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Digging into the New HRA Regulations, Part 3 – Premium Tax Credit and Employer Mandate Impact on Individual Coverage HRAs

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As part of our ongoing series on the final regulations expanding the availability of health reimbursement accounts ("HRAs"), we discussed the newly-created Individual Coverage HRAs, which generally allow for employers to reimburse employees' premiums for health coverage purchased on the individual market. As noted in the final regulations, the new Individual Coverage HRA is a group health plan subject to ERISA and the Affordable Care Act ("ACA"). Therefore, Individual Coverage HRAs can impact employees' access to premium tax credits ("PTCs") available on the ACA Marketplace and play a role in an employer's compliance with the ACA's employer shared responsibility mandate. These issues are described more fully below.

ACA Marketplace Impact

In general, the ACA Marketplace provides access to individual market health insurance coverage, and depending on household income, an individual could get an advance PTC to reduce the cost of coverage. In addition to meeting income requirements, to be eligible for the PTC, an individual generally cannot have access to employer-sponsored minimum essential coverage that is affordable (i.e., the self-only cost is less than 9.86% (in 2019) of household income) and has minimum value (i.e., the plan pays at least 60% of covered services under the plan). If an individual actually enrolls in his or her employer's group health plan, even if it is not affordable or does not have minimum value, he or she will not be eligible for a PTC on the ACA Marketplace.

Individual Coverage HRAs are group health plans. They are also considered minimum essential coverage under the ACA. Therefore, if an employee enrolls in an Individual Coverage HRA, he or she will be ineligible for a PTC on the ACA Marketplace. If the employee opts out of the Individual Coverage HRA and seeks coverage on the ACA Marketplace, eligibility for a PTC depends on whether or not the Individual Coverage HRA is affordable.

Under the regulations, an Individual Coverage HRA is affordable for purposes of the PTC if the "employee's required HRA contribution" for the month does not exceed 1/12 (a) the employee's household income for the taxable year multiplied by (b) the "required contribution percentage." An employee's required HRA contribution amount is determined by subtracting the monthly HRA contribution for self-only coverage by the lowest cost silver-level plan available on the ACA Marketplace. The required contribution percentage is adjusted annually and is set at 9.86% for plan years beginning in 2019. As a technical matter, affordability of an Individual Coverage HRA, and thus an employee's eligibility to claim the PTC, is determined on a monthly basis. However, the regulations state that if, at the time the employee enrolled in a qualified health plan, the ACA Marketplace determines the Individual Coverage HRA is not affordable, the HRA will be considered not affordable for the entire year.

The final regulations require that employers and plan sponsors provide written notice when an Individual Coverage HRA is made available to employees. That notice must contain information regarding the availability of the PTC, an explanation of the right to opt out of the HRA and potentially receive a PTC for any month the HRA is considered "unaffordable," and a statement that opting out of an affordable HRA would make the participant ineligible for a PTC. The Department of Labor's model notice for Individual Coverage HRAs issued concurrently with the final regulations contains the required language. The use of the model notice will generally be considered to be good faith compliance with the notice requirement.

The final regulations also establish a new ACA Marketplace special enrollment event for Individual Coverage HRA eligibility. Open enrollment in the ACA Marketplace currently spans November and December. Outside of that period, individuals need a special enrollment event (i.e., loss of other coverage, birth of a child, etc.) to enroll in Marketplace coverage. Recognizing that Individual Coverage HRAs will first become available on January 1, 2020, and most likely each January 1st thereafter as employers and plan sponsors adopt these HRAs, individuals will have an ACA Marketplace special enrollment event when they obtain access to an Individual Coverage HRA.

ACA Employer Mandate Impact

Under the ACA, applicable large employers, or "ALEs" (generally those that have 50 or more full-time employees and equivalents on a controlled-group basis) must offer an eligible employer-sponsored health coverage (i.e., "minimum essential coverage") to at least 95% of its full-time employees and their dependent children or pay a significant penalty. Even if an ALE meets the 95% requirement, if the coverage that is offered is not affordable or does not have minimum value, the ALE could face a smaller penalty. In order for either penalty to be triggered, at least one employee would need to opt-out of available employer-sponsored coverage and receive a PTC.

The final HRA regulations contain very little substantive guidance regarding the impact that Individual Coverage HRAs will have on employer mandate compliance. Instead, the regulations point to IRS Notice 2018-88 as setting the groundwork for future proposed regulations. Notice 2018-88 provides that Individual Coverage HRAs are minimum essential coverage, and therefore, as long as these HRAs or other forms of minimum essential coverage are made available to 95% or more of the full-time workforce, the massive ACA penalty (under Section 4980H(a) of the Internal Revenue Code (the "Code")) should be avoided.

However, the smaller, individualized penalty (under Section 4980H(b) of the Code) can still be triggered if the Individual Coverage HRA is not affordable (minimum value is assumed if the HRA is affordable). Although Notice 2018-88 explains that the same affordability methodology applied for purposes of the PTC can be used for purposes of the employer shared responsibility mandate, that methodology can be problematic for employers. For one thing, the “required HRA contribution” is based on a formula that includes household income, which is information that employers are unlikely to have. Further, the lowest-cost silver plan available to employees on the ACA Marketplace varies on an employee-by-employee basis, depending on age and place of residence. Given these challenges, Notice 2018-88 requested comments on various affordability safe harbors, including the ability to use the existing employer mandate affordability safe harbors (i.e., W-2, rate of pay, and federal poverty line) when determining Individual Coverage HRA affordability. The Treasury Department is expected to issue proposed regulations on these safe harbors in the coming months.

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Individual Coverage HRAs are a welcome addition to the health insurance space. With this addition comes the potential for missteps, however. For example, the final regulations provide that an offer of an Individual Coverage HRA will qualify as an offer of minimum essential coverage under the ACA’s employer shared responsibility mandate. However, employer mandate penalties are still possible if the Individual Coverage HRA is not affordable. Although determining affordability for PTC purposes is generally straightforward, applying the same affordability methodology to the employer shared responsibility mandate can be problematic. The IRS has indicated that future proposed regulations may (1) propose allowing the use of existing affordability safe harbors to Individual Coverage HRAs and (2) propose new affordability safe harbors for Individual Coverage HRAs.

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