DOBEL INSURANCE AGENCY

BENEFITS OF CORPORATE OWNED LIFE INSURANCE

CONGRATULATIONS

You own your own business and you have incorporated. A smart decision, since corporate structures have significant benefits such as:

- *Limited liability*
- *Continuity of the business*
- *Easier access to capital*
- *Lower income tax rates with the small business tax deduction*
- *Potential tax deferral*

Now that your business is incorporated, have you considered corporate-owned insurance? Not to be confused with insurance purchased for your business operations (also a must), corporate-owned insurance is a life insurance policy purchased by a corporation on the life of a shareholder to protect the business on the death of the shareholder.

Let us consider the advantages of corporate-owned insurance:

CORPORATE VS PERSONAL DOLLARS

In today's tax environment, it is more economical to purchase life insurance using corporate dollars as opposed to using your personal income. Here's a simple example. If your corporation is a Canadian controlled private corporation that qualifies for the small-business tax deduction, it could potentially pay a tax rate of only 9% depending on the province in which your business operates. This means that for every $100 of income, $91 would be available after tax inside your corporation to go towards paying the insurance premiums. Now let's compare this to an individual who has an assumed marginal tax rate of 50%. The individual would only net $50 from the same $100. Therefore, the corporation has more after-tax dollars available to pay for the life insurance premiums. In most cases, the insurance premiums are not deductible to either the corporation or the individual.

ALTERNATIVE INVESTMENT

Corporate insurance can create enhanced asset values in comparison to investing the same amount in a corporate investment account because of the preferential tax treatment of life insurance policies. The Income Tax Act allows for funds (subject to a maximum) to be invested and grow on a tax deferred basis within an insurance policy, which effectively creates an RRSP-like mechanism within your corporation. However, withdrawals could be subject to tax.

FLEXIBILITY

Like any other asset, an insurance policy can be used as collateral with a financial institution to obtain a loan, the proceeds of which could be used in the business or could be used by yourself for investing or to provide retirement income. It is important to consult your accountant or tax specialist to ensure that the steps to put this type of plan in place are properly completed.

ADDED VALUE

Insurance purchased within your corporation allows you to put other unique business strategies in place, including the funding of buy-sell agreements, key-person coverage, and more.

USE OF CAPITAL DIVIDEND ACCOUNT

The CDA is a vital part of estate and tax planning for shareholders since life insurance proceeds are received tax-free by a corporation and are credited (net of the adjusted cost basis of the policy) to the CDA, which in turn can be paid to the shareholders as a tax-free capital dividend.

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PASSIVE INCOME

The passive investment income rules were changed in 2018 and created by the federal government to level the playing field for those that own Canadian-controlled private corporations compared to personal tax rates. Every dollar of passive income per year threshold will reduce the corporation's Small Business Deduction by $5.
For example, A business with a $1 million portfolio that generates $50,000 through a combination of dividends interest and capitals gains, is onside and within the threshold. On the other hand, a business with a $2 million portfolio generating $100,000, would have its Small Business Deduction reduced by $250,000, resulting in $15,000 in additional federal tax.
Investments within a corporately owned life insurance policy do not count towards passive investment income rules and therefore does not affect the Small Business Deduction limit.

As with any business strategy, there are important considerations to take into account when purchasing corporate-owned insurance. It is often not advisable to have the insurance policy owned in the operating corporation since the asset would be subject to creditor claims and if the operating corporation is sold, it is not possible to transfer the insurance to the shareholder on a tax efficient basis if the policy is to be maintained. Most often, the insurance is held in a holding corporation and the operating corporation is the beneficiary. When you are dealing with multiple shareholders, there are additional issues to consider and a shareholders agreement is paramount.
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TAKE AWAY

There are many benefits to corporately owned life insurance, the above points scratch the surface of what is possible and how we can help. Every company has a unique position and requires an in-depth discovery to develop their own unique strategy.

We work with our clients to create a customized strategy for any of their individual, family, or business needs. The process starts with getting to know you. Understanding your priorities helps us develop a solution for the areas that you deem most important. Once we understand what's important to you, what your goals are, and you trust us to work with you, we then start to develop a strategy along with your other trusted professionals. Throughout our process you'll receive professional and transparent advice, with no obligation or fees.

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