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The Learning Kurve

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PHSP Anyone?

There is more than one way to provide employee health benefits.

Owner/managers are often reluctant to provide medical coverage to employees because of the initial cost and the increased cost of premiums that occur when employees use all their entitlements. As a result of these indeterminable expenses, not only do the employees do without, but also the employer and his/her family are, more often than not, denied any medical benefits.

Private Health Services Plan

An often overlooked method of providing medical coverage is the Private Health Services Plan (PHSP), which enables corporations and the self-employed to provide health, dental and vision tax-free benefits to employees and their dependents. The amount paid out as a claim and any third-party administrative costs related to the PHSP are tax deductible. Section 248(1) of the Income Tax Act requires that the terms of the PHSP should be written up as a contract between the employer and a third-party administrator for the benefit of the employees.

Certainly the ability to write off medical costs along with the administration cost is a benefit to both the employee and the employer. The ability to run one's own plan controls costs, removes some of the restrictions an insurance company may place on a small business, removes obstacles to obtaining coverage if employees or shareholders have pre-determined medical issues that may not be covered, and allows the owner/manager to offer benefits that may be limited or not available through an insurance company.

For payments of shareholder medical expenses to be accepted, the shareholder must receive the benefit in his/her capacity as an employee, not as a shareholder. The shareholder cannot be a passive participant but must be actively engaged in the business activities of the corporation, although not necessarily collecting a salary.

An initial registration fee may be required. After that the administrator normally charges an administration fee equal to a percentage of the amount submitted for a medical claim.

Incorporated?

Incorporated businesses are not limited as to the PHSP amount that can be reimbursed. It should be noted that as long as the premiums paid are reasonable and all benefits extend equally to all employees and not simply to the owner/manager(s) and his/her immediate family, medical expenses should not be challenged by the Canada Revenue Agency. Conversely, if the medical expenses are deemed excessive or if it were established that arms-length employees were not receiving equal consideration, then undoubtedly there would be a change in the CRA's attitude. In this event, the payout for owner/managers could end up a taxable benefit in their hands with the possibility that the deduction to the corporation would not be allowed. The CRA could reason that the benefits were incurred as a shareholder to the company and not as an employee actively engaged in the activities of the company.

Positive Incentives

The medical expenses covered are too numerous to list but follow the medical expense definition as indicated in the Income Tax Act subsection 118.2(2). It may surprise the reader to know that many expenses referred to in the Act may not be covered by traditional providers of medical insurance.

Since payments made by the business are not perceived as a benefit to the recipient, the business does not have to make additional remittances for CPP, UIC, health tax or be concerned about remittances to the CRA.

An employer can establish differing ranges of benefits for different groups of employees. Thus, the employer is able to determine for budgeting purposes the maximum cash-flow drain that could occur if use were maximized.

Most external plans require the payment of a monthly premium regardless of whether a claim has been made. The PHSP incurs premiums only in the case of a health, medical or dental expense. This approach allows the owner/manager to control not only the cash flow but also the "premium" that ultimately is paid each year for those who are covered.

How Does It Work?

Assume, for example, an employer agrees that the company will reimburse an employee up to $2,000 for medical costs for the year. The employee visits the dentist, receives a bill for $400 and submits it to the employer, who then submits it to the PHSP administrator along with payment of the $400, plus the administration fee. The PHSP administrator writes a cheque to the employee. The employer expenses the $400 plus the administration fee.

Although the PHSP may not be for everyone, it does allow the small-business owner to provide competitive benefits when trying to attract new employees while at the same time controlling the cost. To ensure that the owner/manager's interpretation of the deductibility does not run afoul of the Income Tax Act, it is certainly advisable to work with an experienced administrator and review the plan with a Chartered Accountant.

This'n That at Logan Katz

Comings and Goings

We would like to take the opportunity and welcome Faysol Kabir to Logan Katz. Faysol will be starting with us in early May. He is a summer student from University of Ottawa.

Also a very special thank you to our co-op students Adam Bleackley and David Hamilton from University of Ottawa, Megan Ni from University of Toronto and Brent McLean and Meng Yu from Algonquin College for all their hard work during this busy tax season.

Hope everyone enjoys the Spring weather!!!