ACA, HIPAA AND FEDERAL HEALTH BENEFIT MANDATES:

Practical Q&A

The Affordable Care Act (ACA), the Health Insurance Portability and Accountability Act of 1996 (HIPAA) and other federal health benefit mandates (e.g., the Mental Health Parity Act, the Newborns and Mothers Health Protection Act, and the Women's Health and Cancer Rights Act) dramatically impact the administration of self-insured health plans. This monthly column provides practical answers to administration questions and current guidance on ACA, HIPAA and other federal benefit mandates.

Attorneys John R. Hickman, Ashley Gillihan, Carolyn Smith, and Dan Taylor provide the answers in this column. Mr. Hickman is partner in charge of the Health Benefits Practice with Alston & Bird, LLP, an Atlanta, New York, Los Angeles, Charlotte and Washington, D.C. law firm. Ashley Gillihan, Carolyn Smith and Dan Taylor are members of the Health Benefits Practice. Answers are provided as general guidance on the subjects covered in the question and are not provided as legal advice to the questioner's situation. Any legal issues should be reviewed by your legal counsel to apply the law to the particular facts of your situation. Readers are encouraged to send questions by E-MAIL to Mr. Hickman at john.hickman@alston.com.

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QSEHRAs: End-of-Year Legislation Provides a New Health Care Option for Small Employers

Tucked at the end of the recently enacted 300-plus-page 21st Century Cures Act (Cures Act)[1] is a provision that offers certain small employers a new opportunity to help employees purchase individual market major medical coverage and pay for other medical expenses.

The new health reimbursement arrangement vehicle, called Qualified Small Employer Health Reimbursement Arrangements (QSEHRAs), is available to employers that are not subject to the Affordable Care Act (ACA) employer responsibility penalties – i.e., employers that have less than 50 full-time equivalent employees and thus are not applicable large employers (ALEs). Many small employers are likely to find QSEHRAs attractive, but there are some features that should be looked at carefully before deciding to move forward. These include a requirement that a QSEHRA can only be funded through direct employer contributions (meaning that no employee salary reduction contributions are permitted), nondiscrimination rules, and a provision prohibiting employers from maintaining another group health plan.

Note that for insurers, brokers and agents, some states consider individual health insurance paid for by employers to be group health insurance. Thus, insurers, brokers and agents working with small employers should carefully consider state-law implications. Some states specifically prohibit employers from reimbursing individual premiums. We expect that states may review these rules in light of the Cures Act, although it may take some time. This article addresses key features of QSEHRAs:

Why QSEHRAs?

The Cures Act provision is designed to overrule agency guidance under the ACA prohibiting employer arrangements that seek to pay or reimburse the cost of individual market major medical insurance purchased by employees. This guidance specifically provides that stand-alone health reimbursement arrangements (HRAs), meaning HRAs that are not integrated with another group health plan, are not permitted. [2] While these restrictions are not clear from the statutory provisions of the ACA, regulations and other administrative guidance preclude this type of arrangement on the basis that they violate one or more ACA requirements applicable to group health plans, in particular, preventive care requirements and/or the prohibition on annual dollar limits on benefits.

The federal tri-agencies (Department of Labor, Department of Health and Human Services, and Internal Revenue Service/ Department of the Treasury) use the broad term "employer payment plan" to encompass the types of arrangements prohibited under this guidance. In some cases, even post-tax arrangements for the cost of individual market major medical insurance are not permitted, depending upon the level of employer involvement in the arrangement. Prior to enactment of the Cures Act, employers that adopted these types of arrangements were subject to a $100 per person per day excise tax under Internal Revenue Code § 4980D (for private employers) or a $100 per day penalty under Public Health Service Act § 2723(for governmental employers).

The Cures Act allows small employers to adopt this type of HRA arrangement, provided the requirements in the Act are followed. QSEHRAs are not subject to the ACA market reforms and are not subject to COBRA requirements.

Eligible Employers

An employer is eligible to adopt a QSEHRA if both the following requirements are met:

(1) The employer is not an applicable large employer (ALE) as defined under the ACA employer responsibility penalties under tax code § 4980H. Under 4980H, ALE status is determined on a controlled group basis, so that for an employer to be eligible for a QSEHRA, the entire controlled group must collectively employee less than 50 full-time equivalent employees in the prior calendar year.

(2) The employer does not maintain a "group health plan" for any employees.

The Cures Act does not specifically define "group health plan" for purposes of the requirement that a small employer adopting a QSEHRA cannot offer a group health plan to any employee. The definition of group health plan in the tax code is fairly broad and includes more than just major medical coverage. For example, health flexible spending arrangements (FSAs) and supplemental benefits such as dental and vision plans are considered group health plans for some purposes (e.g., COBRA). It is most likely that such arrangements were not intended to be prohibited. The purpose of the requirement that the employer could not offer both a group health plan and a QSEHRA is to prevent "cherry picking;" that is, offering a group health plan to some "healthy" employees but not others, with the potential result that higher-risk individuals would be in the individual health insurance market. Supplemental coverage does not present this same risk.

Permitted Contributions

Salary reduction contributions to a QSEHRA are not permitted. Thus, a QSEHRA must be funded solely by the employer. Moreover, as discussed below, the prior agency guidance would seem to continue to prohibit employees from paying any additional cost of the individual major medical coverage on a pre-tax basis.

Nondiscrimination Requirements

In general, a QSEHRA must be provided on the same terms to all eligible employees. However, the employer can vary the amount of reimbursements available under the arrangement based on age of the eligible employee (and family members if the arrangement covers family members) or the number of family members of the employee covered under the arrangement. Any such variation must be made in accordance with the variation in price of an insurance policy in the relevant individual health insurance market. For this purpose, any variation must be determined by reference to the same insurance policy with respect to all eligible employees.

"Eligible employee" means any employee of the employer. However, a QSEHRA may exclude the following employees:

- Employees who have not completed 90 days of service;
- Employees who have not attained age 25;
- Part-time or seasonal employees;
- Employees covered by a collective bargaining agreement; and
- Nonresident aliens who receive no earned income from the employer from sources within the United States.

"Proof of Coverage" Requirement

Part of the definition of a QSEHRA is that the arrangement provides for the payment or reimbursement of medical expenses as defined under tax code § 213(d) "after the employee provides proof of coverage." The term "coverage" is not defined for this purpose. While the overall objective of the legislation is to enable small employers to offer their employees a means of paying for individual market coverage on a pre-tax basis, the statutory language does not on its face restrict coverage in this context to individual market coverage. Thus, it appears that any type of health coverage would potentially meet this coverage requirement. Supplemental indemnity coverage would not be eligible due to the IRS' interpretation that such coverage does not qualify as a 213(d) eligible expense even though such coverage may qualify as an excludable § 106 accident or health plan under when funded by the employer directly or through a cafeteria plan.

It is not entirely clear how this requirement will be enforced. Because this is part of the definition of a QSEHRA, it appears that arrangement will not be exempt from the ACA requirements if the employer does not obtain proof of coverage from the employee. While the statute does not address what steps an employer would need to take to verify coverage, relying on a certification from the employee could be a reasonable approach. As noted above, if the individual does not have minimum essential coverage (MEC), any reimbursements are taxable to the employee.

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Permitted Benefits

Reimbursements that are permitted under a QSEHRA are expenses for medical care as defined under tax code § 213(d). Thus, reimbursement of individual major medical health insurance premiums, as well as other § 213(d) expenses, is permitted. Premiums paid by the employee on a pre-tax basis for coverage under a group health plan of another employer (e.g., the spouse's employer) would not qualify for tax-free treatment.

The maximum amount available under a QEHRA for any year cannot exceed $4,950 ($10,000 if the arrangement provides for payments for medical care for family members). The dollar amounts are prorated if an employee is covered under the arrangement for less than a full year. The dollar amounts are indexed in $50 increments for inflation after 2016, based on changes in the Consumer Price Index for All Urban Consumers (the same index used for purposes of determining rate brackets under the income tax rules).

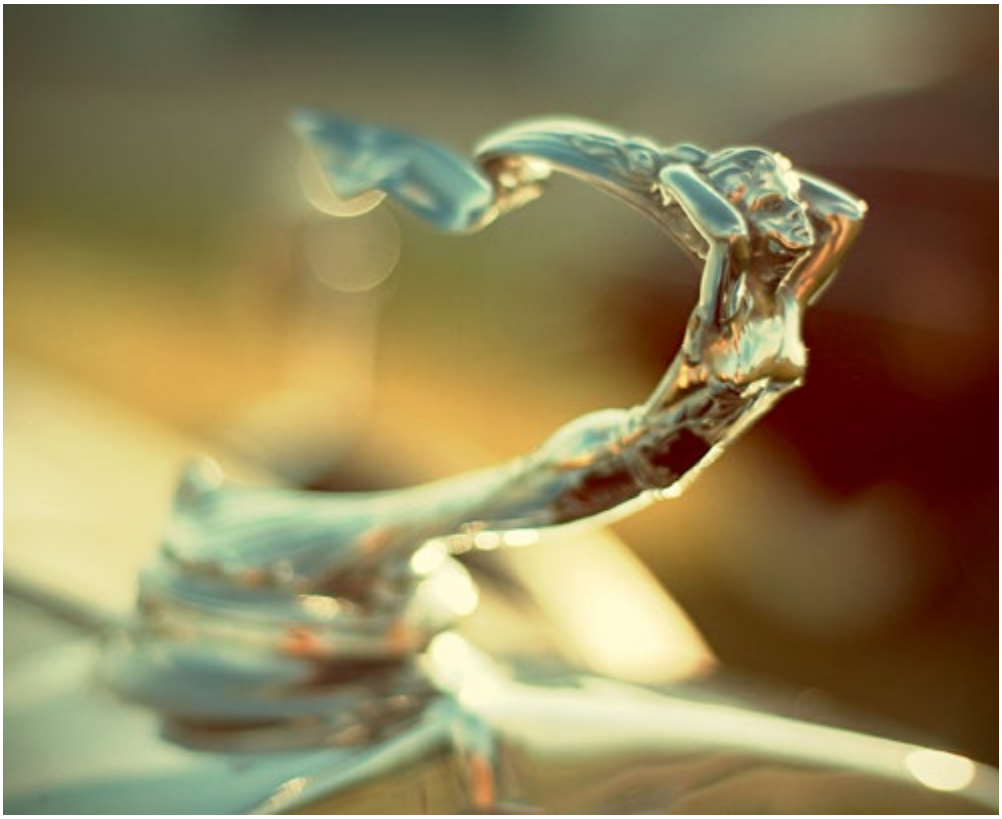
Tax Treatment of Reimbursements

Reimbursements are tax-free to the employee if the employee has MEC for the month in which the expense is incurred. MEC is defined under the ACA rules under tax code § 5000A(f). The QSEHRA itself is not MEC, so the employee must have some other type of coverage (e.g., in many cases, the individual major medical coverage they are purchasing) to qualify for tax-exempt treatment. The language does not restrict MEC to any particular type of coverage and thus, for example, would appear to include individual market coverage whether purchased on or off the Marketplace, group health plan coverage through another employer, and Medicare.

Cadillac Plan Tax

Benefits under a QSEHRA are taken into account for purposes of the so-called Cadillac plan tax under tax code § 4980I, currently scheduled to go into effect in 2020. For Cadillac plan tax purposes, the value of the coverage under a QSEHRA is the maximum amount of permitted benefit available under the arrangement to the employee and not the specific amounts reimbursed.

Even though QSEHRAs are subject to the Cadillac tax, it seems unlikely that the tax would apply with respect to such arrangements, assuming that the tax does go into effect. This is for two reasons. First the maximum permitted benefit is significantly less than the Cadillac plan tax thresholds, which are $10,200 for single coverage and $27,500 for family coverage. These are the 2018 amounts; the thresholds will be higher in 2020 and are indexed in subsequent years. In addition, because QSEHRAs are available only to employers that do not have another group health plan (other than possibly certain types of supplemental coverage), no other coverage of that employer is likely to push the value over the threshold.



Coordination with ACA Premium Tax Credits

There is a special rule for coordinating QSEHRAs with eligibility for premium tax subsidies. An employee who is provided a QSEHRA is not eligible for a premium tax credit if the QSEHRA is "affordable." Affordability for this purpose is computed in a manner similar for other employer coverage.

The QSEHRA is considered affordable for a month if excess of the self-only premium under the second lowest cost silver plan offered in the relevant individual health insurance market over 1/12 of the employee's permitted benefit under the QSEHRA does not exceed 1/12 of 9.5 percent of the employee's household income. The 9.5 number is indexed. The legislation did not provide any safe harbors for employers to determine household income. However, further guidance would be welcome from the IRS on what safe harbors it might allow, such as those it developed to determine affordability of coverage under tax code § 4980H(b).

If QSEHRA coverage does not meet the affordability standard, then the monthly premium tax credit is reduced by 1/12 of the annual benefit under the QSEHRA.

Consequences for Failing to Meet QSEHRA Requirements

The requirement that QSEHRAs be funded by the employer (with no salary reduction contributions), the nondiscrimination rules, and the proof of coverage provision are all part of the definition of a QSEHRA. An arrangement that does not satisfy these requirements is not a QSEHRA and will be

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subject to the ACA market reforms and other requirements applicable to group health plans. Thus, an employer that fails to meet the applicable requirements could be subject to the $100 per person per day excise tax or penalty (as applicable).

Employers adopting a QSEHRA may also be subject to penalties for failing to meet applicable reporting requirements.

Notice, Reporting, and Substantiation Requirements

Employers are required to notify eligible employees of a QSEHRA 90 days before the beginning of the year in which the employer will fund the arrangement. The notice must include the amount of the benefit under the QSEHRA and also inform the employee that payments may be taxable if the employee does not have MEC. Employers must report the permitted benefit on the employee's Form W-2 for the year. Employers will also likely need to have procedures to substantiate the medical expenses that are reimbursed under the QSEHRA. The Cures Act specifically authorizes the Treasury Department to adopt substantiation rules.

Effective Date and Transition Rule

The QSEHRA provisions are effective for years beginning after December 31, 2016. In addition, the legislation extends transition relief previously provided under IRS Notice 2015-17 to any plan year beginning on or before December 31, 2016. The federal tri-agencies have issued a FAQ describing how this transition relief applies after enactment of the Cures Act. [3] The FAQ states that consistent with Notice 2015-17, the relief from penalties does not extend to stand-alone HRAs or other arrangements that reimburse medical expenses other than insurance premiums. Further, the FAQ clarifies that pre-Cures Act agency guidance continues to apply for employer arrangements that reimburse individual major medical premiums that are not QSEHRAs (e.g., employer payment plans and non-QSEHRA HRAs). ■

References

[1] The text of the Cures Act may be found at https://www.congress.gov/bill/114th-congress/house-bill/34/text. The QSEHRA provision is in section 18001. The act was signed by President Obama on December 13, 2016.

[2] The agency guidance prohibits pre-tax salary reduction and most other forms of employer reimbursement of individual major medical insurance. Other than as specifically allowed for QSEHRAs, this prior agency guidance continues to prohibit such "employer payment plan" arrangements.

[3] ACA FAQs part 35, available at https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/faqs/aca-part-35.pdf