



Private Health Services Plans

*A Benefit Option for Uninsured Patients Who Own or Work
for Incorporated Small Businesses*

Some of your patients may be able to write off the dental costs and many other medical costs as a business expense. A patient who has his/her own business and is incorporated can set up a Private Health Services Plan (PHSP). This allows the employer (the company) to pay medical/dental expenses for the employees and their dependants. These payments are a tax-deductible expense for the company and non-taxable benefit for the employees. Since the owner of an incorporated business is legally an employee of the company, owners and their families can participate in the plan as well. Incorporated dental practices would also be eligible for this type of plan.

Making this information available to the patients in your practice creates a win-win situation. These plans help to reduce the cost of dentistry to your patients by making it easier for patients to pay, and therefore, more likely to follow through with needed treatment.

In our society, there is a trend towards entrepreneurship and self-employment. There will be more of your patients who do not have access to group dental plans. A PHSP will help fill that void for small business owners. The CDA is lobbying the federal government to have this benefit extended to unincorporated businesses as well.

We have prepared a package of information suitable for distribution to your patients. We would encourage you to make copies available to your patients, possibly leaving a copy in your waiting room. It is also a good idea to inform the receptionist and other staff who come into contact with patients, so that they can answer basic questions about the PHSPs. The package contains the following information:

1. What is a Private Health Services Plan?
2. How to set up a PHSP in your business.
3. Sample documents which are required to properly establish a PHSP.
4. A copy of Revenue Canada's interpretation bulletin IT-339R2, INCOME TAX, Meaning of "Private Health Services Plan".



Association of Dental Surgeons
of British Columbia



What is a Private Health Services Plan?

A Private Health Services Plan (PHSP) is provided for in the *Income Tax Act* (Canada). In its simplest form, it permits an incorporated employer to reimburse an employee for the cost of most dental, medical or hospital care. Such reimbursements by the employer are not taxable employee benefits, so these expenses should not be used in calculating the employees' personal taxes. The employer is generally entitled to a business expense deduction for the full amount of health care expenses for the employee. Note that these are not subject to the three percent limitation which only applies to individuals when filing for their personal income tax. Under existing rules, the employer must be incorporated.

A major benefit is that almost all medical expenses for the owners/key employees of incorporated businesses and their families can be paid by their businesses as business expenses. It can also be used as a benefit to attract, reward, and keep good employees. A small business can self-administer the plan which greatly reduces costs and allows for more flexible benefits.

Eligible expenses include payments to:

- ✓ medical doctors (not MSP premiums)
- ✓ dentists
- ✓ pharmacists (drugs)
- ✓ optometrists (frames and lenses)
- ✓ chiropractors
- ✓ physiotherapists
- ✓ podiatrists
- ✓ naturopaths
- ✓ psychologists

Eligibility includes employees, their spouses and members of the employees' household with whom the employees are connected by blood relationship, marriage or adoption. The owner is considered an employee of an incorporated business.

When establishing a PHSP, there are a couple of things that are legally required:

1. There should be an employer/employee agreement outlining the parameters of the plan. It should include such things as eligibility for the participation in the plan, the amount of the benefit, the services that qualify for reimbursement and the employer's right of revocation.
2. A director's resolution should be drawn up, signed and placed in the company's minute book. This should cover the creation of the PHSP as well as the matters covered by the employee/employer agreement.

Internal administration is simple. A PHSP account can be set up for each employee (including the owner) to keep track of the amounts reimbursed.

A PHSP can be a very flexible benefit for employees. It can be set up as a direct reimbursement not restricting any eligible services. It may be offered in lieu of a raise in salary. Some employees may want it and others not. There are many possibilities.

How to Set up a PHSP in Your Business

There are three steps:

1. Directors resolution to create the PHSP

The resolution should include:

- a) The establishment of a PHSP.
- b) Who has authority to determine benefits and eligibility.

Sample 1 contains a draft resolution

2. Employee/Employer Agreement

The second item is to establish an employer/employee agreement including the following:

- a) That the employee is eligible for benefits under the plan.
- b) Conditions of employment need to be met to continue as a beneficiary of the plan?
- c) Conditions that would result in a loss of benefit.
- d) The employer has the right to revoke the plan on 30 days' notice.
- e) The amount of the benefits and the services for which benefits will be paid.

Sample 2 contains a draft agreement

3. Set Up an Expense Account

The third item is to set up an expense account in your accounting/bookkeeping system to keep track of how much is being paid out in benefits. It should show:

- a) The level of benefits.
- b) Whether or not the employee is at or below the amount of benefit to which he/she is entitled
- c) The amount of benefits paid to date.

Under the simplest form of PHSP, when an employee incurs a related expense, he/she simply brings a receipt into the office and is reimbursed for the amount. The company will keep the receipt as a record of payment.

The amount of benefits might be set differently for different types of employees. For example, the level of benefits may be dependent on years of seniority. As well, you may choose whether or not to allow any unused benefits in a given year to be carried over to the following years. Outlining the qualifying benefits made available and to whom may be as flexible as desired.



Interpretation Bulletin

Subject: Income Tax Act
Meaning of “Private Health Services Plan”

No. IT-339R2

Date: August 8, 1989

Reference: Subsection 248(1) (also paragraphs 6(1)(a), 18(1)(a), 118.2(2)(q) and 118.2(3)(b))

Application

The provisions discussed below are effective for the 1988 and subsequent taxation years. For taxation years prior to 1988, refer to Interpretation Bulletin IT-339R dated June 1, 1983.

Summary

This bulletin discusses the meaning of a “private health services plan” and describes some of the arrangements for covering the cost of medical and hospital care under such a plan. It also discusses the tax status of contributions made to such a plan by an employer on behalf of an employee and the circumstances under which the premium costs incurred by an employee qualify as medical expenses for purposes of the medical expense tax credit.

Discussion and Interpretation

1. Contributions made by an employer to or under a private health services plan on behalf of an employee are excluded from the employee’s income from an office or employment by virtue of subparagraph 6(1)(a)(i). On the other hand, an amount paid by an employee as a premium, contribution or other consideration to a private health services plan qualifies as a medical expense for purposes of the medical expense tax credit by virtue of paragraph 118.2(2)(q). The amounts so paid must be for one or more of
 - a) the employee
 - b) the employee’s spouse and
 - c) any member of the employee’s household with whom the employee is connected by blood relationship, marriage or adoption.

For further comments on the medical expense tax credit see the current version of IT-510.

For purposes of the Act, a “private health services plan” is defined in subsection 248(1).

2. The contracts of insurance and medical or hospital care insurance plans referred to in paragraphs (a) and (b) of the definition in subsection 248(1) of “private health services plan” include contracts or plans that are either in whole or in part in respect of dental care and expenses.
3. A private health services plan qualifying under paragraphs (a) or (b) of the definition in subsection 248(1) is a plan in the nature of insurance. In this respect the plan must contain the following basic elements:
 - a) an undertaking by one person,
 - b) to indemnify another person,
 - c) for an agreed consideration,
 - d) from a loss or liability in respect of an event,
 - e) the happening of which is uncertain.
4. Coverage under a plan must be in respect of hospital care or expense or medical care or expense which normally would otherwise have qualified as a medical expense under the provisions of subsection 118.2(2) in the determination of the medical expense tax credit (see IT-519).
5. If the agreed consideration is in the form of cash premiums, they usually relate closely to the coverage provided by the plan and are based on computations involving actuarial or similar studies. Plans involving contracts of insurance in an arm’s length situation normally contain the basic elements outlined in 3 above.
6. In a “cost plus” plan an employer contracts with a trustee plan or insurance company for the provisions of indemnification of employees’ claims on defined risks under the plan. The employer promises to reimburse the cost of such claims plus an administration fee to the plan or insurance company. The employee’s contract of employment requires the employer to reimburse the plan or insurance company for proper claims (filed by the employee) paid, and a contract exists between the employee and the trustee plan or insurance company in which the latter agrees to indemnify the employee for claims on the defined risks so long as the employment contract is in good standing. Provided that the risks to be indemnified are those described in paragraphs (a) and (b) of the definition of “private health services plan” in subsection 248(1), such a plan qualifies as a private health services plan.
7. An arrangement where an employer reimburses its employees for the cost of medical or hospital care may come within the definition of private health services plan. This occurs where the employer is obligated under the employment contract to reimburse such expenses incurred by the employees or their dependants. The consideration given by the employee is considered to be the employee’s covenants as found in the collective agreement or in the contract of service.



8. Medical and hospital insurance plans offered by Blue Cross and various life insurers, for example, are considered private health services plans within the meaning of subsection 248(1). In addition, the Group Surgical Medical Insurance Plan covering federal government employees qualifies as a private health services plan within the meaning of subsection 248(1). Therefore, payments made by an individual under such a plan qualify as medical expenses by virtue of paragraph 118.2(2)(q).
9. Private health services plan premiums, contributions or other consideration paid for by the employer are not included as medical expenses of the employee under paragraph 118.2(2)(q) by virtue of paragraph 118.2(3)(b) and are not employee benefits (see 1 above). They are however, business outlays or expenses of the employers for the purposes of paragraph 18(1)(a). On the other hand, contributions or premiums qualify as medical expenses under paragraph 118.2(2)(q) where they are paid directly by the employee, or are paid by the employer out of deductions from the employee's pay. The amounts so paid must be for one or more of
 - a) the employee,
 - b) the employee's spouse and
 - c) any member of the employee's household with whom the
 - e) employee is connected by blood relationship, marriage or adoption.

PHSP premiums 20.01 (1) Notwithstanding paragraphs 18(1)(a) and (h) and subject to subsection (2), there may be deducted in computing an individual's income for a taxation year from a business carried on by the individual and in which the individual is actively engaged on a regular and continuous basis, directly or as a member of a partnership, an amount payable by the individual or partnership in respect of the year as a premium, contribution or other consideration under a private health services plan in respect of the individual, the individual's spouse or any person who is a member of the individual's household if

- (a) in the year or in the preceding taxation year
 - (i) the total of all amounts each of which is the individual's income from such a business for a fiscal period that ends in the year exceeds 50% of the individual's income for the year, or
 - (ii) the individual's income for the year does not exceed the total of \$10,000 and the total referred to in subparagraph (i) in respect of the individual for the year,

on the assumption that the individual's income from each business is computed without reference to this subsection and the individual's income is computed without reference to this subsection and subdivision e; and

- (b) the amount is payable under a contract between the individual or partnership and

- (i) a person licensed or otherwise authorized under the laws of Canada or a province to carry on in Canada an insurance business or the business of offering to the public its services as trustee,
- (ii) a person or partnership engaged in the business of offering to the public its services as an administrator of private health services plans, or
- (iii) a person the taxable income of which is exempt under section 149 and that is a business or professional organization of which the individual is a member or a trade union of which the individual or a majority of the individual's employees are members.

(2) For the purpose of calculating the amount deductible under subsection (1) in computing an individual's income for a taxation year from a particular business,

Limit

- (a) no amount may be deducted to the extent that
 - (i) it is deducted under this section in computing another individual's income for any taxation year, or
 - (ii) it is included in calculating a deduction under section 118.2 in computing an individual's tax payable under this Part for any taxation year;
- (b) where an amount payable under a private health services plan relates to a period in the year throughout which
 - (i) each of one or more persons
 - (A) is employed on a full-time basis (other than on a temporary or seasonal basis) in the particular business or in another business carried on by
 - (I) the individual (otherwise than as a member of a partnership),
 - (II) a partnership of which the individual is a majority interest partner, or
 - (III) a corporation affiliated with the individual, and
 - (B) has accumulated not less than three months of service in that employment since the person last became so employed, and
 - (ii) the total number of persons employed in a business described in clause (i)(A), with whom the individual deals at arm's length and to whom coverage is extended under the plan, is not less than 50% of the total number of persons each of whom is a person
 - (A) who carries on the particular business or is employed in a business described in clause (i)(A), and
 - (B) to whom coverage is extended under the plan,

the amount so deductible in relation to the period shall not exceed the individual's cost of equivalent coverage under the plan in respect of each employed person who deals at arm's length with the individual and who is described in subparagraph (i) in relation to the period;



(c) subject to paragraph (d), where an amount payable under a private health services plan relates to a particular period in the year, other than a period described in paragraph (b), the amount so deductible in relation to the particular period shall not exceed the amount determined by the formula

$$(A/365) \times (B + C)$$

where

A is the number of days in the year that are included in the particular period,

B is the product obtained when \$1,500 is multiplied by the number of persons each of whom is covered under the plan, and

- (i) is the individual or the individual's spouse, or
- (ii) is a member of the individual's household and has attained the age of 18 years before the beginning of the particular period, and

C is the product obtained when \$750 is multiplied by the number of members of the individual's household who, but for the fact that they have not attained the age of 18 years before the particular period began, would be included in computing the product under the description of B; and

(d) where an amount payable under a private health services plan relates to a particular period in the year (other than a period described in paragraph (b)) and one or more persons with whom the individual deals at arm's length are described in subparagraph (b)(i) in relation to the particular period, the amount so deductible in relation to the particular period shall not exceed the lesser of the amount determined under the formula set out in paragraph (c) and the individual's cost of equivalent coverage in respect of any such person in relation to the particular period.

(3) For the purpose of subsection (2), an amount payable in respect of an individual under a private health services plan in relation to a period does not exceed the individual's cost of equivalent coverage under the plan in respect of another person in relation to the period to the extent that, in relation to the period, the amount does not exceed the product obtained when

- (a) the amount that would be the individual's cost of coverage under the plan if the benefits and coverage in respect of the individual, the individual's spouse and the members of the individual's household were identical to the benefits and coverage made available in respect of the other person, the other person's spouse and the members of the other person's household

is multiplied by

- (b) the percentage of the cost of coverage under the plan in respect of the other person that is payable by the individual or a partnership of which the individual is a member.

Equivalent coverage

Canada

Private Health Service Plans

Sample #1

CONSENT RESOLUTION OF THE DIRECTOR OF _____ INC.

I, the undersigned, being the sole director of _____, INC. (the "Company"), hereby consent to and adopt in writing the following resolution:

RESOLVED THAT:

1. Effective _____, 20____, the Company establish a Private Health Services Plan (PHSP) according to the terms and conditions of the *Income Tax Act* (Canada) pursuant to which certain medical and dental expenses incurred by the Company's employees, directors and officers and their spouses, dependent children and other dependents, not otherwise covered under any insurance plan, may be reimbursed by the Company.
2. The Director of the Company be and is hereby authorized to determine in his/her sole discretion which expenses will be eligible for reimbursement, and the eligibility of any individual incurring expenses to be included in the PHSP, and to enter into agreement on behalf of the Company, with the employees of the Company eligible for participation in the PHSP, in form and substance satisfactory to the Director in his/her sole discretion, confirming the terms and conditions of the PHSP and of employees' entitlement to benefits thereunder.

DATED at _____ ,

this _____ day of _____, 20 _____

DIRECTOR



Private Health Service Plans

Sample #2

Private Health Services Plan

A benefit of employment with _____ Inc.

In consideration of your commencing or continuing employment with _____ Inc., you are entitled to participate in a Private Health Services Plan (PHSP) which will cover many medical and dental expenses incurred by you and your immediate family. While this is a non-taxable benefit, you will not be permitted to claim a medical expense tax credit with respect to any amount reimbursed under the PHSP.

In order to be eligible to participate in the PHSP, you must work at least _____ hours per month for the company. If your monthly hours drop below that level, you will no longer be eligible for the benefits under this plan.

The Company has the right to revoke the PHSP on 30 days' notice.

The amount of the benefit reimbursement available to you and your family is limited to a maximum of \$ _____ per calendar year.

Services covered include:

- ✓ most doctors and hospital expenses not covered by the Provincial Medical Plan
- ✓ prescription drugs
- ✓ eye glasses
- ✓ dental expenses
- ✓ user fees from most other health providers (*e.g. chiropractors*)

Services not covered include:

- ✗ MSP premiums
- ✗ services paid by other health benefit plans in which your family already participates (*e.g., spousal plan*)

For a complete list of services included and excluded from the PHSP, please contact _____ at local _____

PRACTICE MANAGEMENT RESOURCES
PRACTICE MANAGEMENT SUBCOMMITTEE – 1999

Purtzki & Associates

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What we do best

| | | |
|------------------------------|-----------------------------|---|
| ▶ Practice transitions | Tax minimization | ◀ |
| ▶ Practice valuations | Personal financial planning | ◀ |
| ▶ Practice management advice | Estate planning | ◀ |
| ▶ Internal control reviews | Accounting | ◀ |

The attached documents are for information purposes only.

No dentist or business person should establish a PHSP without independent legal and accounting advice.

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