

December 2018

As we come to the end of another year, we want to remind you of the reporting method required for deducting the cost of health insurance premiums and/or health savings account (HSA) payments paid by an S corporation on behalf of its more-than-2% shareholders. This includes health insurance and/or Medicare premiums paid by, and then reimbursed to, its more than 2% shareholders during the calendar year.

Please keep in mind that certain family members are treated as if they own each other's stock for purposes of determining who is treated as a more-than-2% shareholder. This rule attributes a shareholder's stock ownership to his/her spouse, parent, child and grandchild. Accordingly, if the S corporation employs any of these family members of its shareholders, these rules may apply to those family members even if they do not own more than 2%, or any, of the stock themselves.

For each applicable shareholder/employee, the total of the above payments made during the calendar year should be included as Federal Taxable Wages in their Form W-2, as well as the Company's final Employer's payroll tax report for the year. These payments are NOT subject to Medicare or Social Security FICA taxes, so the payments should NOT be included in Medicare or Social Security taxable wages on either the W-2 or payroll report.

Since the payments are added to W-2 wages, the shareholder/employee is taxed on these payments on their personal return. However, the shareholder/employee will also subtract the same amount as a "page 1" deduction on the appropriate line of their Form 1040; so the net tax effect may be zero. Please be sure to inform each shareholder/employee about the health insurance/HSA payments included in their W-2 taxable wages by reporting this amount in the W-2 box 14 so they will also know to take an offsetting deduction for the same amount.

For those more-than-2% shareholder/employees who are covered by Medicare or a personal health insurance plan, the S corporation must reimburse the shareholder for the cost of those premiums by the end of the year in order for those premiums to be eligible for reporting and deducting as qualifying employer provided health insurance for the current year.

\*In order for the shareholder/employee to be able to deduct the health insurance premiums and/or HSA payments paid by the corporation for the shareholder/employee and zero out the net tax effect, that shareholder/employee must also be paid cash wages by the S corporation during the year at least equal to the amount of health insurance premiums and HSA payments.

Please let us know if you need our help with, or have any questions on, the proper reporting of these payments.

Sincerely,

StraderHallett PS