

Advisory

LABOR, EMPLOYMENT AND BENEFITS PRACTICE GROUP | MAY 2011

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IRS Issues Guidance on W-2 Reporting of Health Care Costs

The IRS recently issued Notice 2011-28, which provides interim guidance on Form W-2 reporting of health care costs as required by the Patient Protection and Affordable Care Act. Effective with the 2012 Form W-2, due in January, 2013, employers (including tax-exempt entities and governmental employers) are required to report the total cost of employer-provided health insurance coverage on Form W-2.

Despite what may seem like a long lead time, employers should begin working now to make changes to their payroll systems and procedures in preparation for compliance with the new reporting requirement, as data collection may need to begin as early as January 1, 2012.

- Reporting is not required for 2011; however, employers may rely on the guidance issued in Notice 2011-28 if they choose to voluntarily report these costs on the W-2 furnished for the 2011 tax year. Employers may choose to report 2011 costs in order to test their payroll systems.
- Small employers who are required to file fewer than 250 Form W-2s for the prior year will have the option of reporting for the 2012 year, but reporting will not be required until the 2013 tax year (for W-2s furnished in January, 2014).
- Federally recognized Indian tribes are not subject to the reporting requirements.
- Employers who contribute to multiemployer health plans are not required to report the cost of that coverage.

It is important to note that these reporting requirements do not determine the taxability of the benefit -- the report must be provided for informational purposes only.

Employers must report the total cost of coverage under all “applicable employer-sponsored coverage.” This includes the entire cost of employee, spouse and dependent coverage under a group health plan, regardless of the extent to which the cost is paid for by the employee, whether the coverage is insured or self-insured, and regardless of whether the employee is taxed on some portion of the coverage.

Certain coverage is not considered part of the applicable employer-sponsored coverage that must be reported. The following are excluded:

- contributions to a health savings account (HSA);
- contributions to a health reimbursement arrangement (HRA);
- contributions to an Archer Medical Savings Account;
- salary reduction contributions to a health flexible spending account (FSA) – *but note that employer contributions to the FSA (including employer flex credits an employee chooses to allocate to an FSA) are reportable;*
- contributions to a stand-alone dental or vision plan that is not integrated into a group health plan.

continued next page

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The Notice provides some flexibility in determining the amount to be reported on the employee's Form W-2. The default method of calculating cost is to use the applicable COBRA premium (without the 2% COBRA administrative fee). In the alternative, insured plans can use the total premium charged. Other methods are permitted if the employer determines the cost of coverage based on the prior year's cost, or charges a composite premium (for example, the same cost for self-only and family coverage). The cost must be determined on a calendar year basis, even if the plan's coverage period is something other than a calendar year, and must take into account any changes in the cost of coverage that occur during the calendar year.

For employees who terminate employment during the calendar year, the employer can limit the total cost of coverage reported on the W-2 to coverage received while the employee was actively employed, or can also include the cost of COBRA continuation coverage, at the employer's option, as long as the employer chooses one method and applies it consistently. Employers are not required to report the cost of employer-sponsored coverage for any former employee (or surviving spouse or other beneficiary) with respect to whom the employer is not otherwise obligated to issue a Form W-2.

Employers should report the total cost of all applicable employer-sponsored coverage in Box 12 of Form W-2, using code DD. The cost of coverage is not reported on Form W-3.

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