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DOCNUM 9433745
REPLACES
TYPEKEY R
AUTHORDV LEGS
AUTHOR AHUMEN
DESCKEY 5
RATEKEY 1
REFDATE 950505
ETADYEAR
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ACCESSLV LEGS99
SUBJECT HEALTH AND WELFARE TRUST-GENERAL
COMMENTS
SECTION 248
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PRINCIPAL ISSUES:
health and welfare trust -what is required

POSITION TAKEN:
expanding on general comments in it-85r2

REASONS FOR POSITION TAKEN:
not submitted as a ruling request

A. Humenuk
XXXXXXXXXX 943374

Attention: XXXXXXXXXX

May 5, 1995

Dear Sir:

Re: Health and Welfare Trusts

Your letter of November 30, 1994 to John Cunningham of the North Toronto Tax Service office was referred to us for reply. We apologize for the delay in responding.

As discussed with you on April 12, 1995 (XXXXXXXXXX/Humenuk), the Department will only confirm the income tax implications resulting from proposed transactions by way of an advance income tax ruling as described in Information Circular 70-6R2 "Advance Income Tax Rulings" dated September 28, 1990 and Special Release thereto dated September 30, 1992. While we have reviewed the sample documentation submitted with your request, no assurance is given that a particular trust which is set up with such documentation will qualify as a health and welfare trust as described in Interpretation Bulletin IT-85R2 "Health and Welfare Trusts". Nevertheless, we are prepared to offer the following general comments which may be of assistance to you.

The term, health and welfare trust, is not defined in the Income Tax Act but is used in IT-85R2 to describe a trust which is used to administer certain employer-provided benefits described in paragraph 1 of the bulletin.

Accordingly, in order to determine whether a particular trust qualifies as a health and welfare trust, reference must be made to the plan

documentation which outlines an employee's rights under the plan as well as to the trust agreement or other relevant documentation. Plan documentation can take the form of a booklet or manual which is made available to employees covered by the plan. In our conversation of April 12th, you indicated that the schedules relating to extended health care and dental benefits which were attached to the sample trust documentation would be distributed to the employees covered by the plan in any plan administered by you.

It should be noted that the tax consequences described in IT-85R2 are only applicable where the benefits under the plan are restricted to the benefits described in paragraph 1 of that bulletin and are provided solely to employees and their families. Where plan benefits are limited to extended health care and dental benefits, the trust which administers the plan will qualify as a health and welfare trust as long as the plan qualifies as a private health services plan as defined in subsection 248(1) of the Act.

The Department's position with respect to private health services plans is outlined in Interpretation Bulletin IT-339R2 "Meaning of "Private Health Services Plan"". In determining whether a particular plan qualifies as a private health services plan, the Department looks to the type of expenses covered by the plan and whether the plan is a plan of insurance. Thus in order to be considered a private health services plan, expenses covered by the plan must be restricted to expenses which would normally otherwise have qualified as medical expenses as defined in subsection 118.2(2) of the Act. A description of the items which qualify as medical expenses under subsection 118.2(2) of the Act is found in Interpretation Bulletin IT-519R "Medical Expense and Disability Tax Credit". While it is a question of fact as to whether any particular expense qualifies as a medical expense as defined in subsection 118.2(2) of the Act, a list of eligible expenses should be described with sufficient precision of terms to ensure that coverage is not inadvertently extended to non-qualifying expenditures.

It is not clear from the schedule relating to extended health care submitted with your request that the coverage would necessarily be

restricted to amounts which qualify as medical expenses for tax purposes. Depending on how the plan is actually administered, expenses such as the cost of orthopaedic shoes, services of a masseur or durable medical equipment may not qualify as medical expenses for income tax purposes.

As indicated in the Appendix at the end of IT-519R, the cost of orthopaedic shoes will only qualify as a medical expense where the shoe is made to order for an individual in accordance with a prescription to overcome a physical disability of the individual. Thus, ready-made shoes which are advertised to be orthopaedic shoes will not qualify as a medical expense for the purposes of the Act even though the purchase may have been recommended by a physician.

A medical practitioner is defined in subsection 118.4(2) of the Act to be an individual authorized to practice as such in the jurisdiction in which the service is rendered. Accordingly, the services of a masseur provided in Ontario would only qualify as a medical expense where the service is provided in Ontario by a member of the College of Massage Therapists of Ontario.

Equipment which is used for medical purposes will only qualify as a medical expense for the purposes of the Act where it is described in one of the paragraphs of subsection 118.2(2) of the Act or in Regulation 5700. If the type of durable medical equipment covered by the plan does not qualify as a medical expense, then the plan would not qualify as a private health services plan.

If a plan provides benefits which do not qualify for inclusion in a health and welfare trust, the plan will be considered an employee benefit plan or employee trust as described in Interpretation Bulletin IT-502 "Employee Benefit Plans and Employee Trusts".

Even though a plan may qualify as a private health services plan, subsection 15(1) of the Act may apply to include the value of the benefit in a shareholder's income. If plan benefits are provided to shareholders in their capacity as shareholders, the value of the benefit

is included in the shareholder's income and the corporation is not entitled to a deduction for its contributions to the trust. Where a benefit is granted to an individual who is both an employee and a shareholder (or is related to a shareholder of the employer corporation), the benefit is presumed to have been conferred upon that shareholder by reason of the shareholdings unless that benefit is available to all employees of that corporation or the benefit is comparable in nature and quantum to benefits generally offered to employees who perform similar services and have similar responsibilities for other employers of a similar size.

The sample documentation you submitted states that an employer would contribute sufficient funds to the trust to provide the benefits available under the plan. An employer's deduction for amounts contributed to the trust may be restricted depending on the manner in which the contribution level is determined. In order to be deductible in a particular year, the employer must be under a legal obligation to make the contributions in that year and the amount must be reasonable in relation to the amount that is expected to be paid out of the trust in the current year. Where the level of annual contributions is determined on an actuarial basis to be the amount required to provide benefits in the current year, the Department will consider the contribution to be reasonable and thus not restricted by subsection 18(9) of the Act.

In our conversation of April 12th, you indicated that no trust returns would be required since the funds would be deposited to a non-interest bearing trust account. We draw your attention to paragraphs 11 - 14 of IT-85R2 which outlines the manner in which trust income is calculated where the trust invests the funds. As indicated in paragraph 8 and 9 of Interpretation Bulletin IT-129R "Lawyer's trusts accounts and disbursements", interest earned on a trust account will generally accrue for the benefit of the beneficiaries unless there is an agreement to the contrary.

Another point concerning the investment of trust funds is that the funds of a health and welfare trust cannot revert to, be invested in or

otherwise used by the employer or a person related to the employer. Prior to issuing a ruling, we generally look at the clause in the trust agreement which deals with the distribution of trust assets in the event the trust is wound up. Acceptable uses of trust funds upon windup include distribution to a registered charity as defined in section 149.1 of the Act and the provision of additional qualifying benefits as described in paragraph 1 of IT-85R2 to the employees covered by the plan.

While we trust that our comments will be of assistance to you, we would caution that they do not constitute an advance income tax ruling and are, accordingly, not binding on the Department with respect to any particular employer plan or trust. We have enclosed copies of the Information Circulars and Interpretation Bulletins referred to above.

We trust our comments will be of assistance to you.

Yours truly,

P.D. Fuoco
for Director
Business and General Division
Income Tax Rulings and
Interpretations Directorate
Policy and Legislation Branch
Enclosure
c.c. John Cunningham, Business Enquiries
North Toronto Tax Services
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