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New HRA Regulations Part 5 – More on the Employer Shared Responsibility Mandate

Employee Benefits & Executive Compensation Blog on **October 29, 2019**

On September 30th, the IRS issued proposed regulations that establish safe harbors for compliance with the employer mandate in the context of individual coverage health reimbursement arrangements (or "ICHRAs"). These proposed regulations are important for employers that choose to offer ICHRAs and want to be sure they comply with the employer shared responsibility mandate requirements under the Affordable Care Act ("ACA").

The issues being clarified in the proposed regulations stem from prior guidance that we explained in our blog series on the final health reimbursement arrangement (HRA) regulations issued by the Departments of Labor, Health and Human Services, and Treasury (the "Departments") in June 2019. That guidance established basic parameters for how the new ICHRAs would interact with the ACA employer shared responsibility mandate. However, that earlier guidance needed to be fleshed out based on industry feedback and experience. The September 30th proposed regulations (which also cover nondiscrimination issues that will be summarized in a subsequent blog) provide that additional guidance.

The key stumbling block to ACA compliance in this area is in determining whether the ICHRA coverage provided is "affordable" for ACA purposes. This is an extraordinarily complex undertaking. To help solve that problem, therefore, the proposed regulations include several safe harbor methods of compliance, such as a location-based safe harbor, a lookback safe harbor and a general affordability safe harbor. Before we explain these safe harbor rules, let's step back and understand why affordability matters for ACA purposes.

ACA Employer Mandate: Why Affordability Matters

The ACA's employer mandate, codified under Section 4980H of the Internal Revenue Code ("Section 4980H") generally requires (subject to stiff penalties) that applicable large employers ("ALEs," generally employers that employ more than 50 full-time employees on a controlled-group basis) offer eligible employer-sponsored health coverage to at least 95% of their full-time employees and their dependent children. Even if an employer satisfies the 95% requirement, though, a smaller penalty under Section 4980H(b) could still be assessed if the coverage offered is either not "affordable" or does not have minimum value. So it is important to know whether coverage is "affordable" in order to mitigate or avoid ACA penalties.

Here's where it gets complicated. Affordability for purposes of the employer mandate is tied to the same formula used for determining an individual's premium tax credit eligibility on the ACA Marketplace. In that context, affordability is determined based on whether the cost of the second lowest cost silver plan available to the individual on the ACA Marketplace is less than 9.5% (adjusted for inflation) of his or her household income. In the *group* health plan context, the relevant comparator is the employee portion of the self-only premium for the lowest cost minimum value coverage option offered by the employer to the employee.

Determining the coverage option to use for affordability purposes is easy enough in the group health plan environment, but using household income as a measure of affordability is a problem because employers typically do not have that information. Therefore, in prior ACA guidance, the IRS established three affordability safe harbors for employers—the W-2 safe harbor, the rate of pay safe harbor, and the federal poverty line safe harbor.

The problem is that these general safe harbors alone cannot solve the affordability conundrum related to ICHRAs. With IRS Notice 2018-88, the IRS began laying the groundwork for future regulations by outlining some basic parameters for compliance with the ACA mandate. For example, Notice 2018-88 provided that ICHRAs are minimum essential coverage and an affordable ICHRA will be deemed to have minimum value. But even with those basic rules, affordability was viewed as a real challenge and additional guidance was necessary.

Applying Affordability to ICHRAs

The proposed regulations reiterate the position in IRS Notice 2018-88 and state that affordability for purposes of Section 4980H(b) involves a similar methodology to that used for calculating premium tax credit eligibility. For an ICHRA to be affordable in a given month, an "employee's required HRA contribution" (or the difference the monthly HRA contribution for self-only coverage and the lowest cost silver-level plan available on the Marketplace) must not exceed 1/12 of (a) the employee's household income for the taxable year multiplied by (b) the "required contribution percentage" (currently set at 9.86%).

For employers, particularly those with a large, national workforce, applying this formula would be extremely difficult. That is because the "required HRA contribution" is based in part on the lowest cost silver-level plan available on the Marketplace within the relevant rating area. That cost varies on an individual-basis depending on age and place of residence. To help employers apply these rules, the proposed regulations propose the following safe harbors for affordability purposes:

- Location Safe Harbor. Under the location safe harbor for determining affordability, the proposed regulations would allow ALEs to measure affordability against the lowest cost silver-level plan available in the area where an employee's primary site of employment is located. For purposes of this safe harbor, an employee's primary site of employment is the location at which the employer reasonably expects the employee to perform services on the first day of the plan year (or, on the first day the ICHRA takes effect). In some cases (*g.*, when an employee works remotely and cannot be required to report to a particular worksite), the ALE will be required to consider an employee's place of residence. Employers with multiple worksite locations would still be required to determine affordability for Section 4980H purposes separately for each area.
- Lookback Safe Harbor. Employers typically determine the employee cost-share for coverage in the fall of each year (i.e., the open enrollment period for calendar year plans). However, at that time, the premiums for individual market coverage in the following year are typically not yet available. As such, for measuring affordability, the proposed regulations offer a safe harbor through which ALEs with a calendar plan year may use the monthly premium for the lowest cost silver plan in January of the prior calendar year. A similar safe harbor is also available to ALEs with non-calendar plan years; however, the applicable lookback date is the January of the current calendar year, as opposed to the January of the prior year.

- General Affordability Safe Harbors. As discussed above, whether an ICHRA is considered affordable is partially based on the relationship between the employee's required HRA contribution and the employee's household income for the taxable year. Because an employer offering an ICHRA will generally not know an employee's household income, the proposed regulations provide that ALEs offering ICHRAs are permitted to use the three general affordability safe harbors established previously by the IRS (*e.*, the W-2 safe harbor, the rate of pay safe harbor, and the federal poverty line safe harbor).

What about other safe harbors?

The Treasury Department declined to provide an age-based safe harbor, noting that it was limited in its ability to materially deviate from the premium tax credit rules. Nevertheless, the proposed regulations did offer some simplifications to help employers through this problem. First, although affordability is determined on a monthly basis, an employee's age at the start of the plan year (or the date on which the employee becomes eligible to participate) can be used for the duration of the plan year. Second, if within an age band, there is variation among the lowest cost silver plan for different ages in that band, the lowest cost silver plan for that entire age band can be used for all ages in the age band. Employers would still need to make adjustments based on location, however. Finally, the Treasury Department noted that employers could always simplify the process by using the premium applicable to the lowest cost silver plan available to the oldest employee for all employees within the applicable location. This simplification, however, would generally require a higher benefits spend than necessary.

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These proposed regulations make an effort to ease the burden on employers with respect to the affordability calculus for ICHRAs. To some degree, the proposed safe harbors will be helpful for ICHRA sponsors. Even with these safe harbors, though, the administrative burden in determining affordability may be significant, particularly for employers with a widespread employee base. ALEs that are considering adopting ICHRAs should consult with benefit advisors and counsel when designing the plan and assessing affordability.

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