

Impact of Bill C-59 on Immediate Financing Arrangements (IFAs)

Bill C-59, which received Royal Assent on June 20, 2024, significantly expands GAAR, increasing CRA's ability to challenge tax deductions and recharacterize transactions. IFAs, which rely on interest deductibility and collateral loans, are now at serious risk of CRA reassessment, retroactive taxation, and penalties.

Key Risks to IFAs Under the New GAAR Rules

- **Interest Deductibility at Risk** – Under the new definition of an "avoidance transaction" in subsection 245(3) of the Income Tax Act, CRA now has broad authority to determine whether a loan would exist independently of the associated insurance policy. Bill C-59 introduces the "one of the main purposes" test, lowering the threshold for GAAR application—if one of the main purposes of the loan is to obtain a tax benefit, CRA can deny interest deductibility, even if the loan has some business purpose. Since IFAs depend significantly on tax deductions, the strategy cannot survive without them. If CRA denies deductibility, the IFA collapses entirely, leaving the policyholder burdened with long-term debt and no tax relief.
- **Loan Recharacterization** – Under subsection 245(3), CRA has expanded authority to recharacterize collateral loans as taxable policy loans if they lack economic substance. If CRA determines that the loan would not exist without the policy, it may argue that the structure is merely a disguised policy loan engineered to avoid taxation. The result? Once assumed tax-free, loan proceeds can be retroactively taxed at the highest rates, creating an immediate liability and exposing the policyholder to unexpected costs.

CRA shut down the 10-8 leveraged insurance strategy in 2013 on similar grounds—IFAs now face the same risk. With CRA's expanded power to deny deductions and recharacterize loans, the strategy collapses without tax benefits, exposing policyholders to long-term debt and tax liabilities. Given rising CRA scrutiny, anyone considering an IFA should seek written expert advice or a formal CRA opinion before exposing themselves to severe tax consequences.

Sincerely,
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