Qube Investment Management Inc.

Featuring:
Lauren's Story

Self-Administered Health Plans

Updated July 2023

Private Health Service Plans

While corporate sponsored health plans provide employees protection from the expense of drugs, dental, vision and other healthcare, they also provide a tax-efficient form of compensation. Health plans in Canada, also called Private Health Service Plans (PHSPs), are a deductible expense to the corporation and a non-taxable benefit to employees. This means that employees can arrange, through a PHSP, to have medical bills paid on their behalf, without attracting income tax.

Qube offers a simple and cost-effective PHSP Self-Administration Kit for small businesses. In contrast to similar plans that charge ongoing fees, our tax-compliant program only requires a one-time flat fee to define and arrange a comprehensive health program with all the necessary training and support to be self-administered.

WHO ARE WE?

What we now call “Qube” was founded in 2000 and became a registered portfolio management firm in the Provinces of Alberta and British Columbia on June 25, 2012. We are one of the few Canadian Portfolio Managers that are independently owned and operated.

Our team members are passionate about investment research and the development of new financial planning strategies for our clients. Health plans are a great example of the opportunity for creative planning in the current Canadian tax landscape.

Benefits from PHSPs can be significant.

Take Lauren, for example.

Lauren has operated her professional practice for five years and is proud of what she has accomplished. She has a profitable client base, a good work-life balance, and a vision for retirement down the road.

She is satisfied with her choice to incorporate her business but often finds herself reconsidering her decision following family gatherings with the in-laws.

Lauren has two brothers-in-law, whom she normally finds tolerable, until they start talking about work. One is an advisor at a large Canadian bank. The other is a school teacher. At their last family event, the two in-laws began comparing their benefit plans.

This is a sensitive topic for Lauren. Even after five years in business, she has yet to figure out an appropriate benefit plan. She’s paid out-of-pocket for everything—even her eyeglasses.

Lauren might need help sorting out health care opportunities for her small business, and would likely benefit from some creative financial planning.

Why Have Corporate-Sponsored Healthcare?

Employer sponsored healthcare has traditionally been the domain of unionized and national firms. Through these plans, employees receive booklets and pay-direct cards that allow them to access various healthcare products and services, which normally include: dental work, pharmaceuticals, massage, chiropractic care, acupuncture, physiotherapy and eye glasses.

In addition to getting these healthcare products, the employee is not taxed. This is an important consideration, as tax rates can reach upwards of 50% in many Canadian Provinces.

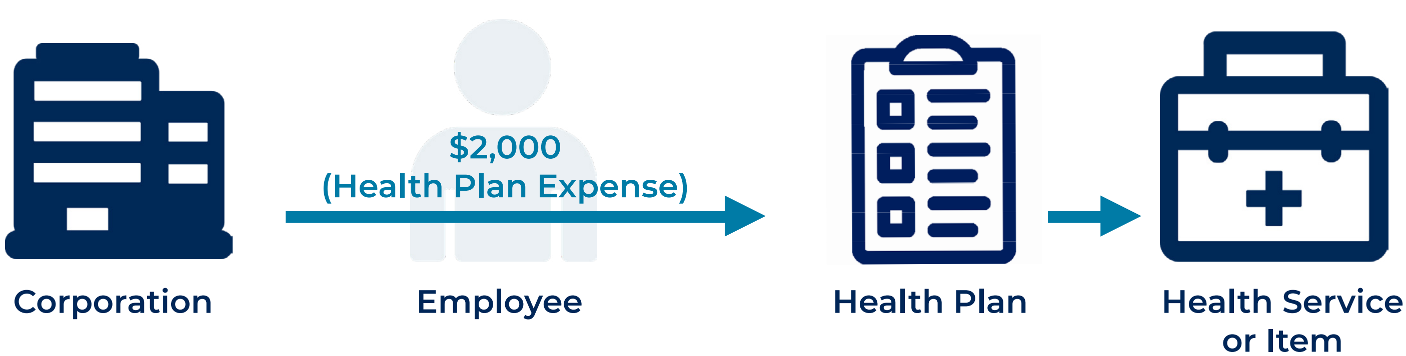
Without a health plan, an uncovered healthcare expense of $2,000 could cost a company like Lauren's $4,000 after taxes are considered.

No Health Care Plan

The company would need to pay $4,000 to the employee to cover this health expense; the employee would need to pay $2,000 in taxes and would have $2,000 left to pay their healthcare bill.

With a Private Health Service Plan (Health Plan)

The company-funded plan can cover the $2,000 bill directly. By being funded by the corporation, the tax cost is excluded, leading to net savings of $2,000. This would also be a tax-deductible expense for the company.



BACKGROUND ON
PRIVATE HEALTH SERVICE PLANS

Historically, insurance companies have primarily managed private Canadian health care. Insurance providers first simplified the arrangement for employers by offering a "health plan" that included the products and services deemed appropriate for a working, middle-class Canadian.

Typically, these health plans included health care services such as basic dental coverage, limited access to health care products and rehabilitation specialists (e.g., basic drug coverage and massage therapy), and eyeglasses & vision care. Insurance companies insured these plans; they charged the employer a premium and, in return, covered all the eligible claims in the plan. This meant the employer had cost certainty and simplicity.

During the high inflation cycle of the 1980s, many employers found the escalation of cost and insurance fees unpalatable. This paved the way for creative health planning. In 1986, the Canada Revenue Agency was asked to comment on health plans managed directly by the employer without the assistance of an insurance company. This advanced tax ruling was called ATR23.

The CRA soon followed up with a definition of a "health plan" in another document called IT-339, which was recently updated into Income Tax Folio S2-F1-C1. Employers now have the option to use an insurance company, a third-party administrator, a trustee, or manage their own plan internally. In all cases though, the health plan had to follow a set number of insurance principles. But what do these options mean for Lauren?

Option 1: Insurance Company Health Plans

Lauren's company has no employees, except for herself. She has looked at various insurance company programs, but upon review of the coverage and costs, lost all interest. The corporation would clearly pay more into the contract than she would typically be able to claim back. The best example in Alberta is the *Alberta Blue Cross Personal Choice Plan.* It comes in three versions, and generally offers the following:

Plan Features	Plan A	Plan B	Plan C
Drugs	70% to $10,000	70% to $10,000	70% to $10,000
Dental	70% Basic only ($600 max)	75% Basic ($600 max) and 50% Extensive (approx. $1250 max)	80% Basic ($600 max) and 50% Extensive approx. $1250 max). Orthodontics $2000 lifetime max.
Medical Travel	10 days	17 days	17 days
Vision & Eye Care	None	$200 every 2 years.	$200 every 2 years.
Paramedicals (e.g., Massage)	Psychologist only $150/yr.	Psychologist to $750/yr. Physio, Chiro & Massage to $350/yr	Psychologist to $750/yr. Physio, Chiro & Massage to $350/yr

What Does It Cost?

Although this information is not publicly available, past quotes from 2017 report the following in regard to the monthly cost—based on the number of family members and their respective ages:

	Plan A	Plan B	Plan C
Ages 4 and under	$8.00	$8.00	$8.00
Ages 5 to 20	$22.00	$23.00	$29.00
Ages 21 to 34	$40.00	$49.00	$63.00
Ages 35 to 44	$41.00	$51.00	$64.00
Ages 45 to 54	$44.00	$55.00	$70.00
Ages 55 to 64	$50.00	$65.00	$82.00

The Cost of Private Health Insurance for Lauren & Her Family

Lauren and her husband are both 45. They have two kids aged 8 and 12. Based on the monthly costs tabled above, their total annual cost for a health plan provided through an insurance company be approximately:

$1,512
Annually
Plan A

$1,776
Annually
Plan B

$2,377
Annually
Plan C

Government-Sponsored Insurance Plans

Many provinces, including Alberta, offer supplemental drug insurance to residents. The Government of Alberta offers what is called “Non-Group Coverage” to all Albertans, which provides access to economical supplementary health benefits, including drugs. Alberta Blue Cross administers this plan.

In summary, the program is subsidized by the Provincial Government, and offers at least 70% reimbursement for eligible drugs. Rates in 2023 run $63.50/month single and $118.00/month for families. If a family member requires $90+ in drugs, or the family together spends more than $170 a month on drugs this plan is a must, as there is only a 3-month waiting period and no medical pre-conditions. Other provinces have similar programs worth investigating.

Option 2: Third-Party Administered Health Spending Accounts

Lauren also looked at health spending account programs offered by third-party administrators. Sign-up fees ran as high as $400 dollars, and claim processing was charged at 5-10% of each claim submitted. Considering the tax savings, this was of interest, but the fees seemed high for the work being offered. Lauren's family had annual medical expenses of around $4,000 per year that would flow through the PHSP and there would be an administration fee charged on every dollar. There had to be another option!

Third-Party PHSP Providers

$4,000 in Annual Medical Expenses

PHSP Provider	Admin Fee	Membership Fee per Year	Total Fees
Olympia Benefits	0%	$249.00	$249.00
Smartin Benefits	5%	$99.00	$299.00
Brock Health Administration	5%	$100.00	$300.00
Cost Efficient Benefit Plan	5%	$100.00	$300.00
Imax Financial Services	10%	$0.00	$400.00
DHC Administrators	10%	$0.00	$400.00
PreTax Health Canada	10%	$99.00	$499.00
Pacific First	10%	$200.00	$600.00
Shield Medical Inc.	10%	$239.00	$639.00
Hub Financial	10%	$250.00	$650.00
Winflex Health Solutions	10%	$250.00	$650.00
Custom Care	10%	$295.00	$695.00
Serre Financial Services	10%	$300.00	$700.00
Trusted Advisors	10%	$315.00	$715.00

All information pertaining to third-party providers is gathered from sources we deem to be reliable and is, to the best of our knowledge, accurate and up to date. We do not, however, guarantee the accuracy or completeness of this information. We encourage you to independently verify any such information.

Option 3: Self-Administered Health Spending Account

After learning all of this, Lauren realizes two injustices are at play. First, she does not have the tax-deductible coverage that her brothers-in-law receive through their employers. Second, she finds that the health plans offered by insurance companies are prohibitively expensive.

What Lauren needs is a health plan that offers everything allowed by the Canada Revenue Agency, but is simple enough to self-administer without the premiums or fees charged by insurance companies and/or third-party administrators. This is entirely possible, but insurance principles and proper documentation are a must.

Tax Ruling ATR23

The ability to self-administer one's own health plan goes back to an Advanced Tax Ruling (ATR23) from 1986. Here, the CRA allowed a company to have a health plan without the involvement of an insurance company. The program is arranged directly with the employees, with the company reimbursing them for eligible health costs as they are incurred. In other words, health plans without an insurance company. This ATR set a new course for health planning in Canada and led to the revision of another key government document called IT-339.

The Meaning of a PHSP

One year after ATR 23, CRA republished IT-339 entitled, "The Meaning of a PHSP." This document clarified what the CRA considered a valid corporate health plan; including the element of insurance when an insurance company is not involved. The CRA explained that the employer, as part of the employment contract, will indemnify agreed medical costs that may be incurred by employees in the year to come. This indemnification must be reasonable in light of the training, experience, and responsibilities of the employees. If the employee incurred no health needs covered by the contract, there can be no indemnification. For example, an RSP deposit could not be made if no health needs arose.

CRA believes the contract benefits must be derived on the basis of their employment relationship to the firm. Items covered in the corporate health contract can include anything that is allowed on the personal tax return as a medical expense (ITA

Key to the discussion in IT-339R2 is what CRA refers to as "acceptable arrangements."

- **Premium Paying Plans** The logical interpretation of a premium paying plan is a health program facilitated by an insurance company on an insured basis;
- **Cost Plus Programs** Some plans are arranged where the employer carries the claim risk, but has a third party administer the plan. The third party will often accept a prepayment of funds, holding them on deposit for the payment of claims. In other cases, they accept corporate funding at the same time a claim is submitted. Generally, this arrangement is done on a "cost plus" basis, meaning the administrator pays the claim cost and then adds a processing fee. It is worth noting that such an arrangement can be offered by a plan administrator (most common), or plan trustee. A trustee (less common) would hold corporate funds in a legal trust, ensuring creditor protection on the monies.
- **Direct and Self-Administered Programs** Here, IT-339R2 offers corporations the authorization to self-administer. CRA states an employer can offer the health benefits as a direct reimbursement under the employment contract.

Note that this IT bulletin has been archived and partially replaced by Information Folder S1:F1:C1 (Medical Expense) and S2:F1:C1 (Health and Welfare Trusts).

PHSPs Now

Since the late 1980s when ATR23 and IT339 were published, the Canada Revenue Agency released hundreds of technical letters affirming and clarifying the position as described above.

The issue of self-administration was directly discussed in Technical Interpretation letter 2003 0050541E5. Here, CRA noted that an in-house PHSP (self-administered plan) could qualify as a PHSP. The employer would reimburse medical expenses incurred by employees or their dependents directly. Under this option, the employer is obligated to reimburse employees for such expenses, and, for the owner-manager situation, the shareholder must be actively engaged as an employee of the company and the PHSP benefits received must be reasonable.

Other letters (2012-0436061E5E, 2004-0071731E5, 2003-005-541E5, 2016-0633741C6) reinforce this position and remind taxpayers that proper administration and documentation, as a health plan, would be necessary for it to qualify for tax exempt status.

A 2020 External T.I. (2020-0846751E5) also provided additional guidance on the reasonableness of excess expenses being carried forward into a future tax year. It was ultimately determined that indefinite carry forward was not in the nature of insurance. Only in exceptional circumstances, such as the COVID-19 pandemic, would it be considered reasonable that costs be carried forward up to 6 months after they were incurred. In more plain terms, it would likely be unreasonable to carry forward expenses into future tax years, outside of exception situations.

One does need to proceed with an abundance of caution when only shareholder-employees are involved.

CRA could view the arrangement as related to shareholdings, not employment; in that case, it would be a taxable benefit (see 2017-0703871C6 and 9516505). Indeed, CRA has warned taxpayers that they will begin a plan review when only shareholder-employees are involved, with the presumption that the PHSP is an arrangement related to shareholdings—not employment. It then becomes the responsibility of the taxpayer to prove the arrangement is reasonable based on employment; which would then qualify the plan for a tax exempt status (see TI 2003-0012665).

In a 2022 discussion (2022-0928901C6 CALU-Q10), the CRA addressed concerns relating to the “reasonable element of risk” that may not exist between an owner-manager, and their corporation. The CRA argued that because the chances are low that an owner-employee (and by extension their family) would not be reimbursed. This means a PHSP arrangement be classified as not in the nature of insurance—putting its tax exempt status at risk. The onus then falls to the taxpayer to show a sufficient transfer of risk occurred within the arrangement.

The solution to these grievances mean that when owner-managers like Lauren are involved, they must be actively engaged as an employee of the sponsoring company, and the PHSP benefits offered/received must be “reasonable.” Reasonable benefits are measured as those that could be attained based on an arm’s length employment relationship with similar experience, responsibility, and training.

In this case, CRA’s general view is that the benefits would be derived by virtue of the individual’s employment (not shareholding); and, therefore, be tax-exempt, as for all other employees (see 2016-0635351E5). Often this can be shown in the form of an owner-manager deriving T4 income (salary). Additional care might be taken through the inclusion of nominal third-party coverage such as with a catastrophic drug plan, or travel insurance.

In summary, when care and diligence is exercised, a self-administered PHSP spending account for a corporation with only shareholder-employees is feasible and should deliver tax exempt benefits to dependent members of each employee’s household related by blood, marriage or adoption. This could also be extended to retired employees (2016-0645581E5).

QIM's Self-Administered Health Plan Kits

We provide planning expertise in the area of health plans and will assist you in setting up a compliant and easy-to-use Private Health Service Plan. Here is a bit more detail on what we offer:

- [ ] Arrangement of a plan text document that creates the health plan with terms and conditions relevant to your situation
- [ ] Assistance in the enrollment and bookkeeping with relevant government programs
- [ ] A training session for your bookkeeper, once the plan documents are prepared, to review the program and learn how it can be self-administered. We assume this session is done in our offices.
- [ ] Support by telephone, for the year following the establishment of the plan, to assist you in plan management
- [ ] An optional plan review after the first plan year to see how the administration is done and to offer advice, if required
- [ ] Simple forms for you to use (both in paper and digital format) to administer the health plan. The administration system will be easy to follow and creates a paper trail that supports the tax position of the plan.
- [ ] Sample employee communication material to assist you in disseminating the plan details to all eligible employees
- [ ] Tax research on health plans, to assist you in evaluating your tax position and the tax fundamentals of a health plan

No Ongoing Fees

We charge a one-time, flat set-up fee based on the number of staff members who will be eligible for the program at the time of Plan Set-Up. Currently, the fees start at $750+GST for companies with 1-2 employees. There are no ongoing admin fees or annual filing fees. We do not charge for our plan review at the end of your first plan year.

PHSP FAQs

Do I need an outside party to administer a PHSP?
No, CRA specifically states that for corporations, PHSPs may be operated without the involvement of a third-party administrator.

Who is eligible to participate in the PHSP?
Anyone who is an employee of the company. The employer determines the level of participation (sets up employee categories for participation and establishes respective annual amounts available for coverage).

What is the maximum annual benefit amount that can be provided through a PHSP?
Reasonability is going to play a role in setting up the annual limit for coverage; so an employer must keep in mind the relative differences between various participating employee classes and their corresponding amounts. Each company will be slightly different, so it is best to contact Qube to discuss your particulars.

Can the annual limit be changed?
Yes, the annual limit may be changed at any time in the future but will require official documentation of this amendment. Changes should not be made arbitrarily.

Are an employee's family members covered through the PHSP?
Yes, all members of the eligible employee's household are included for coverage.

What kind of expenses are covered under a PHSP?
Anything that CRA deems eligible as a medical expense will be eligible through the PHSP like dental, optical, pharmaceutical, paramedical (for example, physiotherapy, chiropractor, acupuncture). Cosmetic procedures (like teeth whitening, for example) would not be eligible. In October 2017, CRA released TI-2016-0636871E5, clarifying that only 90% of the claims have to fall under a strict interpretation of eligibility (ITA 118.2). This allows for more flexibility in plan management. See also 2016-0636871E5, 2016-0651291E5, and 2016-0651291E5.

Can I have insured coverage through insurance and also have a PHSP?
Absolutely. You can pay premiums to an insured plan—like Blue Cross, for example—and use your PHSP as a "piggy bank" to make up for any out-of- pocket medical expenses incurred. Furthermore, premiums to a medical insured plan are eligible for reimbursement through the PHSP as a medical expense.

Once I set up a PHSP for my company, what happens when an employee goes to the drug store and purchases prescription meds?
The employee will pay for their prescription and come back with an official receipt. Your company's in-house administrator will ensure that the claim is eligible and then reimburse the employee for their prescription, tax-free. The company can claim a corporate deduction for this reimbursement amount as an operating expense.

HEALTH PLANS SHOULD BE SIMPLE AND COST EFFICIENT

LET'S TALK ABOUT WHAT A PHSP COULD MEAN FOR YOUR BUSINESS

700+

Self-Administered PHSP Kits provided and supported by Qube since 2010

Contact Us

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Why do we do this?

At Qube, we are passionate about many great topics focusing on Canadians' investment needs. With our passion for financial planning, we promote financial literacy to anyone within our reach. The whitepapers we create aim to bring awareness of the benefits that working with a wealth manager provides. After reading the papers, our objective is to have the opportunity to prepare an investment proposal for potential clients. While the topics we write about are applicable for Canadians, Qube specifically services clients anywhere in Alberta and British Columbia.

Next Steps

Your goals, whether they are focused on ensuring a comfortable retirement, growing a business, taking care of later generations or something more intangible, we are here to make it matter. We want you to reach out to see how we can help.

You can contact Qube at phsp@qubeinvest.ca or by phone: 1.780.463.2688.

Disclaimer

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