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Tax Alert — Canada

Deadline to convert Health and Welfare Trusts to Employee Life and Health Trusts is imminent

The Canada Revenue Agency's (CRA) existing administrative rules with respect to Health and Welfare Trusts (HWTs) are only effective until 31 December 2021.

It is important that existing HWTs consider their options to minimize their exposure to adverse tax consequences now.

Background

HWTs are vehicles for providing health and welfare benefits to employees. The tax treatment of HWTs is not set out in the *Income Tax Act* (the Act), but the CRA has published guidance over the years setting out administrative rules for HWTs. Employee Life and Health Trusts (ELHTs) are also established to provide health and welfare benefits to employees, but unlike HWTs, the Act sets out the tax treatment of aspects of ELHTs.

The 2018 federal budget originally announced that the CRA would no longer apply its administrative rules with respect to HWTs after the end of 2020. On 27 November 2020, the Department of Finance released draft legislative proposals for ELHTs. At the same time, the CRA and the Department of Finance announced a one-year extension in the application of those rules and that the CRA would apply its administrative rules with respect to HWTs until 31 December 2021. Various transitional rules were also proposed.

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Transitional rules

On 29 June 2021, transitional measures (with some modifications since their previous release as part of the 27 November 2020 draft legislative proposals referred to above) relating to the discontinuation of the administrative positions of the CRA on HWTs, as well as other measures concerning ELHTs, received Royal Assent and became law. These transitional measures are intended to facilitate the conversion of certain existing HWTs into ELHTs by extending the application of the ELHT rules to trusts created before 2010 and permitting existing HWTs to convert to ELHTs without any adverse tax implications by amending the trust terms. The transitional measures also permit certain collectively bargained HWTs to elect to be deemed ELHTs until 31 December 2022 if certain conditions are met. HWTs that elect to be deemed ELHTs will need to convert to ELHTs by amending the trust terms by 31 December 2022. See EY Tax Alert 2021 Issue No. 24, *Budget implementation bill receives Royal Assent*.

Implications

An HWT that converts to or elects to be deemed an ELHT is required to notify the CRA in a prescribed form that it has become an ELHT at the time of the election or otherwise no later than the trust's first filing due date after 2021.

However, HWTs that do not convert to ELHTs by the end of 2021 (or by the end of 2022, for HWTs that have elected to be deemed ELHTs) will be subject to the existing tax rules that apply to *inter vivos* trusts. This generally means that the trust would be subject to tax at the highest marginal tax rate, but would not be able to claim the deductions that are available to trusts that qualify as ELHTs.

Learn more

For more information, please contact your EY or EY Law advisor or one of the following professionals:

Toronto

Uros Karadzic
+1 416 943 2087 |
uros.karadzic@ca.ey.com

Lawrence Levin
+1 416 943 3364 |
lawrence.levin@ca.ey.com

Viktoria Maguire
+1 416 941 1891 |
viktoria.maguire@ca.ey.com

Caitlin Morin
+1 416 943 3133 |
caitlin.morin@ca.ey.com

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