintains control of policy

FOR ADVISOR USE ONLY | 39

Policy Transfers – Intergeneration Transfers



You know Robert's family well and you know that his daughter just had a son (Steve). What can you suggest?

• Structure of life insurance policy at issuance :

- Owner: Robert
- Contingent Owner: Emily
- Life insured: Steve

• Structure of life insurance policy after Robert's death:

- Owner: Emily
- Life insured: Steve
- Contingent owner: Steve

FOR ADVISOR USE ONLY | 40

Policy Transfers – Transfer to spouse/common-law partner (*inter vivos*)



Conditions at ss148(8.1) ITA

- Transfer to :
 - Policyholder's spouse or common-law partner
 - Former spouse or common-law partner of policyholder in settlement of rights arising out of their marriage or common-law partnership
- Policyholder and transferee are resident in Canada

Result:

- Proceeds of disposition equal to the ACB to the policyholder
- Acquired by transferee at a cost equal to those proceeds

FOR ADVISOR USE ONLY | 41

Policy Transfers – Transfer to spouse/common-law partner (*at death*)



• Conditions at ss148(8.2) ITA


- Transfer to policyholder's spouse or common-law partner
- As consequence of death of policyholder
- Policyholder and transferee resident in Canada immediately before death

Result:

- Proceeds of disposition equal to the ACB to the policyholder
- Acquired by transferee at a cost equal to those proceeds

ss148(8.1) and ss148(8.2) ITA do not apply to transfer to spousal trust
Such transfer subject to ss 148(7) ITA

FOR ADVISOR USE ONLY | 42


Clients' expectations have been changing 

- More important than ever to make doing business with them as efficient as possible
- You can submit ownership transfer requests quickly and easily through the [My Advisor Dashboard](#)

eSignature forms section

- gives you access to secure online forms and applications that can be signed digitally; convenient, secure, encrypted

eSignature forms on My Advisor Dashboard offer you more flexibility with digital options




Transfer of Ownership form now available


Clients' expectations have been changing and it's more important than ever to make doing business with them as efficient as possible. With the new digital **Transfer of Ownership** eSignature form, you can submit ownership transfer requests quickly and easily through the **My Advisor Dashboard**. The eSignature forms section on the dashboard gives you access to online forms and applications that can be signed digitally, giving you a more convenient way to work with your clients.

New form available for eSignature: Transfer of Ownership (C-0056)

43

Review 

- What is a policy disposition
- Transfers of a life insurance policy
- Case Studies



FOR ADVISOR USE ONLY | 44

Empire Life: A company you can trust 

- Helping Canadians meet their financial needs since 1923
- Rated among top 10 life insurance companies in Canada¹
- Rated A (Excellent) A.M. Best Company²
- Managing segregated funds for over 50 years
- Committed to Guaranteed Withdrawal Benefit since 2008
- Diversified investment choices ranging from fixed income up to 100% equity, including our tactically managed Emblem GIF Portfolios

¹ Globe and Mail Report On Business June 2016, based on revenue
² As of June 14, 2019. For the latest ratings, access ambest.com

45 | FOR ADVISOR USE ONLY

Transferring an Interest in a Life Insurance Policy

Peter A. Wouters
Director, Tax Retirement & Estate Planning Services

For dealer use only | 45