



**November 2017**

## Update: 2018 Health Insurance for S Corporation Owners

If you operate your business as an S corporation, you continue to enjoy good news in 2018 when it comes to your health insurance.

And that good news also applies to your 2017 taxes.

You first have to thank the 21st Century Cures Act for:

1. Reinstating and extending IRS Notice 2015-17 to eliminate the \$100-a-day penalty through December 31, 2016—and this gives new life for 2017 and 2018, as we explain
2. Creating the QSEHRA that can work very well if you have employees in your S corporation

In this article, we give you the ins and outs of what you need to do in 2017 and 2018 with your S corporation to ensure your health insurance deductions and also avoid the \$100-a-day penalties for violating the rules of the Affordable Care Act.

### ***Good News***

The good news is, the old rules still apply as we write this, and we don't expect any changes in 2017 or 2018. The S corporation first establishes a health insurance plan for the owner in one of two ways:<sup>1</sup>

1. The S corporation makes the premium payments for the accident and health insurance policy covering the owner-employee who has more than 2 percent ownership (and his or her spouse or dependents, if applicable).
2. The owner-employee who has more than 2 percent ownership makes the premium payments to the insurance company and furnishes proof of the premium payments to the S corporation, which in turn reimburses the owner-employee for the premium payments.

**This is Step 1**—get the cost of the insurance on the S corporation's books.

**In Step 2**, the S corporation has to include the health insurance premiums on the owner-employee's W-2 form. The income is not subject to payroll taxes (Social Security and Medicare). In other words, the S corporation includes the additional compensation in box 1 of the W-2 but not in boxes 3 or 5.<sup>2</sup>

**In Step 3**, you (the owner-employee with ownership of more than 2 percent of your S corporation) claim the health insurance deduction on page 1 of Form 1040, providing you otherwise qualify for that page 1 deduction, as we explain below.

## ***Beware—Two Hurdles***

To claim the self-employed health insurance deduction on page 1 of Form 1040, you need to watch out for two things:

1. **Second employer insurance for you or your spouse.** You cannot take this insurance deduction if you or your spouse is eligible for employer-subsidized health insurance. Thus, if your spouse can get family health insurance as a tax-advantaged fringe benefit through his or her employer, you lose your eligibility for this deduction—even if your spouse does not actually accept the employer-sponsored insurance.<sup>3</sup>
2. **Salary.** Your deduction for the insurance premiums cannot exceed the amount of your salary from the S corporation.<sup>4</sup>

## ***Examples***

**Example 1.** You are the sole owner of your S corporation, you obtain an accident and health insurance policy in your name, and you pay the premium payments on the policy. The S corporation makes no payments or reimbursements with respect to the premiums.

The S corporation did not establish a medical care plan for you; therefore, you are not entitled to the self-employed health insurance deduction.<sup>5</sup>

**Example 2.** You are the sole owner of your S corporation. You obtain an accident and health insurance policy in your name, and you pay the premium payments on the policy. You submit proof of the premium payments to your S corporation. The S corporation then reimburses you for the premium payments and reports the amount of the premium reimbursements as wages on your W-2.

The S corporation established the medical plan, and you qualify to deduct the insurance premiums included on your W-2 as self-employed health insurance on page 1 of Form 1040.<sup>6</sup>

## ***Small Employer's Rank-and-File Employees and the New QSEHRA***

As a small employer, your S corporation does not have to provide any health insurance benefits to its employees. "Small employer" for this purpose means a business with fewer than 50 full-time employees or full-time equivalents.<sup>7</sup>

But when you do offer medical benefits to employees who are not S corporation owners, you face the \$100-a-day penalty for doing things wrong. The big no-no is reimbursing employees for individually purchased health insurance.

But you can reimburse your employees for at least some of their individually purchased health insurance when you use the new qualified small employer health reimbursement arrangement (QSEHRA).

For details on how the QSEHRA works, see [Announcing NEW Tax-Deductible Penalty-Free Health Plans for Small Businesses](#).

**Good news.** As you will see in the QSEHRA article, you need to give written notice of the plan. The good news is that the IRS in Notice 2017-20 says that you are not required to furnish the initial written QSEHRA notice to eligible employees until after further guidance has been issued by the Treasury and the IRS.<sup>8</sup> That further guidance, when issued, will specify a deadline no earlier than 90 days following issuance of that guidance.

**Do it now.** If you are planning on using the QSEHRA with your employees, get that 2018 plan in place now, before the new notice rules come into play.

### ***Note This***

You can have the S corporation reimburse the owners for individually purchased insurance, and you face no penalties. But reimburse rank-and-file employees for individually purchased insurance without use of the QSEHRA, and you face the \$100-a-day penalty for each employee (\$36,500 a year per employee).

If you want to provide health benefits to employees through the S corporation, there are many tax-advantaged ways to do so. Your S corporation treats the benefits to non-owner employees just as any other business would. To get an idea of how your S corporation can offer employee health benefits under the Affordable Care Act without using the new QSEHRA, see [Small Employer Health Care under Obamacare](#).

### ***Group Insurance and You***



Suppose your S corporation provides group health insurance to all employees, including you, an employee-owner. The S corporation must treat you differently from the way it treats non-owner employees. Here's how this works:

- **Non-owner employees.** The S corporation deducts its contributions to the insurance plan,<sup>9</sup> and non-owner employees receive the health benefits tax-free.<sup>10</sup>
- **Owner-employees.** You and the S corporation follow the three-step deduction process described above. The S corporation completes step 1 when it purchases the group insurance. The S corporation treats your group insurance benefit as W-2 compensation to you (step 2), which you then deduct using the self-employed health insurance deduction (step 3).<sup>11</sup>

## ***Discrimination***

Currently, the IRS does not enforce any nondiscrimination provisions of the Affordable Care Act.<sup>12</sup> That means you and your S corporation can still legally discriminate without the threat of Affordable Care Act penalties. For example, you can

- have your S corporation buy health insurance for you and nothing for the rank-and-file employees, or
- have the S corporation reimburse you for your individual insurance plan and have a separate group plan for the rank-and-file employees.

## ***Premium Tax Credit and Your Deduction***

If you purchased your individual insurance through the government's health insurance marketplace (federal marketplace or state exchange), you can combine the individual premium tax credit (government subsidy for health insurance) with your self-employed health insurance deduction. But when you calculate that deduction, you need to consider the tax credit.<sup>13</sup>

## ***Are Changes Coming?***

Yes. The government agencies, including the IRS, are slowly providing us with additional rules for implementing the Affordable Care Act.



We don't yet have the full and final picture of how these rules will work. The IRS has promised future guidance (likely new rules) on both of the following topics:

- Discrimination under the Affordable Care Act<sup>14</sup>
- S corporation owner health insurance deductions<sup>15</sup>

For now, you can follow the rules as described in this article. The IRS has said that it will give us time to implement changes, and generally, that means any changes will become effective with your next tax year.

## **Takeaways**

The good news is that your 2017 and 2018 S corporation health insurance treatments continue as before. Your S corporation's health insurance plan can cover you and your spouse, dependents, and children under age 27.

But remember that you qualify for the self-employed health insurance deduction only if you go through all the IRS-required steps. This is easy. You simply

1. make the S corporation pay for your insurance premiums, either directly or through reimbursement to you;
2. have the S corporation include the health insurance as wages on your W-2; and
3. deduct the cost of the premiums using the self-employed health insurance deduction on Form 1040.

As for the rank-and-file employees, don't reimburse any individually purchased policies. You can use the QSEHRA, which can enable a limited amount of reimbursements for individually purchased insurance and other medical costs. Alternatively, you can use group insurance as a benefit for the non-owner employees.

**New Feature: Client Letter on This Article for Use by Tax Pros, [Click Here](#).**

**Share this entire article with a friend**



- 1 Notice 2008-1.
  - 2 See How to Escape Payroll Taxes on S Corporation Health Insurance.
  - 3 IRC Section 162(l)(2)(B).
  - 4 IRC Section 162(l)(5).
  - 5 Notice 2008-1.
  - 6 Ibid.
  - 7 IRC Section 4980H(c)(2), which defines a large employer as having 50 or more employees.
  - 8 Notice 2017-20.
  - 9 IRC Section 162(a); Reg. Section 1.162-10(a).
  - 10 IRC Section 105(b).
  - 11 Notice 2008-1.
  - 12 Notice 2011-1.
  - 13 Rev. Proc. 2014-41.
  - 14 Ibid.
  - 15 Notice 2015-17.
- 

