HEALTH PLANS

Canadian Health Insurance
TAX GUIDE

Employee Life and Health Trusts

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Life's brighter under the sun

Sun Life Financial

Introduction

Employee life and health trusts (ELHTs) are similar to health and welfare trusts (HWTs),[1] but derive their authority from section 144.1 of the Income Tax Act (ITA), rather than from Canada Revenue Agency (CRA) guidance, as HWTs do. ITA section 144.1 applies to all trusts created after 2009. Neither the CRA nor the Department of Finance plan to withdraw CRA guidance on HWTs or recommend legislation to eliminate them.[2]

An ELHT is a vehicle through which an employer provides life and health benefits for its employees. Generally, employers may deduct ELHT contributions as long as those contributions are reasonable business expenses. Employees generally are not taxed on lump sum benefits paid from such plans, but are taxed on benefits paid on a periodic basis (like disability income insurance plan benefits) where the employer has contributed to the plan.[3]

Currently, employer contributions are not taxed to employees, except for the following:

- employer contributions to group term life insurance plans,[4]
- employer contributions to group sickness and accident insurance plans (GSAIPs) where the benefits paid from such plans are tax-free,[5] and
- in Quebec, employer contributions to the above plans, and to private health services plans (PHSPs).

Employees in Quebec must report employer contributions as income on their provincial (not federal) tax returns.

Why ELHTs have been added to the ITA

Provide more certainty in the rules governing the delivery of employee benefits through trusts. The rules governing HWTs are not in the ITA, but are instead based on CRA guidance that the CRA can change, withdraw or choose not to follow. The foundation for the CRA's guidance is Folio S2-F1-C1: "Health and Welfare Trusts".[6] The rules governing ELHTs are part of the ITA, and can be changed only by an Act of Parliament. The ELHT rules therefore provide a more certain foundation for an employee benefits plan than those governing HWTs.

1 Refer to our article "Health and Welfare Trusts" for more information.

2 Explanatory Notes Relating to the Income Tax Act, the Air Travellers Security Charge Act, the Excise Act, 2001, the Excise Tax Act and Related Acts and Regulations, published by the Honourable James M. Flaherty, P.C., M.P., Minister of Finance, September 2010, page 41, http://www.fin.gc.ca/drleg-apl/biasept10n-eng.asp, referred to herein as Explanatory Notes. CRA document 2011-0398371C6, dated June 10, 2011.

3 ITA paragraph 6(1)(f).

4 ITA subsection 6(4).

5 ITA paragraph 6(1)(e.1).

6 Last updated November 28, 2015. 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.

Reduce the generosity of tax-assisted benefits for business owners and highly compensated employees. The rules governing ELHTs and HWTs discourage plans that disproportionately benefit business owners and key employees, but the ELHT rules go farther.

Eliminate offshore trusts and tax avoidance schemes. An HWT can be resident in a different country from Canada, but an ELHT can't. Generally, the CRA regards offshore HWTs as potential tax avoidance vehicles.

Enhance protection for employees if the employer restructures, becomes insolvent or goes bankrupt. An ELHT requires several features that an HWT does not.

- An ELHT cannot:
  - Lend money to the employer
  - Own employer securities (or securities of related companies)
  - Be controlled by trustees, a majority of whom are representatives of the employer
- But:
  - An ELHT may accept an employer's promissory note as evidence of the employer's obligation to make a contribution to the ELHT. The promissory note does not have to be secured or have a preference or priority over debt owed to other creditors.
  - ELHT trustees do not have to have the power to enforce an employer's obligation to make contributions to the ELHT. This power is required for trustees of an HWT, and was included in the original draft legislation governing ELHTs, but was dropped from the legislation that received Royal Assent.

Reasons why an employer would want to create an ELHT

In our article "Health and Welfare Trusts", we discuss several reasons for why an employer would want to create an HWT. Those reasons all apply to an employer's decision to create an ELHT.

Requirements for creating an ELHT

General

The ELHT rules apply to all trusts created after 2009 that satisfy the ELHT rules. ITA subsection 144.1(2) contains the requirements that a trust must meet to be considered an ELHT. A trust that meets those requirements, whether by accident or by design, is an ELHT. Most trusts will meet the requirements by design. But if an employer wants its trust to be an HWT, it must draft the trust in a way that causes it to fail at least one requirement in ITA subsection 144.1(2), but still meet the requirements in Folio S2-F1-C1. The employer should get an advance tax ruling on its proposed trust to ensure CRA approval of the trust as an HWT. A trust that fails to qualify as either an ELHT or an HWT will be treated as an employee benefits trust (EBT), with less beneficial tax treatment for the parties. See our article "Health and Welfare Trusts", for more details.

Specific requirements for creating an ELHT

ITA subsection 144.1(2) sets out the specific requirements for creating an ELHT. We discuss those requirements below.

Who may be a beneficiary of an ELHT

An ELHT's only purpose is to provide "designated employee benefits" for the following people:

- **Employees**
- **Their spouses,** and
- **People who are related to the employee,** and are either a member of the employee's household or are dependent on the employee for support.[7]

The wording in ITA paragraph 144.1(2)(d) is exclusive: "the trust may not have any beneficiaries other than…" those listed above.[8] Appendix A contains a chart summarizing the various beneficiaries who can receive designated employee benefits.

- **Employees**

  ITA subsection 144.1(1) defines an "employee" as a current or former employee. A former employee may be someone for whom the employer continues to provide benefits after that person has left, after retiring, for example. An "employee" is also an employee of a business that the employer has acquired, and by so doing may have assumed the former employer's obligations to provide health and welfare benefits for its employees.

- **Spouse**

  The term "spouse" means a person of the same or opposite sex to whom the employee is married, and includes a common law partner (same or opposite sex) of an employee, and the spouse of an employee who has died.[9]

- **Related persons**

  The third class of beneficiaries includes members of the employee's family, whether living with the employee or not. An individual can be a beneficiary if they are "related to the employee" and either "a member of the employee's household" or "dependent on the employee for support".

  #### Related

  ITA section 144.1 does not define the phrase, "related to the employee", but ITA subsection 251(2) describes "related persons" or "persons related to each other" as "individuals connected by blood relationship, marriage or common-law partnership or adoption." ITA subsection 251(2) applies to the entire Act, and therefore controls who ITA section 144.1 treats as related to the employee.

  The phrase, "a member of the employee's household", is not defined in the ITA, but should include family members like children, at least until they leave the employee's home to pursue independent lives as adults.

[7] ITA subsection 144.1(2).

[8] ITA paragraph 144.1(2)(d).

[9] ITA clause 144.1(2)(d)(ii)(A).

Dependent

The phrase, "dependent on the employee for support", could apply to children and former spouses not living with the employee (possibly because of marriage breakdown), but still related to the employee, and dependent on the employee for support. The phrase could also include elderly relatives who don't live with the employee but who still depend on the employee for support (like long term care and medical expenses).

ITA section 144.1 does not specify the degree of support needed for someone to be considered "dependent on the employee for support". But the CRA has considered the question in its guidance on the medical expense tax credit. We discuss this issue in our article "The Medical Expense Tax Credit".

To qualify as a dependent, someone must depend on the taxpayer on a regular and consistent basis[10] for the basic necessities of life, such as food, shelter and clothing.[11] It does not matter whether support is provided voluntarily or pursuant to a legal requirement.[12] A dependent can be dependent on more than one taxpayer.[13] Whether someone depends on another for support is a question of fact in each case.[14]

ITA subsection 118(6) also describes a dependent as:

- A child or grandchild of the individual or individual's spouse or common law partner.
- A parent, grandparent, brother, sister, uncle, aunt, niece or nephew, if resident in Canada at any time in the year, of the individual or individual's spouse or common law partner.

CRA guidance is helpful, but not binding, and ITA subsection 118(6) applies to dependents under ITA subsection 118(1). The courts and the CRA may decide that it does not apply to ITA section 144.1.

Provincial law

Provincial law also adds some complexity to the question of who is a dependent. For example, Alberta's Adult Interdependent Relationships Act[15] describes and sets rules for common law marriages, though the Act uses the term, "adult interdependent relationship". But the Act also allows people related by blood or adoption to enter into a relationship of interdependence. Since such an arrangement contemplates interdependence between parents and children, and between siblings, it cannot be a common law marriage. Yet, depending on the arrangements they create, parents, children and siblings could owe to each other many if not all of the obligations that common law spouses owe to each other. While provincial law does not control the interpretation of federal statutes, the arrangements contemplated in the Alberta Act recognize the diversity and complexity of the living arrangements people are creating, suggesting the need for an open and generous interpretation of the beneficiary provisions in ITA clause 144.1(2)(d)(ii)(B).

[10] CRA Document 2004-0063331E5, dated May 3, 2004.

[11] CRA Document 2009-0326721I7, dated November 9, 2009.

[12] CRA Document 9725807, dated May 15, 1998.

[13] Ibid.

[14] Ibid, note 12.

[15] S.A. 2004, c. A-4.5.

Designated employee benefits

ITA subsection 144.1(1) confines "designated employee benefits" to those benefits allowed under ITA subparagraph 6(1)(a)(i):

- **Group Sickness or Accident Insurance Plans (GSAIP).** These include disability insurance, critical illness insurance, some types of long term care insurance, and accidental death and dismemberment insurance. We discuss GSAIPs in our article "Group Sickness or Accident Insurance Plans".
- **Group term life insurance policies.** We discuss group term life insurance policies in our article "Group Sickness or Accident Insurance Plans".
- **Private health services plans (PHSP).** We discuss PHSPs in our article "Private Health Services Plans."

A trust that provides benefits other than those listed above will fail to qualify as an ELHT.

Classes of beneficiaries

Under ITA paragraph 144.1(1)(e) the trust must have at least one class of beneficiaries, although it could have more. Each member of a class must have rights under the trust identical to every other member of the class.[16] The beneficiaries in at least one class must represent at least 25% of all beneficiaries of the trust who are employees.[17] At least 75% of the class cannot be "key employees".[18] We discuss key employees later in this article.

An example may help make these requirements more clear. Consider ABC, Ltd., a company with 96 employees. 16 of those employees are "key employees". ABC creates an ELHT for its employees with one class of beneficiaries. The members of that class must comprise "at least 25% of all the beneficiaries of the trust who are employees of [ABC]". If the class contains at least 24 employees, the trust satisfies this requirement. There is no upper limit on the number of beneficiaries a class may have, so the class could comprise all 96 employees.

A second requirement is that "at least 75% of the members of the class are not key employees of [ABC]."[19] If the class contains 24 employees, this second requirement means that at least 18 of those employees cannot be key employees. That leaves room for only 6 key employees in the class. At the other extreme, if the class comprises all 96 employees, at least 72 employees in that class cannot be key employees. That leaves room for 24 key employees in the class, more than enough to allow all 16 of ABC's key employees to be beneficiaries of the trust.

With only one class of beneficiaries, the ELHT must offer identical benefits to the key and non-key employees. This could be a problem if ABC wants to provide different benefits for its key employees. However, nothing prevents an employer from creating an ELHT with more than one class of beneficiaries. Since only one class has to satisfy the 25% and 75% rules, ABC could create an ELHT with two classes of beneficiaries, one comprising the non-key employees, and the other comprising the key employees. The key employees do not have to have rights identical to the non-key employees', only rights that are "not more advantageous".[20]

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

[17] ITA subparagraph 144.1(2)(e)(i).

[18] ITA subparagraph 144.1(2)(e)(ii).

[19] ITA paragraph 144.1(2)(e).

[20] ITA paragraph 144.1(2)(f).

Not more advantageous

The ITA does not define what "not more advantageous" means. Certainly identical benefits would satisfy this requirement. But ABC wouldn't need an ELHT with multiple beneficiary classes if it was providing identical benefits for all its employees.

Providing inferior benefits for key employees would also satisfy the "not more advantageous" requirement. ABC could remove some benefits from the key employees' package offered through the ELHT, and provide them with enhanced versions of those benefits outside the ELHT. It could also provide different or additional benefits for key employees outside the ELHT. ABC would have to take care, though, because the tax treatment for itself and its key employees would be different for benefits offered outside the ELHT.

"Not more advantageous" could also mean that benefits are calculated according to a formula that applies equally to key and non-key employees. For example, a formula that pays benefits as a percentage of an employee's earnings could be seen as "not more advantageous" because the same formula applies to all employees even though higher paid employees could receive more money from the plan. The plan could include caps on benefit amounts to reduce potential disparities between the highest and lowest paid employees.

A different approach is to provide the same benefits to key and non-key employees, but to apply different co-payments and deductibles. The key employees would not receive greater benefits, but could reach their coverage limits later than the non-key employees, assuming all other things remained equal.

"Not more advantageous" could also allow ABC to provide benefits to key employees that are different in kind from those it offers to its non-key employees, but still of equal value. Of course, ABC would have to justify its assertion that the benefits were of equal value if the CRA questioned its approach.

Remember that the CRA has approved none of these approaches to the "not more advantageous" issue. Ultimately, it may need to provide guidance on how it will interpret "not more advantageous". An employer considering how to reward its key employees through a benefits package should obtain tax advice about how to do it in a way that's acceptable to the CRA.

On a final note, the CRA has confirmed that if all the employees in a business are key employees, the employer can't offer benefits to them through an ELHT.[21]

An employer's rights under the trust

An employer has only three rights under an ELHT. They are:[22]

- The right to designated employee benefits,
- The right to enforce covenants, warranties or similar provisions, and
- The right to prescribed payments.

[21] CRA Document 2011-0392641E5, dated October 3, 2011.

[22] ITA paragraph 144.1(2)(g).

The right to designated employee benefits

In many smaller businesses the shareholders are also employees. This provision lets shareholder/employees belong to their own ELHTs, and to include their spouses and family members as beneficiaries.[23] Without this rule, a shareholder/employee would be treated as an employer, and would be excluded from their own benefits plan.

The right to enforce covenants, warranties or similar provisions

The employer has the right to enforce covenants, warranties or similar provisions for two purposes. The first is to make sure that the trust is maintained as an ELHT.[24] If the trust is not maintained as an ELHT the employer can lose its deduction for the contributions it makes to the trust.

The second purpose is to make sure that the trust operates in a way that doesn't cause it to lose deductions under ITA paragraphs 144.1(3)(a) or (b). Under those paragraphs an ELHT loses the right to deduct the payment of designated employee benefits under ITA subsection 104(6) if it fails to satisfy all the requirements under ITA subsection 144.1(2),[25] or if it is operated or maintained primarily for the benefit of one or more key employees or their families.[26] While the ELHT's loss of deductions for its own failure to comply with the rules may not seem like the employer's problem, it could be if the ELHT becomes under financed as a result, and the employer has to make extra (possibly non-deductible) contributions so that employees continue to receive their benefits.

As we will consider soon, an employer's representatives cannot form a majority of the ELHT's trustees,[27] so an employer will not be able to use any control or influence it has over the trustees to make sure that the ELHT respects the rules. Instead, an employer will have to draft the trust document in a way that gives it enforceable promises from the trust to operate in conformity with the rules.

The right to prescribed payments

This provision refers to payments prescribed under Regulation 9500. So far, Regulation 9500 is the only regulation prescribed under ITA section 144.1.

Under Regulation 9500, prescribed payments are those made to either General Motors Canada Limited or to Chrysler Canada, Inc. by the ELHT established for the benefit of retired auto workers who are members of the then Canadian Auto Workers Union (CAW), now Unifor. The payments must be reasonable in the circumstances, paid for administrative services provided to the trust or trust beneficiaries, or as reimbursement for payments made on behalf of or in contemplation of the trust being established.

Why was a regulation passed specifically for one ELHT?[28] The reason lies in the financial crisis of 2008 and 2009. At the time, GM Canada's and Chrysler Canada's American parents were restructuring as part of their bankruptcy proceedings. One issue was each company's obligation to provide health and welfare benefits for their retired workers. Until their bankruptcies, GM and Chrysler had been responsible for funding those obligations themselves. Pursuant to the restructuring, they transferred responsibility for all present and future obligations to a "voluntary employees' beneficiary association" (VEBA) in exchange for a one-time cash payment to the VEBA.

[23] ITA subparagraph 144.1(2)(g)(i).

[24] ITA clause 144.1(2)(g)(ii)(A).

[25] ITA paragraph 144.1(3)(a).

[26] ITA paragraph 144.1(3)(b).

[27] ITA paragraph 144.1(2)(i).

[28] The following discussion relies generally on Harnum, James, "Courts Approve Retiree Settlement Providing for Participation in the First Prefunded Health Care Trust in Canada" in Plans & Trusts, January/February 2012, pp. 18-19.

A VEBA is authorized under §501(c)(9) of the Internal Revenue Code (IRC) to provide "life, sick, accident or other benefits" to its members, and to their dependents or designated beneficiaries. According to IRC §501(c)(9), a VEBA must meet the following requirements:

- It must be a voluntary association of employees;
- The organization must provide for payment of life, sick, accident or other similar benefits to members or their dependents or designated beneficiaries and substantially all of its operations are for this purpose; and
- Its earnings may not inure to the benefit of any private individual or shareholder other than through the payment of benefits described in (2) above.[29]

Membership in a VEBA is restricted to individuals who have a common economic bond, such as employees who have or had the same employer, or are members of the same union.[30] VEBAs are tax exempt organizations provided they meet all the qualifications for tax-exempt status.

At the time, there was no equivalent to a VEBA under the ITA. But the CAW wanted the same benefits for its retired members as the United Auto Workers Union had secured for its. The Canadian government proposed amendments to the ITA that ultimately became section 144.1 to facilitate a prefunding of retiree health care benefits for retired Canadian auto workers, similar to the arrangement negotiated in the United States. Since the agreement and obligation to fund the trust predated the passage of ITA section 144.1 into law, Regulation 9500 lets GM Canada and Chrysler Canada treat their contributions and provision of services as if the law had already been passed.

Prohibition against certain financial ties to the employer

An ELHT can't make a loan or investment in a participating employer or to a person or partnership with whom the participating employer does not deal at arm's length.[31] According to the Department of Finance's explanatory notes to ITA section 144.1, "This provision is intended to prevent trust capital from reverting, directly or indirectly, to an employer."[32] But this rule does not prevent the ELHT from accepting a promissory note in lieu of an employer contribution,[33] nor does it prevent an ELHT from accepting shares in the employer as an employer contribution (subject to the trustees' discretion).[34] Instead, it prevents the ELHT from lending or investing its own capital as a new investment in the employer.

Prohibition against employer representatives constituting a majority of trustees

ITA subparagraph 144.1(2)(i) prohibits an employer's representatives from forming a majority of an ELHT's trustees. Folio S2-F1-C1 requires only that an HWT's trustees be independent. We discuss this issue in our article "Health and Welfare Trusts", but CRA guidance allows employees to serve as an HWT's trustees, even if the CRA doubts their independence. The CRA says that an HWT trustee's independence is a question of fact.

[29] http://www.irs.gov/pub/irs-tege/eotopicf84.pdf.

[30] Ibid.

[31] ITA subparagraph 144.1(2)(h).

[32] Explanatory Notes, page 43.

[33] Ibid.

[34] Ibid.

Considering ELHTs, a representative could be, but does not have to be, an employee. A representative could also be a shareholder, partner or anyone with whom the employer does not deal at arm's length. A representative could also include members of the employer's legal, accounting or consulting firms. More generally, a representative could be anyone who could have a conflict of interest were they to serve as a trustee of an employer's ELHT, or anyone whom it's reasonable to think the employer could influence were that person or entity to become a trustee.

Although these prohibitions seem reasonable in the abstract, they could create problems. An employer creating an ELHT will probably want to rely on people whose expertise and integrity it trusts and respects. Typically, those people will have come from the ranks of those on whom the employer has previously relied.

Another problem is controlling costs. If an employer can use its own employees as trustees, rather than outsiders, it can control its costs better.

Winding up or reorganizing an ELHT

Winding up an ELHT means to end it in an orderly way. All its obligations are met, and any surplus funds are distributed. When an ELHT is reorganized, its assets may be transferred, for example to another ELHT. Under ITA paragraph 144.1(2)(b), only the following persons or entities can receive any money from the trust on a wind up or reorganization:

- Employees (current or former) or related persons, on a pro rata basis, but not key employees,[35]
- Another ELHT,[36] or
- After the death of the last of a current or former employee, spouse or related individual, Her Majesty in right of Canada or a province.[37]

It is interesting to note the priorities established in ITA paragraph 144.1(2)(b):

- Key employees may not participate in a wind up or reorganization.
- Provincial governments and the federal government participate last, though there is no stated priority if there is a competing claim between governments.
- To the extent that they participate in a wind up or reorganization, living beneficiaries participate *pro rata*.

There is no order of priorities established between the living beneficiaries, as a group, and another ELHT. Presumably, the living beneficiaries' interests under the ELHT that is being wound up or reorganized would be protected in the new ELHT to which funds are going, but that may not always be the case. There is no mention of money being able to flow to a participating employer, nor is there any mention of money being paid to the estates of any beneficiaries. Another explanation is that the legislation contemplates ELHT property going to an ELHT only on a reorganization, and to the other category of beneficiaries only on a wind up.

[35] ITA subparagraph 144.1(2)(b)(i).

[36] ITA subparagraph 144.1(2)(b)(ii).

[37] ITA subparagraph 144.1(2)(b)(iii).

An HWT is subject to different rules on a wind up or reorganization. Folio S2-F1-C1 and CRA guidance prohibit payments to an employer for any reason, or to employees or their spouses and dependents for any purpose other than as health and welfare benefits. Instead, the CRA lets the trust document name a charity to receive proceeds on a wind up, so that an HWT may end in a way that benefits neither the employer nor the employees, but still distributes the trust's money and allows it to end.

The need for a similar provision to be adopted with ELHTs is less urgent, because of the specific distribution options. Nevertheless, a provision to distribute trust proceeds on a wind up to a charity after the last living trust beneficiary has died, instead of to a provincial government or to the federal government, could be a beneficial alternative.

Tax consequences on a wind up

For employees and employers

Any payment to an employee, spouse or related person on a wind up or reorganization will not be treated as a designated employee benefit.[38] Instead, the distribution will be treated as income to the employee, and will not be deductible to the trust. This should produce a fair tax result where the employer has received a deduction for all its contributions to the trust, because those contributions will not be distributed as tax-free health and welfare benefits.

It may not seem fair where the employer has not been able to claim a deduction or where the employee has had to include the employer's contribution in income. For example, where the employer has made contributions for benefits that extend beyond the current tax year, no deduction is allowed until the tax year for which the contributions should have been made. If the trust is wound up or reorganized before then, the trust will be distributing money that will be taxable in the employees' hands, but for which the employer never received a deduction. Nothing in ITA section 144.1 deals with this potential for double taxation.

Nor does this provision contemplate the double taxation that results from the employee having to treat distributions as income when an employer contribution was treated as taxable income to the employee under ITA paragraph 6(1)(e.1). Again, there is no provision in the ITA that deals with this issue.

Where employees have contributed their own money to an ELHT to pay for benefits like disability income insurance (the insurance benefit is tax-free if funded entirely by employee contributions), ITA section 107.1 deals with the potential for double taxation. Subsection 107.1(a) says that when an ELHT distributes property to an employee who has an interest in that property, the ELHT is deemed to have disposed of the property for proceeds equal to the property's fair market value, and the employee is deemed to have acquired that property at fair market value.[39] ITA subsection 107.1(c) then deems the employee to have received proceeds equal to the property's adjusted cost base.

ITA subsections 107.1(a) and (c) force an employee to recognize any unrealized capital gains or losses in the property in the year the property is transferred. If there are no capital gains or losses, the employee receives the distribution with the property's adjusted cost base equal to its fair market value, leaving the employee with no tax consequences to report.

[38] ITA paragraph 56(1)(z.2).

[39] ITA paragraphs 107.1(a)(i) and (ii).

For an ELHT

ITA paragraph 144.1(11)(b) says that ELHT distributions paid to any person are taxable, except distributions paid to an ELHT that is a beneficiary of the ELHT paying the distribution. But ITA subparagraph 144.1(2)(b)(ii) does not require the recipient ELHT to be a beneficiary in order for it to receive a distribution from another ELHT on a wind up or reorganization. While an ELHT may receive money from another ELHT, the payment will be taxable unless the recipient ELHT is a beneficiary of the ELHT that is being wound up or reorganized.

Residency requirements

An ELHT must be resident in Canada, as determined by the ordinary rules of residency, not by the deemed residency rules contained in ITA section 94.[40] The ordinary rules of residency determine whether a trust is resident in Canada and therefore subject to Canada's income tax system. The deemed residency rules in ITA section 94 deem a trust to be resident in Canada for certain purposes, even if it would not be under the ordinary rules. The most recent judicial guidance from the Supreme Court of Canada on the ordinary rules of residency is *Garron Family Trust (Trustee of) v. R.*[41]

In *Garron*, the Supreme Court of Canada adopted the central management and control theory to determine whether a trust is resident in Canada. Two trusts were settled in St. Vincent (a Caribbean island). The trustee was a corporation resident in Barbados, and the beneficiaries were residents of Canada. The trustee disposed of trust-owned capital property located in Canada, and had to remit withholding tax. It sought a refund, asserting that it was not a Canadian resident (because the trustee was not resident in Canada), and therefore was not liable to pay Canadian tax. Significantly, Barbados does not levy taxes on capital gains.[42] If the trustee's arguments had succeeded, the trust's Canadian property, beneficially owned for Canadian residents, could have been sold for a capital gain without any tax owing.

The Supreme Court of Canada disagreed with the trustee's position. It said that a trust resides "where 'its real business is carried on,... which is where the central management and control of the trust actually takes place." The trial judge had found that the main beneficiaries in Canada carried out the central management and control of the trust from Canada. The trustee merely carried out those beneficiaries' instructions. Since Canada was the country from which the trust was controlled, the trust was resident in Canada, even though its trustee was resident in Barbados.

If an ELHT becomes a non-resident of Canada, it will continue to be a trust, but will cease to qualify as an ELHT. Its property will be deemed to have been disposed of for fair market value, with a cost base of nil.[43] The result will be a taxable gain for the trust.

Contrast with residency rules for HWTs

The residency rules governing an HWT are different from those governing an ELHT. An HWT may be established in a foreign country, and may be a non-resident trust. We discuss the advantages and disadvantages of having an HWT resident outside Canada in our article "Health and Welfare Trusts". As noted above, an offshore HWT is a red flag to the CRA that the trust may be used to avoid paying taxes.

[40] ITA paragraph 144.1(2)(c).

[41] 2012 SCC 14, April 12, 2012.

[42] Barbados Revenue Authority, http://barbados.gov.bb/bra/pages/itg.aspx.

[43] ITA paragraph 128.1(4)(b.1).

Enforcing trust provisions

The original draft legislation contained a provision similar to that governing HWTs: "[T]he trust has a legal right to enforce payment of contributions to the trust."[44]

This provision was removed from the version of the legislation that became law. Still, nothing prevents an ELHT from having such a provision; it's just not a requirement for the trust to gain and maintain ELHT status.

Employer's bankruptcy or insolvency

Although an ELHT depends on the employer for funding, an employer's bankruptcy will not result in the trust losing its status as an ELHT, provided it meets all the requirements in subsection 144.1(2).[45] Still, unless the trust has been funded in advance with enough money to allow it to maintain its obligations into the future, the trust probably won't be able to provide benefits for long after the employer becomes bankrupt or insolvent.

Key employees

Unlike HWTs, ELHTs distinguish between key and non-key employees. Commenting on an earlier draft of the legislation than the one which became law, the Department of Finance said:[46]

> *Paragraph [144.1(2)](d) requires, in general terms, that the trust be maintained primarily for the benefit of beneficiaries who are not key employees.*
>
> *Paragraph [144.1(2)](e) requires, in general terms, that key employees who are beneficiaries of an ELHT be treated the same way as a significant proportion of the non-key employee beneficiaries under the ELHT....*

The wording in the sections referred to above was changed in the legislation that became law, but the legislative intent towards key employees has remained the same.

Under ITA subsection 144.1(1), the definition section, there are two tests for determining whether an employee is a key employee:

a. Income, or

b. Status as a "specified employee"

Satisfying either definition will lead to the employee being defined as a key employee for the tax year. The parties must revisit the question each year to determine whether any non-key employees have become key employees, and whether any key employees no longer qualify for as key employees.

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[44] Early draft of ITA paragraph 144.1(2)(h).

[45] CRA Document 2011-0419811E5, dated February 13, 2012. This decision contemplated both single and multi-employer trusts.

[46] Employee Life and Health Trust – Explanatory Notes, page 7. This is a different document than the Department of Finance's Explanatory Notes, referred to above.

Income test for key employee status

A key employee is someone whose employment income was, in any two of the five taxation years preceding the year, more than 5 times the Year's Maximum Pensionable Earnings (YMPE) for the calendar year in which the employment income was earned. So, in the 2016 tax year, you look at years 2011 – 2015 inclusive. If in any two of the years 2011 through 2015 the employee's employment income exceeded 5 times the YMPE for those years, that person is a key employee.

The term, "employment income" is not defined in the ITA. For most people, "employment income" means salary. But key employees often have additional components to their incomes like bonuses, dividends, stock options, car allowances, and the like. Will the CRA use "total income", "net income" or "taxable income", or will it calculate employment income the same way the Canada Pension Plan calculates earnings for purposes of determining an individual's YMPE? We will have to wait and see how the CRA treats this term.

The following chart sets out the employment income thresholds:

Year	YMPE	5 times YMPE
2016	$54,900	$274,500
2015	$53,600	$268,000
2014	$52,500	$262,500
2013	$51,100	$255,500
2012	$50,100	$250,500
2011	$48,300	$241,500

Source: Canada Revenue Agency, http://www.cra-arc.gc.ca/tx/rgstrd/papspapar-fefespfer/lmts-eng.html

For example, if an employee's employment income was $260,000 in each of 2011 and 2012, that employee would be treated as a key employee for the 2016 tax year, even if their employment income never went above $260,000 from 2013 through 2015 inclusive and even though $260,000 is less than 5 times the YMPE for the years 2013 through 2015 inclusive.[47]

"Specified employee" test for key employee status

The second test is more complicated. Regardless of income, if an employee is a "specified employee", they are a key employee.

ITA subsection 248(1) defines the term, "specified employee" as either an employee who does not deal at arm's length with the employer, or as an employee who is a "specified shareholder" (also a defined term). We'll deal with specified shareholders first.

[47] ITA paragraph 144.1(1)(b), c.f. "key employee".

Specified shareholders

A “specified shareholder” is someone who owns, directly or indirectly, at any time in the year, 10% or more of the issued shares of any class of the capital stock of a corporation or any corporation related to the corporation.[48] Control of the corporation does not matter. The words, “directly or indirectly” mean that a person does not need to own their shares outright to be a “specified shareholder”. The ITA describes four ways in which a person could indirectly own shares in a corporation and still be a “specified shareholder”, provided their ownership interest amounted to 10% or more:

Corporate ownership. If a person or corporation with whom the individual does not deal at arm’s length owns shares in the corporation, like a relative or a different corporation that the individual controls, the individual will be treated as a specified shareholder.[49]

Trust ownership. If the individual is a beneficiary of a trust that owns shares in the corporation, that individual will be treated as owning those shares personally in proportion to their interest in the trust.[50] This rule applies even if the individual’s rights to a share of trust income or capital depend on the trustee’s exercise of or failure to exercise any discretionary power.[51]

Partnership ownership. If the individual is a partner in a partnership that owns shares in the corporation, that individual will be treated as owning those shares personally in proportion to that person’s interest in the partnership.[52]

Personal services business (PSB) ownership. A PSB exists where a person has their own corporation provide their services to a business where it would be natural for the person to be employed directly by the business.[53] If the person may be entitled directly or indirectly to 10% or more of their own corporation’s shares, that person is a specified shareholder.[54]

Non arms’ length persons

Persons who do not deal at arm’s length with their employer can also be key employees. Persons do not deal at arm’s length when they are related by blood, marriage, common law partnership or adoption.[55] A blood relationship exists where one person is the child or descendant of the other, or where they are brothers or sisters of each other.[56]

Persons do not deal at arm’s length with corporations they control, or if they are related to an individual who controls the corporation.[57] The CRA has published guidance on what constitutes control of a corporation.[58] Since any employee owning 10% or more of a corporation’s shares would be a key employee under the “specified shareholder” rule, the question of control in a non-arm’s length situation will not often arise.

[48] ITA subsection 248(1), c.f. “specified shareholder”.

[49] ITA paragraph 248(1)(a), c.f. “specified shareholder”.

[50] ITA paragraph 248(1)(b), c.f. “specified shareholder”.

[51] ITA paragraph 248(1)(e), c.f. “specified shareholder”.

[52] ITA paragraph 248(1)(c), c.f. “specified shareholder”.

[53] ITA subsection 125(7). Individuals create PSBs in the expectation that the combined corporate and personal taxes they pay will be less than the tax they would pay if they were employed directly. The ITA and the CRA discourage the use of PSBs by removing many valuable tax advantages from the corporation, thereby forcing it to be taxed at higher rates.

[54] ITA paragraph 248(1)(d), c.f. “specified shareholder”.

[55] ITA paragraphs 251(1)(a) and (2)(a).

[56] ITA subsection 251(6).

[57] ITA subparagraphs 251(2)(b)(i) and(iii).

[58] IT-64R4 – Corporations: Association and Control [Consolidated], dated October 13, 2004.

Still, it's worth noting that someone can control a corporation with fewer than 50% of the company's shares. For example, a minority shareholder may have superior expertise and experience in the business. Other shareholders may defer to that shareholder to such an extent that he or she could routinely count on their support, and effectively control the corporation.

In other cases a minority shareholder could own the largest block of shares, with the rest of the shares widely distributed among a large number of small shareholders. If such a shareholder could routinely influence enough shareholders to vote with them, and get over 50% of the vote, that shareholder would again be treated as controlling the company. It would not matter that each time the shareholder could be persuading different groups to vote with them, as long as the shareholder could routinely expect to get their way.

Someone could also control a corporation while owning none of the corporation's shares, if they controlled corporations that in turn owned shares in the subject corporation.

Further, if a group of people controls a corporation, and if everyone in the group is related to each other, then no one in the group deals with the corporation at arm's length.[59] A group is a related group where each member of the group is related to the others by blood, marriage, common law partnership or adoption.[60]

Appendix A includes charts that summarize the key employee definitions. The CRA also publishes guidance that discusses the meaning of non-arm's length relationships.[61]

Tax treatment

Tax treatment for the ELHT

Like an HWT, an ELHT is an *inter vivos* trust. We discuss the tax issues common to inter vivos trusts in our article "Health and Welfare Trusts". Those rules are:

- The trust's tax year ends on December 31 of each year.
- The trust is taxed on net income at the highest personal tax rate.
- The trust may not claim any personal tax credits.
- The trust may claim deductions for:
  - Expenses related to the normal operation of the trust, including administrative functions,
  - The cost of providing benefits, including the payment of insurance premiums, and
  - Expenses incurred to earn trust income (such as investment management and advisory fees).

59 ITA subparagraphs 251(2)(b)(ii) and (iii).

60 ITA subsection 251(2).

61 S1-F5-C1: "Related persons and dealing at arm's length", last updated May 4, 2014.

An ELHT is also subject to other tax rules specified in ITA section 144.1:

- Amounts paid as designated employee benefits are deductible.[62] This tax treatment differs from that afforded to HWTs. An HWT may deduct the payment of a benefit to an employee unless the benefit is payable from the proceeds of an insurance policy.[63]
- An ELHT has a non-capital loss where its expenses exceed its income. The ELHT may carry such a loss back or forward for three years.[64] The three year loss carry-back rule is the same as the general rule, but the ELHT carry-forward rule differs from the usual 20-year loss carry-forward rule.
- The definition of an ELHT exempts it from the tax treatment afforded to employee benefit plans,[65] retirement compensation arrangements,[66] and salary deferral arrangements.[67]
- The following rules do not apply to an ELHT:
  - The 21-year deemed disposition rule.[68]
  - The alternate minimum tax rules.[69]
  - The reversionary trust rules in ITA subsection 75(2).[70]

An ELHT can lose its right to deduct expenses for the tax year if it fails to qualify as an ELHT at any time during the year, for example by failing to satisfy a provision in ITA subsection 144.1(2),[71] or if it operates or is maintained primarily for the benefit of one or more key employees or their family members.[72] ITA paragraph 144.1(3)(b) adopts the definition of an employee's family members (ITA clauses 144.1(2)(d)(ii)(A) and (B)) to define a key employee's family members. However, there is currently no guidance as to what the phrase, "primarily for the benefit of" means. We will need to wait for the CRA to provide guidance on this point.

It's important to note that the denial of deductibility is permanent for the tax year. The trust can also lose its right to carry forward or back any losses incurred during the year.[73] Even if the ELHT is offside for a short time during the year, it loses its right to ELHT tax treatment for the entire year. Given the potential severity of the consequences, it's worth noting that ITA section 144.1 contains no saving or grace provisions that could allow the CRA to forgive minor or technical breaches that cause no substantial harm. We will need to wait to see if the CRA provides guidance on how it will deal with such issues.

In the absence of CRA guidance on this point, there are considerable risks for an employer. If an ELHT is a flow through trust, in that only enough money is contributed to provide benefits, or where the employer's contributions are only enough to buy insurance policies and pay the trustee's fees, a loss of deductibility could force the employer to pay extra, non-deductible, contributions.

[62] ITA paragraph 104(6)(a.4).
[63] Folio S2-F1-C1: Health and Welfare Trusts, para. 1.46.
[64] ITA subsections 144.1(13) and 111(7.3 to 7.5).
[65] ITA paragraph 248(1), c.f. "employee benefit plan", (a).
[66] ITA paragraph 248(1), c.f. "retirement compensation arrangement", (f.1).
[67] ITA paragraph 248(1), c.f. "salary deferral arrangement", (f.1).
[68] ITA paragraph 108(1) "trust" (a).
[69] ITA paragraph 127.55(f)(iv).
[70] ITA sections 75-75.2, subsection 75(3), and paragraph 108(1)(a.1).
[71] ITA paragraph 144.1(3)(a).
[72] ITA paragraph 144.1(3)(b).
[73] ITA subsection 111(7.5).

Tax treatment for employers

Employers may deduct the contributions they make to an ELHT pursuant to ITA subsections 144.1(4) – (7). Those subsections deal with the deductibility of employer contributions, actuarial determinations, multi-employer plans, and the maximum amounts deductible – essentially the cost of providing benefits where the employer retains the insurance risk.[74] The ITA also imposes a general reasonableness standard on deductions.[75]

Employers may also deduct ELHT contributions that pay for insurance coverage in the year or prior year to provide designated employee benefits.[76] Contributions used to provide insurance coverage for a later year or years are not deductible until the year in which the benefit is provided.[77] An exception is allowed for insurance premiums paid for group term life insurance. An employer may prepay those premiums and deduct the entire prepaid amount in the year the contribution is made.[78]

While the right to prepay premiums and deduct them in the same year may seem like a benefit for the employer, it's important to remember that employees must include the cost of group term life insurance in their income for the year the premium is paid.[79] The more an employer prepays, the more the employee must include in income.

Further, employers may deduct ELHT contributions that provide designated employee benefits to employees, their spouses or dependents.[80] Instead of paying insurance premiums or establishing a fund large enough to pay anticipated claims, the employer could pay benefits as claims arose, using the ELHT as a conduit.

Even after considering the rules governing what an employer may or may not deduct, there is still a limit on the total amount than an employer may deduct: total ELHT contributions in the current and preceding year minus all amounts deducted in the preceding tax year relating to ELHT contributions.[81] According to the Department of Finance:

> *This rule is intended to prevent an employer from attempting to claim a deduction in the later years of a pre-funded ELHT in respect of amounts related to inflation, income earned by the trust or to higher than anticipated benefit payments which are facilitated by strong investment performance within the trust.*[82]

The Department gives an example of an ELHT that expects to be in existence for 50 years, and expects to pay $50 million in benefits during the first 13 years of its existence. The employer funds it in year 1 with $50 million. During the ELHT's first 13 years, as the $50 million is paid out in benefits, the employer will be able to deduct what the ELHT pays out in each tax year. The trust expects that the money needed to pay the remaining 37 years of benefits will come from growth on the initial $50 million contribution. The employer will not be able to deduct the payment of any designated employee benefit that comes from this investment growth.

While this provision will prevent an employer from benefitting early from its contributions, other types of benefits, like premium holidays that an insurance company may offer to compensate for differences in actual versus projected claims experience, are not captured by this rule.

[74] The ITA does not provide a straight line to a deduction. ITA section 18 denies a deduction for any employer expenses, subject to a list of exceptions. More specifically, ITA paragraph 18(1)(o.3) denies a deduction for an employer contribution to an ELHT, except those deductions allowed under ITA paragraph 20(1)(s). That paragraph lets an employer deduct amounts paid to an ELHT trustee under ITA subsections 144.1(4-7).

[75] ITA section 67.

[76] ITA subparagraph 144.1(4)(a)(i). Premiums must be paid to an insurance company licensed in Canada or a province.

[77] ITA paragraph 144.1(4)(b).

[78] The types of premiums for which a deduction may be claimed are described in ITA clause 18(9)(a)(iii)(B), while the right to the deduction is set out in ITA clause 144.1(4)(a)(ii)(A).

[79] ITA subsection 6(4).

[80] ITA clause 144.1(4)(a)(ii)(B).

[81] ITA subsection 144.1(7).

[82] Explanatory notes, page 45.

We discussed earlier in this article the prohibition against an ELHT lending money to an employer or investing in employer securities (or in the securities of related companies). But an employer may still issue a promissory note to the ELHT as evidence of the employer's outstanding obligation to make contributions.[83] But a promissory note will not be treated as a trust contribution,[84] so the employer will not be able to deduct anything just for having lent money to the trust.

For the ELHT, the employer's interest payments on the promissory note cannot be treated as trust income under the accrual rules in ITA section 12. Liability under ITA section 12 would depend on how principal and interest payments were structured.

The employer will have to treat repayments of interest and principal on the promissory note as contributions to the trust, governed by the rules covering contributions, not as a repayment of principal and interest.[85] As a result, the employer will not be able to deduct interest on the note under ITA paragraph 20(1)(c) because it won't be able to characterize any part of those payments as interest.

On a final note, if the trust was an ELHT when a promissory note was issued, it's deemed to still be an ELHT whenever the employer pays anything on the promissory note.[86]

Tax treatment for employees

Employer contributions to an ELHT are not taxable to employees if they are used to pay for benefits under a PHSP.[87] Employer contributions used to pay for group term life insurance premiums are taxable to employees.[88] Employer contributions used to pay for GSAIP benefits are taxable to employees if the benefits are paid from those contributions are tax-free. This means that employer contributions used to provide benefits like critical illness insurance (CII), income-style long term care insurance (LTCI) and accidental death or dismemberment (ADD) insurance will be taxable to employees, as long as the benefits from such plans are tax-free.

Employer contributions used to pay for disability income insurance will remain tax-free because the benefits paid from such plans are taxable if the employer has paid any part of the premium, and if the benefits are paid on a periodic basis.[89] An employee can ask their employer to contribute their retiring allowance to their ELHT, but the employer will be required to withhold tax on the contribution. The retiring allowance is treated as income received by the employee under ITA subparagraph 56(1)(a)(ii), and then contributed to the ELHT.[90]

Taxation of contributions made to provide CII, ADD and income-style LTCI benefits may not make much of a practical difference in some plans. While many employers continue to offer core benefits (with or without some form of cost sharing with their employees), some are moving to offer "non-core" benefits like CII, LTCI and ADD on a voluntary basis. Employees may choose which non-core benefits they want from a menu of available benefits, and pay for those benefits themselves. Apart from the cost savings to employers from having employees pay for their own benefits, there is a tax advantage for employees who pay for at least one benefit, disability income insurance, themselves: they receive disability income insurance benefits tax-free.[91]

83 ITA subsection 144.1(8).

84 ITA paragraph 144.1(8)(a).

85 ITA paragraph 144.1(8)(b).

86 ITA subsection 144.1(9).

87 In Quebec employees must report the cost of their benefits as income, but only on the provincial tax return.

88 ITA subsection 6(4).

89 ITA paragraph 6(1)(f).

90 CRA Document 2012-0467221E5, dated March 21, 2013.

91 Ibid.

An employee could also make contributions to an ELHT that would pay for benefits under a PHSP. This feature allows employees to treat their contributions as medical expenses, for which they may be able to claim a medical expense tax credit. We compare the tax outcomes from having the employer or employee pay PHSP premiums in our article "Private Health Services Plans".

If employees are the only ones contributing to an ELHT (for example, disability income insurance plans where plan benefits are to be paid tax-free) the ELHT must be worded to make sure that the trust qualifies as an insurance plan. As an alternative, the ELHT could purchase group or individual insurance policies for the employees, with contributions being used to pay insurance premiums. If the CRA concludes that the plan is just a contingency fund lacking the required elements of insurance, the trust will fail to qualify as an ELHT.[92]

The general rule for payments from an ELHT is that all payments are treated as income unless an exception applies.[93] There are several exceptions. The most important is that designated employee benefits are paid tax-free[94] unless included in income for another reason (such as disability income insurance payments under ITA paragraph 6(1)(f)).

Employees would also pay tax on payments of residual surplus from the trust on a wind up or reorganization under ITA subparagraph 144.1(2)(b)(i).

If the beneficiary were a non-resident, an ELHT payment will not be subject to non-resident withholding tax under ITA Part XIII to the extent that it is a payment of a designated employee benefit.[95] Any other payments could be taxable, and would be subject to 25% withholding tax. These would include payments to employees on a wind-up or reorganization. It's uncertain how the payment to a non-resident of taxable designated employee benefits, like disability income payments, which may be taxable under ITA paragraph 6(1)(f), would be treated.

Multi-employer plans

In some industries, like construction, an employee can belong to one union but have many employers. Rather than belong to many different ELHTs, employees can belong to one ELHT that their employers collectively contribute to. Employer contributions to such ELHTs are deductible where the following three sets of conditions all apply:

- It's reasonable to expect that:
  - At no time in the year will more than 95% of the trust beneficiaries be employed by a single employer or by a group of related employers,[96] and
    - At least 15 employers will contribute to the trust for the year, or
    - At least 10% of the employees who are beneficiaries of the trust will be employed by more than one employer (all employers who are related to each other will be deemed to be one employer),[97]

[92] CRA Document 2010-0374891E5, dated March 14, 2011.

[93] ITA subsection 144.1(11).

[94] ITA paragraph 144.1(11)(a).

[95] ITA paragraph 212(1)(w).

[96] ITA subparagraph 144.1(6)(a)(i).

[97] ITA subparagraph 144.1(6)(a)(ii).

- Employers contribute to the trust under a collective bargaining agreement and according to a negotiated contribution formula that does not provide for any variation in contributions by reference to the trust's financial experience,[98] and
- An employer's contributions are determined in whole or in part by reference to the number of hours worked by each individual employee, or by another measure that is specific to each employee for whom contributions are to be made.[99]

An ELHT that administers benefits for employees of more than one employer, and receives contributions for employees of more than one employer, can elect to be treated as more than one separate trust.[100] The trustee must designate in an election that property from an employer that is to be held separately is to be held in a separate trust for the benefit of specific beneficiaries. The trustee must make its election on or before the filing due date of the first tax year of the separate trust.[101] Upon making the election, and under the terms of the trust, contributions from the employer and the income derived from those contributions will accrue solely for the benefit of those beneficiaries.[102]

Conversions and rollovers of property between ELHTs and HWTs

In our article "Health and Welfare Trusts", we discuss CRA and Department of Finance guidance about the future of HWTs. Neither the CRA nor the Department of Finance appear ready to abolish HWTs, and an employer may establish an HWT instead of an ELHT. Two questions arise from the CRA's and the Department's decision to preserve HWTs:

- Can an employer convert from an HWT to an ELHT, and vice versa?
- Can an employer roll over property on a tax-free basis from an HWT to an ELHT, and vice versa?

The answer to both questions is "probably not".

There is no specific section in the ITA, nor is there any CRA guidance, that lets you convert an HWT to an ELHT, or vice versa, or transfer assets from one to the other tax-free. It's possible that the CRA would view an attempted conversion of an HWT to an ELHT as creating a new trust. If so, the CRA could then view any funding of the ELHT using assets from the HWT as an impermissible distribution of the HWT's assets.

Nor is a rollover a likely possibility. ITA section 107.1 permits a rollover of property from an ELHT to an ELHT trust beneficiary, but the range of permissible ELHT beneficiaries does not include an HWT.[103] Nor is there any CRA guidance authorizing the distribution of HWT property in any way except as employee benefits.

The CRA has said that it is possible to roll over assets from one HWT to another HWT on a tax-free basis if the differences between the trusts are administrative, and if there is no change in beneficial ownership.[104] It is not yet clear whether the CRA will apply this reasoning to a contemplated transfer of assets between HWTs and ELHTs or vice versa. Given the different tax treatments to which HWTs and ELHTs are subject, it may be difficult to say that no change in beneficial ownership occurs as the result of an attempted rollover of assets.

[98] ITA paragraph 144.1(6)(b).

[99] ITA paragraph 144.1(6)(c).

[100] ITA subsection 144.1(12).

[101] ITA paragraph 144.1(12)(a).

[102] ITA paragraph 144.1(12)(b).

[103] ITA paragraph 144.1(11)(b).

[104] See the definition of "disposition" in ITA paragraph 248(1)(e), and CRA Document 9412855, dated August 5, 1994.

Health insurance policies allowed in an ELHT

Both HWTs and ELHTs may offer benefits authorized under ITA subparagraph 6(1)(a)(i). To the extent that a health insurance policy conforms to the requirements of that subparagraph, an ELHT should be able to offer it. Since the same rule applies to an HWT, the CRA's guidance developed to deal with allowable products in an HWT should also apply to an ELHT. We discuss this guidance in our article "Health and Welfare Trusts".

Conclusion

ELHTs offer an alternative to HWTs that may appeal to some employers. Large employers, and employers with unionized workforces, may find the certainty of an ELHT's rules appealing, and may not find the restrictions associated with key employees particularly troublesome. Smaller employers may find the key employee rules too burdensome, and may disregard ELHTs in favour of HWTs.

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Appendix A

An ELHT beneficiary can be:

1. **a current, deceased or former employee, or an employee who is employed by a business that the employer has acquired,**

OR

2. **an employer's spouse or common law partner (same or opposite sex),**

OR

3. **someone who is related to the employee by blood, marriage, common law partnership or adoption, and is either**
   a. a member of the employee's household, or
   b. someone who depends on the employee for support.

Note: "related by blood" means that one person is the child or descendant of the other or that the persons are brothers or sisters of each other.

A key employee is:

1. **an employee who earned more than 5 times the Year's Maximum Pensionable Earnings in any 2 of the 5 years preceding the current tax year,**

OR

2. **a specified employee.**

Year	YMPE	5 times YMPE
2016	$54,900	$274,500
2015	$53,600	$268,000
2014	$52,500	$262,500
2013	$51,100	$255,500
2012	$50,100	$250,500
2011	$48,300	$241,500

A specified employee includes a specified shareholder.

A specified shareholder is someone who owns, directly or indirectly, 10% or more of any class of the employer's issued shares or of a corporation related to the employer.

Directly or indirectly means:

1. **through a partnership,**
2. **through another corporation,**
3. **through a trust,**
4. **through a personal services business, or**
5. **through a person or entity that owns the shares and doesn't deal with the shareholder at arm's length.**

A specified employee also includes an employee who does not deal at arm's length with the employer.

Persons do not deal at arm's length with people to whom they are related by:

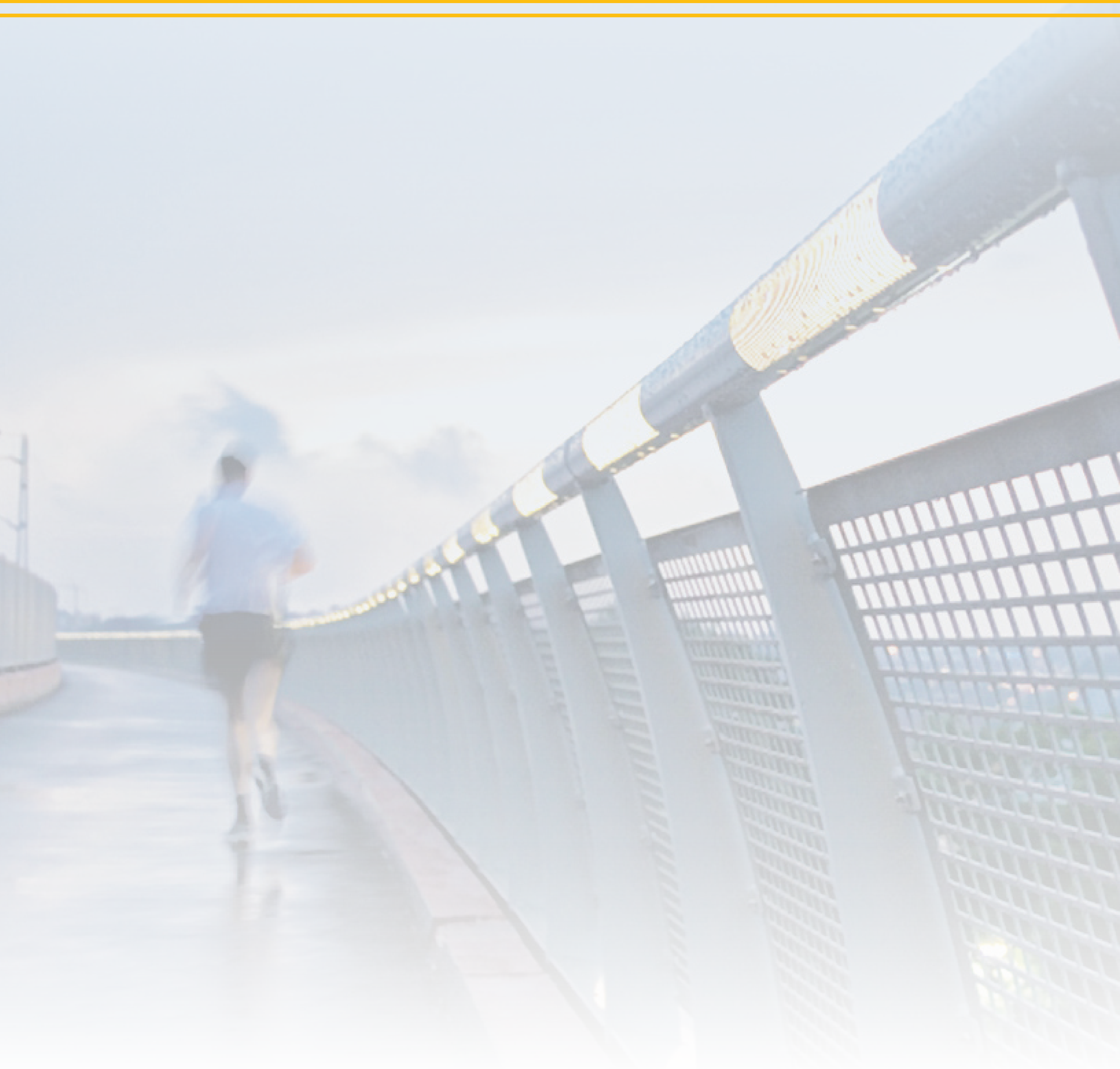
1. **blood,**
2. **marriage,**
3. **common law partnership, or**
4. **adoption.**

Corporations do not deal at arm's length with people or groups who

1. **control the corporation, or**
2. **are related to people or groups who control the corporation.**

Note: "related by blood" means that one person is the child or descendant of the other or that the persons are brothers or sisters of each other.

Note: it isn't necessary to own 50% of a corporation's shares plus 1 to control a corporation. See IT-64R4 Corporations: Association and Control for the various ways the CRA asserts that someone can control a corporation without owning a majority of shares..



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