



Health Care Reform

LEGISLATIVE BRIEF

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Paying Premiums for Individual Health Insurance Policies

The Affordable Care Act (ACA) reforms that took effect in 2014 may make purchasing health insurance in the individual market more accessible. Due to these reforms and the rising costs of health coverage, some employers have considered helping employees pay for individual health insurance policies instead of offering an employer-sponsored group health plan.

On Sept. 13, 2013, the Internal Revenue Service (IRS) issued [Notice 2013-54](#) to address how the ACA's market reforms apply to health reimbursement arrangements (HRAs), cafeteria plans and other employer payment plans. The Notice is effective for plan years beginning on or after **Jan. 1, 2014**.

By eliminating the tax savings associated with contributions toward individual coverage, the Notice discourages employers from helping employees pay for individual policies in lieu of offering a group health plan. **Effective for 2014, if employers want to help employees pay their individual policy premiums, it generally must be on an after-tax basis.** However, employers may continue to provide group health coverage for their employees on a tax-free basis.

This Legislative Brief outlines how employers have traditionally paid for employees' individual policy premiums on a tax-free basis and summarizes how the ACA affects these arrangements starting in 2014.

HRAS

HRAs have been used by employers to help employees pay for the cost of individual insurance policies on a tax-free basis. Unlike health flexible spending accounts (FSAs) and health savings accounts (HSAs), HRAs can be used to reimburse health insurance premiums. Also, unlike an HSA, an individual does not need to be covered under a high-deductible health plan (HDHP) to participate in an HRA. This has made HRAs particularly compatible with individual health insurance policies.

The Notice addresses how the ACA's market reforms apply to HRAs, including HRAs that are not integrated with other group health coverage, or "stand-alone" HRAs. An HRA used to purchase coverage on the individual market cannot be integrated with that individual coverage, and is considered a stand-alone HRA. Some stand-alone HRAs are not subject to the ACA's market reforms because they fall under an exception, such as retiree-only HRAs. However, beginning in 2014, stand-alone HRAs that do not fall under an exception will not be permitted due to the ACA's annual limit prohibition and preventive care requirements.

Thus, effective for 2014 plan years, employers will not be able to offer a stand-alone HRA for employees to purchase individual coverage, inside or outside of an Exchange, without violating specific provisions of the ACA and risking exposure to severe financial penalties.

EMPLOYER PAYMENT PLANS

In [Revenue Ruling 61-146](#), the IRS provided that if an employer reimburses an employee's substantiated premiums for non-employer sponsored hospital and medical insurance, the payments are excluded from the employee's gross income under Internal Revenue Code (Code) section 106. This IRS guidance allowed an employer to pay an employee's premiums for individual health insurance coverage without the employee paying tax on the amount.

The Notice refers to this type of arrangement as an "employer payment plan." An employer payment plan appears to also include any tax-advantaged arrangement to pay for individual health insurance premiums, including employee pre-tax salary reduction contributions paid through a cafeteria plan.



Paying Premiums for Individual Health Insurance Policies

Similar to the guidance for HRAs, the Notice provides that an employer payment plan that reimburses employees for their individual insurance policy premiums will not comply with the ACA's annual limit prohibition and preventive care requirements. Thus, effective for 2014 plan years, these plans will essentially be prohibited.

On May 13, 2014, the IRS issued [FAQs](#) addressing the consequences for employers that do not establish a health insurance plan for their own employees, but instead reimburse those employees for premiums they pay for health insurance (either through an Exchange or outside of an Exchange). Because these employer payment plans do not comply with the ACA's market reforms, the IRS indicated in the FAQs that these arrangements may be subject to an excise tax of **\$100 per day for each applicable employee** (\$36,500 per year, per employee) under Code section 4980D.

However, an employer payment plan does not include an employer-sponsored arrangement that allows an employee to choose either cash or an after-tax amount to be applied toward health coverage. Thus, premium reimbursement arrangements made on an after-tax basis will still be permitted. Employers that plan on using after-tax premium reimbursement arrangements to help employees pay for health coverage should be aware that these arrangements may be considered ERISA plans.

CAFETERIA PLANS

A Section 125 Plan, or a cafeteria plan, can be used by employers to help employees pay for certain expenses, including health insurance, on a pre-tax basis. The proposed cafeteria plan regulations from 2007 allow for the pre-tax payment or reimbursement of individual health insurance policy premiums under a cafeteria plan. However, the ACA changes this rule and prohibits cafeteria plans from paying or reimbursing premiums for individual health insurance policies, effective for 2014.

The ACA's prohibition on including individual health insurance policies under a cafeteria plan applies to policies purchased on an Exchange and through the private market, as follows:

- **Exchange Coverage:** The ACA provides that individual health insurance offered through an Exchange cannot be reimbursed or paid for under a cafeteria plan. Exchange coverage may be funded through a cafeteria plan only if the employee's employer elects to make group coverage available through the Exchange's Small Business Health Options Program (SHOP).
- **Non-Exchange Coverage:** The Notice indicates that, effective for 2014, cafeteria plans may not be used to pay premiums for individual health insurance policies that provide major medical coverage. However, it appears that this restriction does not apply to individual policies that are limited to coverage that is excepted from the ACA's market reforms, such as retiree-only coverage, or limited-scope dental or vision benefits.

Thus, effective for 2014, the tax exclusion provided through a cafeteria plan is only available when group coverage is purchased. Employers that want to contribute toward the cost of individual coverage must do so on a taxable basis.

The Notice provides a transition rule for certain cafeteria plans for plan years beginning before Jan. 1, 2014. For cafeteria plans that as of Sept. 13, 2013, operate on a plan year other than a calendar year, the restriction on purchasing individual Exchange coverage through a cafeteria plan will not apply before the first plan year that begins after Dec. 31, 2013. However, individuals may not claim a premium tax subsidy for any month in which they are covered by an individual plan purchased through an Exchange as a benefit under a cafeteria plan.

MORE INFORMATION

The Department of Labor (DOL) also issued [Technical Release 2013-03](#) on Sept. 12, 2013, which is substantially identical to IRS Notice 2013-54. In addition, the Department of Health and Human Services (HHS) is expected to shortly issue guidance to reflect that it concurs with Notice 2013-54. On Jan. 24, 2013, the DOL and HHS also issued [FAQs](#) that addressed the application of the ACA to HRAs.

This Legislative Brief is not intended to be exhaustive nor should any discussion or opinions be construed as legal advice. Readers should contact legal counsel for legal advice.

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