

Trump Administration Opens Door to Defined Contribution Approach to Employer Health Care Benefits

In October 2018, the Trump Administration published a proposed health reimbursement arrangement rule that if finalized could pave the way for a tax-preferred defined contribution option that large employers could adopt to provide health care benefits to current employees.ⁱ

What are HRAs? A health reimbursement arrangement or health reimbursement account (HRA) is a type of U.S. employer-funded health benefit plan that reimburses employees for out-of-pocket medical expenses and, in some cases, to pay for health insurance premiums. HRAs are funded solely through employer contributions and may not be funded through employee salary deferrals under a cafeteria plan. HRA funds may be used to reimburse an employee for health care expenses (including copays, deductibles, medical expenses not covered by an employer's major medical plan, and premiums for health care coverage) incurred by the employee or the employee's dependents. There are no minimum or maximum limits on the amount of money an employer may contribute to an HRA and the contributions are excluded from an employee's taxable income and wages.ⁱⁱ Employers contribute a fixed dollar amount for a specific period, usually the plan year. Amounts that remain at the end of the year can be carried over to the next year or revert back to the employer, but any balance may not be refunded to an employee at the end of the year or upon termination of employment.

Prior to passage of the Affordable Care Act (ACA), employers could use HRAs to reimburse employees who bought coverage in the individual market, but few did. Because employees with pre-existing conditions could be denied coverage or the coverage might be unaffordable, any HRA program that relied on employees getting coverage in the individual market prior to the ACA was a nonstarter for most employers.

HRAs can be paired with any group health plan, but they are most commonly offered in conjunction with a high-deductible health plan (HDHP). In 2009, two percent of employers who offered health care benefits offered an HRA and the average employer contribution was \$1,052 for single coverage and \$2,073 for family coverage.ⁱⁱⁱ Just three percent of covered workers were enrolled in a plan that included an HRA.^{iv} By 2018, seven percent of employers who offered health care benefits offered an HRA and the average employer contribution was \$1,149 for single coverage and \$2,288 for family coverage.^v Ten percent of covered workers were enrolled in a plan that included an HRA in 2018.^{vi}

Current HRA Rules Current ACA rules do not let large employers offer an HRA for employees to purchase individual coverage without being subject to the ACA's employer penalties (\$100/day per employee).^{vii} However, small employers with fewer than 50 full-time employees can offer a stand-alone qualified small employer health reimbursement arrangement for employees to purchase coverage in the individual market.^{viii} For large employers, an HRA is viable for active employees *only if it is integrated with a traditional employer-provided group health plan* (typically

an HDHP).^{ix} Under IRS rules, employers can also offer a stand-alone HRA to retired employees as long as the HRA is designated as a retiree-only HRA and is administered separately from an HRA for current employees.

Proposed HRA Rule The proposed rule would allow two new types of HRAs for large employers: (1) a stand-alone HRA that would be integrated with individual health insurance coverage; and (2) a stand-alone HRA that would qualify as an excepted benefit.^x The rest of this report will focus on the proposed individual coverage HRA because if finalized the rule could enable large employers to move to a tax-preferred defined contribution approach for providing health care benefits to current employees.

Under the proposed rule, an individual coverage HRA (ICHRA) must meet certain criteria:

- Employees covered by an ICHRA must purchase ACA-compliant individual market coverage offered through a public exchange or directly from a carrier to receive reimbursement;^{xi}
- Employers may not offer an ICHRA *and* traditional group coverage to the same class of employees; either one or the other may be offered, but not both;
 - There are eight proposed classes – full time, part time, seasonal, collectively bargained, employees who have not satisfied a waiting period, employees who have not attained age 25, non-resident aliens and employees who are located in the same rating area;
- Employers must offer the ICHRA on the same terms to all employees within a class with one exception:
 - Employer contributions can be higher for older employees and employees with dependents; and
- Employees must be allowed to opt-out of an ICHRA once a year and upon termination of employment.^{xii}

Like regular HRAs, there are no employer contribution limits for ICHRAs, thus allowing substantial flexibility for employers to determine their ICHRA credits based on employee class, business needs and competitive considerations.^{xiii} Unused amounts in an ICHRA may roll over to the following year.

Employers offering an ICHRA would still be subject to the ACA's employer mandate to provide affordable coverage, and an offer of an "affordable" ICHRA, like the offer of affordable traditional health benefits, would make an employee ineligible to receive a premium tax credit in the ACA exchanges. The IRS also has proposed guidance that would provide a safe harbor for employers to use to determine if an ICHRA meets the ACA's affordability requirement.^{xiv} Further, employer contributions to an ICHRA would be included in the calculation of costs subject to the ACA's Cadillac tax on high value employer-provided health care benefits should it go into effect in 2022.

If finalized, the proposed rule could apply for plan years beginning January 1, 2020. However, this date could slip to 2021, and any final rule is expected to be challenged in court, which could further delay or even derail the rule. Future administrations could also revise or rescind the any final rule.

Impact on Employer Coverage The proposed rule estimates that once employers fully adjust to the final HRA rule, roughly 800,000 firms would offer an ICHRA, and that it would take employers and employees about five years to fully adjust to the new rule.^{xv} It is also estimated that 1.0 million individuals would enroll in an ICHRA in 2020, growing to 10.7 million in 2028, and the number of individuals in traditional group health plan coverage would fall by an estimated 0.6 million in 2020 and 6.8 million in 2028.

The accuracy of these estimates will depend on a variety of factors including the relative attractiveness of coverage offered the individual market. If the market offers employees reasonable coverage at affordable prices, employers may come to view it as a viable alternative to the group market. Adoption will also depend on how employers and employees view the provider networks offered through individual plans, which are generally narrower than employer plans.

Looking forward, the concept also could provide an alternative for employers to offer health benefits to nontraditional workers, but this would require Congress expand the ability of employers to offer HRAs to independent contractors. Such an approach could expand benefits to a growing segment of the workforce.

Outlook for the Rulemaking Although the proposal would allow ICHRAs to be used beginning in 2020, several commenters have recommended delaying implementation to at least 2021. Some commenters have also questioned the legal authority for the proposal, which suggests the final rule may be challenged in court. Moreover, any final rule could be rescinded or changed by any future administration. Finally, Democrats and Republicans have very different visions of what direction health care reform should take in the future, and it is not clear which will prevail. However, the concept of enabling employers to offer an HRA that is integrated with individual coverage purchased on or off the ACA exchanges is not necessarily inconsistent with either vision.

Endnotes

ⁱ 83 Fed. Reg. 54420 (Oct. 29, 2018) and IRS Notice 2018-88 (Nov. 19, 2018).

ⁱⁱ In 2019, a qualified small employer health reimbursement arrangement, only available to employers with fewer than 50 full-time employees, has contribution limits of \$5,150 for self-only employees and \$10,450 for employees with a family.

ⁱⁱⁱ Kaiser Family Foundation, Employer Health Benefits Survey, 2009.

^{iv} *Id.*

^v Kaiser Family Foundation, Employer Health Benefits Survey, 2018.

^{vi} *Id.*

^{vii} IRS Notice 2013-54. In 2013, the IRS ruled HRAs for active employees, on their own, would violate the ACA's prohibition on annual coverage limits for essential health benefits and the requirement that group health plans cover certain preventive services at no cost-sharing. Any large employer that offered this model could be penalized \$100 per employee per day in violation of the rule.

^{viii} P.L. 114-255, December 13, 2016.

^{ix} IRS Notice 2013-54.

^x Under the proposed rule, annual employer contributions for an excepted benefit HRA could not exceed \$1,800 (indexed) and the funds could only be used to reimburse medical expenses and premiums or contributions for COBRA coverage, excepted benefit coverage, or STLDI.

^{xi} 83 Fed. Reg. 54420 (Oct. 29, 2018) and IRS Notice 2018-88 (Nov. 19, 2018). Employers must verify their employees are paying their premiums and provide a notice explaining how the ICHRA affects eligibility for premium tax credits available through a public exchange.

^{xii} *Id.*

^{xiii} John Barkett, Employer Options for Health Insurance May Expand With New Rules on Health Reimbursement Arrangements, Willis Towers Watson, November 29, 2018.

^{xiv} IRS Notice 2018-88 (Nov. 19, 2018).

^{xv} 83 Fed. Reg. 54448.