

How to Highlight the Value of Health Insurance on the Form W-2

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The Patient Protection and Affordable Care Act (PPACA) requires employers to report the cost of providing health insurance to the employees on their Forms W-2. This provision raises many questions: Which employers must report health insurance? What, precisely, must employers report and when? Most of these questions have been answered by the Internal Revenue Service (IRS) in Notice 2011-28, which also provides a bit more time for some employers to comply.

The first issue to appreciate is critical: **health insurance benefits are not being taxed**. Reporting the cost of health insurance on W-2s may seem like a path to taxation, but the reason for reporting is to convey to employees the value of their health insurance, since many employees do not realize how expensive it is. While PPACA does include a provision to tax health insurance starting in 2018, this applies only to so-called “Cadillac” health insurance coverage – coverage that is far more valuable than that provided by most employers. In short, health insurance coverage will not be taxed under current law unless it is very expensive.

Which employers must report?

Eventually, all employers that provide tax-free group health insurance must report the cost of health insurance, but the IRS has given smaller employers an extra year to prepare. In this case, smaller employers are those that filed 250 or fewer Forms W-2 for the 2011 tax year; this date also happens to be the threshold for when employers must file their W-2s electronically. This requirement applies to all employers, including churches and other religious organizations, all levels of government, and those employers not subject to COBRA continuation coverage requirements.

While the reporting requirement applies to all employers, the reporting requirement does not apply to all types of coverage offered under plans. The cost of coverage under church plans—those plans that are offered by religious organizations and are not subject to ERISA or COBRA continuation—does not have to be reported. So while the reporting requirement applies to the religious organizations, if the religious organizations offer nothing but church plans, the organization has nothing to report.

When must employers report?

Large employers must report the cost of health insurance coverage on the 2012 Forms W-2; smaller employers must report on their 2013 Forms W-2. Remember, employers issue Forms W-2 in January following the tax year they cover, so this means the first required reporting starts in January 2013. IRS Notice 2010-68 and IRS Notice 2011-28 also clarify that reporting the cost of health insurance is optional for the years before they are mandatory.

How do employers calculate and report the cost of health insurance coverage?

Employers must report the “aggregate cost of applicable employer-sponsored coverage,” which is the total cost of coverage under all the group health insurance provided to the employee. The IRS provides employers with a few different options for how to relay this. The key principle underlying the employer’s options for cost calculation is that, once the employer chooses a method, the employer must apply that method uniformly to all employees receiving coverage under the same plan.



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So what is it that employers need to report, exactly? Essentially, employers must report the cost of medical coverage under their group health plan that is tax-free. There are several benefits and lines of coverage which do not count towards the reportable aggregate cost:

1. Standalone dental and vision plans;
2. Amounts contributed to Archer MSAs, Health Savings Accounts (HSAs), and Health Reimbursement Arrangements (HRAs);
3. Amounts contributed by the employee to health Flexible Spending Arrangements (FSAs) (NOTE: amounts contributed by the employer to FSAs are included in reportable cost);
4. "Excepted benefits" (including Accident, Death & Disability insurance, liability insurance, and automobile health insurance);
5. Long-term care; and
6. Any health-like insurance (for example, covering a specific condition) that is not excludable from income.

The aggregate reportable cost includes the entire amount of the coverage, including both employer and employee contributions. For fully-insured plans, this is easy enough to calculate: employers may just report the premium charged for the employee's coverage. Employers with self-insured plans (and those with fully-insured ones, if they wish) can use the COBRA premium rate to determine the aggregate cost of covering an employee. Alternatively, if the employer does not calculate precise COBRA premiums from year to year, they can use a good-faith estimate of the total COBRA premium, including employer subsidization.

When the reportable cost changes in the middle of a tax year, employers must ensure that the reported cost accounts for the changes. Most employers will probably calculate the costs on a monthly basis, which makes adjusting for changes easier. Sometimes a change, such as the employee's beginning, ending, or changing coverage, occurs in the middle of a month. In that case, the employer may include, exclude, or prorate the changes in costs for that month, so long as the employer uses the same method for all employees covered by that plan. Employers must also incorporate in the calculation method changes, such as when the employer recalculates the COBRA premium in the middle of the year. When calculated on a monthly basis, the reportable cost is simply the annual sum of the monthly costs.

Once determined, employers must report the cost of coverage in Box 12 on the Form W-2 using code DD. As usual, employers must distribute the Forms W-2 to employees in January following the applicable tax year and then file the forms with the Social Security Administration (SSA).

About the Author

Edward Doherty is a compliance consultant for Cammack LaRhette's health and welfare services practice. Ed provides support and service to clients and vendors regarding compliance issues like HIPAA, COBRA, ERISA, FMLA and healthcare reform. Ed received his bachelor's degree in political science and economics from University of Illinois and his JD from New York University.

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