Discussion of IRS Notice 2015-52

ACA 40% Excise Tax

August 12, 2015

ERIC

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Key categories for discussion

- Payment of the tax
- Employer aggregation
- Cost of coverage
  - Time periods
  - Passing through reimbursements
  - Allocation of contributions to account-based plans
  - FSA contributions
- Age and gender adjustments
- Notice and payment
- Other???

Payment of the 40% excise tax

- "Coverage provider" is liable for excise tax on its share of excess benefit with respect to an employee for a taxable period
- Definition of "coverage provider"
  - Insurer
  - Employer, in case of HSAs and Archer MSAs
  - For all other coverage: Person that administers the plan benefit
    - = the plan sponsor if the plan sponsor administers benefits under the plan
      - Person responsible for day-to-day administration of plan benefits
      - Person with ultimate authority under plan for administration

Questions - paying the tax

- First approach: *person that administers the plan benefits* = the TPA
- 1. What types of administrative functions should be considered under this first approach when determining the *person that administers the plan benefits*?
- 2. Is the *person that administers the plan benefits* easily identified, or would the identity of this person be unclear because more than one entity (such as a pharmacy benefit administrator and a medical claims benefit administrator) would be performing administrative functions for a particular benefit?
- 3. Do you have other concerns with this approach?
- Second approach: *person that administers the plan benefits* = the employer
- 1. Would the *person that administers the plan benefits* be easy to identify under this second approach?
- 2. Do you have other concerns with this approach?

Employer aggregation

- For purposes of the 40% excise tax, all employers are treated as a single employer under the rules of IRC 414 (b), (c), (m), or (o)

Questions – employer aggregation

- Practical challenges of applying the aggregation rules
- Specific comments on:
- (1) identification of the applicable coverage taken into account as made available by an employer;
- (2) identification of the employees taken into account for the age and gender adjustment and the adjustment for employees in high risk professions or who repair and install electrical or telecommunications lines;
- (3) identification of the taxpayer responsible for calculating and reporting the excess benefit; and
- (4) identification of the employer liable for any penalty for failure to properly calculate the tax imposed under § 4980I

Cost of coverage - timing

- Taxable period = calendar year
- Employer determines cost of applicable coverage soon after taxable year ends
  - Notifies IRS and coverage provider
  - Coverage provider is to pay the tax in a "reasonably timely" manner

Questions – cost of coverage - timing

- 1. Recognizing that the timing issues may be different for insurers, self-funded plans, and HSAs, what difficulties are raised for you concerning the anticipated need to determine the cost of applicable coverage for a taxable period reasonably soon after the end of that taxable period?
- 2. Some experience-rated arrangements may provide for payments after the end of a coverage period or may provide for premium discounts for the next coverage period. How are employers addressing these payments or discounts currently for purposes of determining COBRA premiums?
- 3. What processes will be involved in calculating and allocating any excess benefit, and what time period will be necessary to complete these processes?

Cost of coverage – reimbursements

- If coverage provider (who is not the employer) pays the excise tax, the coverage provider may seek reimbursement from employer for tax
  - Payment of excise tax is not deductible
  - Reimbursement will be subject to income tax
  - Coverage provider will also seek reimbursement to offset additional income tax payment
  - Both reimbursements probably will need to be separately billed and identified

Cost of coverage – taxation of reimbursements

- IRS may develop formula to determine income tax reimbursement excludable from cost of coverage
- Two approaches for formula
  - Use coverage provider's actual marginal tax rate
    - Lots of difficulties in using this
  - Use one standard marginal tax rate for everyone
    - Would be less than statutory maximum

Questions – taxation of reimbursements

- 1. Are there methodologies that a reasonably sane person could follow (and remain reasonably sane) that would be able to exclude the income tax true-up for the excise tax reimbursement from the cost of applicable coverage?
- 2. Are there issues or legal barriers to passing through these reimbursements or separately identifying these amounts?
- 3. Are there approaches that would permit billing these amounts before the excise tax is paid by the coverage provider?
- 4. Are there comments on the 2 approaches on the marginal tax rates to use for the formula?

Cost of coverage - allocation of contributions to account-based plans

- Contributions could be allocated pro-rata over plan year, regardless of when contributions are actually made during period
- Would apply to HSAs, HRAs, FSAs, and Archer MSAs

Questions – allocation of contributions

- 1. What do you think of allocating contributions to account-based plans on a pro-rata basis over the period to which the contribution relates, such as the plan year?
- 2. Would you suggest any alternative approaches?

Cost of coverage – FSAs with employer flex credits

- Cost of applicable coverage for FSA = greater of:
  - Amount of employee's salary reduction; or
  - Total reimbursements under FSA
- Cost of non-elective employer flex credit = amount actually reimbursed in excess of employee salary reduction
- Safe harbor to avoid double-counting
  - Cost of coverage = employee's salary reduction, without regard to carryovers
    - Can't be used with non-elective flex credits
    - Variation: could be used with non-elective flex credits, provided amount elected by employee for FSA were less than maximum permitted

Questions – FSAs

- 1. Are these safe harbors administrable?
- 2. For the variation, how would you allocate FSA amounts between non-elective flex credits and salary reduction when the total election for the FSA exceeded the maximum salary reduction amount permitted by § 125(i)?
- 3. Any other comments on the rules outlined in the notice?
- 4. Any other issues presented by valuing FSAs?

Cost of coverage – reimbursements for highly-paid individuals

- Highly-paid individuals may not exclude "excess reimbursements" from income
  - These amounts will not reduce the cost of applicable coverage for purposes of the excise tax

Age and gender adjustments

- Increases to the two thresholds are contemplated for age and gender
  - 2018 limits: Self: $10,200; Family: $27,500
  - Adjusted based on comparison of employer's plan to BC/BS standard option under FEHBP
    - Adjustments done separately for self and family coverage
      - Must calculate number of employees in 5-year age groups by gender
- Timing
  - May use first day of plan year as snapshot to determine composition of employee population

Questions – age and gender

- 1. The notice says that IRS is considering using the first day of the plan year as a snapshot date for determining the composition of its employee population. Is this an administrable approach?
- 2. Should employers be allowed to select a different date? Why would another date be better?
- 3. Comments on overall adjustment approach?

Notice and payment

- Employer required to notify IRS and each coverage provider of excess benefit attributable to that provider
- IRS: may require filing on Form 720 (annually) to pay tax

Questions – notice and payment

- 1. What administrative and other issues are raised by this notice requirement?
- 2. How can errors in calculating the tax and allocating the tax among providers be avoided and potential reallocations limited?

Any additional comments?

- 1. The notice invites us all to make further comments on the first notice, Notice 2015-16.
  - Comments on integrating retiree groups with active employees?
- 2. Do you have concerns about the interaction between the employer shared responsibility provisions of section 4980H and the excise tax provisions of section 4980I?

For further information…

- Chip Kerby
  - Liberté Group LLC
  - chip@libertegroup.com
  - 202/756-2459
- Rich Stover
  - Buck Consultants
  - Richard.Stover@xerox.com
  - 201/902-2684
- Gretchen Young
  - ERIC; gyoung@eric.org
  - 202/627-1920