



Compliance Alert

Agencies Prohibit All Employer Reimbursement of Individual Premiums

November 25, 2014

Quick Facts:

- On November 6, 2014, federal agencies issued FAQs prohibiting all employer arrangements that reimburse employees for individual premiums.
- Both pre-tax and after-tax arrangements will violate the ACA's market reforms.
- These arrangements may trigger an excise tax of \$100 per day for each applicable employee.
- Internal Revenue Code Section 105 reimbursement plans that are established to help employees purchase individual policies are also not permitted.

Due to the rising costs of health coverage, some employers have shown interest in helping employees pay for individual health insurance policies instead of offering an employer-sponsored plan.

In response, on November 6, 2014, the Departments of Labor (DOL), Health and Human Services (HHS) and the Treasury (Agencies) issued [FAQ guidance](#) clarifying that these arrangements do not comply with the Affordable Care Act's (ACA) market reforms and may subject employers to penalties.

Although it was widely believed that these penalties would apply only to pre-tax arrangements, the FAQs clarify that after-tax reimbursements and cash compensation for individual premiums also do not comply with the ACA's market reforms and may trigger the excise tax penalties.

This guidance essentially prohibits all employer arrangements that reimburse employees for individual premiums, whether employers treat the money as pre-tax or post-tax for employees.

Background on "employer payment plans"

In September 2013, [IRS Notice 2013-54](#) first addressed the application of the ACA's market reforms to health reimbursement arrangements (HRAs), certain health flexible spending arrangements (FSAs) and other employer payment plans.

Notice 2013-54 clarified that these arrangements are considered group health plans subject to the ACA's market reforms - including the annual limit prohibition and the preventive care coverage requirement - and cannot be integrated with individual policies to satisfy those requirements. As a result, effective for 2014 plan years, these plans are essentially prohibited.



In May 2014, the IRS issued two [FAQs](#) addressing the consequences for employers that reimburse employees for individual health insurance premiums. Because these employer payment plans do not comply with the ACA's market reforms, the IRS indicated in the FAQs that these arrangements may trigger an excise tax of \$100 per day for each applicable employee (\$36,500 per year per employee) under Internal Revenue Code section 4980D.

However, the Agencies' prior guidance suggested that this prohibition generally only applied to employer arrangements that reimburse individual premiums on a tax-free basis, and not to after-tax reimbursements. Thus, it was widely believed that premium reimbursement arrangements made on an after-tax basis would still be permitted.

Cash reimbursements

According to the new FAQs, an employer arrangement that provides cash reimbursement for an individual market policy is considered to be part of a plan, fund or other arrangement established or maintained for the purpose of providing medical care to employees, regardless of whether the payment is paid pre-tax or post-tax. Therefore, the arrangement is group health plan coverage subject to the ACA's market reform provisions.

The Agencies stressed that such employer health care arrangements cannot be integrated with individual market policies to satisfy the ACA's market reforms. As a result, any such plans will violate the ACA's market reforms, which can trigger penalties, including excise taxes under Code Section 4980D.

Employees with high claims risk

The FAQs also clarify that an employer cannot offer a choice between enrollment in the standard group health plan or cash only to employees with a high claims risk. This practice constitutes unlawful discrimination based on one or more health factors, in violation of federal nondiscrimination laws.

Although employers are permitted to have more favorable rules for eligibility or reduced premiums or contributions based on an adverse health factor (sometimes referred to as benign discrimination), the Agencies assert that offering cash-or-coverage arrangements only to employees with a high claims risk is not permissible benign discrimination.

Accordingly, these arrangements will violate the nondiscrimination provisions, regardless of whether:

- the employer treats the cash as pre-tax or post-tax for the employee;
- the employer is involved in purchasing or selecting any individual market product; or
- the employee obtains any individual health insurance.

The Agencies also noted that the choice between taxable cash and a tax-favored qualified benefit (the election of coverage under the group health plan) is required to be a Internal Revenue Code section 125 cafeteria plan. Consequently, offering this choice to only high-risk employees could result in discrimination in favor of highly compensated individuals, in violation of the cafeteria plan nondiscrimination rules.



Code section 105 reimbursement plans

The Agencies also noted that certain vendors are marketing products to employers claiming that, instead of providing a group health insurance plan, employers can establish a Code Section 105 reimbursement plan that works with health insurance brokers or agents to help employees select individual insurance policies allowing eligible employees to access subsidies for public Marketplace (Exchange) coverage.

The FAQs assert that these arrangements are problematic for several reasons. First, these arrangements are, themselves, group health plans. Therefore, employees participating in the arrangements are ineligible for Marketplace subsidies. The mere fact that the employer is not involved with an employee's individual selection or purchase of an individual health insurance policy does not prevent the arrangement from being a group health plan.

Second, as explained in previous Agency guidance, these arrangements are subject to the ACA's market reform provisions, including the annual limit prohibition and preventive care coverage requirement. As noted before, these employer health care arrangements cannot be integrated with individual market policies to satisfy the market reforms and, therefore, can trigger penalties, including excise taxes under Code Section 4980D.

Recommendations for employers

To avoid potential penalties under various federal regulations:

- Employers that are considering providing payment or reimbursement for employees' individual health insurance policies, whether on a pre- or post-tax basis, will want to review the new guidance in the FAQs and consider stopping such practices.
- Employers may not offer a choice between enrollment in the group health plan or cash only to employees with a high claims risk which violates federal nondiscrimination regulations.
- Code section 105 reimbursement plans are considered group health plans and subject to market reforms. Such plans cannot be integrated with individual policies and therefore, an employer using these types of arrangements may be subject to penalties.

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For further information on this or any other topics, please contact your EPIC benefits consulting team.

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