

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

INTRODUCTION

A group sickness or accident insurance plan (GSAIP) is an employer-sponsored insurance plan that pays benefits to employees who have a covered sickness or accident. GSAIPs can provide the following benefits:

- Long or short term disability insurance (DII)
- Accidental death or dismemberment insurance (ADD)
- Critical illness insurance (CII)
- Income-style long-term care insurance (LTCI)¹

We will discuss each of these types of insurance in more detail later in this article.

The sickness or accident that triggers an employee's receipt of benefits need not be work related. GSAIPs are not related to provincial health insurance or workers' compensation plans and do not have to be integrated with them.

GSAIPs differ from Private Health Services Plans (PHSPs).² PHSPs pay for covered hospital and medical expenses that may or may not arise from a sickness or accident. GSAIPs pay a benefit or benefits when the insured person gets sick or is injured in an accident, and may or may not incur any hospital or medical expenses. For example, many PHSPs cover the cost of routine dental checkups, which generally are preventative in nature. In contrast, a GSAIP may pay a benefit if an employee is injured in an accident, even if the employee incurs no hospital or medical expenses as a result.

Employer contributions to a GSAIP are taxable to an employee if the benefits paid from the plan are tax-free.³

¹ Income style LTCI policies pay benefits when the insured person satisfies the requirements in the policy to receive benefits. The benefits paid are unrelated to the actual cost of long-term care. In contrast, reimbursement style LTCI policies also pay benefits when the insured person satisfies the requirements in the policy to receive benefits, but the policy only pays benefits that reimburse the policy owner for long-term care expenses covered by the policy. Benefits paid under both policies may be subject to deductibles, co-payments and policy limits.

² See our article, "Private Health Services Plans" for more details on PHSPs.

³ ITA paragraph 6(1)(e.1) and subparagraph 6(1)(a)(i).

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

This means that employer contributions for CII, income-style LTCI, and ADD are taxable to the employee,⁴ while employer contributions for reimbursement-style LTCI and DII are not.

Additionally, employer paid premiums for group term life insurance are taxable to an employee. Finally, all employer contributions to a GSAIP are taxable to employees in Quebec on their provincial (not federal) tax return, regardless of the tax treatment of the benefits paid from such plans.

WHAT IS A GSAIP?

GSAIPs are included in subparagraph 6(1)(a)(i) of the Income Tax Act⁵ (ITA) as a benefit that an employer may offer to its employees, but the term is not defined in the ITA. Sections in the ITA and other legislation, legal decisions, and CRA guidance help define the term.

In general terms, the CRA defines a GSAIP as “an arrangement between an employer and employees under which provision is made for indemnification of an employee if an employee suffers a loss of employment income as a consequence of sickness, maternity or accident.”⁶

⁴ See Canada Revenue Agency (CRA) Document 2013-0482151E5, July 08, 2013, for the CRA's comments on the inclusion in an employee's income of the employer's contributions to an Employee Life and Health Trust (ELHT) to pay for CII and ADD. The CRA's guidance contained in its interpretation bulletins, responses to taxpayer inquiries and advance tax rulings is the CRA's interpretation of the law on a given subject and can help taxpayers plan their affairs in order to comply with the law. However, the CRA is not bound by what it says in its interpretation bulletins or by its responses to taxpayer inquiries. The CRA is bound by the Income Tax Act and Regulations, and by judicial decisions, all of which have the force of law. It is also bound by the Advance Tax Rulings (ATR) it issues, but only to the individual taxpayer who requested the ruling, and only as long as the circumstances outlined in the request for the ATR remain unchanged. The CRA is free to take a different position on a same or similar question or ruling request from a different taxpayer.

⁵ Income Tax Act, R.S.C., 1985, c. 1 (5th Supp.), referred to herein as the ITA.

⁶ CRA Document 2009-0314871E5, March 3, 2011.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

The balance of this section expands on the definition of a GSAIP by exploring the meaning of its specific elements.

A GROUP

Canadian courts have ruled that you must have more than one employee in a group insurance plan for there to be a plan.⁷ CRA guidance has confirmed that a group consists of more than one person.⁸ This definition of a group covers group insurance plans (employees insured through certificates of coverage issued under a single contract owned by the employer) and grouped insurance plans.⁹ It is also found in the legislation governing Employee Life and Health Trusts (ELHTs).¹⁰

While these definitions make sense and may even seem obvious, they can have serious implications for employers and employees in small businesses. In one case, a sole shareholder/employee wanted to join the company's GSAIP, but also wanted to receive superior benefits than the other employees in the group. The CRA stated that he had to accept the same benefits as everyone else in the group. Nor could he create a second GSAIP just for himself, because his corporation employed no other employees with responsibilities comparable to his, and because the corporation could not have a GSAIP with only one member.¹¹ The CRA gave no consideration to the potential for an expanded or looser meaning for the term "group" where all employees receiving benefits would be treated as part of a group, even though one employee was receiving more generous benefits than the others.

⁷ Meyer v. M.N.R. [1977] C.T.C. 2581, 1977 77 D.T.C. 413 (Tax Review Board).

⁸ CRA Documents 5-7999, 2000-0055145 and 2006-0174121C6, July 12, 1989, January 9, 2001 and May 9, 2006.

⁹ Grouped plans are discussed in this article. In general, a grouped plan is a GSAIP where employees are insured through individual contracts owned by themselves or their employer, but pursuant to a written plan established by the employer.

¹⁰ The term, "class of beneficiaries" is defined as "a group of beneficiaries who have identical rights or interests under the trust" under ITA subsection 144.1(1).

¹¹ CRA Document 5-7982, July 12, 1989.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

Even if an employer created a GSAIP to provide enhanced benefits for a select few employees, the GSAIP would have to end if it were reduced to only one member, for example by employees leaving or passing away. The CRA said:

{W}here a plan has two employees and one employee subsequently ceases to be covered by the plan, it is our view that the plan would cease to be a group plan at that time and consequently a taxable benefit would be included in the remaining employee's income for any contributions made by the employer to the plan after it ceased to be a group plan.¹²

The CRA has not said whether it would allow a grace period during which a GSAIP could be temporarily out of compliance. Its interpretations currently do not leave any room for temporary non-compliance.

An employer does not need to provide only one plan for all its employees, but may offer different plans to different groups of employees with differing needs and with whom it negotiates in different ways. For example, an employer may provide one plan for its unionized workforce, another for its salaried employees, another for its sales force, and one for its key executives. CRA guidance allows such separate plans, as do the rules in the ITA governing ELHTs.¹³

It's also possible for individuals employed with different employers to form a single group.¹⁴ A multi-employer plan is often used in industries where people may work at different times of the year for different employers as they begin and complete different projects. Rather than belonging to many different plans established by many different employers, they belong to one group to which all their employers contribute.

¹² CRA Document 5-7999, July 12, 1989.

¹³ IT-428, paragraph 8. ITA paragraph 144.1(1)(e) says that an ELHT must have at least one class of beneficiaries, implying that more than one are allowed.

¹⁴ IT-428, paragraph 9, and ITA subsection 144.1(6) (governing multi-employer plans for ELHTs).

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

A multi-employer group must also have at least two members, but those members may come from different employers. It's therefore possible for people who are the sole employees of their respective employers to form a GSAIP through a multi-employer group.¹⁵

In light of the CRA's position, it's worth revisiting CRA Document 5-7982, referred to above. The company that employed the taxpayer in that case could not provide different benefits for him than what it provided for the rest of the company's employees because that would have meant providing different benefits for only one employee. But if the company had another employee with comparable responsibilities to the taxpayer's, it could have provided benefits for both as part of a different group plan. Failing that, the company could have established a multi-employer group plan with another company or companies, and the taxpayer could have become part of that plan.

Within a group, all members of the group should receive equal benefits. The definition of the term, "class of beneficiaries" in ITA subsection 144.1(1) governing ELHTs says that members of a class must have "identical rights or interests under the trust."¹⁶

Regarding other types of GSAIPs, CRA guidance is not so rigid. In dealing with a proposed plan where a group of employees were to own individual policies that would provide them with plan benefits, the CRA said:

[I]t is possible for individual policies owned by the employees to combine to form a common plan and be considered a GSAI plan provided each employee within a particular class or group of employees is eligible to receive the same benefits under the plan and has the same ratio of employee and employer-paid premiums.¹⁷

¹⁵ CRA Document 2011-0422621E5, August 24, 2012.

¹⁶ ITA subsection 144.1(1) c.f. "class of beneficiaries".

¹⁷ CRA Document 2009-0314871E5, March 3, 2011.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

But more recent CRA guidance may have modified the requirement for same benefits:

Where the plan consists of individual policies, the policies should provide similar benefits to each employee and each employer must have the same ratio of employee and employer-paid premiums....¹⁸

Employees and employers cannot be members of the same group. ITA subparagraph 6(1)(a)(i) refers to a benefit "derived from the contributions of the taxpayer's employer." Since partners and sole proprietors are employers, they cannot be part of a group that includes employees. Referring to HWTs, the CRA said that employers can create and contribute to an HWT for their benefit, but will not be able to deduct the contributions they make to such plans, and will have to keep their plans strictly separate from their employees' plans.¹⁹ Although new HWTs may no longer be created, and existing ones will be phased out,²⁰ the same reasoning should apply to grouped plans, though the CRA has not provided guidance. ELHTs deal with this issue differently, by restricting key persons' (a term that includes shareholders) participation in an ELHT, requiring that they receive identical benefits if they are in a class with non-key employees, or that they receive benefits that are "not more advantageous" than the non-key employees if they are part of a separate class of beneficiaries under the trust. See our article, "Employee Life and Health Trusts" for details.

Shareholder/employees can be members of the same group as non-owner employees because shareholders can be employees of the businesses they own. In discussing a PHSP, the CRA said that a shareholder/employee could be a member of a group that received benefits under the PHSP as long

¹⁸ CRA Documents 2006-0174121C6, May 9, 2006 and 2011-0422621E5, August 24, 2012.

¹⁹ CRA Documents AC59422 and 9311685, March 13, 1990, and August 31, 1993, and Income Tax Folio S2-F1-C1, paragraph 1.4.

²⁰ See our article, "Employee Life and Health Trusts" for details.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

as the shareholder/employee received their benefits as an employee, not because they owned the company.²¹ To help counter the CRA's presumption that the shareholder was receiving a benefit because they owned the business, not because they worked for it, it would be important for owner and non-owner employees to be members in this class, and for all members to receive equivalent benefits. In our article, "Private Health Services Plans" we examine the CRA's requirement in Interpretation Bulletin IT-339-R2 that a private health services plan be an insurance plan.²² The CRA has agreed that these requirements apply also to GSAIPs.²³

Benefits from a sickness or accident insurance plan are taxable to the employee if paid on a periodic basis, and if paid for the employee's loss of employment income. This rule generally applies to DII plans. ITA paragraph 6(1)(f) taxes benefits paid on a periodic basis for a loss of income from an office or employment. It refers to benefits paid or payable from a "sickness or accident insurance plan," omitting the word "group".

The CRA has specifically commented on this omission:

It should be noted that while a sickness or accident insurance plan must be a group plan in order that the benefit derived from the employer's contribution to such a plan not be a taxable benefit under paragraph 6(1)(a) of the Act, a plan does not need to be a group plan in order for benefits thereunder to be subject to paragraph 6(1)(f) of the Act.²⁴

As a result, an employee may have to include in income the employer's contributions to a benefit plan if the plan fails to qualify as a group plan under ITA subparagraph 6(1)(a)(i), and may also have to include in income the benefits paid from that plan if it qualifies as a sickness or accident insurance

²¹ CRA Document 2005-0163771E5, March 14, 2006.

²² Interpretation Bulletin IT-339R2 – Meaning of "Private Health Services Plan," August 8, 1989.

²³ CRA Document 2010-0374891E5, March 14, 2011.

²⁴ CRA Document 5-7999, July 12, 1989. See also *Leonard v. R.*, Federal Court (Trial Division) September 13, 1996, unreported, docket no. T-651-87.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

plan under ITA subparagraph 6(1)(f)(i). In creating the plan, the employer must take care to ensure that this result does not occur.

SICKNESS OR ACCIDENT

The term, "sickness or accident" is not defined in the ITA. In deciding whether a given plan is a "sickness or accident" insurance plan, the CRA has taken several approaches.

Under one approach the CRA considers the definitions of "sickness" and "accident" in provincial and territorial insurance acts and regulations, and in the Government of Canada's definition.²⁵ At a minimum, the federal government and all the provinces and territories define sickness or accident insurance as insurance under which the insurer agrees to pay an insurance benefit if, under the insurance contract language, the insured person gets sick or suffers bodily injury because of an accident. There is no requirement for the insured person to have sustained any expenses arising from their sickness or accident.

Under a second approach the CRA considers the definition of sickness or accident insurance provided by the Insurance Institute:

*A form of insurance compensating an individual for loss as a result of an accident or illness. It may pay certain or all expenses for medical and similar services and a weekly or monthly indemnity for loss of income. The amounts and items covered vary from policy to policy and depend to some extent on what coverage is purchased by the insured.*²⁶

This definition differs from that used by the federal, provincial and territorial insurance laws by noting that the policy may pay medical expenses resulting from a sickness or accident (such as expenses for hospital or medical care, therapy, or prescriptions drugs) in order for a policy to be considered a

²⁵ CRA Document 9908430, June 30, 1999 – Conference for Advanced Life Underwriting ("CALU") Conference May 1999, and CRA Document 2002-0160155, April 3, 2003. The appendix to this article contains the relevant sections of each provincial and territorial insurance act or regulation defining sickness or accident insurance, and the relevant section from the Insurance Companies Act of Canada. 8

²⁶ CRA Document 9908430, June 30, 1999.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

sickness or accident insurance policy. The Insurance Companies Act of Canada, and some provinces' laws (though none of the territories') also include this definition, but only in addition to the definition of sickness or accident they share with the other provinces. In those provinces, and under federal law, a policy can satisfy either definition to be considered a sickness or accident insurance policy.

Under a third approach the CRA considers whether the policy's language shows that the purpose of the policy is to provide sickness or accident benefits:

Where the terms and conditions of a critical illness policy provide benefits only in the event of critical illness and the provision of that insurance is clearly the purpose of the contract, the policy in our view would likely be a sickness policy for purposes of the Act.²⁷

INSURANCE

As discussed above, a GSAIP must also be an insurance plan. If the employer provides insurance coverage through a plan without using insurance policies the following rules apply:

- The plan must be a plan of insurance, though there is no need for insurance policies.
- If the employer self-insures, contributions to the plan must be determined by an actuary,²⁸ and can't exceed the amount needed to provide the promised benefits.
- Periodic actuarial testing should be done to make sure that contributions to the plan remain within those actuarial limits.²⁹

An employer may satisfy the insurance requirement by acquiring a single group policy that covers all employees in the group, or by the employer or employees acquiring individual insurance policies providing the same coverage for each employee. The CRA has said, "[I]t is possible for individual policies owned by the employees to combine to form a common plan and be considered a GSAI plan...."³⁰

²⁷ CRA Document 2003-0026385, December 10, 2003.

²⁸ CRA Document 9131905, February 19, 1992.

²⁹ CRA Document 9222735, September 22, 1992.

³⁰ CRA Document 2009-0314871E5, dated March 3, 2011.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

If individual policies are used, one advantage to the employer owning the policies is that it can more easily administer the plan. If employees own their own policies, the employer may not be immediately aware of an employee making changes to a policy or cancelling coverage, unless the employees have allowed the employer access to their insurance companies' records.

PLAN

There has to be a plan; it must be in writing but it need not follow any particular format. The plan should make the plan obligations and benefits clear, and demonstrate the existence of a plan in case the CRA audits the employer.

A corporation may note the details of the plan in its corporate minutes, while an unincorporated business could create a written plan document or provide a letter to its employees documenting the plan.

EXTENT OF COVERAGE

The CRA has commented on who may benefit from a GSAIP: an employee, the employee's married or common-law spouse or a person related to the employee who lives with or is a dependent of the employee.³¹

GSAIPS NOT DEFINED AS EMPLOYEE BENEFIT PLANS

ITA subsection 248(1) excludes GSAIPs from the definition of an employee benefit plan (EBP).³² The exclusion is important because if a plan fails to qualify as a GSAIP, it could be treated as an EBP. **The**

³¹ CRA Document 2011-0406551C6, October 7, 2011.

³² ITA subsection 248(1), c.f. "employee benefit plan."

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

rules governing EBPs are complex.³³ What follows are some of the general tax consequences that could result from characterizing a GSAIP as an EBP. There are specific exceptions that are not discussed here. Generally:

- The employee is not taxed on employer contributions to the plan.³⁴
- The employee is taxed on amounts received from the plan.³⁵
- The employer may not deduct amounts it contributes to the plan.³⁶
- The employer may deduct amounts paid to employees from the plan.³⁷

TRANSFER OF POLICY AT TERMINATION OR RETIREMENT

If an employee is a member of a grouped plan or ELHT that uses individual insurance policies to provide plan benefits, the plan or trust can lapse coverage or transfer the policy to an employee if the employee leaves the employer or retires. If an employer were to continue coverage, it may not be able to deduct contributions to the GSAIP in respect of the employee's coverage after that employee had left, because it could likely no longer assert that the premiums were a reasonable business expense that the business had paid to earn income. On the other hand, if the business had contractually obligated itself to continue coverage to the employee after retirement, it may still be able to deduct contributions.

If the business retained the policy after an employee's retirement, without promising to continue benefits to the employee, claiming policy benefits could be difficult for the business. It would have to support its claim using confidential medical information that it could only obtain from the departed

³³ See generally IT-502 "Employee Benefit Plans and Employee Trusts," March 28, 1985, as amended by Special Release dated May 31, 1991.

³⁴ ITA subparagraph 6(1)(a)(ii).

³⁵ ITA paragraph 6(1)(g).

³⁶ ITA subsection 18(o).

³⁷ ITA section 32.1.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

employee. Further, any benefits that could be realized from the policy could not be distributed to remaining members of the group or to the employer – neither the employer nor the employees would be the subject of the claim. Nor could an ELHT transfer ownership of a policy to the employer after an employee had left because an employer cannot receive anything from the trust it has created. Because of these constraints, an employer or trust's more realistic options are to lapse coverage or transfer the policy to the departing employee. Transferring the policy from the plan or trust to the employee could be costly for the employee. Since an insurance policy is an asset, it will have to be appraised by an actuary, and the employee will have to pay the employer or trust for the policy, or report the policy's fair market value (FMV) as a taxable benefit.³⁸ The policy's value will be based on the employee's health at the time of transfer, the cost of replacement coverage, and other factors. We discuss transfers to employees of trust owned health insurance policies in our article, "Employee Life and Health Trusts."

From the employer's perspective, providing benefits through an ELHT, or owning the policy in a grouped plan, lets the employer turn the insurance benefit into a golden handcuff. If an employee leaves to go to another firm or to start a competing business, then, subject to any prior agreement to the contrary, the trust or employer can lapse coverage instead of transferring the policy. Except for group term life insurance, an employee has no automatic right to continue coverage upon termination unless they negotiate that right with the employer.

If an employer is not concerned about using an employee benefits package as a golden handcuff, one way to avoid the expense of transferring a policy at termination or retirement is to have the employee own the policy as part of a grouped plan. This option is not available for benefits delivered through an ELHT because the trust must own the policy. But it is available for grouped plans because either the employee or employer may own the policy. Upon leaving the employer, the employee can continue coverage by assuming responsibility for paying the insurance premiums, without having to pay anything to the employer or report a taxable benefit.

³⁸ CRA Document 9411015, July 12, 1994.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

If the employer and employee are considering such a strategy, they should be aware that transferring a pre-funded policy to an employee may result in the CRA asserting that the employee has received a taxable benefit, either when the employee leaves the grouped plan or later when the employee receives benefits from the policy.³⁹

According to CRA guidance developed in considering grouped disability income insurance plans, it's a question of fact whether a plan really ends when the employer transfers the policies it owns to the insured employees. The CRA considered two scenarios that could apply to that situation.

Under one scenario, the grouped plan would end, and the policies would be transferred to their respective employees. As discussed above, each employee would have to include in income the FMV of the policy they received. Part of each policy's FMV would be the present value of the premiums the employer prepaid for that policy.

Under the other scenario, the CRA thought that the grouped plan would remain in existence, even if the employer had purported to end it and had transferred the individual policies it owned to its employees. The employees would not have to include the present value of any prepaid premiums in income. But they would have to include in income any benefits they received from the policy under ITA paragraph 6(1)(f).⁴⁰ It's important to remember that group disability income insurance policy benefits are taxable to the employee when the employer has paid any part of the premiums for the coverage. This second scenario may not apply to other types of insurance policies that pay tax-free benefits.

In both scenarios, the CRA noted that an employer would not be able to deduct any contributions it made to fund a benefit for future years.⁴¹ The situation is the same for ELHTs. The employer may

³⁹ CRA Document 2009-0314871E5, March 3, 2011.

⁴⁰ CRA Document 9238025, February 8, 1993.

⁴¹ Ibid.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

only deduct premiums paid to provide coverage in the year for which that coverage applies.⁴² See our article, "Employee Life and Health Trusts" for more details.

The CRA's reasoning could be based on the fact that benefits from a disability income insurance policy for which the employees were paying all the premiums would be tax-free, while benefits from a plan to which the employer had paid any premiums would be taxable under ITA paragraph 6(1)(f). If the employer had paid enough premiums for the policy to pay a benefit after the employee left the plan, the CRA would likely not allow a normally taxable benefit to be tax-free just because the employee now owned the policy personally and was no longer part of the grouped plan.⁴³ The situation could be different for policies that would pay a tax-free benefit in a grouped plan.

Although the CRA's guidance deals with disability income insurance plans, the principle applies to other types of benefits. Where the employer prefunds a policy providing the benefit, and transfers the policy to the employee, or where the employee owns the policy and the employer prefunds it before the employee leaves the grouped plan, the CRA could say that the prefunding is a taxable benefit to the extent that the employee enjoys the coverage after they are no longer a member of the GSAIP.

GROUPED INSURANCE PLANS

As discussed above, an employer can create a GSAIP using individual policies:

[I]t is possible for the individual policies to combine to form a common plan and be considered a GSAI plan provided each employee within a particular class or group of employees is eligible to

⁴² ITA subsection 144.1(4).

⁴³ IT-428 – Wage Loss Replacement Plans, April 30, 1979, paragraph 21. IT-428 refers to a plan changing from an employer-paid to an employee-pay-all plan, but the reasoning applies to cases where the employee retires and assumes responsibility for maintaining their own plan.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

receive the same benefits under the plan and has the same ratio of employee and employer-paid premiums.⁴⁴

The resulting plan is called a grouped plan, owing to the fact that the insurance policies providing the plan benefits are grouped together as part of a common plan.

Just grouping policies is not enough to form a grouped plan. According to the CRA, the policies in a grouped plan "become part of the plan but do not constitute the plan itself."⁴⁵ The employer needs to create a plan, but the procedure for establishing a plan is not complicated. As discussed, the CRA has said that "describing such a plan or undertaking in the corporate minutes would be adequate, [and] that no formal agreement [is] necessary."⁴⁶

Employees in the plan must receive similar benefits under the plan. The CRA has commented on this requirement as follows:

Where the plan consists of individual policies, the policies should provide similar benefits to each employee and each employer must have the same ratio of employee and employer-paid premiums; otherwise it may not be reasonable to consider that the benefits provided under each policy are under the umbrella of a single plan.⁴⁷

It's possible for a grouped plan to use policies that employees already own, instead of having the employer buy individual policies. However, even assuming that all employees who would be part of the group owned policies that provided the same coverage that the plan offered, it's unlikely that the policies would provide the same benefits. The danger in using existing policies in a new grouped plan is that if a particular policy provides a benefit to an employee that other employees do not share, that employee will be deemed to be in receipt of a taxable employee benefit.⁴⁸ In the worst case, the plan

⁴⁴ CRA Document 2007-0227881E5, February 21, 2008.

⁴⁵ CRA Document 2009-0314871E5, March 3, 2011.

⁴⁶ CRA Document 9126876, December 11, 1991.

⁴⁷ CRA Document 2011-0422621E5, August 24, 2012.

⁴⁸ CRA Document 9302035, April 21, 1993.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

could fail to qualify as a GSAIP. The better procedure is to buy policies when the plan is established or when a new employee joins the plan.

Grouped plans may appeal to small employers who do not have enough participants to implement a group plan, or for whom the cost and effort in administering an ELHT would be unreasonable. For employers with more employees, group plans and ELHTs may be a better alternative, because they provide for an insurance company or trustee to administer the plan.

PRODUCTS ALLOWED IN A GSAIP

DISABILITY INCOME INSURANCE PLANS

GENERAL

DII plans pay benefits when the insured person is unable to work because of an illness or accident, as defined in the policy or plan. If the employer contributes anything towards the cost of the plan for any member of the group, all benefits that any employee receives are taxed to the recipient employee under ITA paragraph 6(1)(f).⁴⁹ Any amounts that an employee has contributed to the plan reduce the amount that an employee must include in income if they have to report the receipt of taxable benefits.

Under current law, employer contributions to a DII plan are deductible to the employer as a reasonable business expense under ITA paragraph 18(1)(a), and are not taxable to the employee under ITA subparagraph 6(1)(a)(i).

If all employees in the group are legally obligated to pay the entire cost of the benefit, no part of the benefit that any employee receives is taxable income.⁵⁰

According to CRA guidance, DII qualifies as a GSAIP under IT-428:

⁴⁹ CRA Document 2006-0172261E5, June 27, 2006.

⁵⁰ CRA Document 2010-0371201E5, August 17, 2010.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

A "group sickness or accident insurance plan" is not defined in the Act but paragraph 14 of Interpretation Bulletin IT-428, "Wage Loss Replacement Plans" indicates that this exception would apply to any of the three types of plans described in paragraph 6(1)(f) of the Act (i.e. a sickness or accident insurance plan; a disability insurance plan; or an income maintenance insurance plan and collectively referred to as "wage loss replacement plans") as long as the particular plan is a group plan. A "group" must consist of more than one employee. Where the plan is a group sickness or accident insurance plan, such as a group long-term disability plan, any premium contributions made by an employer to an insurer for its employees would not be taxable under paragraph 6(1)(a) of the Act.⁵¹

If disability insurance is offered, employer contributions to pay for the insurance would be tax deductible to the employer (provided that they were reasonable business expenses under ITA paragraph 18(1)(a)), and not included in employee income (under subparagraph 6(1)(a)(i), except for employees living in Quebec on their provincial return). Any payment of benefits would be treated as taxable income to the employee under ITA paragraph 6(1)(f). The amount the employee includes in income "is reduced by the total amount of any contributions made by the employee to the particular plan before the end of the year and to the extent that such employee contributions have not already reduced the amount of benefits previously received by the employee."⁵²

If the employee is legally obligated to pay the entire premium for a wage loss replacement plan, none of the benefits will be taxable to the employee.⁵³ The important part is "legally obligated". The CRA has made the following comments on that requirement:⁵⁴

It is not a question of who paid the premiums but rather whether the plan itself places upon the employees the legal obligation to pay 100% of the premiums. Such a determination can only be

⁵¹ CRA Document 2008-0278501E5, October 17, 2008.

⁵² CRA Document 2010-0371201E5, August 17, 2010.

⁵³ CRA Documents 9309635 and 2010-0371201E5, June 28, 1993 and August 17, 2010.

⁵⁴ CRA Documents 9309635, June 28, 1993.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

made by looking at the actual wording of a particular plan. Of prime consideration will be whether the plan, either as a term of the policy with the carrier, the employment contract, or some other document, places upon the employees the legal obligation to pay 100 per cent of the premiums (although the employer may still be responsible for remitting the premiums on their behalf). If such an obligation exists and the employer remits the premiums to the plan carrier and accounts for them in the manner of salary and wages, the plan will be considered an employee pay-all plan provided such an arrangement was in place at the time the payment was made.

Because of the way the CRA defines the term “legally obligated”, an employee who pays the premiums for a disability insurance benefit may still be taxed on receipt of that benefit if they were not “legally obligated” to pay those premiums. However, the CRA does not insist on the employee directly paying the premiums in order to comply with the “legally obligated” requirement. An employee will still be treated as having paid the premiums if the employer pays the premiums but collects those premiums from the employee under an agreement between the two.⁵⁵

Further, if employees are to receive their disability income benefits tax-free under an employee-pay-all plan, all employees in the group must pay all of their own premiums. If only one employee in the group receives employer contributions to even part of their disability insurance plan, the entire plan will be tainted, and all employees will have to include their disability income benefits in income. Because of the severe tax consequences that can result from tainting an employee-pay-all plan, it's important that such plans be kept strictly separate from plans where employers make any contributions.

The CRA has said that if a long-term disability plan is funded entirely from employee contributions, but the contributions do not go to pay premiums under a third party insurance contract, the plan may not qualify as a plan in the nature of insurance.⁵⁶

⁵⁵ CRA Document 2010-0371201E5, August 17, 2010, IT-428, “Wage loss replacement plans”, April 30, 1979, paragraph 14.

⁵⁶ CRA Document 2010-0374891E5, March 14, 2011.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

ITA paragraph 6(1)(e.1) taxes employer contributions to GSAIPs where the plan benefits are not taxed to the employee. This paragraph does not apply to GSAIPs where the benefits paid from the plan are treated as taxable income to the insured employee, such as disability income insurance plans where the employer makes any contribution to the plan. As a result, employer contributions to such plans should remain tax-free to the insured employees. But having said that, most disability income insurance plans are structured so that the employees pay the premiums, and receive tax-free benefits if they make a claim.

LUMP SUM DII PAYMENTS

Lump sum payments representing arrears of DII benefits owing under GSAIPs are taxable where the employer has paid at least some of the premiums. This rule applies to cases where the lump sum is calculated with reference to the periodic payments owing, and to cases where the lump sum is paid to settle litigation between the employee and the insurance company without reference to what the employee claimed they were owed.

Before the Supreme Court of Canada's decision in *Tsiapraillis*,⁵⁷ one could have argued that the settlement of a lawsuit based on a claim for arrears of DII benefits represented an award of general damages, not the commuted value of those benefits, and was therefore not taxable. The reason for this position was that the parties may have settled the case for reasons that had nothing to do with the merits of the employee's claim. Both parties may have concluded that the risk of losing and the cost of further litigation made a settlement attractive. As a result, you could not say that the final settlement necessarily represented a payment for arrears of insurance benefits.

But the Supreme Court of Canada decided that the fact that the lump sum was negotiated after a lawsuit was commenced for taxable periodic payments meant that the amount awarded or settled on was taxable under ITA paragraph 6(1)(f).

⁵⁷ *Tsiapraillis v. R.*, [2005] 1 S.C.R. 113, 2005 D.T.C. 5119 (Eng.), 2005 D.T.C. 5126 (Fr.), [2005] 2 C.T.C. 1, 248 D.L.R. (4th) 385 (Supreme Court of Canada).

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

The Court decided that the same tax treatment did not apply to lump sum awards for future DII benefits: "The part of the settlement for future benefits is in the nature of a capital payment and is not taxable under s. 6(1)(f) of the Act."

OPTIONAL COVERAGE

Since a GSAIP can offer only sickness or accident insurance benefits, additional coverage, like a return of premium (ROP) benefit, will disqualify the plan as a GSAIP.⁵⁸ The CRA considered a case where the employer owned and was the beneficiary of disability income insurance policies on its employees under a grouped insurance plan. The purpose of the plan was to provide disability income insurance benefits if an employee could not work because of a sickness or accident. The employees would get no other benefits from the plan. The employer paid premiums for both the disability income insurance and ROP benefit, but deducted only the premiums for the disability income insurance. If there was no claim for a given employee, and the policy was no longer needed, the employer could cancel coverage for a return of premiums. From the CRA's perspective, it did not matter who got the ROP benefit – adding an ROP benefit to a disability income insurance plan disqualified the plan as a GSAIP.

CRITICAL ILLNESS INSURANCE

CII plans pay a lump sum benefit when the insured person is diagnosed with a covered critical illness and the required survival period is met. Because a CII policy pays a benefit if the insured person suffers an illness or injury, it qualifies as a GSAIP. We discuss CII policies in our article, "Private Health Services Plans."

Employer contributions to a CII plan within a GSAIP are tax deductible to the employer if they are reasonable business expenses. Under ITA paragraph 6(1)(e.1), employer contributions that pay for CII plans offered as part of a GSAIP are taxable to the employee.

⁵⁸ CRA Document 2012-0435761C6, May 2012.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

Although CII policies generally pay lump sum benefits, and are considered tax-free, the CRA was asked whether periodic payments from a CII policy would be taxed to the employee under ITA paragraph 6(1)(f). However, the CRA declined to address the question.⁵⁹ The CRA has said that a lump sum payment from a group CII policy will not be taxable.⁶⁰ But the tax treatment would be different if the lump sum CII benefit was paid to replace a stream of taxable income. On this question the CRA said:

It remains a question of fact and law as to whether the lump-sum benefit under such a policy [a CII policy] would be taxable under paragraph 6(1)(f) of the Act. For example, if a lump-sum benefit was considered to represent a payment in respect of the employee foregoing the right to receive periodic payments that were otherwise payable under the policy, or under another accident and sickness plan, the lump-sum payment could, in our view, be taxable under paragraph 6(1)(f) of the Act.⁶¹

The CRA's argument in favour of taxation gains some strength from the fact that part of the needs analysis an insured person undergoes includes an estimate for lost income following a critical illness. But lost income is only one need that a CII benefit addresses. A CII benefit can also supplement a spouse's income if the employee's spouse took time off to care for the employee. It can cover the costs associated with recovering from a critical illness (like the cost for therapies and prescription drugs). Money from a CII policy can help replace contributions to an employee's savings plans that could not be made because the employee was off work and not earning an income. The benefit could also cover expenses for extras like a vacation.

Considering the uses to which a CII benefit can be put, aside from replacing lost income, the CRA could take the same approach to CII taxation that it has taken with LTCI taxation. Although LTCI

⁵⁹ CRA Document 9908430, June 30, 1999.

⁶⁰ CRA Documents 2004-0105491E5 and 2003-0034505, January 14, 2005, and December 9, 2003.

⁶¹ CRA Document 9711505, June 2, 1997.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

policies pay periodic benefits, the CRA says that those benefits are tax-free, and are not taxable under ITA paragraph 6(1)(f).⁶² The agency says that LTCI benefits are not paid to replace income, but to provide for the insured person's care. If this reasoning were applied to a CII policy, one could say that the benefits were paid not to replace lost income, but to help the insured person recover from a critical illness.

Like LTCI, many individual CII policies allow the policyowner to add extra coverage:

- Return of premium (ROP) on expiry or cancelation of coverage, and/or at death
- Disability waiver of premiums.

Some life insurance companies also offer an option to convert a CII policy to LTCI, but restrictions on how the feature is offered vary throughout the industry. A GSAIP should be allowed to provide CII coverage to employees, as long as it offers no optional coverage. In particular, the CRA has said that a CII policy with ROP in an HWT will not qualify as a GSAIP.⁶³ The reasoning is that the tax benefits associated with a GSAIP under ITA paragraph 6(1)(a) must apply to coverage for sickness or accident only. A return of premium is neither. The CRA's reasoning could also apply to optional benefits like LTCI conversion and disability waiver of premiums.

The CRA's reasoning may also apply to an ELHT. Under ITA subsection 144.1(2), an ELHT's only purpose is to provide "designated employee benefits," to specific trust beneficiaries. An ROP benefit is not included in the definition of a "designated employee benefit" under ITA subsection 144.1(1).

LONG-TERM CARE INSURANCE

Long-term care insurance (LTCI) pays a benefit if the insured person becomes unable to perform at least two of six activities of daily living without requiring substantial physical or stand-by assistance. The six activities of daily living are bathing, dressing, feeding, toileting, transferring and continence.

⁶² CRA Document 2004-0090791C6, October 8, 2004.

⁶³ CRA Document 2003-0034505, December 9, 2003.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

LTCI policies also pay benefits if a person becomes physically dependent because of deteriorated mental ability. Alzheimer's disease is one cause for a person to suffer from deteriorated mental ability, but there are others.

As discussed above, although LTCI policies pay periodic benefits, the CRA does not treat those benefits as taxable under ITA paragraph 6(1)(f). ITA paragraph 6(1)(f) speaks of amounts received by the taxpayer that were payable in respect of a loss of income. The CRA regards LTCI benefits as paid to provide care for the insured person, not to replace lost income.⁶⁴

An employer can offer LTCI policies as part of a PHSP or a GSAIP, depending on the terms of the policy. We discuss this issue in our article, "The Medical Expense Tax Credit." The following paragraphs discuss this issue in general terms.

LTCI policies that the CRA has confirmed reimburse the policy owner for specific hospital and medical expenses can be included in a PHSP. These policies are called reimbursement LTCI policies. Before an LTCI policy can be included in a PHSP the CRA must rule on whether it qualifies as a PHSP.

LTCI policies that pay a set amount regardless of the insured person's actual expenses are called income-style LTCI policies. Because they do not pay benefits to reimburse the insured person for particular hospital or medical expenses, they do not qualify as reimbursement LTCI policies. They do however qualify as sickness or accident insurance policies because they pay benefits when an insured person suffers a sickness or accident, as described in the policy.

One drawback to a reimbursement LTCI policy is that the expenses paid for long-term care cannot be used as medical expenses when claiming the medical expense tax credit to the extent the insured person has been reimbursed for them. This is not an issue with income-style LTCI policies because the policy benefit payments are not paid to reimburse the insured person for any particular expense. As a result, it's possible to pay LTC expenses with the LTCI benefit payments and still count those expenses towards a claim for the medical expense tax credit

⁶⁴ CRA Document 2004-0090791C6, October 8, 2004.



Life's brighter under the sun

ACCIDENTAL DEATH OR DISMEMBERMENT INSURANCE

Accidental death or dismemberment (ADD) policies pay a benefit when the insured person dies from an accident or suffers a serious injury. Although the policy name refers to dismemberment, an ADD policy can also cover an insured person for loss of hearing, speech or sight. The CRA treats group ADD policies as GSAIPs.⁶⁵ An employer may deduct contributions to a group ADD policy if the contributions are reasonable business expenses.⁶⁶ Employer contributions to pay for an employee's ADD coverage are included in the employee's income under ITA paragraph 6(1)(e.1).

The CRA has said that an ADD plan is not the same as a group term life insurance plan (GTLIP).⁶⁷ Income Tax Regulation (ITR) subsection 2700(2) reinforces this distinction by saying that a premium paid for insurance on an individual's life does not include an amount paid for accidental death insurance. Before ITA paragraph 6(1)(e.1) became law, one consequence of this distinction was that employer-paid ADD premiums were not a taxable benefit, while GTLIP premiums were taxable (under ITA subsection 6(4)).

The CRA has also said that lump sum payments made to the employee or their beneficiary under the non-death provisions of an ADD policy will be tax-free to the recipient.⁶⁸ Periodic payments made to the employee under an ADD policy may be taxable under ITA paragraph 6(1)(f) if they are paid in respect of the loss of part or all of the employee's income.⁶⁹

The tax treatment applicable to an ADD policy's lump sum death benefit is not clear. ITA subsection 248(1) defines a "death benefit" in part as "the total of all amounts received by a taxpayer in a taxation year on or after the death of an employee in recognition of the employee's service in an office or employment". According to the CRA, whether an ADD policy benefit is paid "in recognition of the employee's service in an office or employment" is a question of fact. If the amount is not paid in

⁶⁵ CRA Document 2001-0090165, June 25, 2003.

⁶⁶ CRA Document AC58980, January 11, 1990.

⁶⁷ CRA Document 2001-0090165, June 25, 2003.

⁶⁸ Ibid, ITA paragraph 6(1)(f).

⁶⁹ CRA Document 2001-0090165, June 25, 2003.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

recognition of the employee's service it will not be taxable. Otherwise, some of the benefit will be taxable under ITA subparagraph 56(1)(a)(iii).⁷⁰

ITA subsection 248(1) provides for a reduction in the taxable amount of an ADD benefit by up to \$10,000. If the death benefit equals or exceeds \$10,000, the surviving spouse or common-law partner will be able to deduct the entire \$10,000 from their taxable amount. If the death benefit to the surviving spouse or common-law partner is less than \$10,000, the entire death benefit will be tax-free. If there are other non-spouse beneficiaries (and if the death benefit to the surviving spouse or common-law partner is less than \$10,000), those beneficiaries may split the remaining part of the \$10,000 among themselves in proportion to the death benefit amounts they received.

GROUP TERM LIFE INSURANCE

Although a GTLIP is not a health benefit, it is included as an employee benefit under ITA subparagraph 6(1)(a)(i), and so discussed here. Unlike GSAIPs, where an employer may implement a plan of insurance without necessarily using insurance policies, an employer must own a group term life insurance policy in order to have a GTLIP. The CRA has said that a "group term life insurance policy must be a 'policy of insurance' under which benefits are paid by an insurer and therefore cannot be self-funded. Accordingly, a life insurance plan that is self-funded could be considered an employee benefit plan."⁷¹

Premiums paid for group term life insurance are not the same as those paid for accidental death insurance.⁷² ITA subsection 248(1) defines a group term life insurance policy as a group life insurance policy under which the only amounts payable by the insurer are:

- Amounts payable on the death or disability of individuals whose lives are insured in respect of, in the course of or because of, their office or employment or former office or employment, or

⁷⁰ CRA Document 2001-0090165, June 25, 2003.

⁷¹ CRA Document 2005-0129961E5, January 4, 2006.

⁷² Regulation 2700(2).

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

- Policy dividends or experience rating refunds⁷³

Group term life insurance does not include policies that provide coverage for only one employee or for anyone other than an employee or former employee (for example, an employee's spouse or dependent).⁷⁴

Although ITA subparagraph 6(1)(a)(i) excludes employer contributions paid for group term life insurance from employee income, ITA subsection 6(4) requires an employee to include in income an amount prescribed by regulation if the employee is covered under a group term life insurance contract. The amount an employee must include in income is determined under Income Tax Regulations 2700 to 2704:

- The employee's "term insurance benefit" for the calendar year in which the taxation year ends,
- The employee's "prepaid insurance benefit" for that calendar year, and
- All sales and excise taxes payable on premiums paid under the policy for the calendar year except:
 - Taxes that the employee paid, directly or by reimbursement, and
 - Taxes in respect of premiums for term insurance that, if the employee were to die, would be paid other than to or for the benefit of the employee or to any person the employee wanted to benefit.

An employee's "term insurance benefit" is determined using either one of two methods defined in the regulations. The first method requires the employee to include in income the premiums the employer paid minus whatever the employee paid. The parties may use this method if the insurance rates do not depend on the employee's age or sex, and where the amounts paid relate only to the insurance in force during the year. The second method requires the employer or insurance company to calculate the benefit by multiplying the amount of insurance coverage in force on the employee's life by the average daily cost of that insurance (or by a reasonable alternative to the average daily cost) minus any amounts the employee has paid.

⁷³ ITA subsection 248(1), c.f. "group term life insurance policy". See also CRA Document 2002-0165695, November 27, 2002.

⁷⁴ CRA Documents 2008-0278501E5 and 2002-0165695, October 17, 2008 and November 27, 2002.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

An employer may deduct GTLIP premiums under ITA paragraph 18(1)(a) as reasonable business expenses, and under ITA paragraph 20(1)(s) for ELHT contributions that pay for GTLIP premiums.⁷⁵ Prepaid premiums are deductible under ITA clause 18(9)(a)(iii)(B) and under ITA subparagraph 18(9)(a)(iv) for ELHTs.

ITA SUBSECTION 6(1)(E.1)

In the March 2012 federal budget, the government introduced a change to the ITA affecting the tax treatment of employer contributions to GSAIPs. Previously, employer contributions to GSAIPs were tax-free to the employee (except in Quebec, where they were taxed to the employee on the Quebec provincial tax return only). But as a result of the changes made in the 2012 budget, employer contributions to a GSAIP are tax-free to the employee only if they provide benefits that are taxable under ITA paragraph 6(1)(f).

As discussed above, ITA paragraph 6(1)(f) taxes DII benefits that are paid to an employee on a periodic basis from a plan to which the employer has contributed. When all employees in the group pay the full (non-deductible) cost for their DII benefits, any insurance benefits they receive from their plan will be tax-free.

The changes affect the tax treatment for CII and income-style LTCI plans offered in a GSAIP. Because the benefits paid from those plans are tax-free to the employee, the employee has to include in income the employer contributions to the GSAIP that pays for those benefits.

ITA paragraph 6(1)(e.1) also taxes employer contributions for group ADD benefits. As noted earlier in this article, a lump sum ADD benefit paid to an employee is tax-free, while the death benefit paid to an employee's beneficiary may be partly taxable. Since it's not possible to tell in advance whether a group ADD plan will pay a death or dismemberment benefit, the tax treatment for the premiums is not clear.

⁷⁵ See also ITA subsection 144.1(7) and paragraph 18(1)(o.3).

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

The changes in ITA paragraph 6(1)(e.1) do not affect the tax treatment for employer contributions to reimbursement LTCI plans that the CRA has ruled are PHSPs. The rule change affects only GSAIPs. Employer contributions to a PHSP are not taxed to employees (except employees in Quebec, and then only on the employee's provincial tax return), and the benefits from those plans are still tax-free. See our article, "Private Health Services Plans" for more details. Nor does the change affect the tax treatment for GTLIPs. Finally, employer contributions to a GSAIP are still deductible to the employer as long as they are reasonable business expenses.

POTENTIAL IMPACT OF THE ADDITION OF ITA PARAGRAPH 6(1)(E.1) ON EMPLOYER BENEFIT PLANNING DECISIONS

As a result of the changes to ITA subsection 6(1), employees will have to pay for some of their benefits by having to include the employer's contribution for that benefit in income. The cost of the benefit to the employee will be the extra tax they will have to pay as a result. If employees did not value a particular benefit, but accepted it because it was free to them, then having to pay for the benefit in the form of higher taxes may persuade them that the benefit is not worth having. If that attitude prevails, then some GSAIP benefits may disappear from many employers' benefits offerings.

On the other hand, if employees value a particular GSAIP benefit, then having to pay for it in the form of higher taxes may not be enough to persuade them to reject the benefit. The reason is that the cost of the benefit provided by an employer will remain less than the cost of the benefit if the employee decides to buy coverage on their own.

For example, if an employee is in a 30% federal/provincial tax bracket, and receives a \$100 non-taxable benefit, the benefit costs nothing to the employee. If the benefit becomes taxable, it costs the employee \$30 ($\$100 \times 30\%$). But if the employee has to pay for the benefit using their own after-tax money, they will need to earn \$143 ($\$100 / (1 - 30\%)$). While receiving a non-taxable benefit is best of all, a taxable benefit is still better than having to pay for the benefit on your own.

The changes to GSAIP tax treatment could also encourage more employers to offer cafeteria-style

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

benefits. Under a cafeteria plan, an employer gives its employees a limited amount of benefit credits to spend as they wish on a menu of benefits. Within limits, employees may tailor their coverage to suit their needs. Employers also limit their cost of providing benefits. Rather than trying to anticipate an employee's preference for taxable versus non-taxable benefits, an employer could simply let employees decide for themselves. An added factor for employees would be which benefits were taxable.

Different considerations may apply to benefit plans created for some small businesses. A small business may have created a benefits plan to provide non-taxable benefits primarily for its shareholder/employees. But to make sure that those benefits were tax-free, the business may have been forced to design its benefit plan in ways it may not have wanted to:

- Rank-and-file employees may have been included in the plan only to protect the plan from the CRA's assertion that benefits were being provided exclusively for owners, and were therefore taxable shareholder benefits, not because the owners wanted to provide benefits for the rank-and-file.
- The plan would not have been able to offer optional coverage, such as return of premium benefits. All plan participants would have received the same or similar benefits, regardless of rank or contribution to the success of the business.

Shareholder/employees may have accepted these limitations and requirements as the price they had to pay for tax-free benefits. But now that plan contributions are taxable to them, they may reason that it makes more sense to eliminate the benefits plan, increase the shareholder/employees' salaries, and allow them to buy their own policies, customized to meet their needs and preferences. From the corporation's perspective, the increased salaries would still be deductible, provided they were reasonable business expenses.

There are at least two downsides to this strategy, though.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

One is that employers that do not offer competitive benefit plans may have trouble retaining and attracting the best people. Prospective and existing employees may care more about whether a benefit is offered, and its generosity, than whether it's taxable.

The second is that the CRA may conclude that the new plan is really a shareholder benefit, not an employee benefit, particularly if the corporation has eliminated benefits for all but the corporation's owners, and if those owners have enhanced their benefits beyond what they were receiving before. The CRA generally assumes that any benefit an owner receives is a shareholder benefit – received because the shareholder owns the company, not because they work for it. Shareholder benefits are treated as income to the shareholder, but the corporation may not deduct the payment of the benefit. We discuss shareholder benefits in our article, "Private Health Services Plans".

CONCLUSION

Employers can provide sickness and accident insurance benefits for their employees through contributions to a GSAIP. Although the term GSAIP is not defined in the ITA, CRA guidance says that it must be an insurance plan created to cover a group of employees against sickness or accident. Covered sicknesses or accidents need not be work related, nor does an employee need to incur any expenses associated with their sickness or accident to make a claim.

Employers may deduct their contributions to their GSAIP, provided they are reasonable business expenses. Contributions will be taxable income for employees unless the contributions pay for taxable disability income insurance benefits paid on a periodic basis.

Employers may offer GSAIPs through different vehicles: group or grouped plans, and ELHTs. If coverage is offered through a grouped plan, the employee may acquire or retain the policy used to provide coverage when they leave the employer or retire, though tax consequences may arise from the transfer.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

Employers may offer different types of coverage under a GSAIP: critical illness insurance, long-term care insurance and accidental death and dismemberment insurance, in addition to disability insurance.

Author: Stuart L. Dollar, M.A., LL.B., CFP®, CLU®, ChFC®, TEP, Director Insurance Tax Solutions. First published February 2013. Last revised September 2021.

This article is intended to provide general information only. Sun Life Assurance Company of Canada does not provide legal, accounting or taxation advice to advisors or clients. Before a client acts on any of the information contained in this article, or before you recommend any course of action, make sure that the client seeks advice from a qualified professional, including a thorough examination of their specific legal, accounting and tax situation. Any examples or illustrations used in this article have been included only to help clarify the information presented in this article, and should not be relied on by you or the client in any transaction.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

APPENDIX A

DEFINITIONS OF SICKNESS AND ACCIDENT INSURANCE UNDER FEDERAL AND PROVINCIAL INSURANCE LAWS

BRITISH COLUMBIA

Insurance Regulation [Revised Regulation] B.C. Reg. 403/2012, paragraph 1(1)

1(2). In the Act [the Insurance Act, S.B.C. 2012, c. 37] and this regulation:

“accident and sickness insurance” means insurance

- (a) against loss resulting from bodily injury to, or the death of, a person caused by an accident,
- (b) under which an insurer undertakes to pay a sum or sums of insurance money in the event of bodily injury to, or the death of, a person caused by an accident,
- (c) against loss resulting from the sickness or disability of a person not caused by an accident, but does not include insurance for losses resulting from the death of a person caused by sickness,
- (d) under which an insurer undertakes to pay a sum or sums of insurance money in the event of the sickness or disability of a person not caused by an accident, or
- (e) under which an insurer undertakes to pay a sum of insurance money in respect of the health care, including dental care and preventative care, of a person;

ALBERTA

Classes of Insurance Regulation, Alta Reg 144/2011, paragraph 1(1)(a)

1(1). In this Regulation:

“accident and sickness insurance” means insurance

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

- (a) against loss resulting from bodily injury to, or the death of, a person caused by an accident,
- (b) under which an insurer undertakes to pay a sum or sums of insurance money in the event of bodily injury to, or the death of, a person caused by an accident,
- (c) against loss resulting from the sickness or disability of a person not caused by an accident, but does not include insurance for losses resulting from the death of a person caused by sickness,
- (d) under which an insurer undertakes to pay a sum or sums of insurance money in the event of the sickness or disability of a person not caused by an accident, or
- (e) under which an insurer undertakes to pay a sum of insurance money in respect of the health care, including dental care and preventative care, of a person;

SASKATCHEWAN

Saskatchewan Insurance Act, RSS 1978, chapter S-26, subsections 2(1)(a) and (fff)

2(1). In this Act, except where inconsistent with the interpretation sections of any Part:

- (a) "accident insurance" means insurance by which the insurer undertakes, otherwise than incidentally to some other class of insurance defined by or under this Act, to pay insurance money in the event of accident to the person or persons insured, but does not include insurance by which the insurer undertakes to pay insurance money both in the event of death by accident and in the event of death from any other cause;
- (fff) "sickness insurance" means insurance by which the insurer undertakes to pay insurance money in the event of sickness of the person or persons insured, but does not include disability insurance;

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

MANITOBA

Classes of Insurance Regulation, Man Reg 221/2014, Schedule, section 1

The class of accident and sickness insurance is insurance under which the insurer undertakes

- (a) to indemnify a person against loss, or to pay insurance money or another thing of value in respect of loss, resulting from bodily injury to, or the death of, a person caused by an accident;
- (b) to pay a specified amount of insurance money in the event of bodily injury to, or the death of, a person caused by an accident;
- (c) to indemnify a person against loss, or to pay insurance money or another thing of value in respect of loss, resulting from the sickness or disability of a person not caused by an accident, other than loss resulting from the death of the person as a consequence of sickness;
- (d) to pay a specified amount of insurance money in the event of the sickness or disability of a person not caused by an accident; or
- (e) to pay insurance money in respect of the health care — including dental care and preventative care — of a person.

ONTARIO

Classes of Insurance and Definitions for Purposes of the Insurance Act, RSO 1990, chapter I-8, Schedule 1, by order of the Superintendent of Financial Services

Accident and sickness insurance means insurance

- (a) against loss resulting from bodily injury to, or the death of, a person caused by an accident;
- (b) under which an insurer undertakes to pay a certain sum or sums of insurance money in the event of bodily injury to, or the death of, a person caused by an accident;

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

(c) against loss resulting from the sickness or disability of a person excluding loss resulting from an accident or death;

(d) under which an insurer undertakes to pay a certain sum or sums of insurance money in the event of the sickness or disability of a person not caused by an accident; or

(e) under which an insurer undertakes to pay insurance money in respect of the health care, including the dental care and the preventive care, of a person.

QUEBEC

Regulation under the Act Respecting Insurance, RRQ, chapter A-32, regulation 1, section 14

14. Insurance in the "accident and sickness insurance" class is insurance whereby the insurer offers one or more of the following protections:

- (1) payment of an indemnity in the event of bodily injury, including death, resulting from an accident sustained by an insured;
- (2) payment of an indemnity in the event of sickness or disability of an insured;
- (3) reimbursement for expenses incurred as a result of the sickness of or an accident sustained by an insured;
- (4) reimbursement for expenses incurred for the health care of an insured.

NEW BRUNSWICK

Insurance Act, RSNB 1973, chapter I-12, section 1

1. In this Act, except where inconsistent with the interpretation sections of any Part, "accident insurance" means insurance by which the insurer undertakes, otherwise than incidentally to some other class of insurance defined by or under this Act, to pay 35

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

insurance money in the event of accident to the person or persons insured, but does not include insurance by which the insurer undertakes to pay insurance money both in the event of death by accident and in the event of death from any other cause;

“sickness insurance” means insurance by which the insurer undertakes to pay insurance money in the event of sickness of the person or persons insured, but does not include disability insurance;⁷⁶

NOVA SCOTIA

Insurance Act, RSNS 1989, chapter 231, paragraphs 3(1)(a) and (s)

3(1). In this Act,

(a) “accident insurance” means insurance by which the insurer undertakes, otherwise than incidentally to some other class of insurance defined by or under this Act, to pay insurance money in the event of accident to the person or persons insured, but does not include insurance by which the insurer undertakes to pay insurance money both in the event of death by accident and in the event of death from any other cause;

(s) “sickness insurance” means insurance by which the insurer undertakes to pay insurance money in the event of sickness of the person or persons insured, but does not include disability insurance;⁷⁷

⁷⁶ Disability insurance under the New Brunswick Act has a different meaning from the ordinary understanding of “disability insurance”. It “means insurance undertaken by an insurer as part of a contract of life insurance whereby the insurer undertakes to pay insurance money or to provide other benefits in the event that the person whose life is insured becomes disabled as a result of bodily injury or disease”.

⁷⁷ Disability insurance under the Nova Scotia Act has a different meaning from the ordinary understanding of “disability insurance”. It “means insurance undertaken by an insurer as part of a contract of life insurance whereby the insurer undertakes to pay insurance money or to provide other benefits in the event that the person whose life is insured becomes disabled as a result of bodily injury or disease.” 36

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

PRINCE EDWARD ISLAND

Insurance Act, RSPEI 1988, chapter I-4, subsections 1(a) and (t)

1. In this Act

(a) "accident insurance" means insurance by which the insurer undertakes, otherwise than incidentally to some other class of insurance defined by or under this Act, to pay insurance money in the event of accident to the person insured, but does not include insurance by which the insurer undertakes to pay insurance money both in the event of death by accident and in the event of death from any other cause;

(t) "sickness insurance" means insurance by which the insurer undertakes to pay insurance money in the event of sickness of the person or persons insured, but does not include disability insurance;

NEWFOUNDLAND AND LABRADOR

Insurance Companies Act, RSNL 1990, c. I-10, Schedule, subsection 1(a)

1. In this Act

(a) "accident and sickness insurance" means insurance

(i) against loss resulting from bodily injury to, or the death of, a person caused by an accident,

(ii) under which an insurer undertakes to pay a certain sum or sums of insurance money in the event of bodily injury to, or the death of, a person caused by an accident,

(iii) against loss resulting from the sickness or disability of a person excluding loss resulting from an accident or death,

(iv) under which an insurer undertakes to pay a certain sum or sums of insurance money in the event of the sickness or disability of a person not caused by an accident,
or

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

(v) under which an insurer undertakes to pay insurance money in respect of the health care, including the dental care and the preventive care, of a person;

THE YUKON TERRITORY

Insurance Act, RSY 2002, chapter 119, section 1

1. In this Act,

“accident insurance” means insurance by which the insurer undertakes, otherwise than incidentally to some other class of insurance defined by or under this Act, to pay insurance money in the event of accident to the person or persons insured, but does not include insurance by which the insurer undertakes to pay insurance money both in the event of death by accident and in the event of death from any other cause;

“sickness insurance” means insurance by which the insurer undertakes to pay insurance money in the event of sickness of the person or persons insured, but does not include disability insurance,⁷⁸

THE NORTHWEST TERRITORIES

Insurance Act, RSNWT 1988, chapter 1-4, subsection 1(1)

1(1). In this Act, except where inconsistent with the interpretation sections of any Part,

“accident insurance” means insurance by which the insurer undertakes, otherwise than incidentally to some other class of insurance defined by or under this Act, to pay insurance money in the event of accident to the person or persons insured, but does

⁷⁸ Disability insurance under the Yukon Act has a different meaning from the ordinary understanding of “disability insurance.” It “means insurance undertaken by an insurer as part of a contract of life insurance whereby the insurer undertakes to pay insurance money or to provide other benefits if the person whose life is insured becomes disabled as a result of bodily injury or disease”.

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

not include insurance by which the insurer undertakes to pay insurance money both in the event of death by accident and in the event of death from any other cause;

“sickness insurance” means insurance by which the insurer undertakes to pay insurance money in the event of sickness of the person or persons insured, but does not include disability insurance;⁷⁹

NUNAVUT

Insurance Act, RSNWT (Nu) 1988, chapter I-4, subsection 1(1)

1(1). In this Act, except where inconsistent with the interpretation sections of any Part,

“accident insurance” means insurance by which the insurer undertakes, otherwise than incidentally to some other class of insurance defined by or under this Act, to pay insurance money in the event of accident to the person or persons insured, but does not include insurance by which the insurer undertakes to pay insurance money both in the event of death by accident and in the event of death from any other cause;

“sickness insurance” means insurance by which the insurer undertakes to pay insurance money in the event of sickness of the person or persons insured, but does not include disability insurance;

⁷⁹ Disability insurance under the Northwest Territories Act has a different meaning from the ordinary understanding of “disability insurance”. It “means insurance undertaken by an insurer as part of a contract of life insurance by which the insurer undertakes to pay insurance money or to provide other benefits in the event that the person whose life is insured becomes disabled as a result of bodily injury or disease”. 39

CANADIAN HEALTH INSURANCE TAX GUIDE

Group Sickness or Accident Insurance Plans
September 2021



Life's brighter under the sun

CANADA

Insurance Companies Act of Canada, SC 1991, chapter 47, Schedule (section 12), Classes of Insurance

“accident and sickness insurance” means insurance

- (a) against loss resulting from bodily injury to, or the death of, a person caused by an accident;
- (b) under which an insurer undertakes to pay a sum or sums of money in the event of bodily injury to, or the death of, a person caused by an accident;
- (c) against loss resulting from the sickness or disability of a person not caused by an accident, but excludes loss resulting from the death of the person as a consequence of sickness;
- (d) under which an insurer undertakes to pay a sum or sums of money in the event of the sickness or disability of a person not caused by an accident; or
- (e) under which an insurer undertakes to pay a sum of money in respect of the health care — including dental care and preventative care — of a person.