



**EMPLOYERS WITH PREMIUM REIMBURSEMENT ARRANGEMENTS
MAY FACE DRACONIAN PENALTIES UNDER ACA;
BRIEF REPRIEVE FOR SMALL EMPLOYERS**

Prior to the Patient Protection and Affordable Care Act (the “ACA”), it was not uncommon for small employers who did not want to spend time and money obtaining a group health plan to instead reimburse employees for all or part of the cost of individual health insurance obtained by the employee. Such arrangements, however, are inconsistent with the ACA, which provides different rules for individual and group health plans and generally allows employers to offer only group plans. Accordingly, between 2013 and 2014, the DOL, IRS and HHS issued several pieces of guidance shutting the door on this practice. The guidance also warned that noncompliant employers could face a hefty ACA excise tax of \$100 per day for each employee who receives reimbursement of individual health policy costs (\$36,500 per year per employee). The penalties apply even if the employer is not required to offer health insurance in the first place (e.g. small employers not subject to the employer mandate).

Earlier this year, the IRS issued Notice 2015-17, which reiterated the agencies’ stance on the issue, but also provided transition relief for certain employers that maintain these types of arrangements. Small employers that meet the requirements under the notice will generally be exempt from excise taxes through June 30, 2015. S Corporations will be exempt from such taxes through December 31, 2015 (or, if later, once guidance is issued), but only with respect to 2% shareholders.

Treatment of Premium Reimbursement Arrangements under ACA

Under the ACA, premium reimbursement arrangements (also referred to as “employer payment plans”) are generally considered group health plans subject to the ACA’s market reforms, including the prohibition on lifetime and annual dollar limits and free preventive care. The agencies have determined that employer payment plans cannot be integrated with individual health policies to satisfy the ACA’s market reforms. Therefore, since employer payment plans cannot satisfy the ACA’s market reforms on a standalone basis, employers offering such plans will be subject to a \$100 per day per employee excise tax. This is the case regardless of whether the employer pays or reimburses premiums on a pre-tax or after-tax basis.

Transition Relief under Notice 2015-17

Notice 2015-17 provides the following transition relief for small employers (*i.e.*, employers with fewer than 50 full-time employees) and S corporations of any size that currently pay or reimburse individual health premiums for 2% shareholders:

- Provides relief from excise taxes through June 30, 2015 for small employers that reimburse or pay premiums for individual health insurance policies for two or more active employees. Note that the transition relief does not apply to any stand-alone health reimbursement arrangement (“HRA”) that reimburses expenses other than individual health insurance policies.
- Allows S corporations to continue to reimburse premiums for shareholders who own more than 2% of the employer (but not for employees) without being subject to the excises taxes, through the end of 2015 or, if later, until additional guidance is issued. This relief applies regardless of whether the S corporation is a small employer. The above relief for small companies also applies to small S-Corps (as to employees and less than 2% shareholders) through June 30, 2015.
- Allows employers to continue to pay or reimburse employees for Medicare Part B or D premiums, or to reimburse medical expenses for employees covered by TRICARE without being subject to ACA excise taxes, provided certain conditions are met. Note that employers are generally prohibited from reimbursing or paying for Medicare premiums of active employees, under the Medicare secondary payer (“MSP”) rules. An exception may be available for employers that meet the MSP small-employer exception (*i.e.*, less than 20 employees). Similar reimbursement prohibitions apply to TRICARE.

Action Plan

Vendors continue to promote premium reimbursement plans that allegedly comply with the ACA. Other employers that are simply trying to “do the right thing” for their employees have been reimbursing employees who purchase individual policies, rather than taking on the burden of offering a group health plan. The IRS has made it clear that these arrangements do not work and that maintaining (or continuing to maintain) such a plan exposes the employer to draconian excise taxes under the ACA.

Employers who are currently paying or reimbursing employees for individual health coverage should stop doing so now (no later than June 30, 2015 for small employers). Large employers who pay or reimburse employees for all or part of the cost of individual policies should stop doing so immediately. Employers are expected to self-report to the IRS and pay any applicable excise taxes.

Employers that need to transition out of employer payment plan arrangements could consider increasing compensation for affected employees, provided the increase is not conditioned on the purchase of health coverage. Alternatively, employers can consider purchasing group health insurance in the small group market (generally 1 to 100 employees), possibly through a SHOP exchange. Employers may be able to offer group health plan coverage on a pretax basis, provided the employer establishes a Section 125 cafeteria plan.

If you have questions regarding Notice 2015-17 or the ACA in general, please contact your relationship attorney or one of the employee benefit attorneys listed below. More information on employer payment plans is provided in IRS FAQs, reproduced in our [health care reform resource center](#).

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Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, you may also contact:

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