

Armstrong

— Financial Services —

November 21st, 2023

Attn: Insurance Memo

Re: Foreign Life Insurance Policy

The definition of CDA in 89(1) of the Act applies to a life insurance policy. This term is defined in 138(12) of the Act as including annuities and segregated funds. The CDA definition does not require that the policy be a life insurance policy in Canada?, rather, it requires that it be a life insurance policy. The CRA has confirmed that this means that a policy that is issued by a non-resident insurer or on a non-resident will qualify for CDA treatment when the death benefit is received by a CCPC.

The foreign policy must pass the Canadian exempt test to ensure that no accrual tax would be owed on the policy annually. If it is exempt, in respect of the CDA, the CRA has said that the policy ACB would have to be calculated in accordance with Canadian rules for the CDA calculation of a CCPC holding a foreign policy.

The life insurance policy in question (the "Policy") is a Term-to-Life type US-issued life policy that is designed to have a de minimus cash value that ultimately dwindles down to zero over a short time horizon. The face value is guaranteed level and the cash value is contractually limited and will have no variance. (The cash value is in fact always below the allowable test policy threshold and will be nil at life expectancy.)

With the objective of qualifying a Policy as an Exempt Policy in Canada and for calculating CDA, we are able to test:

- 1) actuarial certification that a Policy will be an Exempt Policy as defined pursuant to subsections 12.2(11) of the Act and pursuant to Regulation 306 of the Income Tax Regulations for its lifetime based on the contractually guaranteed values shown in the Policy illustration.
- 2) methodology to calculate the Adjusted Cost Basis ("ACB") of the Policy in Canadian dollars, as defined pursuant to subsection 148(9) of the Act, based on the Canadian Institute of Actuaries (CIA) Mortality Tables.

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November 21st, 2023

Attn: Insurance Memo

Re: May 2019 CLHIA Roundtable Q. 6, 2019-0799101C6

Question: Will the CRA provide guidance as to how to apply the exempt test to policies that are not life insurance policies in Canada??

CRA Response: A life insurance policy is essentially a contract between the policyholder and the life insurance company that issues the policy. While there may be types of policies that are issued in the same form to many policyholders, each policy issued by an insurer is conceivably different from every other policy issued by the insurer. An "exempt policy" for income tax purposes, is a life insurance policy that satisfies certain criteria, set out in section 306 of the Income Tax Regulations ("Regulations"). In general terms, a taxpayer who holds an interest in a life insurance policy that is an exempt policy is not subject to annual accrual taxation under section 12.2 of the Income Tax Act ("the Act") with respect to the income earned within the policy, and will not have an income inclusion under subsection 148(1) and paragraph 56(1)(j) of the Act, with respect to the proceeds, received as a consequence of the death of the life insured under the policy.

We acknowledge that the rules for determining whether any particular life insurance policy is an exempt policy under section 306 of the Regulations are themselves complex. The rules in section 306 of the Regulations apply on a policy-by-policy basis and require actuarial calculations and information that only the issuing insurer will possess. The tests in section 306 of the Regulations may be applied at any time but the tests are generally performed by the insurer that issued the policy on each policy anniversary date.

A life insurance policy issued by a non-resident insurer is not specifically precluded from qualifying as an "exempt policy" and thus, such a policy could qualify provided the criteria in section 306 of the Regulations are satisfied. Given that the information to determine the exempt status of a particular life insurance policy is only available in the accounts of the insurer, the onus is on the policyholder to establish that the policy qualifies as an exempt policy. This would include supporting evidence that the life insurance policy satisfies the exempt policy tests in section 306 of the Regulations. The CRA's mandate is to administer the Act and does not include resolving issues between policyholders and their insurers about the terms and conditions of a particular life insurance policy.

Steven Szilagyi, 2019-079910

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Attn: US Life Insurance Proceeds

Re: IRC U.S. Code § 2105 (a)

26 U.S. Code § 2105 - Property without the United States

(a) Proceeds of life insurance

For purposes of this subchapter, the amount receivable as insurance on the life of a nonresident not a citizen of the United States shall not be deemed property within the United States.

Source: <https://www.law.cornell.edu/uscode/text/26/2105>

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