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# Rethinking IFAs: What Accountants Should Consider After Bill C-59

The recent GAAR amendments enacted through Bill C-59 mark a turning point for Immediate Financing Arrangements (IFAs). While previously tolerated due to sequencing and legal form, these leveraged insurance strategies could now be exposed to reassessment on the basis of economic substance and purpose. For accountants advising clients with IFAs—or considering one—the deductibility risk is now central.

## A Reimbursement Loop, Not a Capital Loan

At the heart of an IFA is a reimbursement mechanism:

1. A permanent life insurance policy is funded using after-tax capital.
2. A loan is immediately taken to replenish that capital, secured by the policy and/or corporate assets.
3. The loan proceeds are reinvested, and interest is claimed under paragraph 20(1)(c) as a deductible expense.

While technically structured as a business loan, the arrangement often lacks actual economic exposure. The insured pays a premium and almost immediately recoups the outlay through a loan, meaning the capital was never really at risk. CRA may now view the loan as circular and artificial, with the real purpose being to convert non-deductible life insurance costs into deductible interest.

## Paragraph 20(1)(c): The Carve-Out for Insurance

Paragraph 20(1)(c) allows interest deductibility only where borrowed funds are used to earn business or property income. But it explicitly **excludes interest relating to a life insurance policy**, even indirectly. IFA promoters have historically relied on sequencing to avoid this exclusion, arguing that the loan is not directly tied to the policy. The revised GAAR now allows CRA to disregard that sequence if the economic substance reveals otherwise.

CRA's longstanding position (e.g., Interpretation Bulletin 2000-005146) supports denying deductibility when loans merely replenish premiums. That position now has legal teeth under the revised GAAR framework.

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## Bill C-59: Three Key Changes That Jeopardize IFAs

1. **Lower Threshold for GAAR**
   GAAR now applies if *one* of the main purposes of a transaction is to obtain a tax benefit—not the sole or dominant purpose. Most IFAs fail this test, as the interest deduction is central to the structure's economics.
2. **Economic Substance Test**
   CRA can disregard transactions that are legally valid but lack real economic purpose. If the loan exists only because the premium was paid, the CRA may view the borrowing as lacking substance, even if technically reinvested.
3. **Disclosure and Penalties**
   IFAs may eventually be included in CRA's mandatory disclosure rules if viewed as avoidance transactions. Failure to report could trigger an unlimited reassessment period; even if disclosed, CRA now has three additional years to audit under GAAR. If GAAR applies, a 25% penalty applies to any tax benefit denied. The long-term risk exposure is significant.

## Questions CRA Could Ask

- Would the loan exist if the policy hadn't been purchased?
- Was the borrowing size/timing linked to the premium?

Affirmative answers raise red flags. Documentation of business purpose may not suffice if the economic reality shows the loan functions as a reimbursement for the premium. Furthermore, CRA may pursue legislative or interpretive changes—such as denying interest deductibility on **any debt collateralized by exempt assets like life insurance**, or recharacterizing such loans as **policy loans**. In that case, not only would the interest become non-deductible, but the loan proceeds themselves would be **taxable beyond the policy's adjusted cost basis (ACB).**

If this seems beyond the pale, accountants should revisit the **Department of Finance's 2013 Budget**, which dismantled the 10-8 leveraged insurance strategy on the grounds of circularity and artificial interest deductibility. At the time, Finance warned that **any future attempts to circumvent these rules**—through similar structures or slight variations—**would be dealt with more harshly**, and that **retroactive measures would be considered**.

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Compounding the issue, **IFA marketing materials and policy illustrations often undermine the claim that the loan is independent of the policy**. They frequently include tables showing a direct link between the premium and the loan, implying the borrowing simply replaces the outlay. The strategy's branding often suggests the policy is "no-cost" or "self-financing," **implying that the tax deduction and bank loan offset all out-of-pocket costs**. This framing makes it difficult to argue later that the loan had a separate, arm's-length business purpose.

## Professional Responsibility Going Forward

- **Model IFA scenarios with no interest deductibility** to evaluate whether the structure remains viable absent tax relief.
- **Stress-test policy performance** by reducing illustrated returns by 1% and 2%. In many cases, debt accumulation could exceed collateralized fund value.
- **Disclose GAAR exposure**. Clients must understand that deductibility may no longer be tolerated, even if the loan is technically legitimately invested.
- **Calculate taxable exit costs in later years**, notably when the policy's ACB has declined, as this may result in unexpected tax liability and significant financial loss on policy disposition and loan repayment.

## Conclusion

The revised GAAR rules turn IFA planning into a structurally exposed, audit-prone strategy. Without defensible deductibility, the core financial advantage collapses—leaving clients with long-term debt and no tax relief. The assumptions that may have once justified the risks **no longer hold** under Bill C-59. Accountants should reassess existing structures and advise clients proactively—**before those risks crystallize into lasting financial and tax consequences**.

Sincerely,
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