Accounting of Corporately Held Permanent Life Insurance

This addresses when a corporation is the owner and beneficiary of a permanent life insurance policy:

1) While the life insured is alive, two annual entries need to be made on the books;

To record payment of the life insurance premiums:

Dr - Premium Expense
Cr - Cash

To record annual increase in total life insurance cash values:

Dr - Life insurance cash values (this can be a long term or short-term asset depending on the intended use)
Cr - Income - Increase in Life Insurance Cash Value

For tax purposes, life insurance premiums are generally not deductible. On the flip side, growth in cash values of an exempt life insurance policy are not taxable income. Therefore, adjustments need to be made on the corporation's tax return, specifically the T2S(1). The premium expense needs to be added back to income, while the increase in cash values needs to be deducted from income.

2) On death of the insured another entry needs to be made on the books. For example, assume death proceeds are $1,000,000 and the cash values already recorded on the books are $200,000. Upon death of the insured, the following would occur:

Dr - Cash $1,000,000
Cr - Life insurance cash values $200,000
Cr - Income - Life insurance death proceeds $800,000

For tax purposes, the $800,000 life insurance death proceeds are not taxable, and need to be subtracted from income on the T2S(1). Also the death proceed, less any remaining adjusted cost basis of the life insurance policy (obtained from the insurance company) will increase the notional capital dividend account of the beneficiary corporation. This is assuming it is a Canadian controlled private corporation. The capital dividend account can then be paid out tax-free to the shareholders who are a resident Canada by way of a capital dividend.

Hopefully you found this of value. Please do let us know if we can be of assistance with any other insurance or related advice and/or questions.

Haunn Landers & Co.