Corporate Owned Whole Life Insurance

Preserve Wealth, Reduce Taxes and Protect Those You Cherish Most

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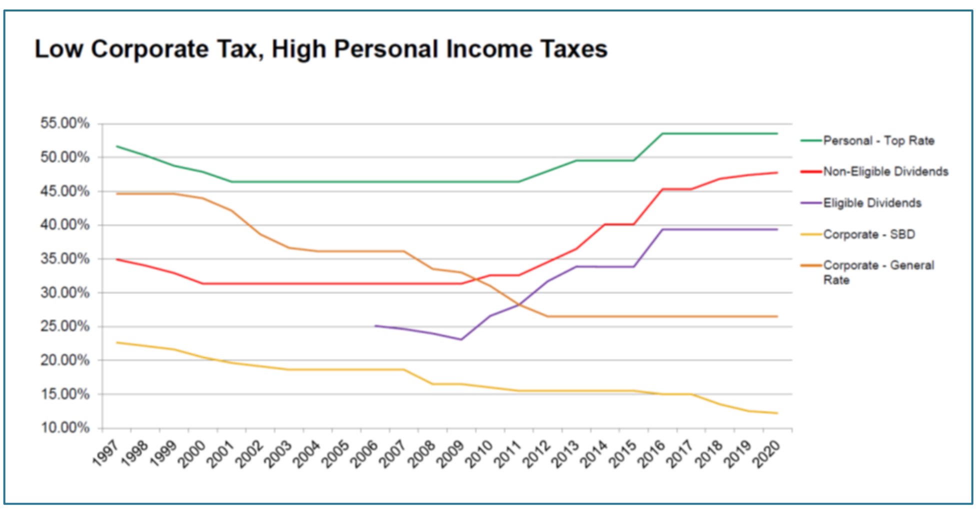
Canadian entrepreneurs have held permanent life insurance in their corporations for years. A great example is Ted Rogers, the founder of Rogers Communications, who held over one hundred million dollars in life insurance in family-owned private corporations. These policies saved him millions in corporate tax for years. After his passing in 2008, these insurance policies were paid in a matter of weeks, creating liquidity to help offset massive capital gains taxes with tax-free capital. While there are many reasons for owning insurance, what's the benefit of permanent insurance and why hold it in the corporation?

Background

Business owners and professionals often have significant wealth tied up inside a corporate entity. Whether it is a lifetime of earnings saved up in a holding company, or a sudden "windfall" when they sell an underlying operating company, they end up with "trapped corporate surplus". We consider it trapped because the growth is highly taxed as passive investment within the company, but taking it out would mean giving up 40% - 47% in the form of dividend tax to get it into their personal account. Although there is a dividend refund mechanism, that only partially reduces the sting of tax.



While active business income tax rates have steadily fallen, personal tax rates have gone the opposite direction. This differential causes many to retain assets inside the corporation, creating more "trapped corporate surplus".

Quite often these same individuals have personal assets to rely on for retirement, or only require a portion of the assets held in the company to supplement their retirement lifestyle. This leaves large sums in the company in perpetuity, at least until death. There is the ability to defer the final taxes by rolling over shares to one's spouse, but on the spouse's passing, the tax would have to be paid. A permanent insurance plan would guarantee liquidity regardless of age to address those taxes. No need to rush to sell assets or real estate to raise cash at a time when the family has more important things on their minds.

Tax-Free Dividends

This is where permanent life insurance can perform alchemy. The use of tax-exempt life insurance converts otherwise taxable dividends into premiums. That may sound like the equivalent of turning silver into brass -- not very appealing; but, ultimately when those premiums result in a death benefit, it results in a credit to the Capital Dividend Account (CDA). This notional account enables tax-free dividends to be paid out of the company. We started with investments that would result in a taxable dividend and ended up with an insurance benefit that is a multiple of the deposits, and it created tax-free dividends. Taxable dividends converted into larger tax-free dividends. Sounds to me like the equivalent of changing silver into gold!

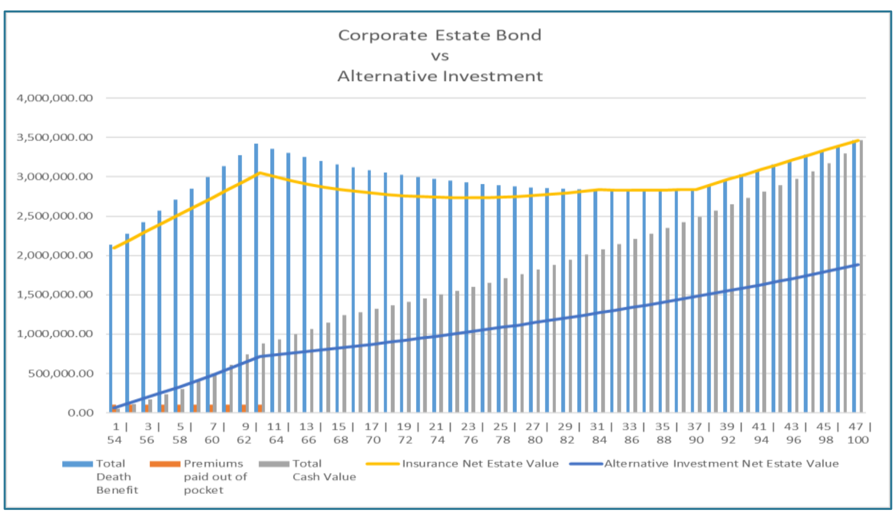
Access To Capital

While the prospect of reduced tax and increased family wealth is great, most of these individuals also like to know they can access the cash if an opportunity or emergency happens. That is where the cash value of these structures plays a role. The tax-exempt cash value remains an asset on the balance sheet, but the growth is not exposed to the annual taxation that other company assets are subject to. This cash value can be leveraged in order to preserve it from tax. If funds are used for a business venture or for another investment, there are tax deductions associated with the interest paid and the underlying cost of insurance. In the unfortunate case of a disability, during prime earning years or well into retirement, some insurers offer access to the cash value on a tax-free basis as a direct withdrawal. This can be a valuable resource in the case of Long Term Care needs.

Bottom Line

For those who have wealth tied up in a corporation, preserving wealth and reducing taxes through permanent life insurance is an opportunity to protect the people and values they cherish most.

Perhaps Mr. Rogers, one of the greatest Canadian business builders of our time, also knew a thing or two about preserving wealth. Here is an example based on a 53 year old male depositing $100,000/year for 10 years. The alternative investment assumes a 4% bond:



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