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Prenez note que ce document, bien qu'exact au moment Émis, peut ne pas reprÉsenter la position actuelle de l'ARC.

PRINCIPAL ISSUES: Whether subparagraph 18(9)(a)(iii) of the Act applies to the employer's contribution to a H&WT.

POSITION: Yes.

REASONS: The contributions to the H&WT are consideration for insurance in respect of a period after the end of the year in which the contributions are made.

November 22, 2004

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Attention: Derek Tolmie
2004-009477

Health and Welfare Trusts

We are writing in response to your e-mail of November 1, 2004, in which you request our comments on the application of subsection 18(9) of the Income Tax Act (the "Act") to an employer's contribution to a health and welfare trust ("H&WT").

In general, where an employer sets up a trust to administer health and welfare benefits for the employer's employees, the employer's contributions to the trust are considered to be on account of capital and no deduction is available to the employer. Administratively, the Canada Revenue Agency ("CRA") has taken the position that where such contributions are made to a H&WT, within the requirements described in Interpretation Bulletin IT-85R2 ("IT-85R2"), the contributions to the trust will be deductible to the employer in the taxation year in which those contributions are used to pay health and welfare benefits to employees.

IT-85R2 applies to health and welfare benefits that consist of a group sickness or accident insurance plan, a private health services plan, a group term life insurance policy or any combination of the above. In your specific situation, we are assuming that the "Group Sickness and Accident Insurance Plan" ("GSAIP") and the "Health and Welfare Insurance Plan" ("HWIP") both fall within these guidelines.

We agree with the argument of the taxpayer's representative that the unfunded pension and employee benefit plan, as defined in subsection 248(1) of the Act, rules were put in place to cause a matching of income to deductions. However, subparagraph 18(9)(a)(iii) of the Act was enacted for the same reason. Subparagraph 18(9)(a)(iii) of the Act provides that a taxpayer is not entitled to a deduction for any outlay or expense that is made or incurred as consideration for insurance where such outlay or expense is in respect of a period that is after the end of the year in which the outlay or expense is made. In this way, the deduction by the employer matches the payment of benefits to the employee(s). The fact that GSAIP's are excluded from the definition of "employee benefit plan" does not lead to the conclusion that the contributions to the

GSAIP are, therefore, deductible in the year they are made.

Where an individual is both a shareholder and an employee of a corporation, it is always a question of fact as to whether a benefit is received or enjoyed by the individual in their capacity as a shareholder or as an employee. The determination of this issue is not relevant to the determination of whether or not a particular health and welfare benefit qualifies as a GSAIP. For tax purposes, where it is determined that benefits under a GSAIP are received by an individual in their capacity as a shareholder, paragraph 6(1)(a) of the Act does not apply to exclude the benefit that arises from the employer's contribution to the GSAIP from the shareholder's income. The amount of the benefit would be included in the shareholder's income pursuant to subsection 15(1) of the Act. Furthermore, the employer would not be entitled to a deduction in respect of such amounts.

Notwithstanding the argument of the taxpayer's representative to the contrary, we would point out that a shareholder could be in receipt of a taxable benefit, that is included in income pursuant to subsection 15(1) of the Act, without an amount actually being paid to the shareholder. For example, the automobile benefit computed pursuant to subsection 15(5) of the Act and included in the shareholder's income pursuant to subsection 15(1) of the Act.

The taxpayer's representative argues that it is the GSAIP and HWIP that create the liability for health and welfare benefits, not the funding of the trust. While we agree that the setting up of the GSAIP and the HWIP may create a liability to the employer, it is our view that no liability arises until the plan incurs an expense as the result of a claim against the GSAIP or HWIP by an employee. An employee is generally not entitled to receive health and welfare benefits until an event occurs that is covered under the relevant plan. At the point in time when an event covered under a plan occurs, and the employee submits a claim to the plan in respect of that event, the plan has a liability to pay the employee the amount specified in the plan for that event. It is our understanding that the GSAIP and the HWIP are self-funded plans and that no claims were ever made against either of

the GSAIP or the HWIP. Accordingly, it is our view that the employer would not be entitled to any deductions for the contributions made to the GSAIP or the HWIP by virtue of subparagraph 18(9)(a)(iii) of the Act.

Furthermore, to argue that the plan itself creates the liability to the employer in the year the plan is set up ignores the words "insurance in respect of a period after the end of the year" and would result in subparagraph 18(9)(a)(iii) of the Act being meaningless, since it could never apply.

We have not been asked to, and do not have sufficient information, to provide any comments with respect to the application of subparagraph 152(4)(b)(iii) of the Act.

Conclusion

As conceded by the taxpayer's representative, it is our view that subparagraph 18(9)(a)(iii) of the Act would apply to any H&WT under review where the funding of the trust exceeds the outlays and expenses incurred by the H&WT in the current year. Where a H&WT provides health and welfare benefits pursuant to a contract of insurance, the employer will be entitled to an annual deduction, for contributions to the H&WT, equal to the amount paid by the H&WT for such insurance coverage. Where a H&WT is funded by the employer, the employer will be entitled to an annual deduction for amounts contributed to the H&WT that are in respect of health and welfare benefits actually paid to employees, by the H&WT, in the current year.

If we can be of any further assistance, please contact the writer.

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