

News Alert – IRS Clarifies that Employers Shall Not Purchase or Reimburse Individual Employee Health Policies with Pre-Tax Dollars

Recently, the Internal Revenue Service (“IRS”) announced clarification to earlier regulations, stating that employers are prohibited from the use of pre-tax employee contributions to cafeteria plans or reimbursement arrangements that purchase individual coverage on a health insurance exchange. Employers who do not comply with this guidance may be subject to a steep excise tax of \$100 per day per employee. The information below provides a summary of clarification by the IRS.

Summary

As previously reported last year, on September 13, 2013, the IRS issued Notice 2013-54, which explained how the ACA market reforms apply to certain types of group health plans, including health reimbursement arrangements, health flexible spending arrangements and certain other employer health care arrangements, including arrangements under which an employer reimburses an employee for some or all of the premium expenses incurred for an individual health insurance policy. As you may recall, Notice 2013-54 began the discussion of “integrated” reimbursement arrangements and stand-alone FSAs and HRAs.

Despite the previous guidance, and due to the continued effort of employers trying to find avenues to lessen the employer mandate, the IRS issued clarification and reiterated that employers shall not use pre-tax employee contributions for arrangements under which an employer reimburses an employee for some or all of the premium expenses incurred for an individual health insurance policy. However, the IRS did opine that employers are allowed to give reimbursement, in the form of taxable wages (i.e., after-tax), for an employee to purchase a health insurance plan through an exchange.

The IRS further urges that if an employer does not establish a health insurance plan for its own employees, but reimburses those employees for premiums they pay for health insurance (either through a qualified health plan in the Marketplace or outside the Marketplace) with pre-tax dollars, then that employer’s plan fails to satisfy the market reforms and may be subject to a \$100/day excise tax per applicable employee (which is \$36,500 per year, per employee) under section 4980D of the Internal Revenue Code. This notice applies for plan years beginning on and after Jan. 1, 2014, but taxpayers may apply the guidance provided in the notice for all prior periods.

Small Employers – How Does This Apply?

Employers with fewer than 50 full-time equivalent employees are not subject to the employer mandate and, therefore, will not be penalized for discontinuing a health plan and giving their employees taxable wages to purchase an individual market plan. If the employee is eligible based on income, they could also access a premium subsidy.

Remember, too, that small employers are permitted to subsidize policies on the Marketplace through the SHOP that is part of the Marketplace. This will allow small employers to establish programs to subsidize coverage that employees choose, but employees will be limited to the plans available under SHOP (limited free choice).

Private Exchanges?

Under the new guidance, the private exchanges that employers may use for their employees are not affected by this ruling. As such, employers may still use private exchanges for purposes of the mandate as well as provide pre-tax premiums for such private exchanges

More Information?

Although the IRS has clarified its stance on this subject, the DOL issued a notice in substantially identical form to Notice 2013-54. The HHS has indicated it will issue concurring guidance shortly. Furthermore, back in early January 2013, the DOL and HHS issued FAQs that addressed the application of health reimbursement arrangements to ACA. If you have any questions or would like to seek additional guidance, please contact your local account representative.