

April 1, 2009

Mr. Mark Symes  
Director  
Canada Revenue Agency  
320 Queen Street  
Ottawa, ON K1A 0L5

Dear Mr. Symes:

**Re: Canada Revenue Agency Technical Interpretation Letter 2007-025759, dated Dec. 15, 2008**

I am writing on behalf of the Conference for Advanced Life Underwriting (CALU) and the Financial Advisors Association of Canada, which operates under the name of Advocis™. We believe that the above noted technical interpretation does not conform to a plain reading of the tax legislation with respect to life insurance policies. It is also at odds with a letter sent to this organization, signed by Lee Workman, on September 11, 2000, and released as Technical Interpretation Letter 2000-003388. This letter was issued in response to our letter to Brian Darling, then Director, Income Tax Rulings Directorate, of June 22, 2000. (Copies attached.)

The current interpretation letter deals with a universal life insurance policy under which the account value<sup>1</sup> is payable upon the insured providing satisfactory evidence to the insurer that the insured is disabled, in accordance with the definition of disability in the policy terms and conditions. This is a relatively common policy provision and allows the insured to receive up to the account value (cash value) of the policy if they become disabled. This is generally a lump sum payment.

As the above noted interpretation letter correctly notes, a disposition of an interest in a life insurance policy in accordance with the definition of “disposition” in subsection 148(9) of the Income Tax Act (“the Act”) excludes, in paragraph (h), “a payment under a policy as a disability benefit...” The Act does not define the term “disability benefit” and in fact there is no definition of the term “disability” for income tax purposes. In the insurance industry, the term “disability benefit” is generally interpreted to mean a “physical or mental impairment that prevents an individual from performing the duties of employment or certain activities of daily living”. There is no requirement that the payment be periodic or a fixed amount nor is there any prohibition against allowing the policyholder to determine the amount of the disability benefit to be received: only that the payment under the terms of the policy is a disability benefit. Consequently, we believe

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<sup>1</sup> A policy’s account value is essentially the sum of premiums paid plus accumulated investment earnings less policy charges (such as the cost of insurance and premium taxes) and withdrawals from the policy.

there is no legislative support for the Agency's position, as stated in the last sentence, that "...payments under such policies should not be capped to the amount of the account value of the policy." While we would differentiate between a disability benefit payable under a life insurance policy and a disability insurance policy, it should be noted that all policies that provide for disability benefits provide some form of limitation on the amount of disability benefit payable, whether such cap is related to income, age (e.g., stopping at age 65) or some other factor.

## **2000 Issue**

The issue under consideration in 2000 was the appropriate tax treatment of a payment made at the first death under a joint-last-to-die (JLTD) life insurance policy. As we stated at that time:

The amount of the benefit payable upon the death of the first person to die may be a fixed amount, may be determined with reference to the accumulating fund or cash surrender value (CSV) of the policy or a combination of a fixed amount and a variable amount dependent on the fund value or CSV of the policy. The amount of the benefit payable upon the first death may be limited to an amount not exceeding the fund value or the CSV of the policy at the time it is paid. The amount of the benefit upon the death of the first to die will reduce the total amount of the death benefits payable under the policy and will generally also reduce the accumulating fund and the CSV of the policy.

It was our view, with which the agency agreed in its response of September 11, 2000, "...that in determining whether a life is insured for the purposes of paragraph (j) of the definition of disposition in subsection 148(9) of the Act there is no express requirement that the insurer be at risk for all or a portion of the benefit payable."

The Agency's response went on to note that in accordance "...with the broad language used in subsection 148(9) and the lack of expressed legislative intent that the Agency agrees that, subject to the terms of a specific policy, the relevant words could be interpreted to include the payment made as a consequence of the first to die under a joint last to die policy with the result that the payment of the benefit would not constitute the 'disposition' of the interest in the policy or a 'policy loan' as defined in subsection 148(9) of the Act."

## **Conclusion**

We submit that the reasoning given by the Agency in its September 11, 2000 letter to this organization is analogous to the position that a payment under a policy of the account value (essentially the same as the CSV of the policy) as a disability benefit should not result in the disposition of an interest in the policy. Further there is no justification for the Agency's position that the amount of a payment under a policy should not be capped at the amount of the account value of the policy.

We respectfully request that the Agency reconsider its position with respect to the payment of a disability benefit from the account value of a policy. This is a significant issue for policyholders who have acquired life insurance policies where provision for such disability payments is made, for financial advisors who have sold such policies and for insurers who have issued such policies. Accordingly, your prompt attention to this issue would be appreciated.

We would be pleased to discuss this issue further with you or your staff. You may contact the undersigned by either phone or e-mail, as listed above.

Sincerely,

A.E. (Ted) Ballantyne, BBA, LL.M., CMA, TEP  
Director, Advanced Tax Policy

Attachments