Tax Facts:

Business Entities and Tax-Advantaged Accounts

Working for yourself has incredible benefits, one of which is the ability to make your own schedule. However, with freedom comes responsibility.

Healthcare costs are no joke. Paying for your own medical costs can get expensive fast. Luckily, tax-advantaged accounts are here to help. Contributing to a tax-advantaged account can help you offset taxes along with other advantages like tax deferred savings and tax-free withdrawals on qualified medical expenses.

Contributing to a tax-advantaged account

Type of Business	Contribution Guidelines
Sole Proprietor/Single Member LLC	As a sole proprietor, the IRS states you are not eligible to contribute to an FSA. You can contribute to an HSA, but the contributions need to be made after-tax. Since you file taxes on your personal tax return, you're able to deduct some of your contributions on your personal income tax return. As long as you made a profit during the tax year, you can file the deduction. You can't just put more in your HSA account than your net self-employment income. You would contribute after-tax dollars to your HSA account and then do a line item deduction in your tax forms. To make sure you're doing everything right, it's best to consult a tax professional on these matters.
LLCs taxed as Partnership *This means that all owners take responsibility for transactions, debt and taxes from the business*	As an LLC taxed as a partnership, you're going to treat your FSA and HSA contribution limitations the same as a sole proprietor. If you have employees, however, you may be able to implement a "cafeteria" or "section 125" plan that can allow them to make pre-tax contributions. However, you, as the owner, can't participate. Owners cannot participate at all in an FSA and **employers cannot make contributions pre-tax to an LLC member's HSA account**. LLC members are not considered employees of the LLC, therefore they cannot participate in a Section 125 pre-tax plan. If an HSA is offered on a post-tax basis outside of a cafeteria plan, then a member may participate. That means whatever you contribute towards your HSA account will reduce your adjusted gross income. Just like a sole proprietor, you can only claim this deduction if you actually made a profit.

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LLCs taxed as a Corporation (C-Corp) *Entity is taxed as its own entity and retains its own profits and losses.*	LLCs that are taxed as partnerships aren't allowed to consider members employees, but LLCs taxed as corporations (C-Corps) are. LLCs taxed as a C-Corp may consider the LLC member as an employee. LLC's taxed as a corporation (C-Corp) may make contributions pre-tax to an LLC member's FSA or HSA account. Keep in mind that those members would most likely be considered highly-compensated employees, so there may be nondiscrimination issues if non-highly compensated individuals are not also receiving the same contributions. If HSA account contributions are made on an after-tax basis, then Section 125 restrictions would not apply. However, comparability rules WOULD apply. The comparability requirements essentially require employers to make comparable contributions to their employee's HSA accounts, either by comparable dollar amounts or a percentage.
LLCs taxed as a Corporation (S-Corp) *Entity isn't taxed. Instead, the shareholders are taxed.*	Any owner who owns >2% is ineligible to participate in a cafeteria plan or any pre-tax contributions. Anyone in this designation is considered an "owner" from an IRS perspective and as such must make HSA account contributions on a post-tax basis and receive the tax benefit at the end of the year. **Owners are ineligible to participate in an FSA.** It is also important to note that if a shareholder owns more than 2% then their spouse, children, parents and grandparents who are also employed by the business are also ineligible to participate in a cafeteria plan.

Regardless of the structure of the LLC, members can always make their own HSA account contributions on an after-tax basis and take the amount contributed as a deduction on their own individual tax return. We suggest consulting a tax advisor concerning this type of contribution.

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