THE JEWISH COMMUNITY FOUNDATION OF MONTREAL

# Insurance Update - 2015

Presented By

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Services d’Assurance • Insurance Services

# Insurance Update - 2015

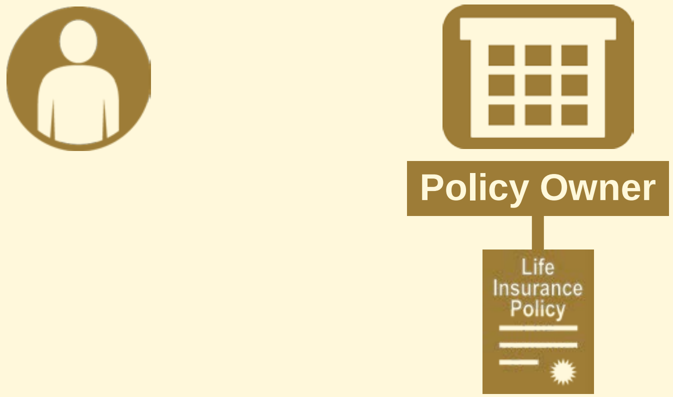
## Topics for discussion

- Policy valuations
- Ownership and beneficiary designations
- Capital dividend account
- Leveraging
- Exempt policy legislation update
- Case Study

# Insurance Update - 2015

## Consider – transfer of personally owned policy

- Deemed proceeds = CSV
  FMV – can be considerably higher than any CSV



# Insurance Update - 2015

## Consider – donation of policies

- If otherwise going to lapse the policy
- CSV and FMV proceeds

# Insurance Update - 2015

- Potential planning with “multi-life” policies

# Insurance Update - 2015 *Potpourri*

**Separating ownership from adjusted cost basis**

- Can increase CDA credit
- Business reasons

# Insurance Update - 2015 *Potpourri*

**Subs 15(1) assessment**

- Sub paid premium for parent

**Subs 246(1) assessment**

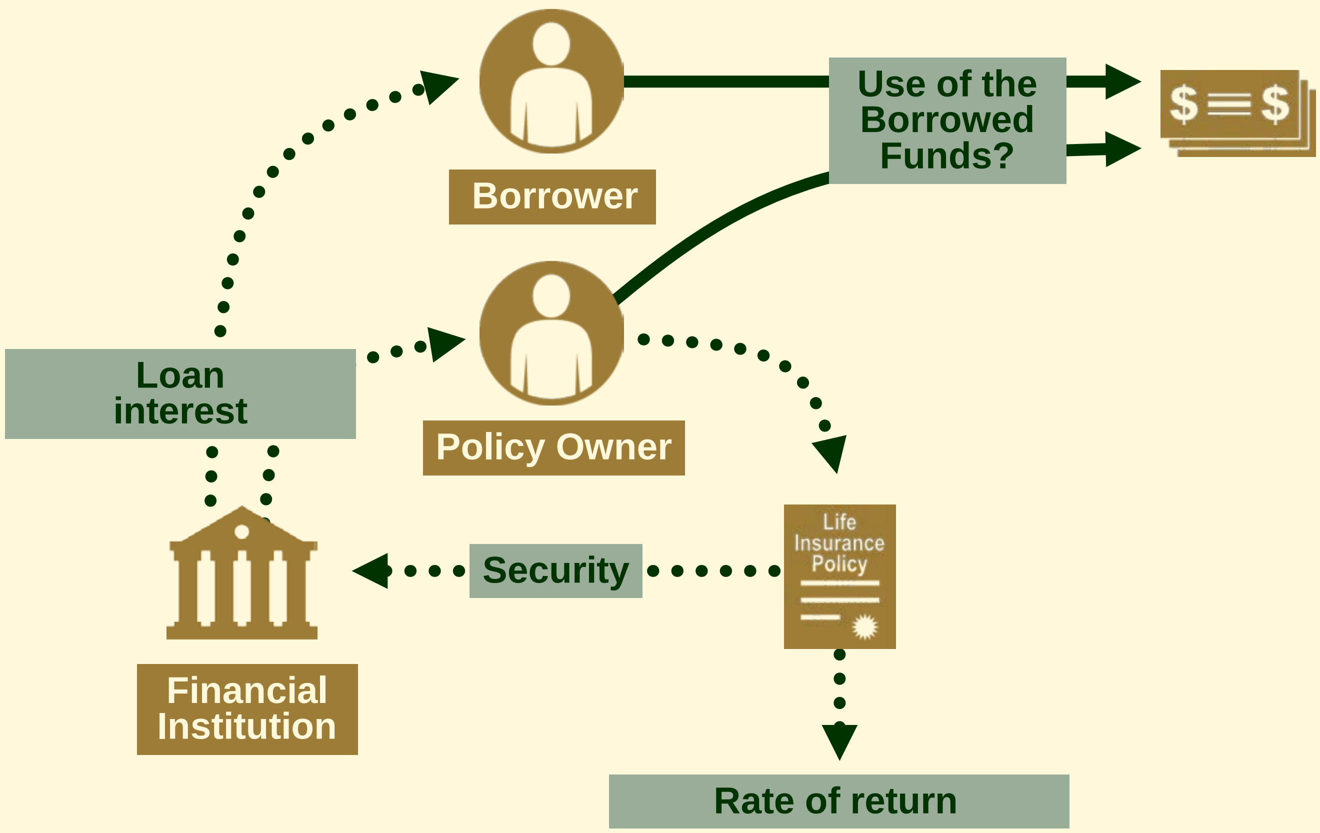
- Parent paid premium in respect of Sub

# Insurance Update - 2015 *Potpourri*

***Rebeiro* decision**

- Refer to CDA in shareholder agreements
- GRIP too??

# Insurance Update - 2015 - Leveraging



# Insurance Update - 2015 - Leveraging

- Considerable value in leveraging in the right circumstances
- Use of Different Structures
  - Flexibility
  - Personal and corporate borrowers
  - Holdco-owned policy and shareholder borrower
  - Trust-owned policy and beneficiary borrower
- Permits access to policy values
- ‘Hedged’ versus ‘unhedged’
- Secure long-term lending commitment

# Insurance Update - 2015 - Leveraging

- Provides cash flow improvements when using borrowed funds for business or investment purposes, such as
  - Funding shareholder agreements
  - Financings and re-financings
  - Acquire income-producing properties
  - Estate planning

# Insurance Update - 2015 - Leveraging

## Plus…

- Tax Savings on Capital Dividend Account

**Traditional Approach**

**ROI @ Life Expectancy**

**6.17%**

**After Tax**

# Insurance Update - 2015 - Leveraging

**Plus…**

- Tax Savings on Capital Dividend Account
- Additional Capital Dividend Account

**Traditional Approach**

**ROI @ Life Expectancy**
**6.17%**


**ROI @ Life Expectancy**
**11.21%**

**After Tax**

# Insurance Update - 2015

- Exempt policy changes – August 29/14
- Single premium is history
- No shelter advantage to high surrender charges
- Minimum premium paying period roughly 8 years
- Reduction in longer-term maximum funding levels for level cost of insurance charges (‘LCOI’)

# Insurance Update - 2015

- Exempt policies
  - Continue to provide shelter for investment income accruals within limits
- “Insurance GAAR” not included in legislation
- Changes to income inclusion portion of ‘prescribed annuity contracts’
- Grandfathering (subsection 148(11))

# Insurance Update - 2015

- Modifications and recalibration of the Investment Income Tax (Part XII.3)
  - 15% of a life insurer's 'taxable Canadian life investment income for the year' – see subsections 211.1(1) and 211.1(3)
- Modifications to the 250% test that applies to policies issued before 2017 after 2016

# Don’t forget grandfathering for stop-loss purposes

- ITTN 12 (February 1998 - stop-loss provisions – grandfathering)
- See PPI Advisory TS-109 (April 2014)
- Snapshot on April 26, 1995
  - Beneficiary of policy – doesn’t have to be the owner of the policy
- Agreements in writing before April 27, 1995

# Estate and Charitable Planning

## A CASE STUDY

# Client Profile

- Jim is a 64-year old single male residing in Montreal
- Sole shareholder of his corporation – prior to the estate freeze
- Started the business 30-years ago
- Valuation of $10 million
- Three children and 4 grandchildren
- None of the children are involved in the business, nor do they have plans to be

# Consider This

- Jim recently completed an estate freeze, exchanging his common shares for $10M of fixed value preferred shares
- New common shares issued to a family trust of which Jim, his Holdco (‘Jimco’), his children and all future grandchildren are beneficiaries
- He doesn’t need to realize the capital on the shares (although he’d like the option)
- There is nominal ACB and PUC, and no GRIP
- Upon his death there is a large tax bill

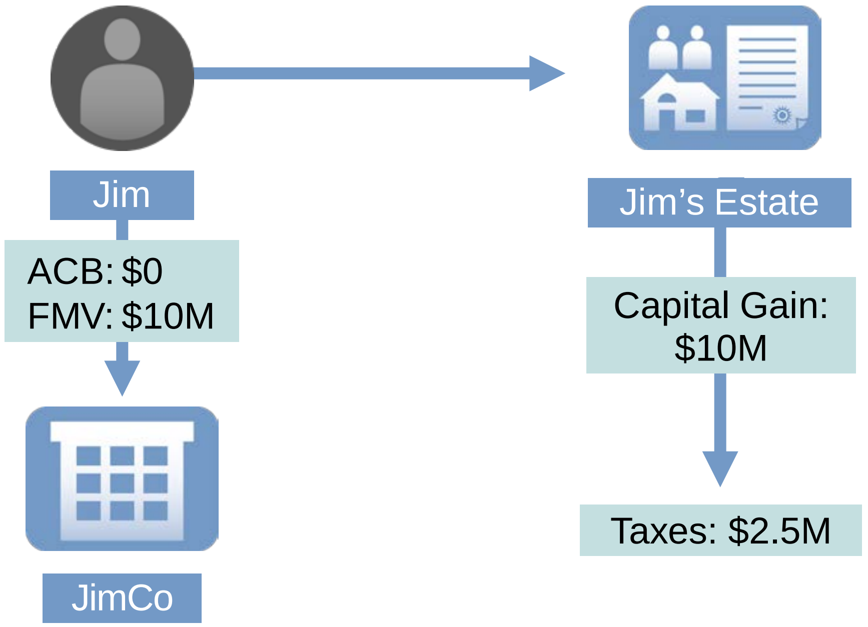
**What do you do?**

# The Options

1. No insurance
2. Life insurance solution to the pay the tax
3. Life insurance solution to reduce and pay the tax
4. Life insurance solution with charitable gift to eliminate tax
5. Life insurance with charitable gift to reduce and pay tax

# No Insurance

## OPTION 1



# Results

| | No Insurance |
|---|---|
| Tax Payable | ($2,500,000) |
| Insurance Proceeds | $0 |
| Insurance Premiums | $0 |
| | |
| Net to Beneficiaries | $7,500,000 |
| Increase over Base | n/a |

# Objectives

- Preferred shares are to pass to the children after death of father
- Value of shares doesn't need to be realized, but…
- Cash is required to pay the tax

# The Problem

“Where does the $2.5M of capital come from to pay the tax?”

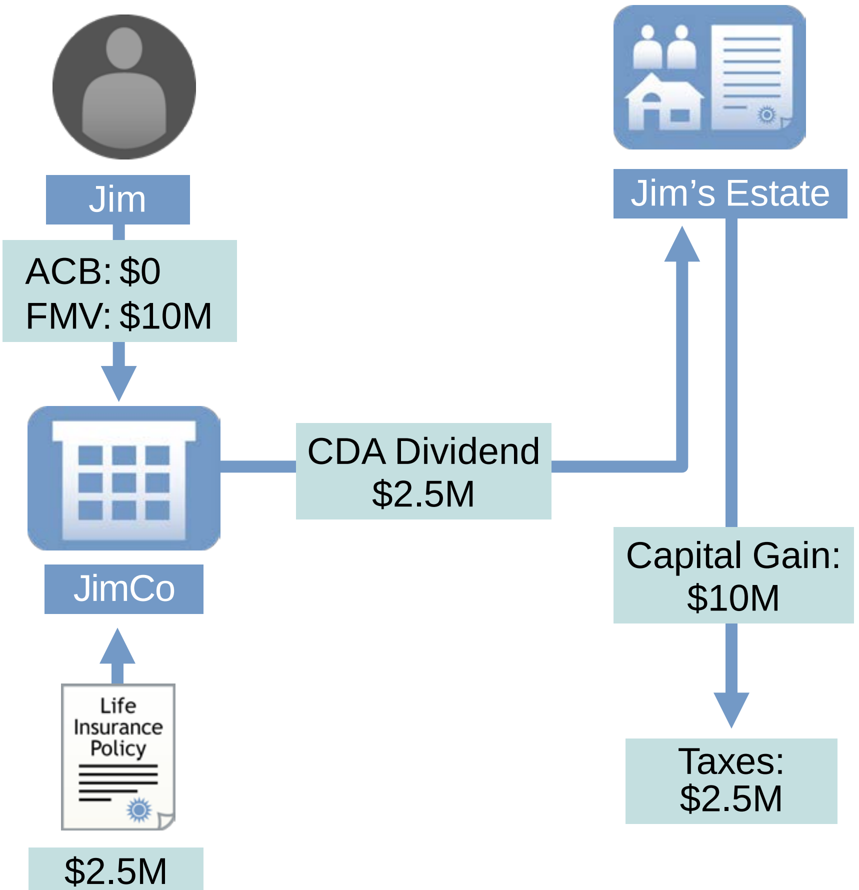
# Life Insurance Solution to Pay Tax

## OPTION 2

- The CA on the file recommended Jim purchase a permanent $2.5M single life insurance policy
- Use the insurance proceeds to pay the tax

# Life Insurance Solution to Pay Tax

## OPTION 2



# Results

| | No Insurance | Insurance to Pay Tax |
|---|---|---|
| Tax Payable | ($2,500,000) | ($2,500,000) |
| Insurance Proceeds | $0 | $2,500,000 |
| Insurance Premiums | $0 | ($1,225,000) |
| | | |
| Net to Beneficiaries | $7,500,000 | $8,775,000 |
| Increase over Base | n/a | 17% |

# Life Insurance Solution to Reduce and Pay Tax

## OPTION 3

- How much insurance?
- Look to the objectives - Pay the tax
- Share redemption
  - Partially taxable
- Reduces share amount for possible pipeline planning
- Actual insurance amount is less than capital gains tax

# Life Insurance Solution to Reduce and Pay Tax

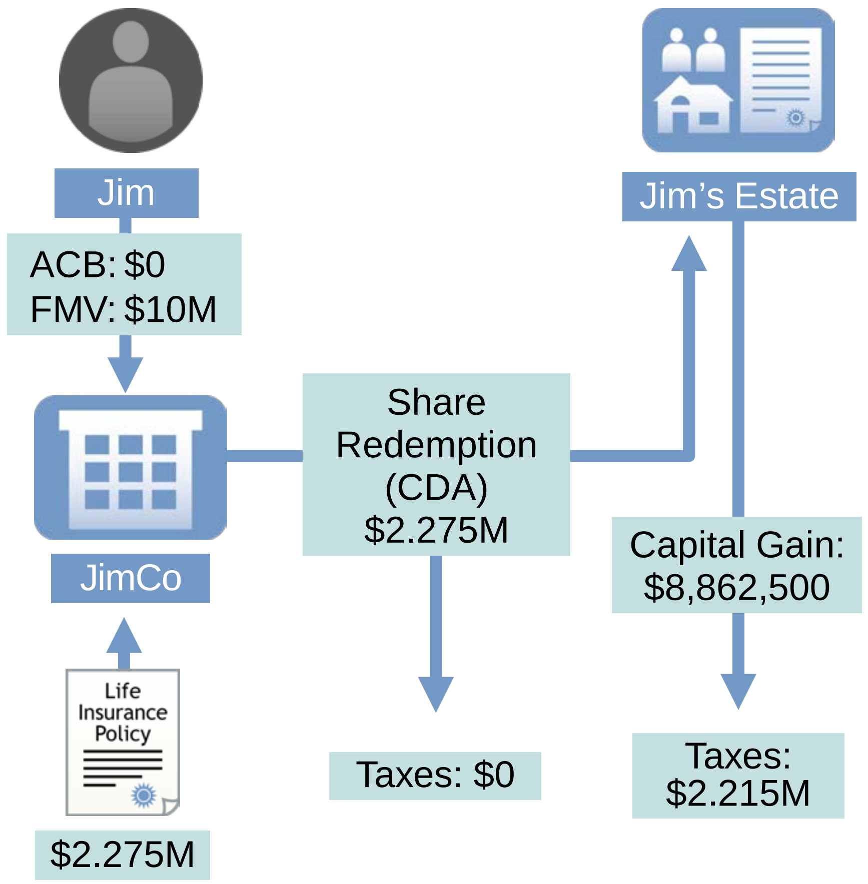
## OPTION 3

| Capital Gains Tax | Tax Otherwise Payable |
|---|---|
| \$10,000,000<br>x 50%<br>x 50% | \$2,500,000<br>÷1<br>+ (.50* - .40**) |
| = \$2,500,000 | = \$2,275,000 |

***Marginal Tax Rate**
****Dividend Tax Rate**

# Life Insurance Solution to Reduce and Pay Tax

## OPTION 3



# Results

| | No Insurance | Insurance to Pay Tax | Insurance to Reduce and Pay Tax |
|---|---|---|---|
| Tax Payable | ($2,500,000) | ($2,500,000) | ($2,215,000) |
| Insurance Proceeds | 0 | $2,500,000 | $2,275,000 |
| Insurance Premiums | 0 | ($1,225,000) | ($1,115,000) |
| | | | |
| Net to Beneficiaries | $7,500,000 | $8,775,000 | $8,945,000 |
| Increase over Base | n/a | 17% | 19% |

# Life Insurance with Charitable Gift to Eliminate Tax

## OPTION 4

The two previous scenarios just dealt with the tax

> “Can we take this even further?”

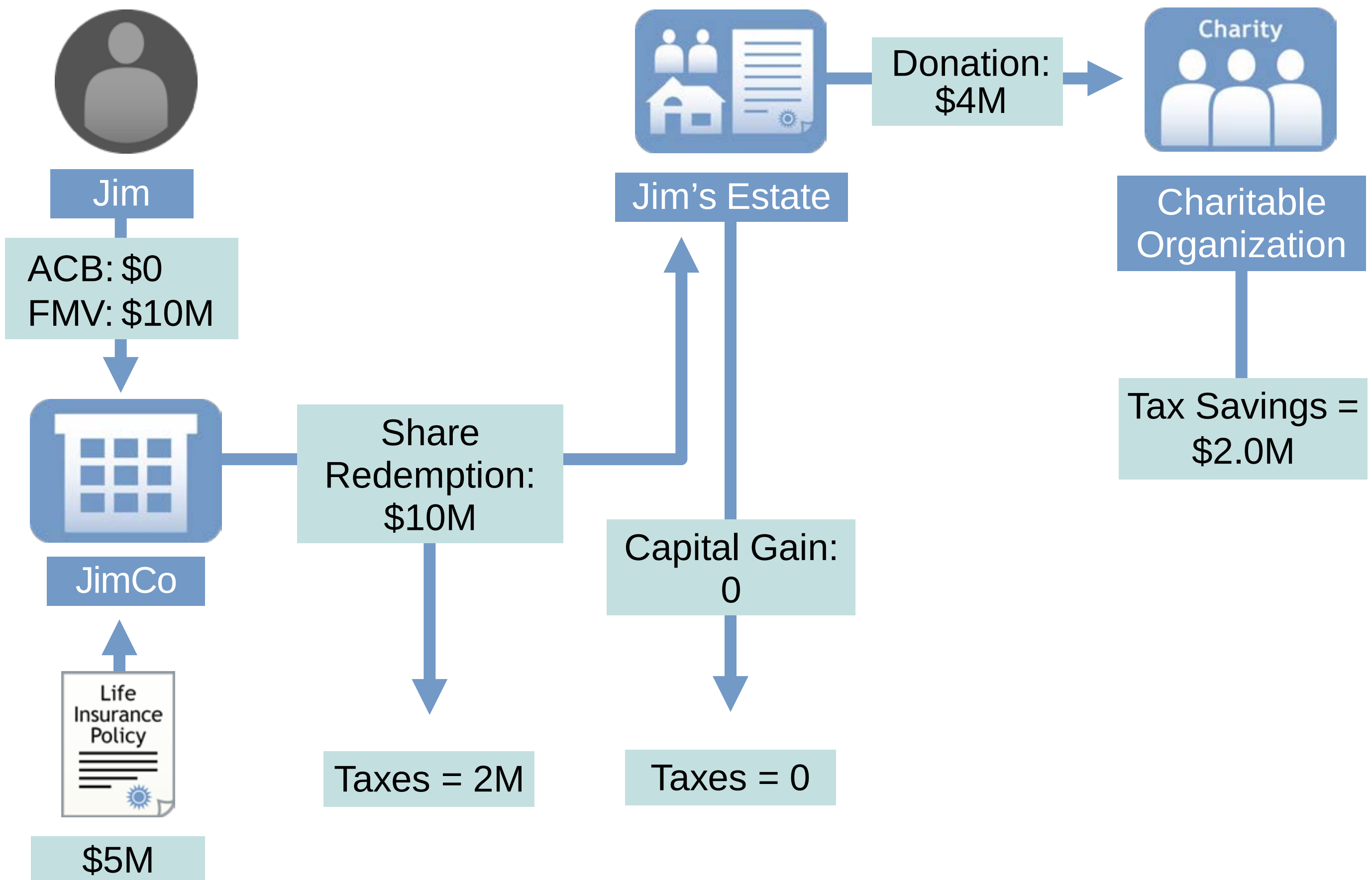
# Life Insurance with Charitable Gift to Eliminate Tax

## OPTION 4

- Client objectives:
  - Eliminate Tax
  - Donate to Charity
  - Preserve Capital for Beneficiaries
- Life insurance and CDA to reduce tax as much as possible
- Charitable donation to further reduce tax

# Life Insurance with Charitable Gift to Eliminate Tax

## OPTION 4



# Results

| | Insurance with Charitable Gift to Eliminate Tax |
|---|---:|
| Tax Payable | $0 |
| Insurance Proceeds | $5,000,000 |
| Insurance Premiums | ($2,450,000) |
| | |
| Charitable Gift | ($4,000,000) |
| Net to Beneficiaries | $8,550,000 |
| Increase over Base | 14% |

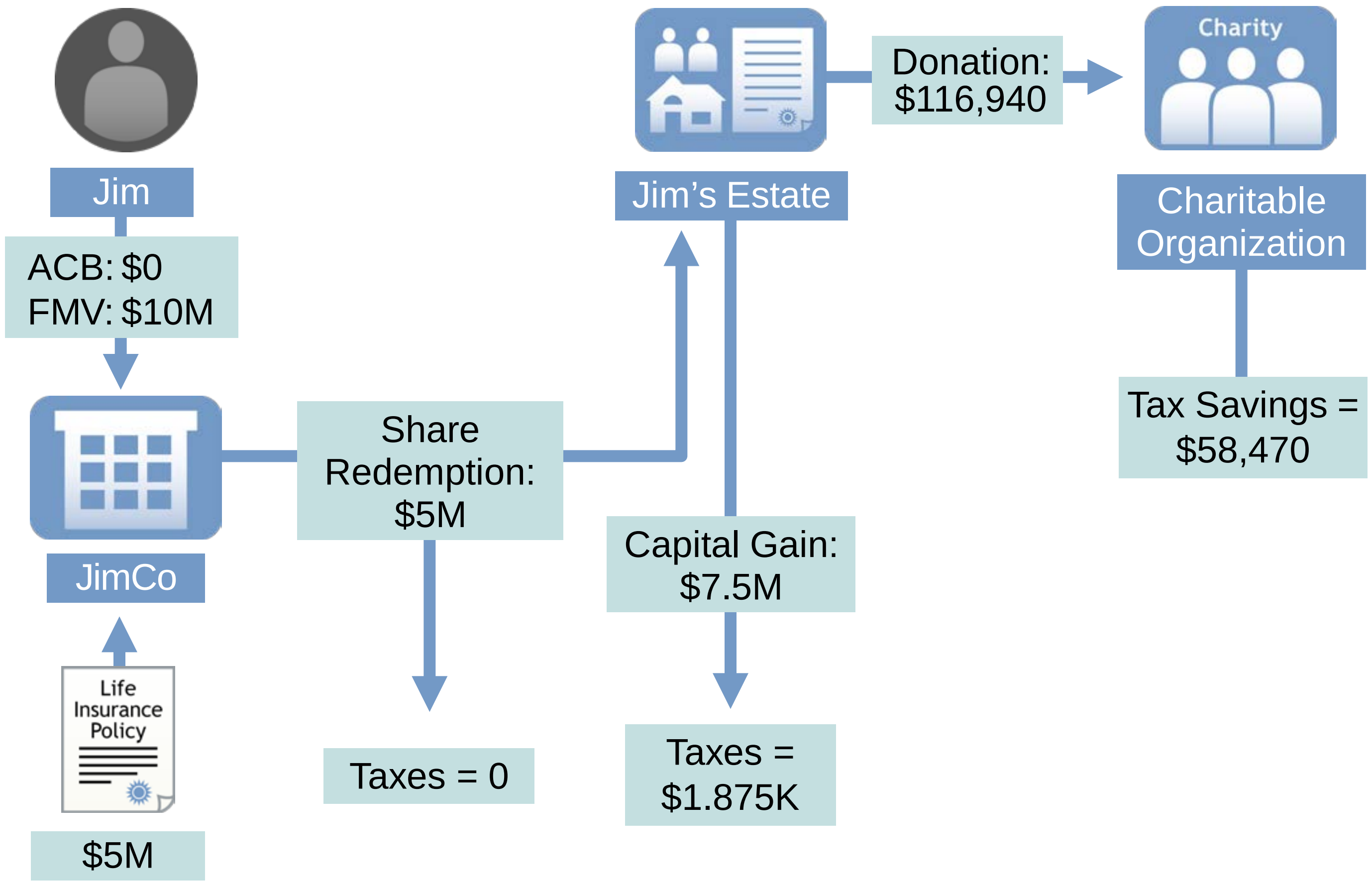
# Life Insurance with Charitable Gift to Reduce and Pay Tax

## OPTION 5

- Same life insurance amount as first gift scenario
- Give away enough to make estate whole
  - After taking into account insurance premiums

# Life Insurance with Charitable Gift to Reduce and Pay Tax

## OPTION 5



# With Gifts Results

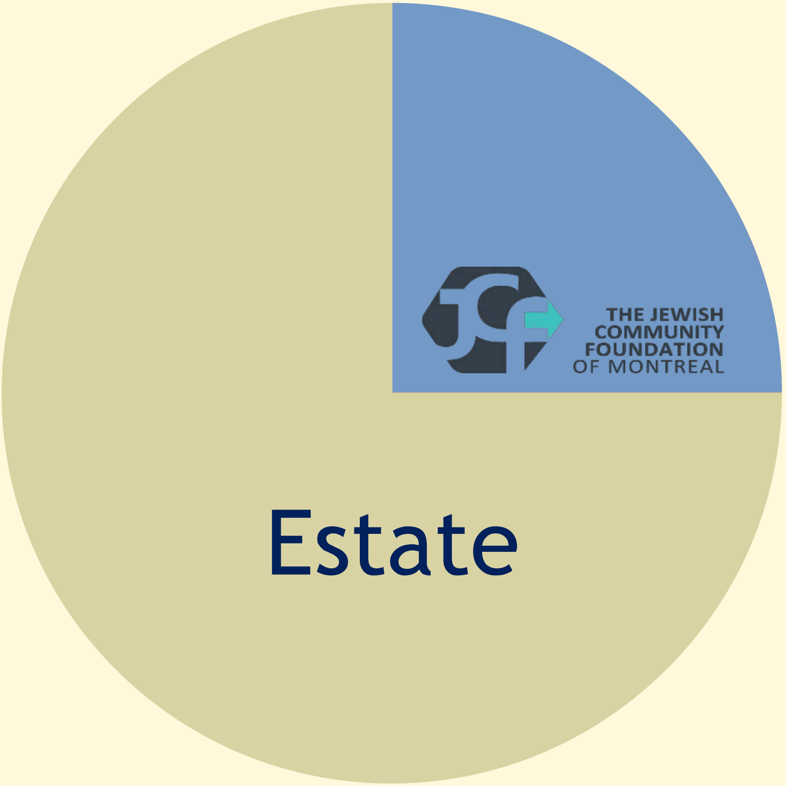
| | Insurance with Gift to Eliminate Tax | Insurance with Gift to Reduce & Pay Tax |
|---|---:|---:|
| Tax Payable | $0 | ($1,816,530) |
| Insurance Proceeds | $5,000,000 | $5,000,000 |
| Insurance Premiums | ($2,450,000) | ($2,450,000) |
| | | |
| Charitable Gift | ($4,000,000) | ($116,940) |
| Net to Beneficiaries | $8,550,000 | $10,616,530 |
| Increase over Base | 14% | 21% |

# Results Comparison

| | Tax | Beneficiaries | THE JEWISH COMMUNITY FOUNDATION OF MONTREAL |
|---|---|---|---|
| 1. No Insurance | ($2,500,000) | $7,500,000 | 0 |
| 2. Insurance to Pay Tax | ($2,500,000) | $8,775,000 | 0 |
| 3. Insurance to Reduce and Pay Tax | ($2,125,000) | $9,035,000 | 0 |
| 4. Insurance with Charitable Gift to Eliminate Tax | 0 | $8,550,000 | $4,000,000 |
| 5. Insurance with Gift to Reduce and Pay Tax | ($1,816,530) | $10,616,530 | $116,940 |

Three beneficiaries

How do we split the pie?



# Thank You



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