A **Private health services plan** (PHSP) is a Canadian tax-free vehicle for financing the healthcare costs of employees. They are similar to a Health and welfare trust. They were introduced in 1989 by Canada Revenue Agency (CRA) in their interpretation bulletin entitled IT-339R2.[1] Today, they are one of the most popular forms of health spending accounts in the Canadian market.

Contents

Overview

In 1986, the Canada Revenue Agency introduced an interpretation bulletin entitled IT-85R2 - Health & Welfare Trusts for Employees.[2] This bulletin provided the basics for what would be known as a Health Spending Account or HSA to most Canadians. The original 1986 bulletin provided a tax-free vehicle for incorporated professionals and companies in the form of an HWT. Three years later in 1989, after pressure from non-incorporated entities, Canada Revenue Agency released another bulletin, IT-339R2 (*Meaning of Private Health Services Plan*), providing details on the concept of a Private Health Services Plan or PHSP for non-incorporated businesses in Canada.

The Canada Revenue Agency, in the annual Guides it publishes for those reporting self-employment income from a business or a profession,[3] or from farming,[4] provides instructions for deducting Private Health Services Plan premiums.

The PHSP resembles the HWT in many ways - particularly when it comes to the requirements for establishing a PHSP. These requirements are as follows:

(a) The funds of the PHSP cannot revert to the employer or be used for any purpose other than providing the health and welfare benefits for which the contributions are made;

(b) The employer's contributions to the fund must not exceed the amounts required to provide the benefits;

(c) The payment made by the employer cannot be made on a voluntary or gratuitous basis. In other words, once the payment plan is established it cannot change during the policy year. The contributions must be enforceable by trustees should the employer decide not to make the payments required;

(d) The trust is a legal arrangement between the employer, with a third-party acting as the administrator and an independent trustee. The expenses to be paid out of the trust must qualify as medical expenses as defined by CRA (specifically subsection 118.2(2) of the Act).

Confusion & Controversy

The funds in a PHSP, as outlined in the guidelines set in interpretation bulletin IT-339R2,[1] *CANNOT* revert to the employer. Canada Revenue Agency released another bulletin in 1998 indicating that the funds could revert to the employer but *ONLY* in the case of a notional credit program tied to a flex benefits or cafeteria style plan. The "notional credit" model, outlined in the Canada Revenue Agency IT-bulletin entitled IT-529[5] was designed to allow companies to add an HSA to a Flex Benefits Plan as an additional benefit for items not covered under the traditional group benefits plan. The bulletin provided the accounting rules for flex benefit programs and using notional credits for the employer.

Today, the major insurers offer PHSPs as part of a notional credit model with a core group health insurance program. In recent years however, several third-party administrators have emerged offering PHSPs as stand-alone benefit solutions with the ability for the employer to have the funds returned if the employee leaves or does not use their funds. This has caused confusion in the marketplace as the IT bulletins clearly state that funds may only be returned to the employer if part of a notional credit system tied to a flex benefits plan. It is always in the best interest of consumers to look for a PHSP supplier following the interpretation bulletins properly.

Funding

The employer shall make contributions to the PHSP for a “plan year” in an amount, which together with employee contributions, if any, are required to provide the benefits under the plans to eligible employees of the employer and their dependants. Each employee shall be allocated a “plan year” not to exceed twelve months. The employer must follow the rules for funding outlined for a PHSP whereas the employees may be provided with an HWT. The amount contributed must be reasonable given the employment services performed by the employee.

Annual Maximums - PHSP can be for self-employed individuals and corporations. But the annual maximums are different.

For self-employed individuals with no employees other than family members:

- Business owner: $1,500/year
- Spouse: $1,500/year
- Dependent over 18 years or older: $1,500/year
- Dependent under 18 years old: $750/year

Example: A household with 1 sole-proprietor, a spouse, and one child under 18 years old would be eligible for 2 X $1,500 PLUS $750, for a total of $3,750.

For self-employed individuals with arms length employees: The business owner may have the same spending limit assigned to full-time staff.

For corporations (incorporated businesses or limited companies):

- Maximum 20% of T4 income
- All full-time employees should be included
- Limits are adjustable

Example: Executives $10,000/year, Manager $5,000/year, Sales $3,000/year, Admin $1,500/year

Forfeiture of Funds - Unlike the HWT, the PHSP also has limits in place for the length of time the funds can be used. For every dollar deposited into a PHSP account, the funds must be used within 24 months from the date of deposit, otherwise they will be forfeited to the administrator.

Participation Rules

A sole-proprietor can establish a PHSP with a third-party administrator. If the sole-proprietor is an individual, they may open a PHSP for themselves and their family members. If the sole-proprietor has employees, they must offer a Health and Welfare Trust to the employees and a PHSP for themselves as owners. Additional limitations exist for the sole-proprietor in terms of contribution maximums if they have employees so it is recommended that most individuals research and use a firm specializing in PHSP and HWTS in order to be 100% compliant with the IT bulletins from Canada Revenue Agency.

Eligible Expenses

The most common definition of a medical expense is a payment made to a licensed medical practitioner qualified to practice under the provincial laws of the place where the expenses were incurred. Medical expenses eligible to be paid out of the PHSP are expenses which would otherwise qualify as medical expenses within section 118.2(2) of the Income Tax Act. Some of the basic healthcare expenditures covered by an HSA include...

Prescription medicines, drugs, & vitamins:

Generally, payments for prescription medicines and drugs (i.e. over the counter drugs) qualify as medical expenses if purchased by the employee, their spouse, or their dependent, as prescribed by a medical practitioner and as recorded by a licensed pharmacist.

In the case of insulin, oxygen and liver extract injectable or vitamin B12 for pernicious anemia, no prescription is required.

If vitamins are prescribed by a medical practitioner, but not purchased from a pharmacist who has recorded the prescription in a prescription record, then the expense is not an eligible medical expense. However, in recent court cases, they can allow the eligibility of prescribed vitamins, herbs, bottled water, organic and natural foods and not dispensed by a pharmacist if the items are required to sustain the life of the user. It is not eligible if it is simply to satisfy a lifestyle the user has chosen.

Vision:

Eyeglasses, if prescribed, are eligible medical expenses.

Dental:

An amount paid to a dentist, dental hygienist, dental surgeon or dental mechanic for dental services provided to the patient (to the extent that the fees are for diagnostic, therapeutic or rehabilitative services) are eligible medical expenses.

Professional services:

An amount paid to a licensed medical practitioner is an eligible medical expense. They can include depending on the provincial jurisdiction:

• Chiropractor • Audiologist • Chiropodist • Christian Science Practitioner • Dentist • Dental Hygienist • Dental Technician • Denturist • Dietician • Osteopath • Physiotherapist • Podiatrist • Psychiatrist • Psychoanalyst • Physician and Surgeon • Psychologist • Radiologist • Massage Therapist • Midwife • Neurologist • Occupational Therapist • Optician • Speech Therapist • Registered Nurse • Respiratory Therapist • Naturopath

All medical doctors, medical practitioners, dentists, pharmacists, nurses or optometrists must be authorized to practice under the laws of the provincial jurisdiction where the service is rendered, in order for the medical expenses to be eligible.

Cosmetic surgery

It has generally been accepted that an amount paid to a medical practitioner for surgery of any kind, whether cosmetic or elective generally qualifies as a medical expense. It is presumed that such surgery is carried out for a valid medical reason.

CRA has however qualified that expenses for purely cosmetic procedures, including any related services and other expenses such as travel, incurred after March 4, 2010, are no longer an eligible expense. Both surgical and non-surgical procedures purely aimed at enhancing one's appearance are a non-eligible expense.

Examples of expenses that are non-eligible include the following: • liposuction; • hair replacement procedures; • botulinum injections; and • teeth whitening.

An expense, including those identified above, will continue to qualify if it is necessary for medical or reconstructive purposes, such as surgery to address a deformity related to a congenital abnormality, a personal injury resulting from an accident or trauma, or a disfiguring disease.

Transportation costs

In addition to ambulance charges to and from hospitals, eligible medical expenses include any commercial transport service transporting a patient and an attendant (if medically necessary to accompany the patient) to a clinic/hospital/doctor's office. The distance traveled must be in excess of 40 km to obtain such equivalent service not readily available closer to home. If the distance traveled is in excess of 80 km, the eligible costs would include meals and accommodation, in addition to transportation expenses.