Johnstone's Journal

JOHNSTONE'S JOURNAL is published monthly, and designed to provide topical information of interest not only to plan administrators, but to all employees who enjoy coverage under the benefit plan. Feel free to make copies, and use as a payroll stuffer.

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Tax Changes to Short- and Long-Term Disability Plans

New Rules from the Canada Revenue Agency

CRA Changes to Taxable Disability Benefits

A change by the Canada Revenue Agency (CRA) will affect the way taxable disability benefit payments are calculated. This change applies only to insured short-term and long-term disability benefits that are already taxable.

For disability contracts that are currently set up as taxable, starting Jan 1, 2015, the CRA will require income tax to be deducted from disability benefit payments as they are issued to claimants throughout the year. Currently, the CRA allows tax to be paid with the filing of a claimant's annual income tax return–tax deductions do not need to be taken from disability benefit payments when they are issued.

If an employee is currently receiving disability payments on a taxable benefit plan, they will be notified of any change directly by the insurer.

Each insurer may phase this change in differently, but it appears many will apply the change as follows:

- For new disability claimants, tax will be deducted from disability benefit payments beginning October 2014.
- For employees currently on claim and receiving taxable disability payments, the change will be phased in from October through December this year. If an existing claimant already has tax deducted from their disability benefit payments, an adjustment to the amount of tax deducted may be required. Existing claimants will be notified directly if a change is required.

Is Your Group Disability Benefit Taxable?

In most cases, group disability benefit premiums are paid 100% by employees, and if they receive a disability payment, it is tax-free.

Whether group disability payments are taxable or not depends on who pays (or is deemed to pay) the premiums.

If the employee pays (through payroll deduction) 100% of the premiums for short or long term disability benefits, then CRA considers any disability income benefits payments made to the employee to be non-taxable income and need not be declared as income. On the other hand, if the employer pays any part of the disability premium, then any disability income payment received by the employee is considered taxable income and the insurance carrier will issue a T4A.

The tax status of group disability plans is declared to the insurer when the benefit is offered to the employee, and is written into the contract. For this reason, employers should review how they manage their disability contributions and understand the implications of the method elected.

For more information, see tax bulletin IT-428 .

The Benefit of Cost Sharing

We know employees place a high value on the benefits component of their total compensation package. When they share in the cost of their benefits, they tend to appreciate the value of those benefits even more.

In many cases, employers share the cost of benefits as a percentage. For example, an employer may only cover 50% of the cost of the entire benefit package (which is generally the minimum requirement set by insurers). Through payroll deductions, employees would cover the difference. In situations where the employee portion does not cover the total cost of the disability premium, it is important for employers to understand and manage the implications and their employee's expectations. For more on this, see the August 2012 *Journal* "Managing Taxable Benefits."

We suggest employers review their current cost sharing structure and the tax status of their disability benefit plan to ensure premiums and payroll deductions are set up correctly. If you have any questions or would like to review your current cost sharing arrangements, give us a call.