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MEMORANDUM

TO: NYSCOPBA Executive Board
FROM: Sheehan Greene Golderman & Jacques LLP
DATE: January 24, 2013
SUBJECT: New W-2 Entry and Taxation of Health Benefits

We have been informed that members' W-2 forms now include an entry in Box 12, with a code DD, indicating a dollar amount. Members have expressed concern about this new entry, what it means, how it is calculated, and any tax implications it may have. While this new entry has no tax implications for members at this time, this memo is provided to address those concerns and explain how certain elements of the federal Affordable Care Act may impact on the taxation of health benefits in the future.

What is the new entry and how is it calculated?

Many employers are now required by the Affordable Care Act to report the cost of their employer sponsored group health plans on employees' W-2 forms. The State provides "applicable employer-sponsored coverage" under a group health plan, and is therefore required to report the information (some employers are exempt from reporting this year, but the State is not one of them).

This does not mean that any portion of the cost of health care coverage is taxable (neither to the employee nor the State). According to the Internal Revenue Service, the reporting on W-2 forms is for informational purposes only and will "provide employees useful and comparable consumer information on the cost of their health care coverage."

The IRS advises that the value of the employer provided health care coverage is to be reported on the W-2 form, in Box 12 with Code DD, to identify the value of the covered health benefits provided (for the purposes of the Affordable Care Act, dental and vision coverage is not included). The amount reported should include both the employer provided portion of the benefits and the portion paid by the employee.

Will health benefits be taxed under the Affordable Care Act and, if so, how will such taxes be calculated and paid?

Some, but not all health plans may be subject to an excise tax under the Affordable Care Act. Commencing in tax years beginning after December 31, 2017, only high cost plans (“Cadillac Plans”) will be taxed. While some plans will be subject to taxation, to some extent in the future, the fact that the cost is listed on current W-2 forms does not mean that the State's plan is considered a Cadillac plan. All employers will be required to report the cost of benefits, but not all plans will be taxed. Only those plans exceeding caps set by the federal government will be taxed and only the portion exceeding the cap will be taxed.

The “Cadillac Tax” is an excise tax equal to 40% of the annual cost of the portion of the health insurance plan exceeding \$10,200 for individuals and \$27,500 for families (dental and vision benefits do not count toward the value of the health insurance plan for excise tax purposes).¹ Additionally, the threshold or cap numbers will be adjusted upward for plans that include individuals in “high risk professions” and should also be adjusted up for plans covering older individuals as well. The IRS is expected to promulgate regulations clarifying what is meant by “high risk professions” and how these adjustments will be calculated.

Technically, the Cadillac Tax will be assessed to and paid by the insurers (or plans) rather than individual employees. Employees enrolled in plans subject to the tax will not see a new or additional tax coming out of their pay check. Where plans are subject to the Cadillac Tax, however, the insurers or plans will likely seek to recover those costs by increasing the amount charged for the benefits. For plans assessed an excise tax, in cases where employers and employees share in the payment for the benefits, the cost would likely be passed on to the respective parties in proportion to their share of the costs.

When the Cadillac Tax commences in 2018, will my benefits be subject to the additional excise tax?

The answer to that question depends on what the cost of the taxable benefits are in 2018, and whether the caps are adjusted upward based on the professions and ages of plan participants. At this point, the annual cost of the taxable benefits under the Empire Plan are approximately \$7300 for individual coverage and \$17,600 for family coverage. As is noted above, the excise tax will not commence until 2018. However, if the tax was currently applicable (and assuming no adjustment for the professions or ages of plan members), the taxable benefits under the Empire Plan would not exceed the current cap levels and, accordingly, the Empire Plan would not be subject to the Cadillac Tax.

¹ For example, if the calculated value of the taxable elements of the plan (i.e. the total value of benefits minus non-taxable benefits like dental and vision) for individual coverage was \$11,200, the portion subject to the excise tax would be \$1,000. ($\$11,200$ value of plan - $\$10,200$ excise tax cap = $\$1,000$ taxable portion). The $\$1,000$ would be taxed at a rate of 40% and added to the cost of the plan. After adding the excise tax ($\$1,000 \times 40\% = \400) to the original $\$11,200$ cost of the plan, the new cost becomes $\$11,600$.