



Timothy D. S. Goodman
Partner
(612) 340-2825
[Email](#)



Courtney Colby
Associate
(612) 492-6071
[Email](#)

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IRS Guidance on Reporting Health Care Costs on Form W-2

The IRS has issued Notice 2011-28 which provides guidance on reporting the cost of employer-provided health coverage on Form W-2, which will be required for Forms W-2 issued in January 2013 for the 2012 tax year. Employers should begin working with their payroll providers to assure compliance to avoid significant penalties for failure to properly report.

Background

The Patient Protection and Affordable Care Act (PPACA) and Health Care and Education Reconciliation Act (HCERA) (collectively, "health care reform") made changes to reporting requirements on Form W-2. Section 9002 of PPACA revised section 6051(a) of the Internal Revenue Code to require employers to report the value of employer-provided health care on Form W-2. Eventually, this information may be used to determine whether the "Cadillac plan" tax applies.

In Notice 2011-28, the IRS provides guidance and relief from this requirement. Notice 2011-28 provides relief from the reporting requirement for small employers, explains the health benefits covered, and describes in general terms how to determine the amount reported. It requires reporting on Forms W-2 issued in January 2013 for the 2012 tax year. Form W-2 reporting for the 2011 tax year continues to be optional, as previously provided in Notice 2010-69.

Failure to prepare for this reporting requirement raises the potential of penalties. Failure to report the amount on Forms W-2 for compensation beginning in the 2012 tax year may result in a penalty of \$200 per Form W-2, up to a maximum of \$3 million.

Employers Required to Report

In general, all employers (including governmental entities, churches, and tax-exempt organizations) are required to provide informational reporting of the value of health benefits provided to employees. Notice 2011-28 provides a few exceptions to the reporting requirements:

- ✦ Small Employers. Employers that file fewer than 250 Forms W-2 are not required to report the amount of health benefit costs.
- ✦ Tribal Governments. Federally recognized Indian tribal governments are not required to report.

See Notice 2011-28, Q&A-3.

Health Benefits Subject to Reporting

In general, employers must report "the cost of coverage under all applicable employer-sponsored" group health plans that is excludable from income under section 106 of the Code. This includes the following group health plans:

- ✦ Coverage under a medical plan (including combined medical-dental or medical-vision plans)
- ✦ Contributions by an employer to a health flexible spending arrangement
- ✦ Coverage under an executive medical plan
- ✦ Coverage under an employee assistance program
- ✦ Health benefits provided at an on-site medical clinic

The following types of group health plans are excluded:

- ✦ Contributions by an employee to a health flexible spending arrangement
- ✦ Contributions to a health reimbursement arrangement (a transition rule)
- ✦ Contributions to a health savings account
- ✦ Contributions to an Archer MSA
- ✦ Coverage for a specific illness or disease
- ✦ Coverage under a hospital indemnity or fixed indemnity plan
- ✦ Coverage under a stand-alone dental plan
- ✦ Coverage under a stand-alone vision plan
- ✦ Coverage under a HIPAA-excepted benefit (except an on-site medical clinic)
- ✦ Coverage for long-term care
- ✦ Coverage under a self-insured group health plan not subject to any federal continuation coverage requirements (such as a self-insured church plan)
- ✦ Coverage provided under a plan maintained by the federal government, a state or local government, or agency or instrumentality thereof that provides coverage primarily for members of the military and their families

See Code § 6051(a)(14). See also Notice 2011-28, Q&A-12, Q&A-16-22.

Cost to be Reported

An employer is required to report the entire cost of coverage under the plan. This includes:

- ✦ All contributions (employer and employee) regardless of whether on a pre- or after-tax basis
- ✦ All contributions for individuals covered (employee, spouse, and dependents)
- ✦ All amounts reported as income as a result of coverage (including the cost of coverage for a domestic partner or discriminatory coverage)

Calculating the Cost

The Notice provides three alternatives that an employer may use to determine the amount to report.

- ✦ **COBRA Applicable Coverage Approach**
The cost equals the COBRA applicable premium for the period. The employer may make this calculation in good-faith compliance with a reasonable interpretation of

the requirements under section 4980B of the Code. See Notice 2011-28, Q&A-25.

✦ Premium Charged Approach

The cost equals the premium charged by the insurer for the employee's coverage (and any dependents). See Notice 2011-28, Q&A-26. The approach may only be used by an employer with an insured health benefit.

✦ Modified COBRA Premium Approach

If the employer subsidizes the cost of COBRA, then the employer may report a reasonable good-faith estimate of the full cost. See Notice 2011-28, Q&A-27. This provision is to recognize situations where an employer with a self-funded health plan subsidizes the cost of COBRA by under-estimating the actual cost of health benefits. For example, if an employer hires an actuary to determine the premium cost one year but then does not hire an actuary the next two years and instead uses the same cost for those years.

Additional Clarifications

The Notice provides other guidance that clarifies the reporting requirement.

✦ Terminated Employees. If a terminated employee requests a Form W-2 in the middle of a year, the employer is not required to report the amount on a Form W-2 provided to the terminated employee before the end of the calendar year. See Notice 2011-28, Q&A-6.

✦ Former Employees. The Notice provides that the amount does not need to be reported if a former employee receives health benefits but would not receive a Form W-2 except for the reporting requirement. For example, an employer does not need to issue a Form W-2 to a former employee who is receiving health benefits (such as under COBRA) during the tax year, but did not receive any compensation from the employer. This indicates, however, that if a former employee is receiving any reportable compensation (such as payments from a nonqualified plan or severance) and health benefits, the health benefits must be reported on the Form W-2 for the former employee. See Notice 2011-28, Q&A-9.

✦ Union Employees. An employer that contributes to a multiemployer plan is not required to include the cost of health benefits under a multiemployer plan. See Notice 2011-28, Q&A-17.

Conclusion

The interim guidance in Notice 2011-28 provides more concrete rules for the upcoming Form W-2 requirement and will assist employers and payroll providers in preparing for the 2012 tax year. If you wish to discuss employer-provided health care reporting, please contact the attorney in the Benefits and Compensation practice group with whom you work.

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