Employee Benefits and Payroll Subgroup

A. Employer and Insurer Shared Responsibilities Under the Patient Protection and Affordable Care Act

Recommendations

1. IRPAC strongly urges the IRS to release proposed and temporary regulations as soon as possible on the shared employer responsibility provision in IRC §4980H.

2. IRPAC encourages the IRS to develop a process to generate the substantiation documents that should accompany the shared employer responsibility assessment.

3. IRS should provide an alternative affordability safe harbor in addition to the currently proposed safe harbor that is based on an employee's wages reported on Form W-2, Wage and Tax Statement.

4. IRPAC encourages the IRS to work with IRPAC in developing educational materials for employers to help them understand the shared employer responsibility provisions and assessment process.

Discussion

Section 4980H was added to the Internal Revenue Code by §1513 of the Patient Protection and Affordable Care Act, and amended by §1003 of the Health Care and Education Reconciliation Act of 2012. IRC § 4980H is effective for months beginning after December 31, 2013.

The employer shared responsibility provisions provide that a large employer (defined as an employer that employed an average of at least 50 full-time employees on business days during the preceding calendar year, which for this purpose includes full-time equivalent employees) could be subject to an assessable payment if any full-time employee is certified to receive a premium tax credit or cost-sharing reduction payment. Generally, this may occur where either: 1) the employer does not offer its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan; or 2) the employer offers its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plans that either is unaffordable relative to an employee's household income or does not provide minimum value.

The IRS released Notice 2011-36 describing potential approaches, which could be incorporated in future proposed regulations. According to the Notice, the IRS contemplated that the proposed regulations would make clear that an employer offering coverage to all, or substantially all, of its full-time employees would not be subject to the IRC §4980H(a) penalties.

The determination of affordability remains a critical issue for employers in designing their benefit plans. Will the affordability determination for purposes of IRC §4980H(b) apply based on the affordability of self-only coverage and not on the affordability of employee plus one dependent, or employee plus family?

IRPAC appreciates the guidance in Notice 2012-58 that addresses some discrete issues in determining full-time employees. However, this notice does not address the broader issues of calculating the assessment and whether employers will be penalized for not offering dependent coverage or offering dependent coverage that is not defined as affordable under the statute.

Employers that provide health care offerings to their employees generally begin the plan design process 18 months to two years before the beginning of a new plan year. For those companies or industries that engage in contract bids, the bidding process is now underway for years 2014 and beyond. The uncertainty with respect to IRC §4980H provisions is currently impeding the bidding process for employer offerings for plan years beginning January 1, 2014, and this uncertainty is already creating long-term employment consequences for large employers (50 or more full-time employees).

The Employee Benefits and Payroll Subgroup of IRPAC has been working this year to map the information flow that will take place among the federal agencies, the exchanges, individuals, employers, insurers and plans. Based on our understanding of the statutory language, it is the IRS that will calculate the actual premium tax credit (not the advance premium tax credit) and send employers a shared employer responsibility assessment. It is imperative that the assessment notice is accompanied by documents substantiating the amount and demonstrating the number of employees who actually received and were entitled to premium tax credits. For those employers declining to use the proposed affordability safe harbor, a thoroughly documented substantiation will be vital to secure taxpayer compliance with IRC § 4980H provisions. The assessments could be potentially very large and an assessment notice without adequate supporting documentation will cause major collection problems for the IRS.

IRS Notice 2011-73 requested comments on a potential proposed safe harbor for determining the affordability of coverage under an eligible employer-sponsored plan for purposes of the IRC §4980H(b) liability. Coverage under an employer-sponsored plan is considered affordable to a particular employee if the employee's required contribution for the self-only premium for the employer's lowest cost plan does not exceed 9.5 percent of the employee's household income for the taxable year.

Household income for this purpose is defined as the modified adjusted gross income of the employee and any members of the employee's family (which would include any spouse and dependents) who are required to file an income tax return.

The IRS acknowledged in Notice 2011-73 that employers may encounter practical difficulties in assessing whether the coverage they are offering is affordable to certain employees given that household income is determined by variables that are generally unknown to employers (i.e. an employee's other sources of income or loss, as well as the income and losses, if any, of spouses and dependents). To address these unknowns, Treasury and the IRS expect to propose an affordability safe harbor for § 4980H purposes, whereby the affordability of an employer's coverage would be measured by reference to an employee's wages from that employer and not household income. Wages for this purpose would be the total amount of wages as defined in §3401(a), which is the amount required to be reported in Box 1 of Form W-2. Notice 2012-58 also permits reliance on the Form W-2 safe harbor at least through the end of 2014.

It is important for the IRS to recognize that not all employers will use the currently proposed affordability safe harbor (an employee's Form W-2 wages), as this will, in most cases, lead to a penalty assessment that is far greater than the assessment that would result from an employee's household income. This is because a large number of employees live in households with two-income earners. Since most employees' wages reported on Form W-2 will be less than their household income, there is a need for an alternative safe harbor. IRPAC suggests the following alternatives for consideration.

1. Since the applicant for the premium assistance tax credit must complete an application and submit this to the Exchange, it would be appropriate to ask that the applicant provide the anticipated household income for the year. The employer/plan would provide the Exchange with the required employee contribution and the Exchange would determine affordability and notify the employer. No anticipated household income information would be shared with the employer/plan. The Exchange would simply notify the employer/plan whether or not the coverage was affordable and the employer/plan would rely on that in determining the liability.

This approach would build on the methodology proposed by the Department of Health and Human Services to determine whether an individual's household income meets the eligibility requirements for advance premium tax credits. Under this proposal, the Exchanges would project an individual's household income for the plan year using household income reported on the applicant's most recently filed tax return.

2. The Exchanges would use the prior year's household income for an applicant, provided by IRS records, to determine affordability and notify the employer. The Exchanges would not provide any household income information to the employer.

After guidance is released addressing the issues surrounding the shared employer responsibility provision, IRPAC believes the employer community will need plain language explanations, along with tools to help employers understand their responsibilities and the consequences of various approaches. IRPAC offers its combined industry expertise to assist the IRS in this endeavor.

IRPAC encourages the IRS to work with consumer advocates in developing educational materials for individual taxpayers who will access the premium tax credits and cost-sharing reductions.

B. Employer and Insurer Reporting Under the Patient Protection and Affordable Care Act

Recommendation

IRPAC made numerous recommendations in the 2011 IRPAC Public Report. We encourage IRS to again review those recommendations. IRPAC would also like to highlight the need for a separate form other than the Form W-2 to report this new information.

Discussion

IRC §§ 6055 and 6056 were added by the Patient Protection and Affordable Care Act, Public Law 111-148, which was amended by the Health Care Education Reconciliation Act of 2010, Public Law 111-152. The reporting requirements apply to coverage provided on or after January 1, 2014. The first information returns will be filed in 2015.

According to IRS Notice 2012-32, IRC §6056(d) permits the Secretary to provide, to the maximum extent feasible, that any return or statement required under IRC §6056 may be provided as part of a return or statement under IRC §6055 or IRC §6051 (relating to reporting by employers on the Form W-2.) The inclusion of additional data on the Form W-2 will undoubtedly cause this form to become a multiple page form and will make the preparation of the form increasingly difficult and costly.

In response to IRS Notice 2012-32 and Notice 2012-33, IRPAC submitted two comment letters on June 11, 2012, which are attached in the Appendix B.

C. $2,500 Limit on Health Flexible Spending Arrangements

Recommendation

IRPAC recommends that the IRS provide transitional relief for all health flexible spending arrangements (Health FSAs) that adopted the $2,500 limit before Notice 2012-40 was issued. The transitional relief should permit an exception to the cafeteria plan election change rules for these Health FSAs that would allow plan participants to increase their elections for the 2012 plan year and allow the increase to apply for the entire plan year.

Discussion

In response to the issuance of IRS Notice 2012-40 that provides guidance on the effective date of the $2,500 limit (as indexed for inflation) on salary reduction contributions to Health FSAs under §125(i), IRPAC submitted a comment letter (see Appendix C) on July 13, 2012.

D. Health Care Valuation on Form W-2

Recommendation

IRPAC created a health care value chart for Form W-2 to facilitate compliance with the interim guidance on informational reporting to employees of the cost of group health coverage (IRS Notice 2011-28). The chart provides a quick visual reference.

Discussion

IRS published a chart in early 2012 on IRS.gov after making modifications to the chart submitted by IRPAC. The IRS chart is found in Appendix D. The reporting community has enthusiastically praised this chart and applauds the IRS for offering this assistance to the reporting community.

E. Patient-Centered Outcomes Research Trust Fund

Recommendation

IRPAC requests that the IRS clarify the applicability date for self-insured plans.

IRPAC requests that the IRS publish a chart showing which plans are subject to the fee and which plans are not subject to the fee.

Discussion

The IRS released a proposed rule on the fees imposed by the Patient Protection and Affordable Care Act on issuers of certain health insurance policies and plan sponsors of certain self-insured health plans to fund the Patient-Centered Outcomes Research Trust Fund (REG-136008-11). The applicability date has served as a source of confusion. As stated in our July comment letter, found in Appendix E, IRPAC requests some examples that clearly demonstrate the effective date.

IRPAC created a chart to assist the employer/plan community in understanding the plans that were subject to the fee and provided this chart to the IRS.

F. Integrated Plans

Recommendation

IRS should clarify that non-Health Reimbursement Account (HRA) integrated plans are not required to satisfy the lifetime and annual rules on a stand-alone basis, provided that the combined benefit satisfies the requirements.

Discussion

The Patient Protection and Affordable Care Act prohibits group health plans from imposing lifetime and annual limits on the dollar value of essential health benefits, but allows “restricted annual limits” for plan years beginning before January 1, 2014. The preamble of the Interim Final Rule on lifetime and annual limits (26 CFR 54.9815-2711T) distinguishes between stand-alone health reimbursement arrangements (HRA) and HRAs that are integrated with other group health coverage. The preamble states that when an HRA is integrated with other health coverage, if the other coverage alone would meet the lifetime and annual limits requirements, the HRA need not satisfy the requirement on its own because the combined benefit satisfies the requirements.

Non-HRA plans exist that are integrated with other health coverage which satisfies the lifetime and annual limit rules. These non-HRA plans do not permit unused portions of the maximum dollar amount to be carried forward to increase the maximum reimbursement amount in subsequent coverage periods. These integrated plans should be given the same treatment as integrated HRAs for purposes of the lifetime and annual limit rules, as contemplated by the statute.

G. Third Party Sick Pay

Recommendations

IRPAC recommends that IRS should receive and process the third party sick pay filings.

Discussion

Third party sick pay is now reported to the Social Security Administration (SSA) who does not need or use the information. The SSA is revamping their Annual Wage Reporting System and wants to eliminate third party sick pay reporting.

Many employers use third party sick pay providers to handle Forms W-2 for short-term and/or long-term disability payments. These providers operate on separate systems from employers and in most cases do not have access to health coverage data on individual employees. Reporting directly to the IRS would decrease the burden on third party sick pay providers as they would only need to interact with the IRS on reconciliation matters.

H. Proper Reporting for Flexible Spending Arrangement improper payments

Recommendations

IRPAC recommends that the IRS provide guidance in the form of Frequently Asked Questions (FAQ) on IRS.gov to address the steps involved in correcting improper payments from cafeteria plan flexible spending arrangements/accounts (FSAs) by employer contracted Third Party Administrators (TPAs) and/or employers. These FAQs would specifically address the “basic rule” governing these improper payment corrections (i.e., to restore the participant and plan back to original status as if no error had occurred), who is responsible for correcting the improper payment (i.e., TPA or employer), and the listed/ordered steps necessary to accomplish an employee and plan restoration under such “basic rule.”

IRPAC recommends the below FAQ be released to the public on IRS.gov**.**

Category: Flexible Spending Arrangements/Accounts

Question: In the event of an administrative error resulting in a cafeteria plan FSA improper payment to an employee, what are the corrective steps necessary to restore the employee and the cafeteria plan back to their/its original status?

Answer: The basic rule is that the employer is responsible for restoring the employee and the cafeteria plan back to where they/it would have been if the error had never occurred. The steps involved in correcting a cafeteria plan FSA improper payment are listed below:

1. The employer requests that the improper payment be returned by the employee to repay the cafeteria plan in an amount equal to the improper payment. In the event that this does not occur in full then,
2. The employer should include the improper payment in the employee’s taxable income or withhold the amount of the improper payment from the employee’s pay or other compensation, to the full extent allowed by law. In the event that this does not occur in full then,

3. The employer should apply a claims substitution or offset to future reimbursements in the amount of the improper payment. In the event that none of the above occur in full then,
4. The employer should treat the improper payment as it would any other business indebtedness.

When employee/account restoration is reached by following the above listed steps, cafeteria plan FSAs will alleviate any jeopardy of losing their overall tax-favored status.

Category: Flexible Spending Arrangements/Accounts

Question: In the event that a TPA, engaged by an employer to manage the payments to its employees from a cafeteria plan FSA, distributes an improper payment to an employee, who carries the burden of correction for this improper payment? Is it the TPA’s responsibility to issue a Form 1099-MISC, Miscellaneous Income, to the individual who received the improper payment? Or, does the burden rest with the employer to include such improper payment in the employee’s Form W-2?

Answer: The responsibility for the plan ultimately rests with the employer. Employers may contract with TPAs to perform administrative duties at the employer’s direction, but this type of relationship does not relieve an employer’s responsibility of reporting correct taxable income to its employees. The responsibility of the correction for such improper payments rests ultimately with the employer. Only an employer can authorize and control increases in the taxable wages of its employees.

Discussion

IRPAC is concerned with the clarity of the guidance within IRC §125 related to the corrective steps for improper payments from FSAs that are not specifically incurred by debit card plans. It is IRPAC’s opinion that the guidance available within IRC §125, Prop. Treas. Reg. §1.125-6(d)(7), Rev. Rul. 2003-43 and various other sources, while offering reasonable approaches, is unclear as to the corrective steps to be taken when such administrative errors result in improper payments from FSAs. Also, this guidance is unclear about who (i.e., TPA or employer) carries the burden of correction. The underlying questions that need resolution are:

1. Is the correction of the improper payment the responsibility of the employer or the TPA, in the event that there is a TPA involved?
2. What is the proper order of events in which to reach corrective resolution on FSA improper payments (*e.g.*, request return of money from plan participant; include in taxable income; offset future reimbursements; add to gross income through Form 1099-MISC)?

IRPAC recognizes that legitimate administrative errors resulting in FSA improper payments, although rare, can occur. When these errors occur, plan/participant restoration should be key and corrective measures considered without threat of the overall disqualification of the plan involved.

I. Form 5558, Application for Extension of Time to File Certain Employee Plan Returns, Penalty Relief

Recommendations

1. Consideration of non-enforcement of penalties for late filing of the Form 5500, Annual Return/Report of Employee Benefit Plan, if the filer can demonstrate that a Form 5558, Application for Extension of Time to File Certain Employee Plan Returns, requesting an extension was timely filed, and subsequently the Forms 5500 were timely filed by the extension-requested due date.

2. Clarification whether in the above-mentioned situation it is all plans listed in the filing, or only those listed in any attachments and not in the three lines provided for plans on the form itself, that will be considered not to have timely filed an extension.

3. Consideration of similar relief for those Form 5558 filers whose filings received by the IRS before July 31, 2012, were returned, but not received by the filers before the July 31, 2012 due date, unless specific transition relief was provided with the return of the original filing.

Discussion

Form 5558 is used by employers, plan sponsors and plan administrators to request an extension of time to file the Form 5500. For a calendar year plan, Form 5558 is due July 31. Prior to an August 2012 revision, the Form 5558 could accommodate the listing of up to three plans for an extension request. (The August 2012 revision requires a separate Form 5558 for each plan requesting an extension.)

Employers, plan sponsors and plan administrators have over the years routinely included attachments to their Form 5558 filings to include additional plans, beyond the lines for three plans that are on the form. In early 2012 the IRS alerted taxpayers that it would NOT process a Form 5558 requesting extensions for more than three plans. The IRS noted that Forms 5558 received through July 31, 2012, that requested extensions for more than three plans would be returned to the filer to submit separate Forms 5558 to request the extension. Further, the IRS indicated that Forms 5558 requesting extensions for more than three plans that were received after July 31, 2012 would NOT be returned, nor would they be processed.

The IRPAC acknowledges that the IRS provided taxpayers adequate warning about its position regarding the attachment of lists of additional plans to Form 5558. However, we believe the IRS should consider providing some transitional relief under certain circumstances. Filers of a timely filed Form 5558 that was received by the IRS after July 31, 2012, but that was not processed or returned, are left with no knowledge that the requested extensions have not been accepted or processed.

J. Employee Stock Ownership (ESOP) and Cash Balance Plan Prototypes

Recommendations

IRPAC recommends the IRS develop prototype and volume submitter procedures for ESOPs and cash balance retirement plans. The IRPAC would wholeheartedly endorse an IRS effort in this area and would provide assistance and input into the process as applicable.

Discussion

The IRS has established a series of procedures for taxpayers to submit applications for advanced determination letters on the tax-qualified status of retirement plans. These procedures give sponsors of prototype and volume submitter plans the opportunity to receive an advanced determination letter on plan document templates that can be adopted by different employers and plan sponsors with no or only a limited opportunity for variation. The prototype and volume submitter program permits plan sponsors to gain assurances about the tax-qualified status of the form of their plans without the necessity of submitting individualized determination letter applications, saving taxpayers time and money. Further, the prototype and volume submitter programs afford the IRS the opportunity to review and provide guidance to an increased number of plan sponsors in an efficient and cost effective manner.

The prototype and volume submitter programs, however, are not available for all types of tax-qualified retirement plans for which individual plan determination letter applications can be filed. TEGE has requested the IRPAC's thoughts on the development of prototype and volume submitter processes for both ESOPs and cash balance plans.

The IRPAC believes that the development of prototype and volume submitter procedures for ESOPs and cash balance retirement plans would be welcomed by the retirement plans community, and would be a valuable addition to the guidance and compliance programs developed by the IRS. The IRPAC wholeheartedly endorses an IRS effort in this area, and looks forward to providing assistance and input into the process as applicable.

K. Withholding of Tax on Nonresident Aliens and Foreign Entities

Recommendations

IRPAC recommended corrections be made in Table 1 on page 40 and 42 in Publication 515, Withholding of Tax on Nonresident Aliens and Foreign Entities, with respect to royalty income withholding rates for Film & TV for Egypt, Germany, Netherlands, Norway and Switzerland. The table indicates 30% withholding while the appropriate rate for these countries is zero.

Discussion

The entertainment industry, a supporter of IRPAC, noticed the IRS changes in the rates made to Publication 515 in 2011 for Egypt, Germany, Netherlands, Norway and Switzerland, but found there were no changes to the income tax treaties for these countries that would have justified the changes to the rates. The table in the publication indicates that 30% withholding applies while the rate for these countries under the applicable treaties is zero. The industry brought this concern to the IRPAC. Although definitive guidance is provided in the treaties themselves and not the publication, IRPAC recommended that the IRS review the table and correct the errors due to the then upcoming 2012 Summer Olympics. The IRS accepted the IRPAC recommendation and made the changes within 24 hours in time for the 2012 Summer Olympics. IRPAC understands that the publication will be updated during its next revision.