Life insurance and the Captial Dividend Account

Throughout the video, a presenter is on the left side of the screen, speaking to the audience. Presentation slides appear on the right, displaying key points as the speaker discusses them.

Description: The slide is titled **Life insurance and the Capital Dividend Account**. The presenter's information is provided: Carol Foley, Director, Tax and Estate Planning Group.

Presenter: Thank you for joining us for today's webinar on Life Insurance and the Capital Dividend Account. Today's presentation will give you a deep dive into the Capital Dividend Account. Now that we are in this season of Fall, some of you may have taken a road trip during your summer vacation, or maybe you've done it years ago. Like a road trip, you have a destination. So, our destination today is CDA, the Capital Dividend Account. You may have had a reason for doing your road trip, so we'll set out why we have the Capital Dividend Account and what it includes. A road trip usually has some stops along the way, so we are going to have examples of how the CDA is calculated with a focus on life insurance and how it's added to the CDA. As well, on road trips, you may have unexpected stops, so ours will review charitable giving with a corporation and how to maximize the CDA. Finally, with driving in general and road trips, we need to be aware of our blind spots. I will review some examples of CDA blind spots. And finally, we'll reach our destination and we'll review what we've discovered on our CDA road trip. I will also provide some things you may want to do to be proactive in sharing knowledge that you have gotten from this road trip with your clients and advisors. Let's get started.

Description: The slide is titled **Important Considerations**. The presenter discusses five bullet points.

Presenter: Like all things when we're dealing with tax and estate planning, this information is based on current legislation and interpretations for Canadian residents and is accurate to the best of our knowledge. Future changes to tax legislation and interpretation may affect this information. This information is general in nature and is not intended to be tax or legal advice. And as always, for specific client situations, your client should consult their appropriate legal accounting and tax advisors. This information is current as of September 2025.

Description: The slide is titled **Capital Dividend Account**.

Presenter: And now let's get into the presentation. So, as I started, this is the Capital Dividend Account and let's look at what we're first going to look at in the next slide.

Description: The slide is titled **Capital Dividend Account (CDA)** with two topics highlighted: (1) Set the context of the CDA and (2) What gets added to the CDA.

Presenter: So, I think it's always good to have some context about how we have the capital dividend and what gets added to the Capital Dividend Account. So, we'll get into more specifics.

Description: The slide is titled **CDA – Context**. The presenter discusses “What is the Capital Dividend Account?”.

Presenter: So, what is the Capital Dividend Account? The Capital Dividend Account is a notional account and it begins from the later of 1971 and the time that the corporation became a private company, which could have been on its incorporation, or it became a private company after it ceased to be a public company. And the Capital Dividend Account is going to track certain tax free amounts that are received by private corporations. The Capital Dividend Account is defined in the provisions of the Income Tax Act of Canada in subsection 89 (1). And the calculation of the CDA is cumulative. So, it starts from after 1971, so the beginning of 1972, if the company had been incorporated then, and it will continue during the whole time that the company is in existence. So therefore, the calculation of the CDA is cumulative and you need to have the historical information of the CDA before paying a capital dividend. And you may have wondered why there had been the year 1971, the later of after 1971. Well, in 1972, Canada started taxing capital gains. So before that, capital gains were not taxed, so that's why we have that date in the Income Tax Act.

Description: The slide is titled **CDA – Why do we have the CDA?** The presenter discusses the principle of “integration”. An image on the left depicts the net income for an individual versus an image on the right depicting net income for a corporation and shareholder.

Presenter: And so, why do we have the Capital Dividend Account? I've been talking about just the non-taxable portions go into this account. So, in the Canadian tax system, one of our principles is that of integration. And the principle of integration is that the tax on income earned by a private corporation and then paid out as dividends to an individual shareholder should be approximately the same. That would have been the situation as if the individual had earned the income directly. So, when everything is in balance, that means the individual would be indifferent as to whether they were earning their income as just an individual or whether it was being earned in the corporation and then paid out, the after tax amount paid out to the shareholder as a dividend. And so that's when we have perfect integration, if we're indifferent to how we're earning it. Like all things in Canada, it's not perfect integration, but that's a concept behind our principle of integration. And in Canada, the Capital Dividend Account is really important because if a corporation is earning something like capital gains, we know that right now only half of the capital gains is subject to tax and the other half is received tax free. So, when that tax free amount goes into the Capital Dividend Account, that can be paid out to a shareholder on a tax free basis. If we did not have this concept, then something like those non-taxable capital gains that would be paid out to a shareholder would be taxed. And the average non-eligible tax rate for individuals at the highest marginal tax rate is about 45% in Canada. Actual rates will vary by province. The rate in Ontario is 47.74% and in Quebec it's 48.70%. So, the bottom line is if we didn't have the Capital Dividend Account, these tax free surpluses to the corporation would need to be distributed from the corporation as a taxable dividend and that would be in conflict with our principle of tax integration. Please note that this is what happens in Canada, but not all other countries have this concept of integration between the individual and the corporations. For example, the US does not have a concept of a Capital Dividend Account.

Description: The slide is titled **CDA - Review of four main components**. The presenter discusses the four main components in detail.

Presenter: So, as I said, this is a tax driven account, it's a notional account. And so the Income Tax Act has set out what are the main components of the Capital Dividend Account, and there are four main components. The excess of the non-taxable portion of the capital gains over the non-deductible portion of capital losses. The capital dividends received by the corporation. So that means that the corporation can receive capital dividends from other corporations. And then we have the non-taxable portion of gains resulting from the disposition of eligible capital property. And one of the most common assets that would be falling into this account would be goodwill. Now like all things tax, there are different rules and gains from dispositions of eligible capital property are only credited to the CDA at the end of a taxation year. So there is a risk of over electing tax free capital dividend if the gain was added to and included in a dividend in a tax free capital dividend if it was paid before the corporation's year end. And then what we're going to spend a lot of time today is the 4th component which is the proceeds of life insurance policy. And so what is added is the proceeds less the policies adjusted cost base. And then those are the components and then of course we're adding all of those things. And if a corporation pays a tax free capital dividend, that amount is deducted from the balance of the Capital Dividend Account.

Description: The slide is titled **CDA – Life insurance component** and the presenter discusses each bullet on the slide, including key person insurance.

Presenter: And what's really interesting about the Capital Dividend Account is it's not tied to the actual insurance payout received by the corporation. So, if the corporation had gotten life insurance on a key employee to mitigate financial losses if they happen to pass away, the corporation can receive the life insurance proceeds on the death of that key person. And the corporation is able to use those life insurance proceeds for business purposes. They could use it to recruit and hire a new key person employee. And so they still are able to use the CDA credit and they could use it to pay capital dividends out of their retained earnings. The other thing is our corporate clients may want to use corporate life insurance for borrowing purposes. So, let's in the next couple of slides, we're going to review two ways that a corporation can use their life insurance proceeds for borrowing. And the two ways that this can be done is through collateral borrowing of the policy or on getting a policy loan. So, let's look at both of these in more detail.

Description: The slide is titled **CDA – Life insurance component – borrowing** with a focus on collateral assignment.

Presenter: So, the collateral assignment of a corporate owned life insurance policy is that the policy is collaterally assigned to a bank for a loan. And so how does that work? They're going to assign it to the bank for a loan. And in this example, we are assuming that the corporation is also the beneficiary of the policy. Now let's assume that the insured passes away and the corporation receives the death benefit. So, we have talked about that the amount of the death benefit received by a corporation less the adjusted cost base is added to the corporation CDA. So, if the insured passes away while the loan is outstanding, all or a portion of the insurance payout would first be used to pay off the loan.

However, the corporation is still able to receive the CDA based on the full insurance payout less the policy's ACB because the proceeds are considered to be constructively received by the corporation, even though the amount would have been paid directly to the financial institution. So that's a really important nuance in how the collateral assignment works, and with the addition to the Capital Dividend Account. Now, like many things in life, these are some of the benefits and there are risks with this kind of strategy. Collateral loans involve risk. We'd recommend that they should only be used by sophisticated investors with a high risk tolerance and that they get professional advice from their lawyer and accountant. The loan would be subject to the lender's financial underwriting and other requirements. And of course, the policy owner should have enough income and capital to cover the interest and loan repayment as well as the insurance premiums. And I had mentioned before, it's really important that the corporation remain the owner and beneficiary of the policy. And in a technical interpretation that is referenced here in the slide, the CRA noted that the requirement in the CDA definition that life insurance proceeds be received as a consequence of death of the life insured will be met when the proceeds are received by the corporation as beneficiary of the policy. And even if the life insurance policy has been assigned to a financial institution as collateral on a debt owed by the corporation, the corporation remains the beneficiary. The proceeds as I mentioned before are considered to be constructively received and this allows the ability for the corporation to get the credit to its Capital Dividend Account. So now let's look at another way that a corporation could borrow using a life insurance policy. So, this next way is that the corporation could get a policy loan and it would be secured by the life insurance's cash value. Canada life policy owners have a contractual right to obtain a policy loan based on their policy's cash value. The specific amount that they can borrow will depend on the rules regarding their particular life insurance product such as whether it's a participating life insurance policy or it's a universal life insurance policy. Other factors that need to be considered when you're dealing with a policy loan is no financial underwriting would be required, and it could preserve the policy's growth potential as opposed to what would happen if the clients had done a partial surrender of the policy. Other things to consider is policy loan interest rates are typically higher than bank loans and the policy loans may be taxable depending on the policy's ACB. The other thing that will happen with the policy loan is the CDA credit will not be as much as what would happen in the collateral assignment. So, if you look at this slide at the bottom loan for the policy loan with the life insurance policy, the CDA credit will be based on the full insurance payout less the outstanding policy loan and the policy's adjusted cost base. This is unlike the collateral assignment where the CDA amount is based on the full insurance payout less the policy's adjusted cost base.

Description: The slide is titled **CDA – Examples of calculating the CDA** and the presenter outlines what will be covered in the next few slides.

Presenter: So now let's switch gears a bit and look at some examples. So, we've started out on a road trip. We've determined why we were going on the road trip and now we're going to start to stop and see some sights along our road trip. And we're going to look at examples of how the Capital Dividend Account is actually calculated. So, there's nothing like looking at an example to see how something works.

Description: The slide is titled **CDA – Example**. An image shows a shareholder has a Holdco and a Subco. An example is outlined on the right.

Presenter: So, in this example, we have a shareholder who has a Holdco and a Subco, and the shareholder's accountant is starting to calculate Holdco's Capital Dividend Account. And what's nice about this situation is there have been no other transaction in Holdco's history that would affect its Capital Dividend Account before September 30th, 2016. Now on September 30th, 2016, Holdco realized a capital loss of $100,000 and it received a capital dividend from Subco of $50,000. So, when we had talked about the different components of the Capital Dividend Account, we talked about whether there were capital gains or capital losses, and then we're dealing with the non-taxable portion so we've got a capital loss, so the non-taxable portion of that capital loss is $550,000. And then we had talked also that it's possible for another corporation to get capital dividends from other corporations. So, I'm wondering if you would like to think for just a minute about what you think Holdco's Capital Dividend Account balance would be.

Description: The slide is titled **CDA calculation – Components are calculated independently**. A table is displayed on the slide. The table has three columns titled CDA component, CDA component calculations and Total. The presenter walks through the figures in the table.

Presenter: We have the non-taxable capital gains, we didn't have any. We have the non-deductible capital loss which is $50,000. And so you may be looking at the far column which has a $0. And so that's our capital gain / capital loss component. And it's not possible for a component to have a negative amount so that's why it has gone to zero. And then we have the capital dividends that Holdco got from Subco and that's an addition to that component of the Capital Dividend Account. So, when we put $0 + $50,000, we have a Capital Dividend Account balance of $50,000. And so this means that Holdco has the ability to pay a tax free capital dividend to its shareholder of $50,000.

Description: The slide is titled **CDA – Observations / Recap**. The presenter summarizes the content presented on the slide.

Presenter: So, this is just to recap that each component of the Capital Dividend Account is calculated independently. So, we have the non-taxable capital gains and the non-deductible capital losses. And while we appear to have a negative balance for purposes of calculating the Capital Dividend Account, that negative amount will go to zero in the computation of figuring out what the balance is in the CDA. Capital dividends. We also had the capital dividends from the other corporations which deduct any capital dividends paid and that's our Capital Dividend Account balance. So, let's look at building on this first example.

Description: The slide is titled **CDA – Examples of calculating the CDA**. To build on the previous example, a bullet indicates Holdco will receive an insurance death benefit.

Presenter: And in this case, as we built on this, the company Holdco is going to receive an insurance death benefit.

Description: The slide is titled **CDA – Example 2 – Building from Example 1**. An image shows a shareholder has a Holdco and a Subco. An example is outlined on the right.

Presenter: So, we're building on the situation that we already had where the accountant had been calculating the Capital Dividend Account for Holdco. So now we have some additional facts. On October 15th, 2016, Holeco paid a $50,000 capital dividend to its shareholders and we knew that we had that Capital Dividend Account balance and so that is fine. And then on October 31st, Holdco recognizes a capital gain of $80,000 and the non-taxable portion of that capital gain is $40,000. And then on October 31st, this is where we have the life insurance component, they receive a $500,000 death benefit from a key person life insurance policy, and the policy had an ACB, adjusted cost base of $100,000. And the policy is not part of a 10/8 arrangement and it wasn't transferred to a corporation in a non-arm's length transaction. Just sit with those facts, the last couple facts that I explained and later in the presentation we'll get into more depth of why those facts will be important in calculating the capital dividend but it's not important for this particular example. So, let's look at the computation of the Capital Dividend Account for Holdco with these additional facts.

Description: The slide is titled **CDA – Company receives an insurance death benefit**. A table is displayed on the slide. The table has three columns titled CDA component, CDA component calculations and Total. The presenter walks through the figures in the table.

Presenter: We now have non-taxable portion of capital gains of $40,000 because it was a total capital gain of $80,000. And then we still have the carry forward of the non-capital losses that we had at the beginning in Example 1. And again, 40 - 50 is still negative, so for purposes of the components of the Capital Dividend Account that goes to zero. We had the capital dividends that were paid from the other corporation, from the Subco, of $50,000. And now we're looking at the life insurance death benefit received. We have the death benefit of $500,000, the policy's adjusted cost base is $100,000 so that component of the Capital Dividend Account is $400,000. We had paid capital dividends of $50,000, so in this case, the company at this point in time has a CDA balance of $400,000.

Description: The slide is titled **CDA – Observations – Company receives a death benefit**. The presenter summarizes the content presented on the slide.

Presenter: Again, just to say that we can't have that negative balance, it will go to zero. We include capital dividends from other corporations. And then with the life insurance death benefit, it's the death benefit minus the adjusted cost base and we deduct capital dividends that have been paid and that gives us our balance. So, this is looking, I think fairly straightforward. So, let's move on to another example.

Description: The slide is titled **CDA – Examples of calculating the CDA**. Presenting another example, a bullet indicates CDA can appear to have a negative balance.

Presenter: And this is that the CDA can appear to have a negative balance when we think we have a certain amount in the Capital Dividend Account and you might think we can pay this amount and then we need to look at the calculation. So, let's look at this example.

Description: The slide is titled **CDA – Example 3 CDA apparent negative balance**. The presenter walks through the content on the slide.

Presenter: So we have again a Holdco situation and it's realizing a capital gain of $1,000,000 and we know that the non-taxable portion would be $50,000 and that was added to the CDA, and then it declared a capital dividend of $500,000 in 2015. So we had an input and then we essentially have deduction. And now we're into 2016 and the company has realized a capital loss of $1,000,000 and the non-taxable portion of the loss of 50% was included in the CDA calculation as a deduction. And now it's receiving a death benefit of $1.5 million and it has no adjusted cost base. So what is the CDA balance of Holdco? Let's go through the computation.

Description: The slide is titled **CDA – Appears to have a negative balance**. A table is displayed on the slide. The table has three columns titled CDA component, CDA component calculations and Total. The presenter walks through the figures in the table.

Presenter: So again we're looking at the capital gains and losses. We had the $1,000,000 capital gain, so the non-taxable portion of $500,000, and we also have non-deductible capital loss of $500,000 so that works out to zero. And then we've got the death benefit of $1.5 million, no policy adjusted cost base so that's $1.5 million. So, you may have been thinking when I first went through the facts that the company Holdco would be able to pay out a capital dividend of $1.5 million. However, the company had paid out a capital dividend after it received its capital gain, it had paid out the non-taxable portion of that capital gain as the capital dividend. So, the CDA balance that's available at this particular point in time is $1 million.

Description: The slide is titled **CDA – Observations – Apparent negative balance**. The presenter summarizes the content presented on the slide.

Presenter: So again, just to recap, the CDA balance could appear to be negative, but it's not. And because of the cumulative nature of the Capital Dividend Account, things that have happened in previous years can impact the Capital Dividend Account when we're dealing with the current year. So, I hope you're getting a sense that the Capital Dividend Account calculation is not always the most straightforward and it takes care and attention to make sure that it's being done appropriately.

Description: The slide is titled **CDA – Examples of calculating the CDA**. Presenting another example, a bullet indicates a non-arm's length policy transfer to a corporation after 1999 and before March 22, 2016.

Presenter: So, let's move on and we're going to look now at a different example where we've got a non-arm's length policy transfer to a corporation that was after 1999 and before March 22nd, 2016.

Description: The slide is titled **CDA – Example prior to March 22, 2016**. On the left is an image with the words "Controlling shareholder" and "Corporation". A scenario is outlined on the right.

Presenter: So in this case, we're going to start with what would happen before March 22nd, 2016. And we had a corporation and we had a controlling shareholder, and the controlling shareholder had had a policy that they had owned personally and now they were going to transfer it to the corporation.

And under the rules of the Income Tax Act then, the transfer price was deemed to be amount equal to the policy's cash surrender value even if the corporation had paid fair market value for the policy. And so this meant that the corporation could withdraw an amount equal to the fair market value of the policy tax free. And a number of this was all within the provisions of the Income Tax Act. It will not probably come as a surprise to you that CRA was not necessarily happy with this situation so in the 2016 federal budget, they made changes to the provisions of the Income Tax Act.

Description: The slide is titled **CDA – Example prior to March 22, 2016 after 2016 Federal budget**. The same image from the previous slide is on the left and an "X" appears on the right crossing out the sentence "Shareholder could withdraw amount equal to FMV of the policy tax-free".

Presenter: And so now if we had that situation of the controlling shareholder transferring the policy to the corporation, the proceeds of disposition are deemed to be the greatest of the cash surrender value of the policy, the adjusted cost base of the policy, the fair market value of the consideration given, which is the price paid for the policy. So I've axed through the following sentence that before the 2016 federal budget that a shareholder could withdraw an amount equal to the fair market value of the policy tax free. That is no longer possible after the 2016 Federal Budget.

Description: The slide is titled **CDA – 2016 Federal Budget**. The presenter walks through the content on the slide.

Presenter: So not only did the 2016 Federal Budget make the changes that I just talked about, they also amended the CDA calculation where private corporation had acquired a life insurance policy for a non-arm's length person (and that's a person, not a corporation) anytime between January 1st, 2000 and March 21st, 2016. And the payout is received after March 21st, 2016. So, in addition to our usual grind to the CDA credit when you've got life insurance proceeds minus the adjusted cost base, this budget introduced 2 new grinds. We have a fixed grind and a declining grind.

Description: The slide is titled **CDA – Non-arm's length policy transfers to a corporation after 1999 and before March 22, 2016**. The subject of the slide is "Fixed grind". The presenter walks through the content on the slide.

Presenter: And so let's go through the details of those. The fixed grind is the fair market value of the consideration given by the corporation for the policy less the greater of the policy's cash surrender value and adjusted cost base immediately before the transfer. Now the one thing about the fixed grind is it will not change over time. If the corporation paid more for the policy than its cash surrender value or adjusted cost base, then that amount will reduce the CDA credit. So that's component one. The second component is the declining grind, and this is the amount if any, by which the lesser of the fair market value of the consideration given by the corporation for the policy and the policy's ACB before the transfer. So the lesser of those two exceeds the policy's cash surrender value immediately before the transfer and then you subtract the absolute amount of any negative ACB at the time of death. Determining the policy's negative ACB involves tracking the net cost of pure insurance grind on a policy's ACB that would be an amount below $0. So, if your head's spinning a little bit with all of this wording, let's look at an example because I think that will help it make a little bit more sense or make it more concrete.

Description: The slide is titled **CDA – Transfer for FMV consideration between January 1, 2000 and March 21, 2016**. On the left is an image with the words “Controlling shareholder” and “Corporation”. A scenario is outlined on the right.

Presenter: So, this is a situation where we had that kind of transfer that is now under those new rules that came as a result of the 2016 Federal Budget. So the transfer took place sometime between January 1st, 2000, and March 21st, 2016. And so this controlling shareholder was transferring their personally owned policy to the corporation. And we're going to look at a situation where we have a hypothetical level cost universal life policy on the life of a 50-year old female. We have $100,000 policy coverage and its minimum funded. The transfer by the controlling shareholder to the corporation took place at year 20. The fair market value of the consideration was $35,000. The ACB of the policy was $12,500 and there was no cash surrender value in the policy. Holdco's new ACB and the policy was nil and now is according to the provisions of 148(7) of the Income Tax Act, that was for the policy transfer prior to the 2016 budget, which allowed that to be done. And the corporate policy owner, corporation, continues to pay premiums, which is added to the policies adjusted cost base each year. And then the net cost of pure insurance is applied to decrease the adjusted cost base each year. So now we'll look at three examples where the life insured dies at policy year 21, 25 and 30. So let's look at this next chart with some numbers.

Description: The slide is titled **CDA – Fixed and Declining Grind**. A table is displayed on the slide. The presenter walks through the figures in the table.

Presenter: So, we had looked at the cash surrender value at the year of transfer for year 21. There was none for any of the years. The adjusted cost base at the year of the transfer was $12,500. The fair market value paid by the corporation was $35,000. The new ACD was $0. Our cumulative premium from year 21 is $1,250. Our cumulative net cost of pure insurance from year 21 was $1,800. So in year 21, we are looking at a negative adjusted cost base on depth of $550. Then when we go to year 25, the beginning stuff is the same. Our cumulative premiums at year 25 are now $6,250. Our cumulative net cost of pure insurance is $11,500, so the negative ACB in year 25 is $5,250. And in year 30, the cumulative premiums have gone up to $12,500. Cumulative net cost of pure insurance is $31,750 and our negative ACB on death would be $19,250. So, we're going to continue to keep working through this sample and let's first go and look at what the fixed grind would be on this policy.

Description: The slide is titled **CDA – Observations – Fixed and Declining Grind**. The presenter summarizes the content presented on the slide.

Presenter: So one of the things we had talked about was the fixed grind doesn't change, so once it just stays the same. So we had the fair market value was $35,000 and it was the greater of the cash surrender value and the ACB before the transfer. So the greater of that is the $12,500 which is the ACB on the policy. So our fixed grind on this life insurance policy is $22,500. So now we've done with the fixed grind and the fixed grind attempts to claw back the tax benefits that were achieved from this transaction by reducing the corporation CDA by the fair market value consideration over the policy’s adjusted cost base. So that's what they were trying to achieve with this fixed grind. Now let's move on to looking at how the declining grind will work.

Description: The slide is titled **CDA – Fixed and Declining Grind**. A table is displayed on the slide. The presenter walks through the figures in the table.

Presenter: So again, more numbers. And so when we're looking, we had already gone through what the negative ACB was. And so really, we've done the fixed grind and now we're going to look at the declining grind. And in year 21, the declining grind is the lesser of the fair market value consideration of $35,000 and the ACB before the transfer. So the lesser of that that exceeds the cash surrender value before the transfer which was $0. And then we start to subtract the negative ACB at death. And we had gone through the computations that was $550 in Year 1, $5,250 in Year 25, and $19,250. So our CDA credit with a death benefit of $100,000 in Year 21 has a fixed grind deduction of $22,500 and then the declining grind of $11,950. So, the CDA credit in Year 21 is $65,550. And then I'll just talk to Year 30. Again, we're looking at the death benefit of $100,000. That fixed grind does not change, it's $22,500. And the CDA credit will be $77,500. The declining grind is trying to claw back the tax benefits that were achieved from the corporate policyholder by obtaining a lower adjusted cost base than that of the transfer order. So that would have resulted in a larger CDA credit if the life insurer had died shortly after the transfer. Over time the amount of the declining grind is reduced, which makes sense as the net cost of pure insurance would have reduced the policy's adjusted cost base to the corporation.

Description: The slide is titled **CDA – Observations – Fixed and Declining Grind**. The presenter summarizes the content presented on the slide.

Presenter: So, just to recap what's going on with this is the fixed grind is straightforward. It doesn't change over time. So essentially if the corporation paid an amount that was more than the policy's cash surrender value or adjusted cost base, that amount is going to reduce the Capital Dividend Account credit. The declining grind is complicated and involves the negative ACB and so that's the tracking of the net cost of pure insurance grind to a policy's ACB and then we're looking at being in a negative amount.

Description: A new title slide introducing another topic. The title is **Capital Dividend Account & Charitable Giving**.

Presenter: So, I'm thinking we did some of our major stops as we looked at the different components of the Capital Dividend Account. So maybe we want to take a side trip and look at a different situation. So this is going to be a stop that was not originally on the agenda but let's look at Capital Dividend Account and charitable giving.

Description: The slide is titled **CDA – Charitable Giving and Life Insurance**. The presenter walks through the content presented on the slide.

Presenter: As you know, there are many benefits of charitable giving with life insurance for our clients. They are able to support a charity's ongoing activities. They can create a legacy for your clients and their family and it can come with potential tax benefits.

Description: The slide is titled **CDA – Charitable giving and life insurance**. The presenter walks through the content on the slide. On the left is a box indicating 90% of advisors feel they've discussed philanthropy with their clients. On the right is a box indicating 13% of Canadians feel they've had a fulfilling conversation about philanthropy with their advisors.

Presenter: So, I thought I would just share this slide because a lot of times we think we're saying something, and what we think we've said and what somebody else has heard is not always congruent. So, this is from an article that said that there is a potential disconnect between what advisors are offering and what clients are hearing in relation to philanthropy. 90% of advisors had felt like they had been discussing philanthropy with their clients, but only 13% of Canadians have felt like they had a fulfilling conversation about philanthropy with their advisors. So that does seem to be quite a big contrast between the two different parties in this conversation. And this is from an article from the Philanthropist Journal by Sharon Wiley, and it was entitled "Financial Advisors are Talking to Canadians About Money but are they talking about charity?". And this was based on research that had been conducted in 2013 and it's often quoted and referred to, but I thought it was important so that people may be thinking that they've been talking to their clients about philanthropy and life insurance. And maybe, it might require just sometimes you can ask your clients what did they hear about what you were saying? And just to make sure that you're both on the same page.

Description: The slide is titled **Charitable giving and life insurance - Individual**. On the left is the word "Helen" and on the right is "Gift to charity".

Presenter: So before we get into the corporate giving with life insurance, I thought I would just start with how an individual could make use of charitable giving and life insurance. And then we'll move into the corporate situation. So donations by an individual will create a tax credit and it can be used to reduce taxes within certain limits. And generally when we're looking at charitable giving and life insurance, an individual can donate the life insurance proceeds of a policy by naming the charity as the beneficiary of the life insurance policy, or they can pay premiums on the life insurance policy that is owned by the charity. And when the policy is individually owned and the charity is named as the beneficiary of the policy proceeds, the death benefits, the tax rules related to donations by individuals permit a graduated rate estate and deceased individuals to claim the charitable donation tax credit. And this credit will generally be equal to the proceeds which can be used to address income taxes that may have risen on the individual's death. And this way of getting tax deduction is possible because there's this specific provision in the Income Tax Act 118.1(5.1) that permits an individual to directly designate a charity as the beneficiary and claim the death benefit as a charitable gift. And the other option is if the donor pays the premiums on a life insurance policy that's owned by the charity, then the donor would get those tax deductions for the premium payments during their lifetime and there would not be any deduction for that individual on the life insurance proceeds when they pass away.

Description: The slide is titled **Scenario 1 – Corporate - Charitable giving and Life insurance**. On the left is "Helen Inc." and on the right is "Charity named as beneficiary".

Presenter: So that's the individual context. So, let's say we have our client Helen and she considered doing it personally, but then she said I have a corporation and I want to name the charity as a beneficiary of my corporate owned policy. So, I'm going to give you just a second to think whether you think that would be a good idea. And since I have a big "X" in the next slide, maybe we'll just take care of that now.

Description: The slide is titled **Scenario 1 – Corporate - Charitable giving and Life insurance**. The slide is the same as the previous slide but with an "X" through "Charity named as beneficiary".

Presenter: So one of the things is the donations by a corporation create a tax deduction instead of a tax credit, and that tax deduction can reduce corporate income. Again, like all things in tax, subject to limits. Now if we name the charity as the beneficiary of the corporate owned policy, it will not qualify as a donation. From CRA's point of view, they consider that the payment to the charity is by virtue of legal obligation under the policy because the charity was named as the beneficiary. And the other thing is in that kind of situation from a tax perspective, there is no addition to the corporation's CDA for the life insurance proceeds, and we certainly have just gone through all the benefits of the corporation being able to get a credit to its Capital Dividend Account for life insurance proceeds less the adjusted cost base of the policy. And so, it's not possible in the corporate situation and that's because under the Income Tax Act, there's no similar provision that allows the charity named as the, as that I talked about when we had the individual situation where there was a provision under the Income Tax Act that allowed the individuals to get that tax deduction even though the charity had been named as a beneficiary of the policy. There is no similar provision to that 118.1(5.1) of the Income Tax Act for corporate donors.

Description: The slide is titled **Scenario 1 – Corporate - Charitable giving and Life insurance**. The presenter walks through the content on the slide.

Presenter: So, I wanted to put the individual and the corporate together to kind of say what happens individually does not necessarily work as well for a corporation. So, I've now given you kind of the problems about it, so what could Helen do to be able to still make use of her corporate owned insurance to be able to make a life insurance donation? So, one of the things is she should name Helen Inc. as the beneficiary of the life insurance policy and then Helen Inc. could claim the tax deduction for the charitable gift, again subject to the limits with the corporation and their circumstances. And by also having Helen Inc. named as the beneficiary of the life insurance policy, Helen Inc. can get a credit to its CDA, which insurance proceeds less the adjusted cost base. And then to make sure that the gift actually happens, Helen can direct the use of the insurance proceeds to make a charitable gift through corporate resolution. Helen Inc. could potentially pay the tax free capital dividend to the deceased's estate or the surviving shareholders who could then make the charitable gift. So, there are solutions to deal with this situation. And another option is, or if you want more information about this, we have a new section in our Tax and Estate Planning Group website that's called **Insights and Analysis**. And we have an article that talks about doing charitable giving with a corporation. So, there's additional reading there if you'd like to think about doing this in a bit more.

Description: The slide is titled **Corporate – Charitable Giving and Life Insurance - Recap**. The presenter summarizes the content presented on the slide.

Presenter: So, let's just recap that corporate charitable giving with life insurance requires attention to details to ensure that you get tax effective results. And we certainly know that clients that are charitably minded can do this to support their charity's ongoing abilities, create maybe a legacy and also take advantage of tax benefits. But it's really important that time and attention be placed into making sure that this planning is done in a way that all the benefits can be maximized.

Description: A new title slide introducing another topic. The title is **Capital Dividend Account - Blind spots**.

Presenter: So, we're still on our road trip, and we've been going quite a while, and I mean, certainly we should be looking for blind spots along the way. But I'm thinking you might be getting a little overwhelmed with all the different details that we've been covering. So, I thought I might spend some time on some blind spots, and these are a little bit more like quick hits to talk about things.

Description: The title of the slide is **CDA for Corporations – Blind spots**. The slide lists four blind spots which the presenter reads.

Presenter: So, we're going to cover four different blind spots when we have multiple corporations as beneficiaries, if we're looking at co-ownership arrangements, if we have non-resident shareholders, and if there were outstanding amounts of 10/8 policy borrowing.

Description: The title of the slide is **CDA – Blind spots – Corporate beneficiaries - Background**. The presenter walks through the content on the slide.

Presenter: So, let's get started. So corporate beneficiaries. For debts that were before March 22nd, 2016, a corporation CDA was reduced by the adjusted cost base of the policy to the corporation receiving the death benefit. And if the corporation was a beneficiary and not the owner, the full death benefit would be a credit to its Capital Dividend Account. So that resulted in a higher capital dividend credit for that corporation.

Description: The title of the slide is **CDA – Blind spots – Multiple corporate beneficiaries**. The presenter walks through the content on the slide.

Presenter: So, you may have been thinking now that 2016 Federal Budget was full of a lot of life insurance impacts for the industry. So, with the 2016 Federal Budget, for debts occurring after March 21st, 2016, the CDA will be reduced by the ACB of the policy, even if the receiving corporation is not the owner of the policy. So, what had been possible before this budget is no longer possible. And there's even more on this, is that, if the policy had two corporate beneficiaries, the policy's full ACB will reduce the capital dividend credit for each beneficiary. And you may be thinking this is not fair, but this is how CRA is interpreting the section, and so there is no proration. So, if for some reason clients have arranged their affairs, maybe they did this before budget changes. So, if it's possible, maybe they can make changes to how they have things set up, that they are not caught by this new rule. So, you just don't know what's going on with your corporate clients. So, but this is a really important thing, that there's no proration, so CRA is administering, it’s just a deduction for both of the corporations.

Description: The title of the slide is **CDA – Blind spots – Co-ownership arrangement**. The presenter walks through the content on the slide.

Presenter: And so that was if you know different corporations were named. It's also possible that we may have a co-ownership arrangement and again, in a co-ownership arrangement, the policy’s full adjusted cost base will reduce the CDA calculation for each of the corporate owners. Again, the ACB won't be prorated by the portion of the death benefit by the corporate beneficiary. And again, the amount will be deducted for each corporate co-owner. So effectively it's getting double counted and that's what's going to happen in those situations.

Description: The title of the slide is **CDA – Blind spots – Non-resident shareholders**. The presenter walks through the content on the slide.

Presenter: Now this is an interesting one because we always talk about how the Capital Dividend Account is a tax free capital dividend. However, if we have shareholders of the corporation who are non-residents, there is withholding tax that is required on a capital dividend that is paid to a non-resident shareholder. And it also would be required if the capital dividend was paid to an estate and subsequently distributed to a non-resident. So, withholding tax may be reduced by a tax treaty between Canada and the recipients’ country of residence. So in general, this is a really important thing. So, whether or not it's possible that the structure is such that a capital demand isn't going to be paid out to the shareholder, there's another way for them to get funds. That would definitely depend on the particular circumstances. But the other thing that's really important to remember about this situation is at the time your clients set up these corporate structures and they had their shareholders or they had their trusts and everything, it's not uncommon for at that time that the shareholders and/or the beneficiaries of an estate were residents of Canada. But I certainly know that we've been seeing a lot of cross-border people moving to different countries, children go off to school in the States or in Europe and then they stay and they become non-residents of Canada. So, it's quite possible that at the time the planning was first done, we all had, we had Canadian resident shareholders, but over time we could have a change to the situations and we now have non-resident shareholders. So consideration could be whether any planning could be done to deal with this now when they now know they have non-resident shareholders. Again, it would depend on the particular circumstances and whether there could be some planning done to deal with this. But it would certainly be better to have this highlighted for your clients to see if anything can be done to deal with this issue.

Description: The title of the slide is **CDA – Blind spots – Other CDA reductions**. The presenter walks through the content on the slide.

Presenter: And this is another thing that came out of the 2016 Federal Budget. This is if the Capital Dividend Account can also be reduced by the amount of the paid up capital withdrawn from a corporation if the paid up capital resulted from a contribution of capital by way of a transfer of a life insurance policy. And so, this is if that had been done before the 2016 Federal Budget and then we have the payout from the life insurance policy after that, this reduction can still apply. So the Budget 2016 made amendments and this is from the budget documents. They made amendments to the Income Tax Act to ensure that amounts that were not, are not inappropriately received tax free by a policyholder as a result of the disposition of an interest in a life insurance policy. And we have already reviewed the changes in applying the policy transfer rule and that it would include the fair market value of any consideration given for an interest in insurance policy in the proceeds of disposition and the acquiring person's cost. And so, in addition, where the disposition arises on a contribution of capital of the corporation, any resulting increase in the paid up capital and respective shares of that corporation and the adjusted cost base of the shares will be limited to the amount of the proceeds of disposition. And so, again, we could look at the amount of the Capital Dividend Account being reduced.

Description: The title of the slide is **CDA – Blind spots – 10/8 policy borrowing**. The presenter walks through the content on the slide.

Presenter: So, we have another blind spot. Earlier in the 2000s we had 10/8 arrangements and they were where you were looking at having an over funding of a life insurance policy and then obtaining a loan or investment, a business or investment loan and you were using the policy’s cash surrender value as collateral. And under these arrangements, the rate of return on the policy’s account value and the loan interest rate were linked and the growth in policy as we know is tax advantage and the interest on the loan was a tax deductible expense and a portion of the premiums paid may also have been deductible. So, that's what the situation was. Let's look at what happened with some tax changes. And so, in the 2013 Federal Budget, they ended tax advantages that were associated with the 10/8 arrangements and one of these measures applies to deaths after 2013. And so, they say that the capital dividend credit will be reduced by the borrowed amounts outstanding under the 10/8 arrangement at the time of death. So result of this change, they're just they essentially lost the tax effectiveness that they had had.

Description: The title of the slide is **CDA – How to be pro-active**. The presenter walks through the content on the slide.

Presenter: So now we covered the blind spots and so I thought what else to spend some time to think about. What are things as a result of you having learned about the Capital Dividend Account that you might be able to share with your clients and/or their accountants and tax advisors about the Capital Dividend Account? We do have a tax topic on the Capital Dividend Account. And one of the other things I wanted to talk about is, as you have seen from the computation of the Capital Dividend Account, there are a lot of components and it's accumulative and it takes time. So, while we say somebody passes away with corporate owned life insurance policy goes in the capital dividend and then they can pay out the capital dividend. And that's true. But we also want to maybe set expectations that while the life insurance proceeds can be received in a timely manner and everything's working, it still might take some time for the client’s accountants to make sure that the Capital Dividend Account is calculated before the actual capital dividend is paid out of the corporation. And one of the other cautions is, as you have seen how complicated doing the Capital Dividend Account computation is, the client's tax advisors should be the ones that are doing that calculation. And the other thing is there are adverse tax consequences, penalties and things, if an amount is paid out of the Capital Dividend Account that is in excess of the Capital Dividend Account balance. And a Capital Dividend Account can be calculated at any point in time, not necessarily at the company's year-end. And that means the Capital Dividend Account can be, you know, paid out at a particular point in time. And we saw in the examples that the corporation had a capital gain and then that Capital Dividend Account was paid upon the receipt of the capital gain. And the caveat on that is, it's on most things except that eligible capital property that can only be calculated at year end. And so, I also wanted to talk about we're dealing with corporate owned policies so we're dealing with situations where you have business owners and we always talk about, you know, it's important for them to have insurance. It's also important for them to have shareholders' agreements. And if they have a shareholders' agreement, or maybe they do not have a shareholders' agreement, the Capital Dividend Account is something that they may wish to consider dealing with in their shareholders' agreement. If they bought the life insurance policy for purposes of buy/sell, it is prudent for them to address the Capital Dividend Account in this shareholders' agreement. If the agreement is silent on who would get the benefit of the Capital Dividend Account, there may be no obligation on the corporation to use the Capital Dividend Account for the buyout of a deceased shareholder. In 2009, we had a case of Rebero estate versus Braun Nursery, it was an Ontario decision and in that case, Mr. Rebero had worked at the nursery and he became a shareholder in the nursery, of the company, and he passed away and there was a shareholders' agreement and the shareholders' agreement provided that life insurance was purchased and it was for the purpose of buying shares upon the death of the shareholder. However, the shareholders' agreement was silent about whether the company had to actually use the Capital Dividend Account to purchase those shares. A lawsuit was started by the deceased spouse and it went through the courts and the decision was there was nothing in the shareholders' agreement that said that they were going to use the Capital Dividend Account to buy back the shares. So, in this case, Braun Nursery, the corporation, bought back the shares to <unintelligible> shareholder and they did not use the Capital Dividend Account. And so, there are clients that may have done shareholders' agreements before 2009 and may not have actually dealt with the Capital Dividend Account about whether they will or won't, but if it can be dealt with in the shareholders' agreement, then we could look at not having to go to court to deal with these kinds of situations.

Description: The title of the slide is **Key Takeaways – CDA with focus on life insurance**. The presenter walks through the content on the slide.

Presenter: So, let's look at what some of the key takeaways are. So, we've completed our trip. We've gotten to CDA and what have we learned and what will we be able to take away from today? We understand why we have the Capital Dividend Account because it's part of our concept of integration between in our tax system, so that a person, if they earn it as an individual or they earn income from a corporation, we should essentially be indifferent to how we're doing that. And so when we have things that are tax free such as the life insurance proceeds and capital gains, the non-taxable portion of capital gains, things like that, we have the Capital Dividend Account is a mechanism that allows us that if the corporation has those things, they can then transfer those things out through the use of the capital dividend to a shareholder. So, it's a really powerful and useful mechanism in our tax system. We also went through, you know, that if somebody wants to gift insurance through a corporation, it's certainly possible, but that care and attention needs to be taken. And we also went through a number of examples which were our stops along the way on how the various components of the CDA were computed and we had specific examples. And then I talked about how you could be proactive with your client's tax advisors and maybe also highlight some things at in risk minimization that they don't have the shareholders' agreement, or if they have one, whether they've dealt with this in their shareholders' agreement. So just another way that you can add value to help your clients have the best experience of dealing with putting everything in place to make it easier upon death, and that they just continue to make sure as much as possible can be done in advance.

Description: The title of the slide is **Canada Life resources**. The presenter walks through the content on the slide.

Presenter: So, I hope you've enjoyed our road trip today. We've reached our destination. We have a number of resources. We have local expertise, and we have head office expertise and we have the Canada Life's advisor hub on Workspace. We have the Taxes and Estate Planning Group. We have articles, and I have mentioned we have a new tab in that group, in that section, that is **Insights and Analysis**. And there is information there about charitable giving with a corporation and we have other information as well. And we have some other stuff on Capital Dividend Account, and we also have a tax article on the Capital Dividend Account.

Description: The final slide says "Thank you".

Presenter: So, I thank you for your time and I hope that this has been beneficial for you today. Thank you.