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Marketplace premium payment plans may be unhealthy for employers

The IRS recently posted a question-and-answer on its website advising employers that they may be subject to significant excise taxes if they reimburse employees' individual health insurance premiums on a pre-tax basis. This applies to insurance purchased both in and outside the marketplace.

Background

Because health coverage is now available through the public marketplace, some employers have decided that they will no longer offer coverage to part-time employees (i.e., those working less than 30 hours a week) and/or retirees. Employers will not face shared responsibility assessments if they fail to offer coverage to these groups.

To offset the loss of at least part of the employer subsidy that the employees or retirees may have received towards the cost of the employer-provided coverage, some employers have considered reimbursing at least a portion of the premium that these individuals will be paying for marketplace coverage. Because historically employers have been able to reimburse properly substantiated premiums paid for individual health coverage (or remit payment directly to the insurance company) on a tax-free basis, they may have assumed that they could do the same for marketplace premiums. An FAQ issued by the Departments of Treasury, Labor and Health & Human Services as well as guidance issued by the IRS suggest that this is not advisable — not only for employers, but for their employees and retirees.

Payment of marketplace premiums by employer payment plans

In January 2013, the Departments of Treasury, Labor and Health & Human Services issued an FAQ that, in part, addressed how the ACA's prohibition on annual dollar limits on essential health benefits applies to health reimbursement arrangements (HRAs). The FAQ defines HRAs as group health plans that "typically consist of a promise by an employer to reimburse qualified medical expenses (defined in the Code under section 213(d)) for a year up to a certain amount, with unused amounts available to reimburse medical expenses in future years." Generally, unless an HRA is integrated with other group health plan coverage that does not have annual dollar limits, the HRA will violate the prohibition on annual dollar limits because there is a maximum amount that an HRA can pay out during a year (i.e., an "inherent" limit). The FAQ states that an HRA cannot be integrated with individual marketplace coverage. See our February 21, 2013 *For Your Information.*

In Notice 2013-54, issued last September, the IRS provided further guidance on how the ACA market reforms apply to HRAs and other arrangements in which an employer contributes towards the cost of an individual health insurance policy either by reimbursing the employee for substantiated premium expenses or directly remitting funds to the insurance company. The notice refers to arrangements that make these payments on a pre-tax basis (i.e., the value is not included in employees' income) as "employer payment plans." The IRS stated that these employer payment plans are group health plans subject to the ACA's market reform provisions and, like HRAs, cannot be integrated with individual marketplace coverage. Thus, these plans will fail to comply with certain ACA requirements, including:

- **The prohibition on annual dollar limits on essential health benefits**. Employer payment plans will be considered to impose an annual dollar limit up to the cost of the individual insurance policy purchased through the arrangement.
- **Coverage of preventive services with no cost-sharing**. Employer payment plans may not provide preventive services without cost-sharing in all instances.

After-tax premium reimbursements

Only programs that reimburse individual premiums on a pre-tax basis are considered "employer payment plans." Employers can reimburse premiums on an after-tax basis without running afoul of ACA requirements.

The guidance also notes that although stand-alone retiree-only HRAs, (i.e., HRAs with fewer than two current employee participants on the first day of the plan year) are not subject to the market reform provisions, they are considered to be employer-provided minimum essential coverage if they reimburse medical expenses. As a result, a retiree who enrolls in marketplace coverage will not be eligible for a low-income subsidy for any month in which he or she has access to funds in an HRA.

> Buck comment. Although not addressed in the notice, the same rule applies to active employees — employees *enrolled* in employer-sponsored minimum essential coverage are not eligible for a low-income subsidy if they enroll in marketplace coverage. This is the case even if the employer coverage is not affordable or fails to provide minimum value.

FAQ discusses employer payment plans and penalties

The IRS recently posted a question-and-answer regarding employer payment plans on its website. Although the question-and-answer generally just summarizes the guidance set out in Notice 2013-54, it also points out that an employer sponsoring an employer payment plan could be subject to an excise tax of $100 per day ($36,500 per year) under Code section 4980D for each participating employee because of the plan's failure to comply with the ACA market reforms. (See our February 28, 2014 *For Your Information.*)

> Buck comment. Over the last several months, some vendors have suggested that employers can contribute to accounts that can fund (i.e., pay or reimburse) employees' and/or retirees' premiums for individual health coverage on a tax-free basis. This most recent IRS question-and-answer, highlighting the potential penalties, may be in response to vendor assertions that this type of arrangement either is a benefit excepted from ACA market reform compliance or does not violate

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the ACA. Some vendors have asserted, for example, that this arrangement can be offered to fewer than two current employees — such as to an executive in upper management, like a CEO — or to a retiree population. Others promote offering the arrangement to an active (full and/or part-time) population.

The issues raised by such an offering are complex and employers must carefully analyze all the compliance concerns. For example, in addition to ACA compliance issues, payment of premiums could potentially create COBRA obligations and have implications under the Code's nondiscrimination provisions.

In closing

Employers wanting to assist employees and retirees in paying for marketplace coverage should consider all their options and consult with legal counsel before setting up any program that would pay or reimburse individual premiums on a pre-tax basis. The "wrong" decision not only could expose the employer (and possibly employees) to substantial adverse tax consequences but also disqualify employees and retirees from receiving low-income subsidies if they purchase coverage through a public insurance marketplace.

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