TRUCKER ✦ HUSS

IRS Notice 2015-87: A Grab Bag of ACA, HRA and FSA Guidance

CALLAN CARTER

Please note: This article was updated on March 8, 2016

In a welcome set of "Questions and Answers," IRS Notice 2015-87 (the "Notice") formalizes and clarifies previously issued FAQs and informal guidance for group health plans implementing the Affordable Care Act ("ACA") and further explains how health flexible spending account ("FSA") carryovers may be administered. The major topics in the Notice are described below.

Health Reimbursement Arrangements (HRAs) and the ACA

Individual Plan Premium Reimbursements Permitted for Retiree HRAs Only: Reiterating its guidance in Notice 2013-54 and Notice 2015-17, the IRS confirms that a health reimbursement arrangement ("HRA") may only reimburse individual medical policy premiums of participants who are not current employees, such as a retiree-only HRA, without running afoul of the ACA's preventive care coverage requirement and the prohibition against dollar limits on "essential health benefits." The Notice also reiterates that such a standalone HRA is considered a group health plan that disqualifies the former employee from the premium tax credit for individual Marketplace/Exchange coverage under Section 36B of the Internal Revenue Code (the "Code"). As such, a plan sponsor may wish to disclose this fact in the HRA's summary plan description (SPD) and enrollment materials.

Integrated HRAs for Employees: To avoid violating the above referenced ACA reform requirements, an HRA that reimburses most expenses incurred by a current employee must be "integrated" with a group health plan as described in Notice 2013-54. The Notice further clarifies what constitutes an "integrated HRA":

- An HRA that reimburses employees for individual Marketplace coverage is NOT an "integrated HRA" and violates the ACA's reform requirements referenced above;
- If an HRA reimburses expenses incurred by an employee and the employee's spouse and/or dependents, the employee, spouse and dependents must all be enrolled in the group health plan for the HRA to be "integrated." (Note: Recognizing that many HRAs currently do not require family members to be covered under the group health plan as a condition to receiving HRA reimbursements, the Notice provides for a one year transition rule. Such an HRA, based on its plan terms as of December 16, 2015, would be considered "integrated" for the plan year beginning before January 1, 2017 if the "family member" provision is the sole reason why the HRA would not be treated as "integrated.");

- A standalone HRA for employees is permissible if it reimburses premiums for individual coverage that covers "excepted benefits" only (for example, the HRA reimburses premiums for dental insurance coverage); and
- An employer arrangement that reimburses the cost of individual market coverage offered under a Section 125 cafeteria plan (from funding from salary reduction or employer contributions, like flex credits) is considered a group health plan for purposes of the ACA reform requirements referenced above. Such a plan is NOT "integrated" and violates the ACA.

ACA Employer Mandate (Play or Pay Rules)

"Affordability"

"Applicable Large Employers," or "ALEs," may be subject to an excise tax under the ACA's play or pay rules for any month in which a full-time employee enrolls in coverage through the Marketplace/Exchange and receives a premium tax credit under Code Section 36B. However, an employee is not eligible for a premium tax credit for any month when he or she is eligible for coverage under an employer-sponsored group health plan that provides "minimum value" and is "affordable." A plan is unaffordable if the employee's required contribution for the lowest cost option for self-only coverage under the employer's group health plan exceeds 9.5% of the employee's household income. The Notice requires the following to be considered when determining whether the ALE has made an offer of affordable minimum value coverage for purposes of the "pay or play" assessment on employers under Code Section 4980H(b); determining eligibility for the premium tax credit for Marketplace/Exchange coverage under Code Section 36B, and administering the requirement for individual taxpayers to maintain coverage for themselves and their tax dependents under Code Section 5000A:

- **HRA Accruals:** Accruals under an integrated HRA that an employee may use to pay for premiums, other cost-sharing or other benefits under the integrated group health plan must be counted towards the employee's required contribution, if the accrual is required under the terms of the HRA or is otherwise determinable within a reasonable time before the employee must decide whether to enroll in the eligible employer-sponsored plan (for example, the contribution relates to the immediately following period of coverage for which the employee could enroll and use the HRA contribution). For purposes of Code Section 4980H(b) and the related reporting of offers of coverage to full-time employees under Code Section 6056, employer contributions to an HRA (and any resulting reduction in the employee contribution) will be treated as made ratably for each month of the period to which it relates.

  For example, if an employer makes $1,200 available under an HRA for the current year for an employee to use for cost-sharing under an integrated group health plan whose monthly premium is $200, 1/12 of the $1,200 will reduce the employee's share of the cost of coverage under the plan to $100 each month and will be taken into account as an employer contribution. This treatment of the HRA payment as an "employer contribution" will apply irrespective of whether the employee actually uses the HRA to pay for his or her share of the cost of major medical plan coverage. Employers relying on integrated HRA

accruals to meet the affordability requirement may wish to ensure that an accrual is required under the terms of the HRA document.

- **Health Flex Credits:** Employer flex credits to a cafeteria plan which may not be cashed out by the employee AND may only be used by the employee to pay for "minimum essential coverage" and health care (as defined by Code Section 213) will count towards the employee's required contribution (reducing the amount of the employee's required contribution). If an employer flex credit may also be cashed out or used to pay for non-health care benefits, such as dependent care under a dependent care flexible spending account, the credit will not be taken into account for purposes of determining whether the ALE made an "affordable" offer of coverage because the credit could be used for non-health coverage, irrespective of whether the employee actually used the credit towards health coverage.

  Transition Relief: Recognizing that many employer flex credits currently have not been designed to be limited to health care, the Notice provides for transition relief for plan years beginning before January 1, 2017. Under the relief, all employer flex credits will be treated as reducing the employee's required contribution until the first plan year beginning in 2017 and will be taken into consideration in the "affordability" determination. The transition relief is not available for non-health flex contribution arrangements that are adopted after December 16, 2015, or employers that substantially increase the amount of the non-health flex contribution after December 16, 2015.

- **"Cash-in-Lieu" and "Opt-Out" Payments:**
  Employer opt-out or cash-in-lieu payments that are made if the employee waives medical coverage must be taken into account when determining the amount of the employee's required contribution for coverage. For example, if Employee A must pay $300 per month for the cost of medical coverage but will receive $100 per month in cash if she declines medical coverage, Employee A's required employee contribution will be considered to be $400 per month because the employee must forgo $100 per month in additional compensation if she elects coverage.

  Transition Relief: Until regulations are issued by the IRS regarding the inclusion of such payments in the "affordability" determination for Code Section 4980H(b) purposes (and related reporting under Code Section 6056), the Notice employers are not required to include payments if the opt-out arrangement was already in effect, adopted or communicated to employees on or before December 15, 2015. However, for purposes of the premium tax credit for individual Marketplace/Exchange coverage under Code Sections 36B and 5000A, an individual taxpayer may treat payments he or she may receive from an opt-out arrangement in effect on OR after December 15, 2015 as increasing his or her contribution.

- **Increase in "Affordability" Percentage:** The IRS intends to amend the regulations under Code Section 4980H to provide that the 9.5% threshold under the Form W-2, rate of pay, and federal poverty line "affordability" safe harbors will be adjusted with the "individual affordability" percentage in Code Section 36B (9.56% for 2015 plan years and 9.66% for 2016 plan years). Employers may rely on the adjusted percentage for their 2015 Form 1095-C reporting.

Penalty Amounts Increase

The Code Section 4980H(a) and (b) penalty amounts will increase for 2015 and 2016. Under the ACA, there are two types of excise taxes that the IRS can levy against ALEs when a full-time employee obtains subsidized coverage through an exchange. An ALE that fails to offer "substantially all" of its full-time employees and their dependents "minimum essential coverage" may have to pay an excise tax under 4980H(a) ("the A penalty"), which is a set dollar amount multiplied by the number of full-time employees less 30 (less 80 in 2015). An ALE that fails to offer full-time employees "affordable" coverage that provides "minimum value" may have to pay an excise tax under Code Section 4980H(b) ("the B penalty"), which is a set dollar amount multiplied by the number of full-time employees who obtain a premium subsidy for their coverage on an exchange. The Notice provides for a "premium adjustment percentage" to these set dollar amounts to account for inflation. For 2015, the A penalty amount is $2,080 per year and the B penalty amount is $3,120 per year. For 2016, the A penalty amount is $2,160 per year and the B penalty amount is $3,240 per year.

"Hours of Service"

Counting Inactive Hours of Service: The IRS clarifies its reference to DOL Regulation 29 CFR 2530.200b-2(a) in its regulations regarding which hours must counted as "hours of service" for purposes of determining full-time employee status under Code Section 4980H. The Notice clarifies that an "hour of service" does NOT include any of the following:

- Any hour for which an employee is directly or indirectly paid or entitled to payment, on account of a period during which no duties are performed if such payment is made or due under a plan maintained solely for the purpose of complying with applicable workers' compensation, or unemployment or disability insurance law; or
- Any hour of service for a payment which solely reimburses an employee for medical or medically related expenses incurred by the employee; or
- Any hour of service during which an employee is not performing services but is receiving "non-taxable" short-term or long-term disability benefit payments because the employee paid for such disability benefit plan coverage, such as monthly premiums, with after-tax dollars.

[Note: Any hour of service during which an individual is not performing services but is receiving short-term or long-term disability benefits and retains status as an employee, must be treated as "hours of service" if the employer contributed directly or indirectly towards the benefit. For example, if coverage under the short-term or long-term disability benefit plan is paid by the employer or with employee pre-tax salary reduction, disability benefit payments will be counted as "hours of service."]

Healthcare FSAs

COBRA and the FSA Carryover: Pursuant to IRS Notice 2013-71, healthcare flexible spending accounts (FSAs) may provide for a carryover of up to $500 of unused amounts remaining at the end of the plan year. There are special COBRA rules for healthcare FSAs: 1) no COBRA continua-

tion offer is required if the remaining FSA balance exceeds the COBRA premium for the rest of the lan year, and 2) COBRA only has to be offered until the end of the plan year in which the qualifying event occurs and not for the usual 18, 29 or 36 month COBRA period. In the Notice, the IRS provides several new pieces of formal guidance on the application of COBRA to healthcare FSAs that have adopted the carryover feature:

- Any carryover amount from a prior plan year must be counted towards the remaining FSA balance when determining if an offer of COBRA must be made for the current plan year and the amount that the qualified beneficiary is entitled to receive for the remainder of the year if COBRA is available;
- Amounts carried over from prior years may not be taken into account for purposes of determining the FSA's COBRA premium (the premium may only be based on the employee's salary reduction election for the current year and any nonelective employer contributions to the employee's healthcare FSA);
- A healthcare FSA that provides a carryover must offer a COBRA beneficiary the opportunity to carryover up to $500 into a subsequent plan year, despite the special COBRA rule that would normally terminate healthcare FSA COBRA rights at the end of the plan year. However, the Notice clarifies that the health FSA is not required to allow a COBRA beneficiary to elect additional salary reduction amounts for the carryover period or to have access to any employer contributions to the health FSA made during the carryover period.

If you have any questions regarding the Notice or this article, please contact the author.

FEBRUARY 2016