



Interact With Your Accountant

Memorandum

To: Clients, Associates & Friends of Pro@ctive CPA

Form: Mark L. Wyssbrod, Managing Member

Date: October 15, 2013

Re: S-corporation Reporting Requirements Reminder

The Internal Revenue Service (IRS) has been targeting S-corporations for a number of years in very specific areas. The rules and regulations have been around for several decades; however, in December 2007 the IRS issued IRS Notice 2008-1. I believe this notice affirmed the IRS's intention to begin enforcing the S-corporation rules and regulations which S-corporations have become out of the practice of following.

After 5 years of IRS communications their intentions, we have noticed an increase in paper-work requested for S-corporation tax audits by the IRS. What are the items the IRS is targeting above and beyond the financial information? Is your company prepared to pass an audit?

- Certain employee benefits need to be added to S-corporation owner's W-2
 - For owner's who own greater than 2% of an s-corporation:
 - Should report the following items on their W-2 if they want a tax benefit:
 - Health insurance premiums (for individual)
 - Dental insurance premiums (for individual)
 - Vision insurance premiums (for individual)
 - Long-term care insurance premiums (for individual)
 - How do I report the insurance premiums?
 - Generally speaking:
 - If the benefits are offered to all employees:
 - Add premiums to taxable income (box 1)
 - Add to information box (box 14)
 - Add premiums to state taxable income (box 15)
 - If the benefits are not offered to all employees:
 - Add premiums to:
 - Taxable income (box1)
 - Social Security income (box 3)
 - Pay the increase in Social Security taxes and add to box 4
 - Medicare income (box 5)
 - Pay the increase in Medicare taxes and add to box 6
 - Add to information box (box 14)
 - Add premiums to state taxable income (box 15)

- IRS Notice 2008-1
 - Under IRS Notice 2008-1, S corporation shareholders may deduct premiums paid for themselves, their spouses and their dependents if:
 1. A two-percent or greater shareholder has earned income from the S corporation exceeding the total of all premiums paid;
 2. The shareholder is not eligible to participate in any subsidized health plan maintained by the shareholder's or a spouse's employer;
 3. The S corporation includes the premium cost in the shareholder's Form W-2;
 4. The shareholder includes the premium cost in gross income on Form 1040;
 5. If the S Corporation reimburses the premiums, it must be in the same tax year.
 - Whether the policy is in the individual's or S corporation's name or who initially pays for the premiums are not the determining factors.
- S-corporation owner compensation
 - Is your officer compensation to distributions reasonable?
 - Zero wages (i.e. no W-2) can lead to the IRS telling you what your wages should be
 - Officer compensation needs to be “reasonable”
 - Officer wages should be the same or greater than distributions
 - Officer wages should equal the same salary a third-party employer would have to pay an employee to retain their service
- S-corporation documentation
 - S-corporation should document all related party loans
 - Including, but not limited to:
 - Loans to shareholder
 - Loans from shareholder
 - Loan documents generally include:
 - Borrower
 - Lender
 - Amount
 - Interest rate
 - Terms
 - Collateral

- Distributions
 - Generally, a board meeting should occur, a distribution amount should be voted upon, and the meeting and results should be documented
 - The IRS states this is a corporate issue (i.e. Coke has similar process before a distribution) and without these actions the cash outflow cannot be “distributions” since distributions are voted upon and documented.
 - The IRS states these cash outflow are not loans or advances, because loans and advances are documented
 - **So what are they?**
 - *The IRS classifies the distributions as compensation, subject to Social Security and Medicare*
- S-corporation ownership rules
 - Generally speaking:
 - A domestic (US) company
 - No more than 100 owners
 - Owners are individuals
 - Certain trusts, non-profits and estate can qualify
 - Owners cannot be non-resident aliens
 - Each owner must consent to the treatment (initially)
 - Only one class of stock can be issued
 - Tax year is calendar year
 - **Where do s-corporations go wrong?**
 - S-corporation treat ownership as a partnership with profits and losses instead of the single class of ownership rule
- General Businesses
 - Review structure of employee benefit rules
 - The Health Care Act has changed the discrimination rules and testing
 - You should hire an employee plan expert (not health insurance agent) to review and update your employee benefit plans
 - **Prepare written documentation for employee benefit plans**
 - **Without a documented plan there is no benefit allowed**
 - Hold annual corporate meeting and update minutes
 - Review (or create) business plan and strategy
 - Set up or change retirement plan type
 - Calculate cash flow projections and financial forecasts
 - Review financial position and working capital requirements



In conclusion, S-corporation rules and regulations can be complicated. Be certain to review your documentation and incorporate best practices. Please contact your Pro@ctive CPA team should you have any questions at (770) 664-8583. We wish you the best for the rest of the year and the beginning of your Holiday Season!

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