

MEMO FOR 2% OR MORE S CORPORATION SHAREHOLDERS

IMPORTANT NEW IRS REQUIREMENTS RELATED TO THE TREATMENT OF HEALTH INSURANCE PREMIUMS

Pursuant to IRS Notice 2008-1:

For purposes of this memo "health insurance" includes premiums paid for health, dental, vision, long-term care and HSA contributions made by the corporation on behalf of the 2% or more shareholder (and any payments made on behalf of related parties e.g. spouse and children of 2% shareholder).

This notice states that eligible health insurance for an S corp can either be through a plan in the S corp's name or through an individual plan held by the shareholder, as long as premiums for the individual plan are either paid directly to the insurance company through the S corp or if the premiums are paid by the shareholder, the S corp must reimburse the shareholder. (Thus, in effect, the health insurance policy is being adopted by the S corp). If payments are paid on a personal policy directly by the shareholder and not reimbursed to the shareholder by the S corp, these payments are NOT eligible for deduction on Form 1040 Individual Income Tax Return as Self-Employed Health Insurance Premiums.

In addition, for 2% or more S corporation shareholders to deduct their health insurance premiums on their Forms 1040, this notice requires the health insurance premiums to be included within the shareholder's W-2.

The "health insurance" payments are included in wages for income tax withholding purposes only and are NOT wages subject to Social Security, Medicare taxes or Federal Unemployment Wages. (Note - 2% or more S corporation shareholders are NOT eligible for Section 125 plans thus these "health insurance" payments do not qualify for exclusion from taxable wages.)

W-2 Preparation:

Box 1 (Wages) - include health insurance payments

Box 3 (Social Security Wages) - do NOT include health insurance payments

Box 5 (Medicare wages) - do NOT include health insurance payments

Box 14 (other) - identify amounts paid for health ins premiums (including dental and eye) as **2%HI**, identify employer HSA contributions for 2% or more shareholders as **2%HSA** & identify amounts paid for long term care premiums as **LTC**.

Form 941 Preparation:

Box 2 (Wages) - include health insurance payments

Box 5a (Social Security) & 5c (Medicare Wages) - do NOT include health insurance payments

Form 940 Preparation:

Box 3 (Total Payments to all employees) - include health insurance payments

Box 4 (Payments exempt from FUTA tax) - include health insurance payments

Form UCT-6 Preparation:

Box 2 (Gross Wages) - do not include health insurance payments

Payroll Service Companies:

If you are using a payroll company to prepare your payroll, we recommend you contact them immediately and notify them that you qualify as a 2% or more shareholder and are not eligible under Section 125 to exclude health insurance/fringe benefits from taxable income. Please provide them with information regarding health insurance premiums paid on your behalf by the S corporation to ensure correct treatment.

TREATMENT OF PERSONAL AUTO USE

The Personal use of company automobiles is a taxable fringe benefit that should be included within an employee's compensation (W-2). Please contact our office to assist in calculating each employee's personal use for inclusion in 4th Quarter and year-end payroll tax returns. This benefit is subject to Income Tax Withholding, Social Security, Medicare and Federal Unemployment taxes.