

## Absurdly problematic – Life interest trusts and corporate-owned life insurance

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On September 28, 2023, at the Canadian Life and Health Insurance Association (CLHIA) CRA Roundtable Q3 (2023-0971721C6) dealt with whether the existence of corporate-owned life insurance could taint a spousal trust for purposes of the rollover of capital property (including the shares of the corporation) from a deceased spouse to the trust under subsection 70(6) of the Act. In a prior Conference for Advanced Life Underwriting (CALU) Roundtable, the CRA was unable to confirm that it would not taint the status of a testamentary spousal trust and impact the rollover of capital property to the trust. See [What's the problem with trusts and life insurance? \(manulife.ca\)](https://www.manulife.ca/en/insights/articles-and-news/what-s-the-problem-with-trusts-and-life-insurance) for history.

In particular, the CLHIA question pointed to subsection 70(5.3) as supporting the idea that the Act seems to contemplate the use and ownership of life insurance by a corporation whose shares could rollover to a spouse trust. Subsection 70(5.3) applies for purposes of 70(5) (deemed disposition of capital property on death), 104(4) (trust deemed dispositions) and 128.1 (dispositions on immigration/emigration). Subsection 70(5.3) deems the value of corporate owned life insurance (on the individual and those not at arm's length) to be its cash surrender value immediately before death or immigration/emigration. Since 70(5.3) contemplates the existence of life insurance in a corporation in respect of a deemed disposition in 104(4) (on the death of the life interest beneficiary) how could it cause a spousal trust to be tainted by the corporation holding it?

The CRA didn't budge. The CRA concluded that 70(5.3) is a valuation rule and has no bearing on whether a testamentary spouse trust meets the requirements of the Act. Their response to the prior CALU question remains unchanged.

Try as we may, it does not seem possible to get through to the CRA on issues relating to life insurance in the context of life interest trusts. The most recent effort in this respect was a submission made by CALU in November 2022 to the Department of Finance ([CALU submission to Finance on LI in LI trusts - CALU](#)) seeking an amendment to allow a life interest trust to own and fund life insurance.

The idea that life insurance (or any asset for that matter) held by a corporation could taint a spouse trust and deny rollover treatment for the shares is problematic. The only saving grace here is that the CRA suggests it is a question of fact. And factually, life insurance (or any asset) owned by a corporation is authorized by its Board of Directors. The trustees are not involved in the decision to purchase and fund the policy. The trust document need not speak to the ownership of insurance in this context. And if not, how then could it be said that the trust allows for someone other than the spouse to receive or otherwise obtain the use of income or capital of the trust during the spouse's lifetime?

(And by this statement we are not suggesting that if the trust document did permit the purchase of life insurance, that someone other than the spouse would receive or otherwise obtain the use of income or capital of the trust. The counter arguments to that proposition are in the first link above.)

The fact that we even have to talk about this is absurdly problematic.

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#### FOOTNOTE:

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