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smart benefits for smart people

The Accountant's Guide to Private Health Services Plans (PHSP)



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PHSP's are in demand within Canada's small business community. Viewed as a viable and cost effective alternative to traditional health insurance, PHSP's make paying for medical expenses affordable and easy.

Although straightforward to use, the product does require proper explanation and understanding before it is adopted by any particular small business. PHSP's directly involve matters of taxation and ultimately business owners should speak with their accountant for clarification.

The purpose of this guide is to summarize and explain PHSP's in order to provide a reference and resource for accountants to use in discussions with their small business clientele. Inside you'll find a definition and criteria, an explanation of our product, and a concrete example to show your clients.

Company Background

navancorp was created in 2016 and operates out of Ottawa, Ontario. After using PHSP's in the past, the founders were amazed at the apparent under-utilization of this tax-efficient tool by the typical incorporated small business owner.

navancorp was launched to fulfill a legitimate service need within the industry and to provide awareness to the Canadian small business owner to allow them to retain more of their hard-earned money.

Unlike some other PHSP providers, **navancorp** does not charge annual fees nor premiums. Furthermore, **navancorp** offers a Referral Program to accountants/accounting firms, and in some instances, preferred Administration rates for their clients.



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The **navancorp** PHSP is a Private Health Services Plan (PHSP). The Canada Revenue Agency defines a PHSP within Section 248(1) of the [Income Tax Act](#) and the subsequently issued [Interpretation Bulletin IT-339R2](#). On January 1, 2015 [CRA issued a new position on PHSP's](#), which made the plans even more beneficial and encompassing.

A **navancorp** PHSP enables an employer to reimburse an employee (including those who are shareholders AND employees) for eligible medical expenses on a tax-free basis while deducting these expenses. Medical benefits paid on behalf of an employee by an employer are not taxable as a benefit to the individual; nor are the claim benefits themselves taxable to the individual employee.

The cost of these benefits (including the Administration Fee and applicable taxes) is considered a business expense.

Eligible medical expenses are defined as those expenses for which an individual can apply for a Medical Expense Tax Credit on their personal income tax. Eligibility is determined not only by the expense itself, but also that it is performed or prescribed by a qualified medical practitioner. Examples of fully eligible expenses include:

- All dental work, including orthodontics
- All optical (including laser eye surgery)
- All prescription drugs
- Physiotherapy
- Massage Therapy
- Cancer treatments
- Medical certificates
- Hearing aids
- Laboratory procedures, tests or services
- Medical marijuana
- Nursing services
- Orthopaedics
- Pacemakers
- Vaccines
- Walking aids
- Ambulance Service

The full list is available from the [CRA website](#).

A **navancorp** PHSP is not an Employee Life and Health Trust nor a Health and Welfare Trust. The Income Tax Act allows a PHSP to take a number of different forms, but one fundamental principle is that it must be “a contract of insurance” with respect to hospital or medical expenses of similar insurance plans. This implies that CRA would expect to see a formal contract of employment incorporating the requirement that the employer provide this medical coverage as a condition of employment.



navancorp PHSP

navancorp PHSP's are available to corporations across Canada (with the exception of Quebec), from incorporated independent consulting firms comprised of one shareholder/employee on up to larger enterprises.

In order to qualify as a true PHSP, there are a number of conditions which must be met:

- The PHSP is in the nature of insurance;
- The employer is under legal obligation to fund up to the self-imposed spending limits for each employee;
- All employees in a particular classification must be offered equivalent benefit levels;
- Employees not forego any amount to which he/she would otherwise be entitled in order to obtain the increased benefit (eg: requesting/accepting a salary increase/decrease to accommodate for enrollment or non-enrollment within the PHSP);
- All reimbursement credits must be claimed in the year in which they are incurred or within 12 months of the plan year, in part to mitigate/eliminate risk;
- Eligibility is maintained with respect to medical expenses, employees, and dependents; and that
- No allowance is made for cash payments for unused reimbursement amounts.

navancorp, in its role as PHSP Administrator, ensures that each of its PHSP's are established in accordance with CRA rules. The business-owner is responsible and accountable for ensuring that they do not breach any of the conditions with internal policies/practices which may cause the PHSP to be voided (such as providing employees with cash/bonus payments for unused reimbursements).

As it relates to sole-proprietors, as part of the conditions noted above, the plan must be a "plan or contract of insurance". This essentially means that there must be one part that indemnifies another party against loss with respect to an event (the happening of which is uncertain).

In an incorporated company, the corporation indemnifies the employee(s). Even in single-person corporations, the employee and the company are two distinctly different entities. Sole-proprietors cannot indemnify him/herself as they are legally the same individual. We encourage sole-proprietors (unincorporated entities) to subscribe to traditional health benefits programs to allow for a contract of indemnity of insurance between them and a traditional insurer.



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PHSP Eligibility

In order to be covered through a **navancorp** PHSP, an individual must be gainfully employed by an incorporated entity. Covered employees may claim expenses for themselves as well as individuals who are living in their household (note that “their household” means principal residence at a single address where the full time occupants, regardless of age, are dependent upon the employee for their living expenses).

There are no age limits or medical exams required. Pre-existing medical/dental conditions are fully covered (up to the employee's annual maximum). It bears mentioning that that a **navancorp** PHSP is not an employee life or Health and Welfare Trust.

What is the enrollment process?

The enrollment process is very straight-forward:

1. Your client goes to www.navancorp.ca and clicks on “Enroll”
2. There they will find an online form for automatic submission, or, if they prefer, there is also a fill-able PDF which they can email or mail to us.
3. The client submits their owner enrollment form and remits the \$49 administration fee in order to activate their account (fee waived if they are moving from another PHSP provider)
4. The client registers its employees, noting their “Class” (individual spending cap) and effective date.
5. The employee provides details on who will be covered under their plan.

navancorp then issues an individualized Plan Member ID. Upon receipt of their Plan Member ID, individuals are then able to submit claims.



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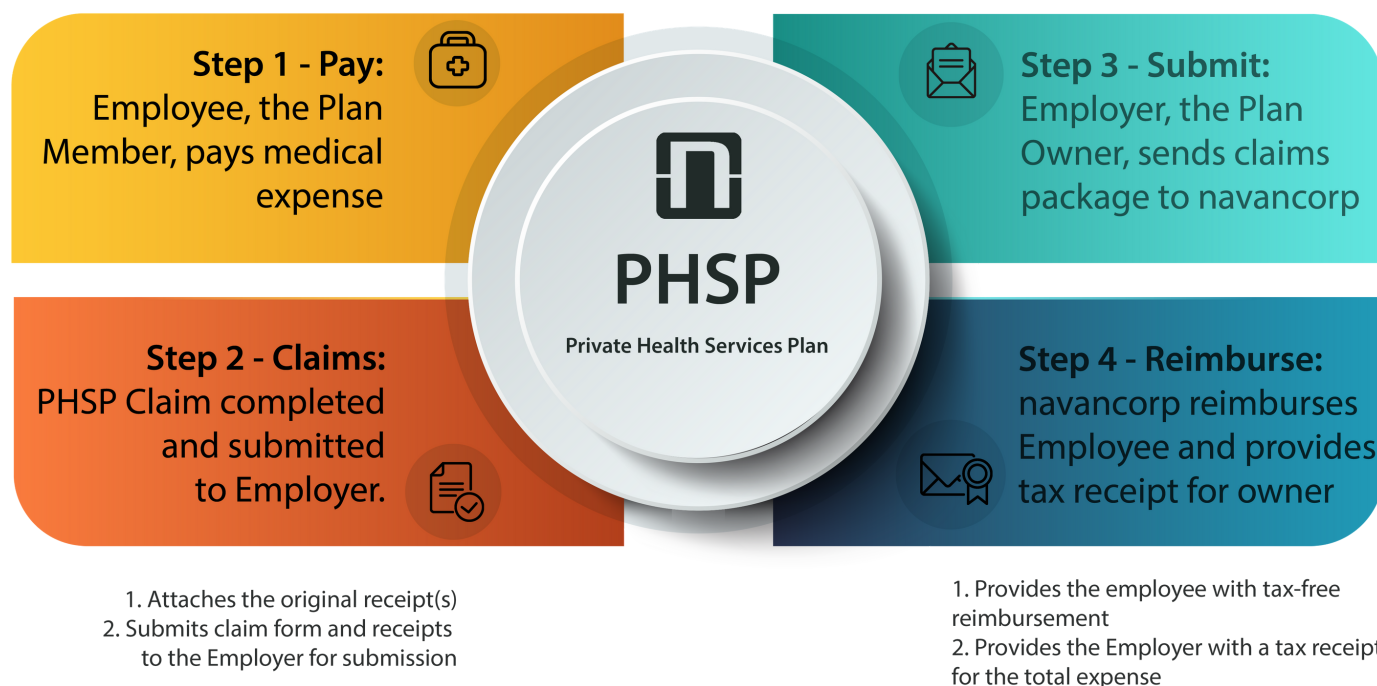
What is the enrollment process?

Employee (Plan Member) receives medical service

1. Pays for medical expenses out of pocket
2. Obtains original receipt(s) from medical service provider

Employer (Plan Owner) sends items to navancorp

1. Completed navancorp PHSP claims
2. Original medical expense receipts
3. Payment: Cheque or electronic transfer



Employee (Plan Member) completes PHSP claim

navancorp reviews & ensures CRA compliance

What are the “all-in” costs?

The sole cost outside of the Administrative Fee (one time \$49, no tax) is the Administrative Fee (typically 10%) plus applicable taxes added on to the amount of the claim. There are not any setup fees, annual fees, account change fees – nothing. Many PHSP providers charge hidden fees or ongoing annual costs in addition to the claim Administration Fee. Not at **navancorp**. There is no minimum claim amount and no additional costs regardless of how many claims an individual files each year.



Do you offer a referral program?

Let's use an example of an incorporated business owner in Ontario. She pays herself a salary of \$100,000 and has a marginal tax rate of 43%. In the upcoming year, she has a child who needs braces, another who needs glasses and prescriptions for herself and her husband. She expects to spend about \$15,000 on her family's medical and dental costs. She has no current form of insurance in place, so 100% of the cost is going to be paid out of the family budget.

In the diagram below, we see a savings comparison between paying for the costs out of pocket versus using a Private Health Services Plan.

Without PHSP			With PHSP
\$100,000.00		Taxable Income	\$100,000.00
\$15,000.00		Eligible Medical Expenses	\$15,000.00
Federal	Provincial		
\$2,152	\$2,167.00	Medical Tax Credit (MTC) Threshold	N/A
\$12,848.00	\$12,833.00	Amount Eligible for MTC	N/A
15%	5.05%	Medical Tax Credit Percentage	N/A
\$1,927.20	\$648.07	Medical Tax Credits	N/A
\$2,575.27		Combined Federal & Provincial MTC	N/A
\$12,424.73		Out of Pocket Health Costs After Medical Tax Credit	N/A
\$9,530.97		Taxes Paid on Earnings Used By Employee to Fund Health Costs	\$0.00
N/A		Company Funds Used to Reimburse Eligible Medical/Dental Expenses	\$15,000.00
N/A		navancorp PHSP Claim Admin Fee (10%)	\$1,500.00
N/A		HST Paid on Claim Admin Fee (13%)	\$195.00
N/A		Provincial Premium Admin (2%)	\$330.00
\$21,955.70		Total Amount Used to Pay Health Costs	\$17,025.00
		Total Savings Using a navancorp PHSP	\$ 4,930.70
** A marginal tax rate of 43.41% was used for these calculations (updated for 2016)			



Can you provide a scenario?

Option 1 - Out of Pocket (After Tax Expense)

With no insurance plan, the cost is paid for out of pocket expenditures with after tax dollars. For her marginal tax rate, the company will have to pay out \$7,120, with 43% of that amount being reserved to pay her income tax (\$3,120).

In other words, each dollar she spends on her dental costs require the company to pay her \$1.78. 78 cents (43%) of this pay goes to Canada Revenue Agency in the form of provincial and federal taxes. The true cost for a \$1 of dental work is therefore \$1.78 when you factor in the additional cost of taxes.

Option 2 - Health Spending Account: Before Tax

By using a Health Spending Account, she is able to write off 100% of her dental costs through her corporation. The after tax expense from choice 1 now becomes a before tax expense. Instead of paying an additional 43% on every dollar she spends on dental, a flat rate annual fee is paid to the provider of her Health Spending Account.

In our example, her company will save approximately 40% on every dollar she spends. The higher the tax bracket (the top tax bracket in Ontario for 2016 was \$49.53%), the more she saves. For top earners in Ontario, this means you can cut your dental costs in half. In every tax bracket, you will save money by paying for your dental costs through your company, as a before tax expense, with a Health Spending Account.

Do you offer an affiliate program?

Yes, navancorp does offer an affiliate program for accounting firms, bookkeeping entities and registered insurance/financial product providers. Once you are approved as a designated affiliate, navancorp may arrange preferred rates for your corporate clients, reducing the 10% Administrative Fee in some cases. As an example, all referred clients of XYZ Accounting Firm could pay an 8% Administrative Fee.

We are open to tailoring a costing model that works for all involved. Interested affiliates can reach us at info@navancorp.ca for further details.



Shareholder vs Employment Benefits

With respect to the shareholder/manager of a corporation, there is a general presumption that a benefit with respect to a private health services plan would be conferred on the individual in his or her capacity as a shareholder and included in income pursuant to subsection 15(1) (see Technical Interpretation No. 9505265).

In a recent interpretation, the Canada Revenue Agency indicated that “when equivalent coverage under a private health services plan is extended to all employees, including the employees who are shareholders, the benefit provided to the employee-shareholders from such coverage is normally considered to be an employment benefit rather than a shareholder benefit”.

Where all employees of the corporation are shareholders, Revenue Canada states:

“Similarly, when all employees of a corporation are shareholders and it is reasonable to conclude, based on the particular facts of the situation that the private health services plan coverage has been provided as part of a reasonable remuneration package, the benefit from such coverage is also considered to be an employment benefit rather than a shareholder benefit. In such a case, the benefit is not included in the employee-shareholders’ income by reason of the exclusion in subparagraph 6(1)(a)(i) of the Act, and the corporate employer is entitled to a deduction in respect of the contributions made for such coverage, subject to any limitations imposed under the Act”.

For these reasons, navancorp insists that any registered PHSP’s include provisions for coverage across the company, to every employee. We work directly with you or the corporation to establish “Classes” of employee, with appropriate maximums for each “Class”. Though there are not any pre-established acceptable standards by the CRA in this regard, the sole guidance is that the “Class” structure meets the case of reasonableness. Typically navancorp suggests a “Class” structure similar to this:

Class	Position	Annual Maximum
1	President/CEO/COO	\$12,000-\$15,000
2	Middle Management	\$5,000 - \$7,500
3	Full-Time Employees	\$2,000-\$4000
4	Part-Time Employees	\$1,000



Shareholder vs Employment Benefits

Note that these are merely suggestions/guidelines. The actual maximums are dependent upon a) ability of the corporation to cover the costs b) the willingness of the President/CEO (or corporation owner) to cover costs at these levels. Regardless of the maximums, in order to ensure adherence with CRA guidelines, a corporate class structure must be in-place which includes all employees of the corporation. navancorp, as part of its value proposition to your clients, tracks all claims to ensure that the class structure (and associated maximums) are respected.

Risk & Plans of Insurance

It is the CRA's belief that a health insurance plan must involve a reasonable degree of risk to meet the definition of "private health services plan". Plans that provide an indefinite carry forward of unclaimed medical expenses would not involve a reasonable degree of risk. However, a plan would have a reasonable degree of risk if it provided that any unused balances be forfeited.

For the health care plan to qualify as a PHSP, the plan must involve a reasonable element of risk that is assumed by the employer. Plans that permit the choice of a rollover or a cash-out of unused credits will not qualify as PHSPs. A plan that permits the rollover of unused expenses as well as credits also is not likely to qualify. Plans that permit the rollover of unused credits to be applied to other plans are not considered PHSPs.

It bears noting that eligible amounts may be claimed in the plan year in which they are incurred or within 12 months of the end of the plan year. The individual subscriber forfeits any credit remaining at the end of a plan year.

In order to meet the standard for a "Plan of Insurance", there are three essential components:

- 1) One entity indemnifies another
- 2) for an agreed consideration
- 3) from a loss or liability in respect to an uncertain event happening (i.e.: risk)



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Risk & Plans of Insurance

With a **navancorp** PHSP, the employer indemnifies the employee and the benefit level is established (through the identification of "Classes" upon setup).

With regards to point "3" above, the Employer accepts a reasonable degree of risk by establishing a set benefit level for employee and is uncertain if the employee will claim the amount available. Likewise, the employee is uncertain if the allowable level offered will be used. The employee will forfeit any unused credits after the prescribed period of time.

Summary

navancorp has provided this booklet to aid in facilitating discussions with your clients regarding the establishment of a Private Health Services Plan.

As matters of taxation can be complex, it is not intended to be a complete compilation of all related issues and scenarios. The intent is to provide you, in your professional capacity as a trusted financial partner to your clients, an overarching summary of how the use of a PHSP may form part of a tax-efficient strategy.

Should you have any questions, feel free to visit our website at www.navancorp.ca. You are also encouraged to follow us on Twitter, Facebook and/or LinkedIn.



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