

S Corporation Shareholders,

The IRS has recently clarified its position as to the deductibility of health insurance premiums for S Corporation shareholders. In Notice 2008-1, the IRS clarifies that health insurance costs are deductible for S Corporation shareholders, subject to the following rules:

1. The health insurance policy is either in the Corporation's name or the shareholder's name.
2. The Corporation makes the premium payments directly to the insurance agency or, if the shareholder makes the premium payments, the shareholder provides proof of payment to the Corporation and is reimbursed by the Corporation in the current tax year.
3. The Corporation must report the amount of the premiums paid or reimbursed in box 1 of the shareholder's W-2. These additional wages are subject to withholding taxes, but not Social Security or Medicare taxes. The amount of health insurance premiums paid will be specified in box 14 of the W-2.
4. The shareholder must report the premium payments or reimbursements from the Corporation as gross income on his or her Form 1040.

This does not apply to shareholders whose health insurance is covered by their spouse in a business unrelated to the Corporation.

Illustrative Examples:

EXAMPLE 1: In 2008, John obtains an accident and health insurance policy in his name and makes the premium payments on the policy. The S Corporation makes no payments or reimbursements with respect to the premiums. A plan providing medical care for John is NOT established by the S Corporation and John is NOT entitled to the deduction.

EXAMPLE 2: In 2008, Doug obtains an accident and health insurance policy in his name. Doug makes the premium payments to the insurance company and furnishes proof of premium payment to the S corporation. The S Corporation then reimburses Doug for the premium payments. The S Corporation reports the amount of the premium reimbursements as wages on Doug's form W-2 for 2008 and Doug reports that amount as gross income on form 1040 for 2008. A plan providing medical care for Doug has been established by the S Corporation and Doug is entitled to the deduction.

If this applies to your Corporation, you must report your premiums paid or reimbursed to your payroll provider. If we are currently handling your payroll needs, call us as soon as possible so we can properly report your required information.

Make sure you don't miss out on your health insurance deduction! Noncompliance with any of the above rules will render you ineligible. Please feel free to contact us if you have any questions or concerns about this matter.

Best regards,

A handwritten signature in black ink that reads "Jack M. Burke". The signature is written in a cursive style with a large initial "J" and a distinct "B".

Jack M. Burke, CPA, MBT