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Minnesota Conforms State Tax Law to Health Care Reform Changes – Wisconsin Does Not

Minnesota has amended its state tax law to conform to federal tax law with respect to the changes made by health care reform, including conforming Minnesota state tax law to provide for tax-favored treatment of coverage of children through the end of the year in which the child attains age 26. Wisconsin, however, did not amend its state tax law to extend tax-favored treatment to health coverage provided to an adult child through the end of the year in which the child attains age 26; although it made a few other changes to conform its state tax law. This means employers may have to report different amounts of income for federal and Wisconsin state tax law purposes on employee Forms W-2 issued in January 2012 for the 2011 tax year.

Background

Section 1004(d) of the Health Care and Education Reconciliation Act (HCERA) amended section 105(b) of the Internal Revenue Code (Code) to provide that employer-provided health coverage of children through the end of the year in which the child attains age 26 is not subject to federal income tax (it is excluded from an employee's income to be reported on Form W-2). Health care reform also made several other changes to federal tax law, including generally requiring a prescription for tax-favored reimbursement of medications (other than insulin, but including over-the-counter medications). These changes, however, caused federal and state tax laws in certain states, such as Minnesota and Wisconsin, to diverge from federal tax law. This is because they are states where the legislature must act to update the state tax law when there is a change at the federal level.

Minnesota's Legislature Acts

Minnesota's legislature has now amended state tax law to conform to federal tax law. See Minn. Stat. § 289A.02, subd. 7 (2011) (amended by 2011 Minn. 1st Spec. Sess. Law Chap 7, Art. 2, section 1; enacted July 20, 2011). Previously, Minnesota had amended its state tax law to conform for 2010, but not future years. See 2011 Minn. Sess. Law Chap 8, section 1. Minnesota's state tax law conforms in all aspects to the changes health care reform made to federal tax law.

Wisconsin's Legislature Holds Back

In contrast, Wisconsin did not amend its state tax law to provide tax-favored treatment of employer-provided health coverage through the end of the year in which the child attains age 26. See 2011 Wis. Sess. Laws § 1753d, page no. 269-70 (2011 Wis. Act 32; 2011 Wis. Assembly Bill 40; enacted June 26, 2011) (adding Wis. Stat. § 71.01(6)(un) (2011)). The result:

- For federal income tax purposes, the value of health benefits provided to adult children through the end of the year in which an adult child attains age 26 are excluded from income reported in box 1 of Form W-2 for an employee.
- For Wisconsin state income tax purposes, the value of health benefits are excluded if a dependent is a qualifying child or qualifying relative under section 152 of the Code (for example, a child who will not attain age 19 before the end of the year). The value of health benefits provided to children who do not satisfy one of these criteria are reported in box 16 of Form W-2 for an employee. This means complexities that existed in federal tax law prior to health care reform still exist for purposes of Wisconsin state tax law. For example, if an employee covers a 22 year old adult child on an employer's health plan, whether the cost of health coverage is excludable under Wisconsin state tax law depends on whether the 22 year old is a full-time student or otherwise is a dependent.
- For Wisconsin state income tax purposes, it appears that the reimbursement of medical expenses to a child who is not a dependent under section 152 of the Code must be included in an employee's income and reported on Form W-2. For example, if an employer reimburses an employee for a prescription medication for a child who is 25 under its flexible spending account program (cafeteria plan) or health reimbursement arrangement (HRA), then that amount would be income for purposes of Wisconsin state tax law (but not federal tax law).

Wisconsin's legislature amended Wisconsin state tax law to conform to a few aspects of the changes under health care reform to the federal tax law. For example, Wisconsin amended state tax law to require a prescription for tax-favored reimbursement of medications (other than insulin, but including over-the-counter medications) and to add the provisions that allow a small employer to adopt a SIMPLE cafeteria plan. See 2011 Wis. Sess. Laws § 1753d, page no. 270 (indicating that Wisconsin's state tax definition follows the changes made by section 9003 of the Patient Protection and Affordable Care Act (PPACA) (changing the tax-favored treatment of reimbursement of medications) and section 9022 of PPACA (adding the SIMPLE cafeteria plan)).

Form W-2 Reporting For Compensation and Benefits Paid in 2012

When reviewing their state tax reporting, employers should begin working with their payroll providers to assure that the cost of employer-provided health coverage is reported on Form W-2, which will be required for Forms W-2 issued in January 2013 for the 2012 tax year. See our prior update on this requirement.

Conclusion

Employers with employees in Minnesota should review their payroll practices now that Minnesota has conformed its state law to federal tax law. More importantly, employers with employees in Wisconsin should verify that the amount being reported as taxable income for Wisconsin state income tax purposes accurately reflects Wisconsin state tax law. If you wish to discuss this, please contact the attorney in the Benefits and Compensation practice group with whom you work.

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