

TAXABLE INCOME ON IMPUTED PREMIUMS FOR PRE-RETIREMENT DEATH BENEFITS FOR 2024 (ERS)

Internal Revenue Code (IRC) Section 79 requires each employer to report imputed premiums on the cost of group-term life insurance provided directly or indirectly for their employees to the extent that it exceeds \$50,000. For purposes of IRC Section 79, the computation of taxable income on imputed premiums for group-term life insurance should include: (1) the Pre-Retirement Death Benefit and (2) any additional group-term life insurance provided to your employees.

- (1) The **Pre-Retirement Death Benefit (PRDB)** is considered group-term life insurance for purposes of IRC Section 79. The PRDB is equal to the salary on which the member made retirement contributions for the previous FISCAL year (**October 1, 2022 - September 30, 2023**). The computation of taxable income on imputed premiums on PRDB should include the annual salary for the prior fiscal year on all employees who have at least one year of contributing membership service (including retirement eligible members) and are not participating in the Deferred Retirement Option Program (DROP). When computing the imputed premiums, it is inappropriate to include those employees who are either (1) in their first year of employment or (2) participating in DROP, since neither one is eligible for the PRDB (see Note A.)
 - a) **"Transfer Employees"**: Those employees who transferred to your unit during the year from another unit or agency participating in either the Teachers' or Employees' Retirement System will be considered to have uninterrupted retirement membership, and therefore will not be considered to be in their first year of employment. Caution must be taken in computing the PRDB on employees who transferred to your unit during the current calendar year from another unit or agency participating in the Teachers' or Employees' Retirement System. For "transfer employees", use the salary for the previous fiscal year (information may need to be obtained from the previous employer) to compute the imputed premium for the number of months in the current calendar year the employee worked for your agency. The previous employer is responsible for computing the PRDB for the number of months in the current calendar year the employee worked for the previous employer.
 - b) **"Terminated Employees"**: If your agency is not computing the imputed premiums each payroll period, it is important to compute the imputed premiums on those employees who terminate service with your agency at the time of termination (retirement, transfer, or general termination of employment). This is necessary to withhold the required taxes on the taxable income from imputed premiums from the final payroll check
- (2) If your unit furnished (paid) additional group-term life insurance to your employees, this also must be included in the computation of taxable income from imputed premiums on group-term life insurance.

The imputed premiums are taxable for Federal and Alabama Income tax purposes and subject to Medicare and Social Security tax (subject to the Social Security wage limits). The Social Security and Medicare tax must be withheld from each employee's earnings and matched by the employer before the end of the calendar year and reported as part of the normal payroll reports for Social Security and Medicare taxes. The imputed premiums are not subject to retirement withholding for the Employees' Retirement System. The amount of taxable income from imputed premiums on PRDB and additional life insurance (if applicable) should be reported on Form W-2 in Box 12 (Fringe Benefits) Code "C", and should be included in the total reported in Box 1 (Wages, Tips & Other Compensation), the total reported for Social Security wages, up to the Social Security wage base (Box 3), the total reported for Medicare wages (Box 5), and the total reported as State wages (Box 16). (See the IRS published Instructions for Forms W-2 and W-3.)

Note A - PRDB is prorated in the first year of DROP participation for the number of months of employment prior to DROP participation. In subsequent years, PRDB is not applicable.

Calculation of Taxable Income on Imputed Premiums for the Current Calendar Year:

IMPORTANT: The computation of taxable income from imputed premiums on group-term life insurance should include: (1) the Pre-Retirement Death Benefit, and (2) any additional group-term life insurance provided to your employees. The PRDB is the amount of the employee's annual salary for the previous fiscal year. In computing the imputed premiums for PRDB you should use the annual salary for the PREVIOUS FISCAL year, rounded to thousands, multiplied by the appropriate rate and number of months in the CURRENT CALENDAR year the employee worked for your agency (the only time you will use the fiscal salary is to compute the PRDB). You must add any other group-term life insurance furnished (paid) by the unit to the annual salary to determine if the employee will exceed the \$50,000 limit and thus have taxable income on imputed premiums. Your unit will not have to compute the taxable income on imputed premiums if your unit does not have any employee whose prior fiscal salary plus additional group-term life insurance (if applicable) exceeds \$50,000.

Example 1: The Pre-Retirement Death Benefit (PRDB) and any unit furnished group-term life insurance exceed \$50,000. Thus, the employee will have taxable income on imputed premiums for PRDB and unit furnished group-term life insurance.

Example 2: The Pre-Retirement Death Benefit (PRDB) and any unit furnished group-term life insurance do NOT exceed \$50,000. Thus, the employee will NOT have taxable income on imputed premiums for PRDB and unit furnished group-term life insurance.

Example 3: The Pre-Retirement Death Benefit (PRDB) and any unit furnished group-term life insurance exceed \$50,000, and the employee only worked for six months during the current calendar year. Thus, the employee will have taxable income on imputed premiums for PRDB and unit furnished group-term life insurance based on 6 months of the calendar year.

The taxable income for the Current Calendar Year is determined from your records as follows:

| | <u>Example 1</u> | <u>Example 2</u> | <u>Example 3</u> |
|--|------------------|------------------|------------------|
| PRDB (Annual salary for previous Fiscal Year: Oct 1, 2022 - Sept 30, 2023) | \$35,400 | \$41,000 | \$55,000 |
| <u>Additional</u> life insurance furnished (paid) by Unit, if applicable | <u>25,000</u> | = | <u>20,000</u> |
| Total Value of Insurance provided to | \$60,400 | \$41,000 | \$75,000 |
| Insurance in excess of \$50,000 | \$10,400 | 0 | \$25,000 |
| Excess Coverage in <u>Thousands</u> | 10(a) | 0(a) | 25(a) |
| Monthly cost per \$1,000 of coverage (assumed age 39 - see table below) | \$.09(b) | \$.09(b) | \$.09(b) |
| Number of months employee covered (worked for your agency) | 12(c) | 12(c) | 6(c) |
| Taxable income reportable on W-2 and subject to Social Security & Medicare taxes ((a) x (b) x (c)) | <u>\$10.80</u> | \$ <u>-0-</u> | <u>\$13.50</u> |

The amount of taxable income (i.e., cost of group-term life insurance in excess of \$50,000) will be determined on the basis of uniform premiums computed on the basis of 5-year age brackets prescribed by the Internal Revenue Code Regulation Section 1.79. The cost for each month of coverage is the number of thousands of dollars of coverage over \$50,000 (rounded to the nearest thousand) times the amount in the following table for the employee's age group:

| <u>5-Year Age Bracket</u> ** | <u>Cost per \$1,000 of Protection for one month</u> |
|-------------------------------------|--|
| Under 25 | \$0.05 |
| 25 through 29 | 0.06 |
| 30 through 34 | 0.08 |
| 35 through 39 | 0.09 |
| 40 through 44 | 0.10 |
| 45 through 49 | 0.15 |
| 50 through 54 | 0.23 |
| 55 through 59 | 0.43 |
| 60 through 64 | 0.66 |
| 65 through 69 | 1.27 |
| 70 and above | 2.06 |

** Based on the employee's age at December 31 of the year for which the W-2 is issued.

Please Note:

Employees of your agency who **are** participating in the Deferred Retirement Option Program (DROP) are not eligible for these death benefits. Accordingly, the PRDB should not be considered in determining imputed premiums.

If you have any questions concerning this memo, please call
334.517.7000 or 877.517.0020