

New Guidance on Qualified Small Employer Health Reimbursement Arrangements

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Practice Area: Compensation and Benefits/ERISA

In coordination with our past *Updates* on Qualified Small Employer Health Reimbursement Arrangements ("QSEHRAs") and health reimbursement arrangements under the Affordable Care Act ("ACA"), this *Update* identifies important notification deadlines and addresses a few surprises from IRS Notice 2017-67 regarding the implementation of QSEHRAs.

Background

After the passage of the ACA, the IRS confirmed that a health reimbursement arrangement ("HRA") is a group health plan that is subject to the coverage mandates under the ACA, including the rule prohibiting annual limits on benefits. The annual benefit under an HRA is limited to the amount contributed by the employer, so by design, an HRA does not comply with the ACA coverage mandate. Subsequent guidance indicated that an employer could avoid potential penalties under the ACA by integrating its HRA with an employer-sponsored group health plan, providing a solution for some, but not all employers.

On December 13, 2016, the 21st Century Cures Act ("Cures Act") was signed into law to allow small employers to reimburse employees' medical costs without having to navigate the complex requirement mandates of the ACA. The Cures Act established QSEHRAs and excluded QSEHRAs from the definition of "group health plan" under the ACA, thus allowing eligible employers to reimburse employees for health care costs without running afoul of the ACA.

QSEHRA Requirements

Eligible Employer. There are two requirements for an employer to offer a QSEHRA. First, the employer must be a "small" employer, meaning the employer must have fewer than 50 full-time employees, including full-time equivalents. The employer's size is determined using the same rules as those for determining whether the employer is an Applicable Large Employer under the ACA's employer shared responsibility (i.e. employer mandate) provisions. Second, the small employer cannot offer a group health plan to any of its employees. "Group health plan" is defined broadly, so an employer cannot offer any plan that provides health care such as a dental or vision plan or a health FSA.

Eligible Employee. Generally, QSEHRA coverage must be offered to all employees. Certain classes of employees, however, such as part-time or seasonal employees, union employees, non-resident aliens with no U.S. source income, and employees under the age of 25, can be excluded from the QSEHRA. A QSEHRA may only be offered to employees – it may not be offered to former employees such as retirees.

Benefits

- Except as provided in the statute, a QSEHRA must be offered to all eligible employees on the same terms and conditions. Employers may offer different benefit levels for single and family coverage or based on the employee's age and number of family members. The variation in benefit levels must be tied to the premiums charged based on a benchmark policy in the individual health insurance market.
- For 2018, the maximum benefit under a QSEHRA cannot exceed \$5,050 for single coverage or \$10,250 for family coverage. The benefit amount must be prorated if the employee is not covered by the QSEHRA for the entire year such as in the case of a new hire or terminated employee. Further, the benefit must be solely funded by the employer with no contributions from employees.
- Employees may use QSEHRA funds to pay for individual health insurance premiums, as well as medical expenses (as defined under Section 213(d) of the Internal Revenue Code), such as copays, deductibles and coinsurance, as well as dental and vision expenses.

Notice. An employer offering a QSEHRA must provide eligible employees with an annual notice at least 90 days before the beginning of the QSEHRA plan year. However, as our prior Update stated, the IRS delayed the notice requirement until additional guidance was released.

New Guidance – Notice 2017-67

On November 17, 2017, the IRS issued Notice 2017-67. Notice 2017-67 established that the deadline to submit initial notices for 2017 QSEHRAs and 2018 QSEHRA plans beginning January 1, 2018, is February 19, 2018. Notice 2017-67 also stated that the written notice must include:

- A description of the benefits, including the maximum annual benefit;
- A statement that the employee should disclose the amount of the QSEHRA benefit when purchasing coverage through the Exchange/Marketplace and that the QSEHRA benefit will offset the amount of any premium tax credit; and
- A statement that if the employee is not enrolled in minimum essential coverage, he or she may be subject to the individual mandate penalty under the ACA and that any reimbursements from the QSEHRA may be taxable income. The recent reduction of the individual mandate penalty to \$0 should not affect the QSEHRA notices that must be issued in 2018, because the reduction of the individual mandate penalty does not take effect until 2019.

In addition to establishing the notice requirements, Notice 2017-67 specifies that because the Cures Act requires that the QSEHRA be provided to all eligible employees, no eligible employee may waive coverage. The Notice also clarifies that the IRS controlled group rules apply in determining an employer's eligibility to offer a QSEHRA. Based on the new guidance, if any member of a controlled group is not an "eligible employer," no member of the controlled group may offer a QSEHRA. In addition, if one member of a controlled group offers a QSEHRA, each member of the controlled group must provide a QSEHRA to its eligible employees.

Notice 2017-67 also provided extensive guidance on how the annual dollar limits are applied. For example, if a newly hired employee is first provided a QSEHRA on a day other than the first day of the calendar year, the dollar limit is prorated to reflect the actual number of months that the employee is provided the QSEHRA. In addition, although an employer is not required to allow an employee to carry over unused QSEHRA amounts from one year to the next, the Notice clarified that if an employer does allow for such a carryover, the employee's total permitted benefit in the next year, taking into account both carryover amounts and newly available amounts, may not exceed the applicable dollar limit.

The new guidance also further clarifies the requirement that a QSEHRA must be offered "on the same terms and conditions to all employees." According to the Notice, a separate benefit up to the maximum permitted benefit must be provided to each eligible employee, regardless of whether employees are covered under an individual health policy or a family policy. Therefore, spouses who work for the same employer and who are covered under a family policy must both receive the full family benefit coverage. For example, suppose an employer provides an arrangement that reimburses all medical expenses with a self-only permitted benefit of \$3,960 and a family permitted benefit of \$8,040. Employee A and Employee B are covered under the same family health insurance policy (not sponsored by their employer) with a \$10,000 annual premium. To satisfy the same terms and conditions requirement, Employee A and Employee B must both be allowed the family permitted benefit of \$8,040 based on their family coverage. However, eligible employees may not be reimbursed for duplicate costs, so the total premium reimbursement for Employees A and B may not exceed the \$10,000 annual premium for their family health insurance policy.

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