

Seminar Fact Sheet: Taxation of Life Insurance

(key words appear in bold type)

- Life insurance death benefits are received **tax-free** by the beneficiary.
 - ✓ True for personal, business, and group policies.
- A&S benefits are received **tax-free** by the insured.
 - ✓ True for personal and group policies.
- **Cash value** in a life insurance policy:
 - Only exists for whole life and universal life policies
 - Cash value in universal life is the account value of the policy

Taxation of the Cash Value

- Cash value accumulates in whole life and universal life policies by payment of premiums.
- Policies **last acquired** before December 2, 1982 are **tax exempt**.
- Policies acquired since December 2, 1982 must pass an **exemption test** annually to ensure they are tax exempt. The test measures growth in the cash value above the policy's **adjusted cost basis (ACB)**.
- The **ACB = premiums (minus) net cost of pure insurance** [for par policies only: (minus) dividends]
 - The net cost of pure insurance is the life insurance cost.
- Growth must not exceed the limit set in the Income Tax Act called the **maximum tax actuarial reserve (MTAR)** for the policy to maintain its tax exempt status.

Taxation of the Cash Surrender Value

- Cash surrender value is the amount the whole life or universal life policy owner receives when the policy is surrendered (terminated).
- Amount that is taxed is the difference between the CSV and ACB.
- **ACB (prior to 1982) = premiums** [for par policies only: (minus) dividends]
- **ACB (since 1982) for par policies = premiums (minus) net cost of pure insurance** [for par policies only: (minus) dividends]

Personal Notes
