



IMMEDIATE FINANCING ARRANGEMENT · CANADA

Is Borrowing Against Life Insurance Legal in Canada?

Why Isn't Everyone Doing It?



By Conor McGowan · Published Oct 28, 2026 · Updated Oct 28, 2026 · 14 min read

SIMPLE SUMMARY

You can put money into a life insurance policy, borrow against it, continue using that capital, potentially deduct the loan interest, and eventually use the death benefit to repay the loan.

For incorporated business owners, the strategy can also create substantial Capital Dividend Account (CDA) room, helping transfer corporate wealth to shareholders tax-free.

90–100%

OF ELIGIBLE CASH VALUE

65%

TYPICAL HELOC LIMIT

\$4.7M

CDA ROOM IN THE EXAMPLE

1848

PAR DIVIDENDS SINCE

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You can put money into a life insurance policy, borrow against it, continue using that capital, potentially deduct the loan interest, and eventually use the death benefit to repay the loan.

For incorporated business owners, the strategy can also create substantial Capital Dividend Account (CDA) room, helping transfer corporate wealth to shareholders tax-free.

It sounds almost too good to be true.

So naturally, two questions come up:

Is this actually legal? And if it's such a good strategy, why isn't everyone doing it?

The short answer is yes, borrowing against life insurance is legal in Canada. In fact, the underlying principles are not particularly unusual.

What's less familiar is how permanent life insurance, commercial lending, and corporate tax planning can work together.

To understand why, start with something you probably already know.

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You're Already Familiar With Borrowing Against Assets

Think about how people borrow money every day.

A homeowner can use a Home Equity Line of Credit (HELOC) to access the equity in their property without selling their house.

An investor can use a margin account to borrow against a portfolio without selling their investments.

A business owner can borrow against commercial real estate, equipment, or other assets to fund expansion.

Borrowing against permanent life insurance follows the same basic principle.

You own an asset. A lender recognizes its value. The lender advances money against that asset as security.

The difference is the type of asset securing the loan.

How different assets compare

ASSET USED AS COLLATERAL	POTENTIAL LOAN-TO-VALUE	WHY LENDERS TREAT IT DIFFERENTLY
Stocks and investment portfolios	Commonly 50%, potentially 70% on eligible securities	Market prices fluctuate daily, and falling values can trigger margin calls
Residential real estate	HELOC generally up to 65%; combined mortgage and HELOC financing may reach 80%	Property values fluctuate and selling a property takes time
Participating whole life insurance	Up to 90–100% of eligible cash surrender value with some lenders	Contractual cash values and guarantees can provide relatively stable collateral

These are general lending examples, not guaranteed borrowing limits. Each lender establishes its own criteria.

Notice something interesting.

Lenders may be willing to advance a considerably higher percentage against eligible permanent life insurance cash values than against many other assets.

Why? Because the nature of the underlying security is different.

Why Would a Bank Lend Against Life Insurance?

Banks are in the business of lending money and collecting interest.

They don't provide these arrangements as a favour, and they're certainly not participating because they've discovered a secret tax loophole.

They participate because there is a commercial opportunity.

With a properly structured insurance-backed loan, a lender may benefit from:

- **Interest income:** The bank earns interest for as long as the financing remains outstanding.
- **Strong collateral:** Eligible participating whole life policies contain contractual guaranteed values, making them different from securities whose prices change every trading day.
- **Long-term lending relationships:** Some arrangements are designed to remain outstanding for decades.
- **A potential repayment source at death:** Provided the policy remains in force, the contractual death benefit can be used to settle the outstanding loan.

Some lending arrangements even permit interest to be capitalized, meaning unpaid interest is added to the loan balance instead of being paid from current cash flow.

That can allow the bank to continue earning interest on a growing loan balance.

And there is another important difference between life insurance and other types of collateral.

A homeowner may never sell their house. An investor may never liquidate their portfolio. But every insured life eventually ends.

A permanent life insurance policy is designed to pay a contractual death benefit when that happens, provided the coverage remains in force.

For lenders, that can provide an additional source of repayment.

Of course, banks still assess the borrower's financial position, the value of the policy, available collateral, interest payments, and the terms of the lending agreement. No bank is obligated to lend indefinitely or allow unpaid interest to accumulate until death.

But the underlying business model is straightforward.

The bank earns interest. The insurance policy provides security. The borrower gains access to capital.

Why Would a Business Owner Want to Do This?

For business owners, the value extends well beyond accessing a loan.

Consider an incorporated owner who has accumulated substantial retained earnings.

They want to continue investing and expanding their business. But they also want to protect their family, prepare for future estate taxes, and eventually transfer wealth to the next generation.

Ordinarily, allocating substantial capital to life insurance could reduce the amount available for other investments.

An Immediate Financing Arrangement (IFA) can help address that trade-off.

The corporation purchases a properly designed permanent life insurance policy. As the policy builds cash surrender value, the corporation can use that value as collateral for financing from a third-party lender.

The borrowed capital can then be redeployed into the business or other investments.

This can provide several advantages.

Capital can continue working. Rather than permanently tying up all the funds allocated to insurance, the business may regain access to a significant portion through financing.

The corporation gains permanent protection. The policy provides a contractual death benefit that can support estate liquidity, succession planning, and other financial obligations.

Borrowing may create tax deductions. When loan proceeds are used for qualifying income-producing purposes, interest may be deductible. A separate, limited collateral insurance deduction may also be available.

The policy can support a tax-efficient estate transfer. Upon death, qualifying insurance proceeds can increase the corporation's CDA, potentially allowing substantial capital dividends to be paid tax-free to Canadian-resident shareholders.

This is the real opportunity.

It isn't simply about borrowing money against life insurance.

It's about coordinating insurance, financing, and corporate wealth planning instead of treating them as three unrelated decisions.

Is This Actually Recognized Under Canadian Tax Law?

Yes.

Permanent life insurance, collateral borrowing, interest deductions, and capital dividends are all addressed within Canada's established legal and tax framework.

An IFA is not itself a special tax exemption. Rather, it combines several existing provisions and established financial arrangements.

Three are particularly relevant.

Borrowed money is generally not taxable income

When a bank lends money to your corporation, that loan generally doesn't create taxable income for the corporation.

Why?

Because the corporation has an obligation to repay the borrowed amount.

The same basic principle applies when someone borrows against their home or investment portfolio.

Importantly, a corporate loan does not automatically become tax-free personal spending money. How borrowed funds are used, and whether corporate assets support a shareholder's personal borrowing, can create different tax consequences.

Interest may be tax-deductible

Paragraph 20(1)(c) of the *Income Tax Act* addresses the deduction of qualifying interest expenses.

Generally, the use of borrowed money is central to determining whether interest is deductible.

For example, borrowing to fund an income-producing business or investment may qualify, subject to the applicable requirements. Borrowing for personal consumption generally does not.

A separate provision, paragraph 20(1)(e.2), can also permit a limited deduction associated with life insurance assigned as required collateral for qualifying borrowing.

These provisions are established parts of Canada's tax system, not newly discovered loopholes.

Insurance can create Capital Dividend Account room

Section 89(1) of the *Income Tax Act* includes rules governing the Capital Dividend Account.

When a private corporation receives qualifying life insurance proceeds following an insured person's death, those proceeds—generally reduced by the policy's adjusted cost basis—can increase its CDA.

This can allow the corporation to distribute funds as tax-free capital dividends, subject to the applicable rules and required election.

The Canada Revenue Agency even specifically discusses situations where a corporation's life insurance policy is assigned as collateral and the insurer pays part of the proceeds directly to the bank.

In a properly structured collateral assignment, the corporation may still receive the applicable CDA credit, even though some insurance proceeds are used to repay its debt.

That distinction creates an important estate-planning opportunity.

The CRA explains these rules in its official guidance on [Capital Dividends, including life insurance policies used as security](#).

How Can the Loan Be Repaid While the Corporation Still Receives CDA Room?

This is one of the most valuable—and often misunderstood—parts of corporate insurance planning.

Let's use a simplified example.

A corporation owns a life insurance policy with a \$5 million death benefit.

Over time, it has borrowed against the policy to invest in the business, and has an outstanding loan balance of \$2 million, including any accumulated interest.

When the insured person dies:

WHAT HAPPENS	AMOUNT
Life insurance death benefit	\$5,000,000
Outstanding loan repaid to the bank	-\$2,000,000
Insurance proceeds remaining for the corporation	\$3,000,000
Assumed policy adjusted cost basis	\$300,000
Potential CDA credit	\$4,700,000

Notice the difference.

The corporation has \$3 million of insurance proceeds remaining after the loan is repaid.

But, assuming the required legal conditions are satisfied, the insurance can create approximately **\$4.7 million of CDA room**.

That means the corporation could potentially use the additional \$1.7 million of CDA room to distribute other existing corporate assets or cash as tax-free capital dividends.

The CDA does not create additional cash or eliminate taxes incurred in generating investment proceeds. Instead, it can change how an available amount is distributed from the corporation.

This is why the structure of the collateral assignment, policy ownership, loan, and beneficiary designation matters.

For business owners with substantial investments or retained earnings, the ability to access capital during their lifetime while planning for tax-efficient distributions at death can be extremely valuable.

06

Is Permanent Life Insurance Really That Stable?

One reason insurers' participating whole life policies are used as collateral is the contractual guarantees they can provide.

And these products have a considerably longer history than many people realize.

For example, Canada Life reports that it has distributed participating policyholder dividends since **1848**.

That history spans the First World War, the Great Depression, the Second World War, numerous recessions, the global financial crisis, and many different interest-rate environments.

This does not mean every policy earns the same return every year.

Participating policyowner dividends are not guaranteed, and future dividend scales can rise or fall.

However, when dividends are used to purchase paid-up additional insurance, the additional coverage generally carries its own contractual guaranteed values. Once those guaranteed values are established, future dividend-scale reductions do not ordinarily reverse them, provided the policy is maintained in accordance with its terms.

This creates an important distinction between participating whole life insurance and a conventional stock portfolio.

An equity portfolio's market value can decline substantially in a single year.

A participating whole life policy has a foundation of contractual guarantees, with potential additional values supported by participating dividends.

That doesn't make insurance risk-free or necessarily a superior investment.

It does help explain why certain lenders view eligible policy cash values as attractive collateral.

For more information, see [Canada Life's participating life insurance information](#).

So What's the Catch?

There is no single hidden catch.

There are costs, commitments, and risks that need to be evaluated—just as there are with any other form of insurance, borrowing, or investing.

The insurance has a cost. Permanent life insurance requires sufficient funding and is generally more expensive than term insurance. Cash surrender value can also be less than premiums paid, particularly in the early years.

The bank charges interest. Borrowing keeps capital available, but it creates a real liability. Variable rates, changing lending terms, and compound interest can affect the long-term outcome.

The policy must perform as planned. Guaranteed values provide a foundation, but illustrated dividends and non-guaranteed policy growth may differ from projections.

The loan must remain supportable. If interest accumulates faster than the available collateral grows, the lender could require additional security, repayment, or changes to the arrangement.

Tax treatment depends on the structure. Deductions and CDA credits depend on statutory requirements, the legal agreements, and how borrowed funds are used.

In other words, the opportunity is not that the insurance or borrowing is free.

The opportunity is that the combined financial and estate-planning benefits may be worth considerably more than the costs for the right client.

That is what needs to be evaluated.

We believe a strategy should make sense after its borrowing costs, insurance costs, and reasonable downside scenarios are considered—not simply because an illustration looks attractive.

Why Isn't Everyone Doing This?

Because not everyone needs it.

Someone with very little accumulated capital, no permanent insurance requirement, or an immediate need for their savings probably won't benefit from an elaborate insurance-backed financing arrangement.

And even among successful business owners, the right strategy depends on their circumstances.

An IFA is generally most relevant to people who:

- Own profitable incorporated businesses with meaningful retained earnings or investments.
- Have a long-term need for permanent insurance, estate liquidity, or succession planning.
- Want to preserve access to capital for business or investment opportunities.
- Have sufficient income, assets, and borrowing capacity to support the financing.
- Are comfortable with long-term lending arrangements and ongoing reviews.

It is less attractive where capital is needed in the short term, the permanent insurance need is limited, or the economics do not justify the additional complexity.

There's another reason the strategy isn't universally discussed.

It sits at the intersection of **life insurance, commercial lending, corporate taxation, and estate planning**.

Most people deal with separate professionals for each of those subjects.

Their banker handles credit. Their accountant handles taxes. Their investment advisor handles the portfolio. Their insurance advisor handles protection.

But the opportunity often becomes more apparent when those areas are reviewed together.

That doesn't mean everyone should implement an IFA.

It means the strategy deserves to be considered when a business owner's financial circumstances justify it.

Frequently Asked Questions

Is borrowing against whole life insurance legal in Canada?

Yes. Canadian policyowners may use eligible life insurance cash surrender values as collateral for loans from third-party financial institutions. The availability and terms of the loan depend on the lender and policy.

Are loans against life insurance tax-free?

A genuine third-party collateral loan generally does not create taxable income when advanced because it must be repaid. However, policy loans made directly by insurers, policy withdrawals, corporate-to-shareholder transactions, and personal borrowing secured by corporate assets can have different tax consequences.

Can I borrow 100% of my life insurance cash value?

Potentially. Certain lenders may advance up to 100% of eligible cash surrender value, depending on the policy, financial underwriting, and collateral requirements. This is different from borrowing 100% of all premiums paid. Some arrangements require additional security.

Can I capitalize the interest until death?

Some lenders permit interest capitalization or additional advances to cover interest. This can reduce immediate cash-flow requirements, but it increases the outstanding loan balance and may affect the timing and availability of tax deductions. Under CRA guidance, compound interest is generally deductible only when actually paid, if the relevant requirements are satisfied. Capitalization is not guaranteed for the lifetime of the policy.

Does the bank receive the life insurance death benefit?

If the policy has been properly assigned as collateral, the outstanding indebtedness can be repaid from the death benefit when the insured dies. The remaining proceeds are payable according to the policy and lending arrangements.

For corporate-owned insurance, an appropriately structured collateral assignment may allow the corporation to retain the associated CDA treatment even where the bank receives a portion of the proceeds directly.

Is an IFA a tax loophole?

No. An Immediate Financing Arrangement combines permanent life insurance with a secured lending arrangement and existing Canadian tax provisions. Its tax treatment depends on the exact structure and circumstances, and Canadian tax authorities do not automatically approve every arrangement simply because it is described as an IFA.

Is borrowing against life insurance better than investing directly?

Not automatically. It depends on the permanent insurance need, the opportunity cost of premiums, investment returns, borrowing costs, corporate tax circumstances, and estate objectives.

For some clients, conventional investing is the more appropriate choice. For others, the combined value of permanent insurance, retained access to capital, and estate planning can make the insurance-backed strategy attractive.

The Better Question: Does It Make Sense for Your Corporation?

The fact that a strategy is legal doesn't mean it is automatically worth implementing.

And the fact that it isn't suitable for everyone doesn't mean it cannot be exceptionally valuable for the right business owner.

The real question is whether your corporation would be in a stronger financial position using this approach than it would be by continuing with its existing investment and estate plan.

At GOALD & Co Financial, we believe that comparison should be made using your actual numbers.

That includes your retained earnings, existing investments, borrowing capacity, insurance needs, future estate liabilities, and the amount your beneficiaries could ultimately receive.

We can then compare the outcomes of maintaining your current structure against implementing corporate-owned permanent insurance, with and without an Immediate Financing Arrangement.

The goal isn't to make a complicated strategy look attractive. It's to determine whether it creates a measurable advantage for your corporation and your family.

[Explore our complete Immediate Financing Arrangement guide, including actual insurance illustrations.](#)

RELATED GUIDES

Continue with the *related references*.

CONTINUE READING

Immediate Financing Arrangement

The complete IFA guide, including actual insurance illustrations.

CONTINUE READING

Capitalizing IFA Interest

Real lender numbers on financing IFA interest until the death benefit repays it.

CONTINUE READING

Capital Dividend Account

How the CDA works and how tax-free capital dividends are paid.

CONTINUE READING

Accessing Cash Value

Bank loans, policy loans and withdrawals from a whole life policy.

Primary references

- [CRA — Interest Deductibility, Income Tax Folio S3-F6-C1](#)
- [CRA — Capital Dividends, Income Tax Folio S3-F2-C1](#)
- [Equitable Life — Life Policy Collateral Loans](#)
- [Financial Consumer Agency of Canada — Home Equity Lines of Credit](#)
- [Canada Life — Participating Whole Life Insurance](#)

Important information: This article provides general Canadian insurance and tax-planning information and is not individualized legal, tax, insurance, or credit advice. Illustrations and examples are hypothetical. Policies, lending terms, available deductions, and CDA treatment depend on individual circumstances. Consult qualified tax and legal professionals before implementing a strategy.

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