

# Healthcare Reform Update

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## Paying Premiums for Individual Health Insurance Policies

Provided by GCG Financial, Inc.

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Starting in 2014, the Affordable Care Act (ACA) may make purchasing health insurance in the individual market more accessible for individuals. Due to the ACA's reforms and the rising costs of health coverage, some employers have considered whether they should help 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 (Notice) to address how certain ACA 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.

The Notice discourages employers from helping employees pay for individual policies in lieu of offering a group health plan by eliminating the tax savings associated with contributions toward individual coverage. 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

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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.

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.

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.

## 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.

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