



# Accounting for Life Insurance

An Accountant's Guide

# Booking the insurance transaction

Canadian businesses continue to discover the strategic advantages of corporate-owned permanent life insurance. Not only does it help protect shareholders and business growth, it's also an asset that can add significant value on the balance sheet — making it a powerful tool in the hands of sophisticated business owners and their advisors.

When we first published our white paper on booking insurance transactions in 2020, the response from financial professionals was overwhelmingly positive. You told us that clear, practical guidance on accounting for corporate-owned life insurance filled a critical gap in your practice. You also told us you wanted more.

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## Now, there's an opportunity.

The Accounting Standards Board has issued new comprehensive guidance on this topic: Accounting Guideline (AcG) 21\*, *Accounting for Life Insurance Contracts with Cash Surrender Value*, Part II of the CPA Canada Handbook — Accounting. Effective for fiscal years beginning on or after January 1, 2026, this guideline provides specific instructions for recognition, measurement and accounting treatment of life insurance contracts with cash value.

For financial professionals working with sophisticated business owners on complex planning scenarios, understanding how to properly account for this valuable asset isn't just good practice — it's a competitive advantage. When accountants, tax professionals, insurance advisors, and legal experts collaborate effectively around the table, that's when truly comprehensive strategies emerge for business owners seeking to maximize protection, growth and tax efficiency.

Whether the business holds universal life, participating whole life or non-participating whole life insurance, this updated guidance provides the clarity needed. What follows are accounting entries and practical examples using the new guideline for typical transactions encountered with corporate-owned permanent insurance — instructions designed to help unlock the full potential of insurance as a strategic corporate asset.

Provided here are accounting entries, using the aforementioned guideline for typical transactions encountered with corporate-owned permanent insurance — guidance that can help you get insurance on the books successfully. In all examples, the business is both the owner and the beneficiary of the policy, a common setup in Canada.

\*Accounting Standards Board (AcSB), *Accounting for Life Insurance Contracts with Cash Surrender Value*, Exposure Draft, November 2023.

# Recording payments and policy value

If an insurance policy has a cash surrender value (CSV) component, it can be overfunded — within allowable limits — by making payments above the base premium (the cost of the insurance plus other potential costs or expenses such as policy loans). This policy overfunding builds the CSV and can grow over time sheltered from tax. When accounting for overfunding policy payments, split them between the balance sheet and income statement according to the transaction examples below.

Transaction	Debit	Credit
Component of insurance payment that generates CSV	CSV (balance sheet)	Cash account or (balance sheet)
Component of insurance payment not reflected in the increase to CSV	Insurance expense/gain (income statement)	Cash account or (balance sheet)

For accounting purposes, measure a corporate policy as an asset. According to the guideline, the asset should be measured at its CSV (i.e. the amount that would be realized by the policyholder upon surrendering the policy). That means that accounting for the payment of the insurance premium is an exercise in truing up the CSV on the balance sheet every year. Life insurance premiums are typically a non-deductible business expense. Reverse out any amounts booked on the income statement using Schedule 1 of the T2 Corporation Income Tax Return.

## Things to know

- CSV is the realizable value of a policy net of charges levied in the event of an early surrender.
- Surrender charges are unique to each insurance product.
- The guideline requires that the difference between the aggregate policy premiums and the aggregate change in the CSV for the period be recorded on a net basis.
- In the early years of a policy, the insurance expense will likely be greater than any increase to the CSV. If this occurs, record the excess over CSV as an “insurance expense” on the income statement.
- If the increase to CSV exceeds the annual insurance expense, record the excess in CSV as “insurance income,” or “insurance gain,” on the income statement. This income or gain is not subject to income tax and should be reversed on Schedule 1 of the T2 Corporation Income Tax Return.
- CSV growth within a tax-exempt life insurance policy does not generate annual taxable income as long as it stays within the limits set by the Maximum Tax Actuarial Reserve (MTAR).

## When are corporate-owned life insurance premiums deductible?

Both for individuals and corporations there are only a few places in the Income Tax Act where life, health or disability insurance premiums are deductible. It's best to assume that the premiums are not deductible until you consult with a tax professional and are advised otherwise.

# Skipping premium payments

Permanent insurance policies may offer policyholders the option to use accrued CSV to skip premium payments. Doing so, however, is likely to change the book value of the insurance asset. How much the value changes depends on the CSV, the return inside the policy and the policy's ongoing costs.

To book this transaction, record the insurance expense on the income statement. Then, for income tax purposes, reverse it out as a non-deductible expense on Schedule 1 of the T2 Corporate Income Tax Return. By truing up the CSV at the end of each fiscal year on the balance sheet, the other side of the entry, whether income (i.e. CSV is increasing) or expense (i.e. CSV is decreasing) will flow to the income statement.

Transaction	Debit	Credit
No cash transaction	Insurance expense	Cash account or (balance sheet)

## Things to know

- If CSV is used to pay ongoing insurance costs, it's important to keep an eye on long-term viability. To do so, evaluate the projected growth in policy CSV against the projected annual charges for the policy itself. Be sure to use minimum guaranteed rates and values and consult your insurance professional to review potential outcomes.

## Don't forget the illustration

Policy growth is often projected within a policy illustration. If a policyholder skips premium payments, it's a good idea to obtain a new in-force illustration from the insurance provider, particularly if planning to pay the total cost of the policy within a set number of years.



# Partial policy surrender

A partial policy surrender occurs when a policyholder withdraws funds from a policy. It typically results in reduced coverage for the policyholder — often greater than the cash withdrawn — and it permanently alters the policy. It's best to consult your insurance professional before proceeding, especially if you're dealing with a policy issued under previous rules. These policies may be subject to tax rules that have since changed, and a partial surrender could expose them to new taxation.

For accounting purposes, a partial surrender reduces the CSV of the policy. Be sure to reflect this change on the balance sheet. However, the proceeds of disposition will not be the same as the reduction in CSV. Record any residual amount of the disposition as miscellaneous income and reverse this amount on Schedule 1 of the T2 Corporate Income Tax Return.

Transaction	Debit	Credit
Cash withdrawal	Cash account	CSV (balance sheet) misc. income

For income tax purposes, treat a partial policy surrender as a partial disposition. Paragraph 56(1)(j) of the Income Tax Act requires a policyholder to include income from the disposition of an interest in an exempt life insurance policy as determined under subsections 148(1) & 148(1.1). The amount of income to include — also called the “policy gain” — is the amount by which the proceeds of the disposition exceed the adjusted cost basis (ACB) to the policyholder. The taxable policy gain arising from the surrender should be included on a T5 slip provided by the life insurance company and reported on Schedule 7 of the T2 Corporate Income Tax Return. If the disposition does not exceed the adjusted cost basis, enter zero as the amount.

## Things to know

- A policy gain always generates a T5 slip.
- The ACB of a policy will change following a partial surrender.
- The CSV of a policy reduces following a partial surrender.
- While a realized policy gain is taxable income to the policyholder, a taxpayer cannot deduct a realized policy “loss” from taxable income. A loss could happen, for example, if a policyholder cancels a policy before it earns more in CSV than it has cost in premiums.

## How to calculate the adjusted cost basis of a policy

Several factors contribute to the calculation of the ACB of a policy, including payments, the taxable portion of any withdrawals or even loan interest. To calculate the ACB for a specific policy, contact the insurance provider.

# Receiving the death benefit

It takes two steps to account for a corporate policyholder receiving a death benefit:

1. Take the amount of the death benefit proceeds equal to the policy's CSV at the time of death and apply them as an accounting credit. This removes the CSV asset from the balance sheet.
2. Credit the remainder of the death benefit proceeds as insurance income on the income statement. The business will receive the full death benefit tax-free, so reverse this insurance income component on Schedule 1 on the T2 Corporate Income Tax return.

Transaction	Debit	Credit
Total death benefit proceeds	Cash account (balance sheet)	
Portion of death benefit represented in the CSV balance		CSV (balance sheet)
Amount of death benefit in excess of CSV balance		Insurance income (income statement)

## Things to know

- The beneficiary might receive proceeds in excess of the ACB of the policy. Credit the excess to the capital dividend account (CDA). The business can then distribute the excess as a tax-free capital dividend.
- The CDA credit available to a policy equals the death benefit less any policy loans, minus the ACB.
- To pass the death benefit to shareholders tax-free, it must move through the CDA.

## The capital dividend account and health insurance

It's important to understand the type of insurance policy employed because not all death benefits function the same way. For instance, a critical illness policy might feature a return of premium on death option. This optional benefit, just like the base critical illness coverage itself, does not generate a credit to a corporation's CDA.

## The capital dividend account and multi-life insurance policies

Multi-life insurance policies can prove challenging when it comes to tax planning because even though a multi-life policy covers more than one insured life, it only has one ACB. It's important to discuss insurance needs with a qualified insurance professional who also understands the needs of a business owner.

# Using cash value for liquidity

There are several ways corporations might leverage the CSV of a policy to access liquidity:

- 1. Policy loan:** A policy loan is issued by the insurance company. Easy to obtain, these loans don't affect the growth of cash value within a policy. Loan amounts equal to or less than the policy's ACB are also tax-free. Loan amounts that exceed the ACB are taxable. Clients can, however, deduct loan payments that repay the taxable portion of any policy loan. The insurer will issue a T5 slip to report the taxable gain.

Note: A policy loan reduces the ACB of a policy. A policy loan is considered a disposition, as per paragraph (b) of the definition of "disposition" in subsection 148(9) of the Income Tax Act. Taking one may therefore affect the CDA credit available to the beneficiary, or the amount of tax payable if the death benefit is paid out to shareholders or to the Client's estate. If a policy loan is outstanding at the time of death, the policy's CDA will be reduced by the amount of the outstanding loan.

- 2. Policy withdrawal (partial surrender):** Policyholders can surrender part of the cash value of a policy but may incur a tax obligation. For instance, if 40% of a policy's cash value is tax-free, then typically only 40% of the withdrawal will be tax-free. More importantly, a withdrawal permanently modifies the insurance policy, reducing the death benefit by an amount equal to or greater than the withdrawal. To determine the percentage of cash value that is tax free, contact the insurance provider.

- 3. Third-party loans:** This type of loan is issued by a third-party lender, such as a bank. Unlike policy loans, third-party loans are not considered disposition and do not create income and typically do not affect the CDA credit at death. If a policy is collateral for such a loan, the policyholder may also deduct the net cost of pure insurance (NCPI) from their corporate income in certain cases. Still, it's best to review the outcomes of this type of loan before pursuing it. Speak with your insurance professional.

## Net cost of pure insurance (NCPI)

NCPI is an annual amount and federally regulated. When calculating with NCPI, it's important to remember that the fiscal year of the corporation may not reflect the calendar year of an insurance policy. The insurance provider can give accurate calculations.

## CSV and insurance funding: other considerations

In some instances, business owners require permanent insurance but won't require their policy to provide any ongoing liquidity. In fact, a contrasting strategy exists whereby business owners seek to minimize certain asset values to ensure their corporation's shares remain qualified small business corporation (QSBC) shares, and therefore eligible for the lifetime capital gains tax exemption.

For shares to qualify as QSBC at the time the business owner sells their shares or dies, at least 90% of the fair market value of their company's assets must be used in carrying on an active Canadian business. This can pose a problem because life insurance is a passive asset and its value is included in this 90% test. According to the Income Tax Act s. 70(5.3), if the business owner or a shareholder is the person insured, the fair market value of the policy is its CSV.

As a result, some corporations may find it advantageous to hold a permanent life insurance policy with little or no CSV. Even with little or no cash value an insurance policy may still provide permanent insurance protection, but without the risk of a tax obligation that a high CSV can carry.

## Leveraging insurance: what advisors need to know

When businesses use permanent life insurance as collateral for third-party loans — particularly where interest and net cost of pure insurance (NCPI) may be deductible — the accounting complexity increases significantly. This complexity creates both servicing challenges and opportunities for advisors who understand the nuances.

The key accounting consideration centers on proportionality. If a corporation borrows \$1 million against a \$10 million life insurance policy, the business may be entitled to deduct only 10% of that period's NCPI. This proportional calculation must be tracked accurately throughout the loan period, requiring coordination between multiple parties.

Another often-overlooked factor: NCPI isn't necessarily distributed evenly throughout the year. A policy with a December 1st anniversary date, for example, will likely incur more than one-twelfth of year-one's projected NCPI in that first month. While these timing differences typically resolve over time, they can create planning opportunities — or challenges — depending on the corporation's fiscal year-end.

The coordination challenge extends beyond calculations. Insurance policy statements rarely align with either calendar year-ends or corporate fiscal year-ends. This mismatch means accountants frequently need additional calculations — and additional information — to accurately book insurance transactions based on the corporation's reporting period. Advisors who anticipate these needs and provide proactive support distinguish themselves in the marketplace.

# What key centres of influence need

## **Accountants/CFOs/Comptrollers will require:**

- An in-force policy illustration (advisors should request this proactively)
- Loan statements from the lending institution showing amounts borrowed and interest paid
- Documentation showing how loan proceeds were reinvested or used. Ideally, two permanent insurance statements annually: one as of December 31st and another aligned with the corporate year-end.

## **Lending Institutions will require:**

- Current loan statements detailing outstanding balances and interest paid during the period
- Current life insurance policy statements showing cash value (CV), death benefit (DB) and premiums paid to date
- **Critical figures for accurate accounting:**
  - Net cost of pure insurance (NCPI)
  - Cash value (CV) and cash surrender value (CSV)
  - Death benefit (DB)
  - Premiums paid during the current period
  - Premiums paid to date

Note that some of these figures may require specific requests to the insurance provider, as they aren't always produced automatically.

## **Year-end procedures checklist: practical guide for accountants reconciling CSV balances**

When fiscal year-end arrives, accurate reconciliation of corporate-owned life insurance requires systematic coordination between multiple parties. Here's a streamlined checklist to ensure nothing falls through the cracks.

### **Before year-end (60 – 90 days out):**

- Request policy statements dated as close to fiscal year-end as possible from the insurance provider.
- For policies with third-party loans, request updated loan statements from lending institutions.
- If policy anniversary dates don't align with fiscal year-end, request pro-rated CSV values and NCPI calculations for the fiscal period.

## **At year-end:**

- Verify CSV balances on the balance sheet match year-end policy statements (adjusted for any timing differences).
- Confirm all premium payments during the fiscal year are properly allocated between CSV increases and insurance expense.
- Review Schedule 1 of the T2 to ensure all non-deductible insurance expenses and non-taxable insurance income are reversed.
- For leveraged policies, verify NCPI deductions are calculated proportionally based on loan-to-CSV ratios.
- Reconcile any T5 slips received for policy gains against amounts reported on Schedule 7 of the T2.

## **Post year-end verification:**

- Confirm ACB calculations with the insurance provider, particularly if partial surrenders or policy loans occurred during the year.
- Update CDA tracking for any death benefits received.
- Review in-force illustrations if premiums were skipped or if significant withdrawals occurred.

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## **Document retention matters**

Maintain organized files for each corporate-owned policy including, annual policy statements, premium payment records, T5 slips, ACB confirmations, loan statements (if applicable) and in-force illustrations. These documents become critical during CRA audits or when calculating CDA credit at death.

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# Common errors and how to correct them: real-world troubleshooting

Even experienced accountants encounter challenges when accounting for corporate-owned life insurance. Here are the most frequent missteps and how to fix them.

## **Error #1: Recording the entire premium as an expense**

Many accountants initially treat insurance premiums like any other corporate expense, debiting the full amount to the income statement. This overlooks the asset-building component of permanent insurance.

*The fix:* Split each premium payment between the CSV increase (balance sheet) and the insurance expense (income statement). Request year-end CSV values from the insurance provider and true up the balance sheet accordingly.

## **Error #2: Failing to reverse non-deductible expenses on Schedule 1**

Life insurance premiums are typically non-deductible, yet it's easy to forget this when preparing the T2 Corporate Income Tax Return.

*The fix:* Review Schedule 1 carefully. Reverse any insurance expense recorded on the income statement. Similarly, reverse out any insurance income (CSV gains) as non-taxable income.

## **Error #3: Ignoring timing differences between policy years and fiscal years**

Insurance policies operate on calendar years or policy anniversary dates — rarely matching corporate fiscal year-ends. This mismatch creates reconciliation headaches.

*The fix:* Request pro-rated values from the insurance provider. For example, if a corporation's fiscal year ends September 30th but the policy anniversary is December 31<sup>st</sup>, ask for CSV and NCPI calculations covering the specific fiscal period.

## **Error #4: Mishandling partial surrenders**

When businesses withdraw funds from a policy, accountants sometimes simply reduce CSV by the withdrawal amount — missing the taxable policy gain component.

*The fix:* The cash received often differs from the CSV reduction. Verify the T5 slip from the insurance provider shows the taxable policy gain (proceeds minus ACB). Report this on Schedule 7 of the T2. Record any difference between cash received and CSV reduction as miscellaneous income on the income statement, then reverse on Schedule 1.

## **Error #5: Forgetting to update CDA calculations**

The capital dividend account calculation depends on accurate ACB tracking — especially when policy loans or partial surrenders occur.

*The fix:* Confirm ACB with the insurance provider annually. Remember: policy loans reduce ACB, affecting the CDA credit available at death. Track these changes systematically.

## **Error #6: Not requesting necessary documentation**

Accountants can't reconcile what they can't see. Many errors stem from incomplete information.

*The fix:* Develop a standard request list for Clients: year-end policy statements, T5 slips, loan statements, ACB confirmations and in-force illustrations. Make these requests routine at fiscal year-end.

# Conclusion: from complexity to competitive advantage

The introduction of AcG 21 marks a turning point for corporate-owned life insurance in Canada. What once required interpretation and best-guess practices now has clear, authoritative guidance. For financial professionals, this clarity transforms a bookkeeping challenge into a strategic planning opportunity.

Corporate-owned permanent life insurance isn't just another line item on the balance sheet — it's a multi-functional asset that protects businesses, supports tax-efficient wealth transfer, and provides accessible liquidity when structured properly. When accountants, tax advisors, insurance professionals and legal counsel work together with a shared understanding of how to properly account for these policies, sophisticated business owners benefit from truly integrated planning.

The accounting entries and practical examples provided here reflect current best practices under the new guideline. But best practices evolve, and so do the needs of Canadian businesses. As policies mature, business circumstances change, and new planning opportunities emerge, staying current with both accounting standards and insurance strategies becomes essential to delivering comprehensive advice.

**The businesses that thrive are those surrounded by professionals who see beyond their individual specialties — who understand how accounting, tax, insurance and legal considerations intersect.**

With AcG 21 providing the clarity needed to properly value and account for corporate-owned permanent insurance, the path forward is clearer than ever.

For questions about specific policy values, in-force illustrations, or how particular insurance products align with business objectives, connect with qualified insurance professionals who specialize in corporate planning. For accounting and tax implications unique to individual circumstances, consult with CPAs and tax advisors who understand the intersection of insurance and corporate taxation.

The opportunity is here. The guidance is clear.  
The next move is yours.



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