

Group Term Life Insurance Tax Issues

Internal Revenue Code (IRC) Section 79 generally allows an employer to provide each of its employees up to \$50,000 in tax-free group term life insurance coverage. The cost of the first \$50,000 in employer-provided group term life insurance coverage is excludable from the employee's income. Without the protections of Section 79, employees would pay federal income tax on the cost of this life insurance coverage.

Under IRC Section 79, employees are taxed on the "cost" of group term life insurance coverage in excess of \$50,000, to the extent that the "cost" exceeds the individual employee's own contributions. "Cost" for this purpose generally is NOT based on the rate the employer pays for the coverage, but on the so-called "Table I" rates set by the IRS. These Table I rates appear in IRS regulations, and the IRS cannot revise them without issuing new regulations.

This *Employee Benefits Alert* is a reminder of the mandatory year-end payroll reporting requirements with regard to the taxation of group term life insurance. If your group plan provides life insurance coverage over \$50,000 for any employee or if your group plan discriminates in favor of officers or owners, you will need to pay special attention to the attached information and comply by December 31, 2003.

The Table I rates, FICA, and related information for 2003 are shown below:

Table I Rates for Group Term Life Insurance
Monthly Cost/\$1,000 of Coverage

<u>5-Year Age Bracket*</u>	<u>Rates</u>
Under 25	\$0.05
25-29	.06
30-34	.08
35-39	.09
40-44	.10
45-49	.15
50-54	.23
55-59	.43
60-64	.66
65-69	1.27
70 and over	2.06

* Employee's age on the last day of the calendar year.

Note that if an employee is covered by more than one group term life plan, the coverages are aggregated so that the employee may not exclude the cost of more than \$50,000 in coverage for the year.

Group Term Life Insurance Tax Issues (continued)

Discriminatory Schedule of Benefits

If your group life insurance schedule of benefits discriminates in favor of officers and owners, the greater of the Table I cost or the actual cost of the full amount of insurance should be reported on the affected employees' W-2 as taxable income. ("Affected employees" will be certain officers and owners. Non-officers and non-owners will not be impacted.) "Actual cost" for this purpose may not be the composite rate employers typically pay, but must be related to the employee's age.

A schedule that provides the same amount of coverage for all employees would not be considered discriminatory. Similarly, a life insurance schedule that provides the same multiple of earnings for all employees would not be discriminatory. However, providing a higher multiple of earnings to employees who are officers or owners would be considered discriminatory.

Dependent Life Insurance

The cost of employer-provided dependent term life insurance, if the benefit is more than \$2,000, is to be treated as imputed income to the employee and reported on the W-2. The Table I rates for the dependents' ages are to be used in calculating the amount of income to the employee. If the benefit provided is \$2,000 or less, its cost (generally regarded as a "de minimis fringe benefit") is not usually taxable income to the employee.

FICA Tax

FICA (Social Security) tax applies to the cost of group term life insurance coverage to the same extent that income tax applies. Therefore, FICA taxes are payable on any life insurance costs that are included on W-2 forms for income tax purposes. For 2003, the Social Security tax rate is 6.20% on annual pay up to \$87,000. The Medicare tax rate is 1.45% on all pay, without a maximum limit.

The information provided above is summarized for your convenience and is not intended as legal advice. We encourage you to consult with your tax and legal advisors for answers to specific questions.

U.S. Benefit Office Locations

Benefits Brokerage & Consulting Services Rx Purchasing Coalition HR Consulting Data Analysis Benefits Administration Retirement Services
Predictive Modeling Call Center Services Voluntary Benefits Consumer Driven Healthcare Legislative & Compliance International Benefits

Anchorage, AK
(907) 562-2266

Eugene, OR
(541) 687-2222

Naples, FL
(239) 514-2542

St. Louis, MO
(314) 721-8400

Atlanta, GA
(404) 224-5000

Florham Park, NJ
(973) 410-1022

Nashville, TN
(615) 872-3700

San Diego, CA
(619) 297-7111

Baltimore, MD
(410) 527-1200

Ft. Worth, TX
(817) 335-2115

New Orleans, LA
(504) 581-6151

San Francisco, CA
(415) 981-0600

Birmingham, AL
(205) 871-3871

Greenville, SC
(864) 232-9999

New York, NY
(212) 344-8888

San Jose, CA
(408) 452-7555

Boston, MA
(617) 437-6900

Knoxville, TN
(865) 588-8101

Orange County, CA
(714) 953-9521

Seattle, WA
(206) 386-7400

Cary, NC
(919) 459-3000

Lexington, KY
(859) 223-1925

Orlando, FL
(407) 302-4972

Tampa, FL
(813) 281-2095

Charlotte, NC
(704) 376-9161

Los Angeles, CA
(818) 548-7500

Philadelphia, PA
(610) 964-8700

Washington, DC
(301) 530-5050

Chicago, IL
(312) 621-4700

Louisville, KY
(502) 499-1891

Phoenix, AZ
(602) 787-6000

Wichita, KS
(316) 264-5311

Cleveland, OH
(216) 861-9100

Miami, FL
(305) 373-8761

Portland, OR
(503) 224-4155

Wilmington, DE
(302) 477-9640

Columbus, OH
(614) 766-8900

Milwaukee, WI
(414) 271-9800

Raleigh, NC
(919) 459-3000

Dallas, TX
(972) 385-9800

Mobile, AL
(251) 433-0441

Rochester, NH
(603) 332-5800

Detroit, MI
(248) 735-7580

Minneapolis, MN
(763) 302-7100

Roswell, NM
(505) 317-3397