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for December 2015*

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Rules for Deducting Health Care Costs — by Diane DeClercq

For many years, businesses have paid health insurance premiums for their employees. The IRS extends a deduction for this expense. There are rules and conditions on this deduction, as well as a new wrinkle in the tax code that needs to be considered.

Limited Partnerships and Corporations.

In addition to employee premiums, businesses may deduct health insurance premiums for partners and key shareholders. A liability company, or "C" corporation that pays for its partner/owners' health insurance can deduct the expense as guaranteed payments.

An "S" corporation can also deduct the expense for shareholders holding more than 2 percent of the stock. However, the shareholder must report the premiums paid by the corporation as income from the business. And then, deduct any premiums reported as income from the business as paid individually under the self-employed health insurance deduction rules on their individual 1040.

Sole Proprietors.

If you operate as a sole proprietorship, you can deduct health insurance costs for you, your spouse and children under the age of 27, even if they are not living with you or are not your dependents. The insur-

ance policy can be in your name or the business name if you file Schedule C, C-EZ or F to report your income. To take a deduction, report the premiums paid on Line 29 of Form 1040. Your "out of pocket" medical expenses, if over 10% of your AGI is listed on Schedule A, under "Itemized Deductions".

Employer Payment Arrangements and the new wrinkle.

Sometimes the employer pays the premium on behalf of the employee. However, according to the IRS and Department of Labor, under the new market reform provision, this is not allowed. There are some



complex alternatives under a limited-purpose Section 105 medical reimbursement plan or tax-preferred Premium Reimbursement Arrangement or Healthcare Reimbursement Plan (HRP). These require assistance from a qualified benefits or insurance administrator to make sure the plan is in compliance.

Or, Employers can offer the following Acceptable Alternatives:

1. Provide a tax free fringe benefit by purchasing an Affordable Care Act approved employer sponsored group plan. Small employers with 50 or fewer employees can provide a group plan through the SHOP Marketplace, a public health insurance exchange for small businesses. Starting in 2016, employers with more than 50 employees will be subject to penalties if they do not offer group coverage to employees.
2. Set up a traditional group Cafeteria Plan for pretax funding of the employee portion of the premium (saving both income and FICA taxes for the employee, and payroll taxes for the employer).
3. Employer can simply pay the employee additional compensation without any requirement that the amount be used for insurance premiums. The employee must be free to do with the extra compensation whatever they choose.

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