





EY Payroll NewsFlash

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Minnesota updates guidance on withholding state income tax from third-party sick payments

The Minnesota Department of Revenue has updated its [guidance](#) on the state income tax withholding and reporting requirements for disability payments made by a third-party insurance provider (third-party sick pay). Third-party sick pay includes amounts employees receive for absences due to injury, sickness or disability and includes benefits for both short-term and long-term disability that are generally a percentage of the employee's regular wages.

The Department explains that whether state income tax withholding is required from third-party sick payments depends on who paid for the disability insurance.

- **If employees pay for the disability insurance**

If employees pay the disability insurance premium, the disability payments are not subject to Minnesota income tax or income tax withholding and the payments are not reported on a Form W-2 or Form 1099. This is true whether employees purchase the disability insurance independently or pay the cost of insurance provided by the employer.

- **If employers pay for the disability insurance**

State income tax withholding is required if the employer makes disability payments directly to the employee through a self-insured plan or the benefits are paid by a third-party insurance company. In the case of a self-insured plan, the employer is responsible for withholding the state income tax and for reporting the payments on Form W-2.

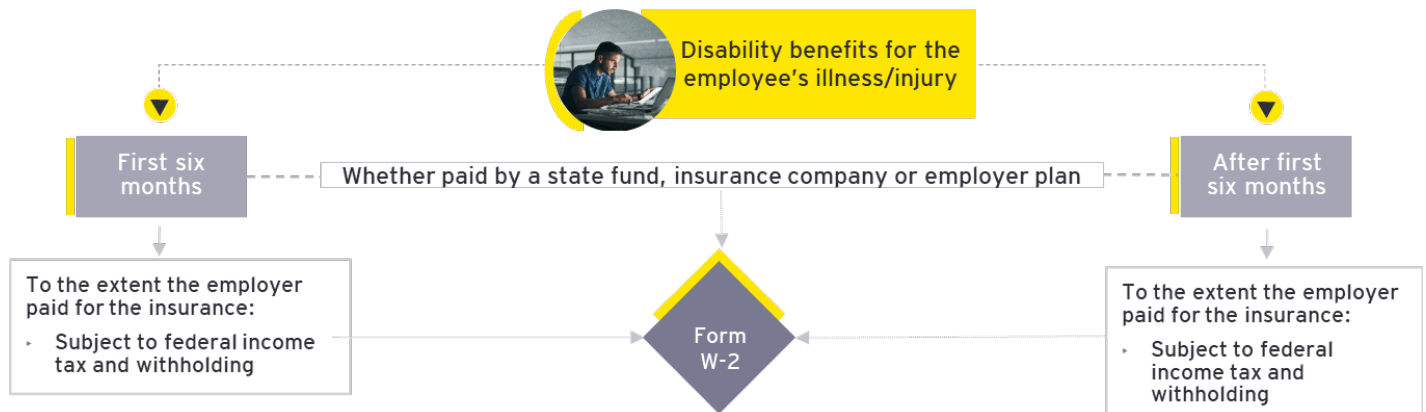
When payments are made by a third-party income provider, the third party is responsible for withholding the state income tax and for reporting the payments on Form W-2. Whether the federal employer identification number of the third-party or the employer is used on the Form W-2 depends on the contractual agreement between the employer and the third party.

As explained in the Department’s [Withholding Fact Sheet 9](#), Minnesota follows the federal rules governing the income tax treatment of third-party sick pay. For more information concerning the federal taxation and reporting of third-party sick pay, see IRS [Publication-15-A](#).

Ernst & Young LLP insights

Under federal law, income tax and withholding applies only to the extent the employer pays for the disability insurance premium. For example, if the employer pays 40% of the disability insurance, 40% of the third-party sick pay is subject to federal income tax and withholding.

Overview of federal income tax treatment of third-party sick pay (see Publication 15-A)



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