

Taxation of disability insurance plans

Structure	Personally-owned disability insurance policy	Personally-owned disability insurance policy structured as an employee benefit ¹	Grouped individual disability insurance policies ¹	Overhead expense policy
Description	An individual owns and pays for a disability insurance policy (including self-employed owners of an unincorporated business).	An individual owns a disability insurance policy and his/her employer pays the premium.	A group of individual disability insurance policies owned and paid for by the employer with benefits payable to the employee (e.g. wage loss replacement plan).	A business owns and pays the premium for a disability insurance policy covering overhead expenses.
Deductibility of premium	The premium is treated as personal or living expenses for income tax purposes and is not deductible.	The premium cost is deductible to the employer as a salary expense.	The premium cost is deductible as an expense to the employer.	The premium for overhead expense coverage is deductible as a business expense regardless of whether the business is incorporated or not.
Tax treatment of premium payment for insured individual	Not applicable	The premium paid by the employer on an employee-owned policy must be included in the employee's income as a taxable employee benefit.	Properly implemented, the arrangement is considered a group sickness or accident insurance plan for income tax purposes. ² The premium payment will not be included in the employee's income as an employee benefit. ³	Not applicable
Taxation of benefits	Disability benefits received are not taxable.	Disability benefits received are not taxable.	Disability benefits received by the employee are taxable. ³ If the employee pays a portion of the premium, the benefits reportable are reduced by the amount of any premium paid by the employee.	Disability insurance benefits payable in the event of a claim are taxable. In turn, the benefits received are used to pay expenses which are deductible as business expenses.

¹ If one or more insured persons are both shareholders and employees, this summary assumes coverage is provided to the insured(s) in their capacity as employees, not shareholders. Canada Revenue Agency presumes the benefit is received as a shareholder unless there is evidence to the contrary.

² Policies that include return-of-premium benefits may or may not qualify for inclusion in a group sickness or accident insurance plan. If the policy does not qualify, the employer-paid premium will be considered a taxable employee benefit.

³ As a result of 2012 federal budget, effective for coverage after 2012, employer-paid premium for an accidental death and dismemberment rider will be considered a taxable employee benefit. Consequently, the accidental death and dismemberment benefit is not taxable.

Canada Revenue Agency and Revenu Quebec have not provided a formal ruling about the tax treatment of return-of-premium benefits that are included in an individual disability insurance policy. The tax treatment of optional return-of-premium benefits is subject to interpretation.

The tax information provided here is for general information only. It should not be relied upon as providing legal or tax advice. Clients are encouraged to consult with their own professional tax and/or legal advisor about their particular circumstances.