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For your information

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# IRS Provides New Guidance on Form W-2 Reporting of Health Care Coverage

As a follow-up to interim guidance issued last year, the IRS provided additional clarifications to assist employers in complying with the W-2 reporting requirements. This new guidance applies to W-2 reporting for 2012.

## Background

The Patient Protection and Affordable Care Act (PPACA) amended the Internal Revenue Code (Code) to require employers to report the aggregate cost of applicable employer-sponsored group health plan coverage on Form W-2 for taxable years beginning on or after January 1, 2011.

In Notice 2010-69, the IRS made this reporting optional for 2011. Interim guidance on the reporting requirements (Notice 2011-28) was released in the spring of 2011 (see our May 6, 2011 For Your Information).

The IRS has released additional interim guidance applicable to 2012 reporting obligations. Notice 2012-09 follows the same question and answer (Q&A) format as Notice 2011-28 and provides additional clarifications. This new notice replaces Notice 2011-28.

This guidance applies to 2012 reporting, which will take place in January 2013, and is applicable until further guidance is issued. Employers voluntarily choosing to comply in 2011 can rely on this guidance. If the IRS later decides to apply W-2 reporting to additional categories of employers or additional types of coverage, such guidance will be applicable only to calendar years beginning at least six months after the changes.

## Notice 2012-09

Notice 2012-09 provides new guidance with respect to W-2 reporting applicable to 2012 through changes and additions to the Q&As in Notice 2011-28.

**EAPs, Wellness Programs, and On-Site Clinics.** Costs of employee assistance programs (EAPs), wellness programs, and on-site medical clinics must be included in the W-2 cost reporting only if the coverage is provided under a program that is considered a group health plan. However, the Notice

states that the employer will not have to report those costs if the employer does not charge a premium with respect to that type of coverage under COBRA continuation rules.

COMPLIANCE ALERT: Under ERISA rules, EAPs that provide medical services such as counseling by credentialed professionals (psychologists or licensed social workers for example) are considered group health plans and subject to COBRA. Sponsors of these coverages should allow COBRA participants to continue participation in such EAPs. An employer that chooses to impose a separate COBRA cost on an EAP must take these costs into account when complying with the W-2 reporting rules.

**Inclusion of Non-Reportable Costs.** The Notice allows employers to report costs even if they are not required to do so. For example, if employers wish to report the costs of coverage under a Health Reimbursement Account (HRA) or EAP, they may do so. For some employers, this may be helpful administratively if their systems include these costs in the overall medical rates.

**Allocation Methods.** Under the Notice, employers are allowed to use reasonable methods to allocate costs where a portion of a program is not subject to the reporting rules. The IRS indicated that where medical benefits are "incidental" to the rest of the plan (as may be the case with some disability programs), these costs do not have to be reported.

**Election Changes.** Where employees request retroactive coverage changes after the close of the calendar year, employers may rely on the information they had on December 31 for reporting purposes. If, for example, an employee gives notice in January of a divorce that occurred in December, and this event would have caused the spouse to lose coverage effective before December 31, the employer can report based on the information it had as of December 31 (which would have the coverage in effect through the end of the year).

INSIGHT

The guidance only addresses retroactive changes brought to the employer's attention in the following year. It does not address late-year election changes not yet fully processed as of that December 31.

**Coverage Periods That Straddle Calendar Years.** For plans with coverage periods that include December 31 but continue on into the subsequent calendar year, employers are allowed to choose one of three options (as long as the one chosen is applied consistently to all participants):

- Treat the costs as all falling into the first calendar year
- Treat the costs as all falling into the second calendar year
- Allocate between the two using a reasonable allocation method that is based on the number of days of coverage in each of the two calendar years

**Hospital or Fixed Indemnity Plans.** The Notice requires that the employer report the applicable cost of a hospital indemnity plan or other types of fixed indemnity plan such as a cancer policy if the employer contributes towards the cost of coverage, or if the employee purchases the insurance with pre-tax dollars. The only reporting exception is where the employee pays the full cost of the insurance with after-tax dollars.

COMPLIANCE ALERT: Many employers that offer hospital indemnity plans, cancer plans, and the like as voluntary plans have allowed employees to use pre-tax dollars to purchase these plans. These employers will have to report the costs on the employee's W-2.

**Third-Party Sick Pay Administrators.** The Notice clarifies that where a third party is used to administer sick pay, the W-2 obligations of that third-party payer generally do not include reporting on health plan costs. The employer's own W-2 form (if required) must still include the applicable health care costs.

**Other Clarifications.** Notice 2012-09 provides a number of minor clarifications related to previous guidance for employers attempting to comply with the W-2 reporting rules in 2012:

- For the reporting exemption applicable to employers who filed less than 250 W-2s in 2011, the Notice clarifies that the number of W-2s is calculated without regard to whether the employer utilizes an agent.
- Where related employers do not use a common paymaster, and those employers concurrently employ an individual, the employers will have the option of either aggregating all costs on one W-2 or allocating the costs among the W-2s from the related employers.

- A new example on flexible spending accounts (FSAs) makes clear that the value of FSAs that are funded solely by employee elections does not have to be reported.
- For dental and vision coverage, the Notice directly references the rules regarding HIPAA-excepted benefits. Therefore, if a dental or vision plan is either offered under a separate insurance policy or offered on a stand-alone basis with its own separate contribution, then the cost of these coverages will not have to be reported on the W-2.
- If a highly compensated employee is provided with discriminatory (and therefore taxable) benefits, those amounts are not included as applicable costs. The taxable amounts are included as reportable income elsewhere on the W-2. Similar treatment will apply to the taxable benefits of an individual who owns more than 2% of an S Corporation.

## Conclusion

In general, this guidance provides welcome relief for employers. The biggest concern created by this new Notice is the requirement that voluntary hospital indemnity, cancer, and similar plans will be subject to employer reporting if employees purchase them with pre-tax dollars.

### Buck Can Help

- Review all of your programs to identify those subject to W-2 reporting in 2012
- Calculate appropriate costs for each line of coverage
- Review systems to ensure they are gathering and aggregating the costs of all plans correctly
- Work with employee benefits and payroll staff to ensure compliance with all aspects of the rules
- Keep you informed of further developments in the guidance