

THE TAXATION OF CRITICAL ILLNESS INSURANCE

Corporately Owned Critical Illness Insurance

(Corporation is the Policyholder and Receives all Benefits Payable Under the Contract)

The Arrangement	<ul style="list-style-type: none"> • The corporation owns the individual Critical Illness insurance policy • The shareholder or a key employee who is not a shareholder is the insured
Purpose	<ul style="list-style-type: none"> • The corporation will receive a lump-sum benefit (or partial benefit) upon the diagnosis of a covered condition (subject to survival period requirements) • The corporation will receive any Return of Premium on Death (ROPD) benefit, or any Return of Premium on Surrender (or Expiry) (ROPS or ROPE) benefit • The corporation has complete discretion as to how the lump-sum benefit (or partial benefit) is spent, including (but not limited to): <ul style="list-style-type: none"> ➢ Paying off corporate debts, including mortgages, lines of credit ➢ Redemption of shares from the shareholder ➢ Paying expenses associated with loss of a key person
Tax Treatment	<ul style="list-style-type: none"> • Premiums are not deductible for tax purposes • The shareholder (or employee) will not have a taxable benefit since the corporation receives all benefits under the contract • The Canada Revenue Agency (CRA) generally accepts that stand-alone CI contracts that do not provide for ROP benefits are “accident and sickness” contracts. Thus, lump-sum benefits (including partial benefits) are non-taxable¹ • A return of premiums (where no investment element is added on) should be tax free² • Benefits received under the contract are <i>not</i> credited to the Capital Dividend Account
Additional Considerations	<ul style="list-style-type: none"> • CI insurance provides the corporation with an essential source of funds in the event that certain unforeseen events occur. • The corporation should review all existing insurance arrangements to ensure that the appropriate types and amounts of coverage are in place. • Insurance coverage should be coordinated with the provisions of any shareholder agreements and buy-sell agreements. With CI contracts, take care to ascertain when a receipt of benefits will trigger certain provisions. • The corporation’s professional advisors should determine whether the CI contract should be owned by the corporation or the shareholder. • ROP benefits, if any, will reduce the corporation’s net cost of the program. • When the corporation no longer has a need for the CI coverage, the ownership may be transferred to the shareholder and/or employee. Moving the ownership may be desirable if one of the insureds has later become uninsurable. Review the employee/shareholder benefit tax rules at that time.

This analysis is not necessarily appropriate for contracts issued by other insurers, as the product features, etc. are not necessarily identical to those of Standard Life’s Protecta contract. It is intended for general information only. It should not be construed as legal, accounting, tax or specific investment advice. Clients should consult a professional advisor concerning their situations and any specific investment matters. While reasonable steps have been taken to ensure that this information was accurate as of the date hereof, The Standard Life Assurance Company of Canada and its affiliates make no representation or warranty as to the accuracy of this information and assume no responsibility for reliance upon it.

¹ CRA has stated that the existence of a ROP feature will not necessarily disqualify a CI contract from being considered an “accident and sickness” contract. However, CRA and the Department of Finance (Finance) have not concluded their review. It is the industry’s view that lump-sum benefits (or partial benefits) received under a contract having ROP features should also be non-taxable. For contracts issued in Quebec, CRA appears to be of the view that under Quebec Law, the contract is an “accident and sickness” contract. Thus, in Quebec, lump-sum benefits received are non-taxable, which should not change where an ROP feature is present.

² The industry believes that a return of premiums (where no investment element is added on) should be non-taxable. Again, CRA and Finance have not concluded their review.