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Employee Benefits

Proposed Regulations Provide Employers with More Flexibility in Offering HRAs to Employees

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The Departments of Treasury, Labor, and Health and Human Services jointly issued proposed regulations (the “Proposed Regulations”) providing employers with greater flexibility in offering health reimbursement arrangements (“HRAs”) to employees.¹ Importantly, if the Proposed Regulations are finalized in substantially its current form, employers would be able to offer employees an HRA that “integrates with” individual health insurance coverage. As a result, these Proposed Regulations, in essence, would enable employers to offer HRAs in lieu of a traditional group health plan to their employees. Additionally, the Proposed Regulations set forth conditions under which an HRA can be recognized as a limited excepted benefit HRA, which provides employers with another vehicle to provide employee benefits to their employees.

The Proposed Regulations are set to take effect for plan years beginning on and after January 1, 2020, although this is dependent on the regulations being finalized. The deadline for submitting comments on the Proposed Regulations was December 28, 2018.²

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BACKGROUND

An HRA is a type of account-based group health plan funded solely by employer contributions (with no salary reduction contributions or other contributions by employees) that reimburses an employee solely for medical care expenses incurred by the employee, or the employee's spouse, dependents, and children (who have not attained age 27 as of the end of the taxable year), up to a maximum dollar amount for a coverage period.³ An account-based group health plan is an employer-provided group health plan that provides for reimbursement of expenses for medical care (as defined under Section 213(d) of the Internal Revenue Code of 1986, as amended (the "Code")) ("medical care expenses"), subject to a maximum fixed-dollar amount of reimbursements for a period (e.g., a calendar year).⁴ The reimbursements under these types of arrangements are excludable from an employee's income and wages for Federal income tax and employment tax purposes.⁵ Depending on the terms of the HRA, amounts that remain in the HRA at the end of the year may be used to reimburse medical care expenses incurred in later years.⁶

When employers sponsor HRAs, the HRAs are typically established as unfunded "bookkeeping" accounts to reimburse eligible employees for medical care expenses that are not covered by group health insurance, such as deductibles and copayments.

The Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (collectively, the "ACA") amended the provisions of part A of title XXVII of the Public Health Service Act ("PHS Act") relating to health coverage requirements for group health plans and health insurance issuers in the group and individual markets.⁷ The term "group health plan" includes both fully-insured and self-insured group health plans.⁸ Section 2711 of the PHS Act, which was added by the ACA, generally prohibits group health plans and health insurance issuers offering group or individual health insurance coverage from establishing a lifetime or annual limit on the dollar value of essential health benefits ("EHBs"), as defined in Section 1302(b) of the ACA, for any individual. Section 2711 of the PHS Act, however, does not prevent a group health plan, or a health insurance issuer offering group or individual health insurance coverage, from placing an annual or lifetime dollar limit for any individual on specific covered benefits that are not EHBs, to the extent these limits are otherwise permitted under applicable law.⁹

HRAs are subject to Section 2711 of the PHS Act. Generally, an HRA will fail to comply with Section 2711 of the PHS Act because the arrangement is a group health plan that imposes an annual dollar limit on EHBs that the HRA will reimburse for an individual.¹⁰ If an HRA is "integrated" with other group health plan coverage that complies with the PHS Act, the HRA would be considered in compliance with these requirements because the combined arrangement complies with the PHS Act.¹¹ Under current guidance, HRAs may not be integrated with individual health insurance coverage for purposes of complying with the PHS Act.

In order to expand access to HRAs, President Trump issued Executive Order 13813, “Promoting Healthcare Choice and Competition Across the United States,” stating, in part, that the “Administration will prioritize three areas for improvement in the near term: Association health plans (AHPs), short-term, limited-duration insurance (STLDI), and health reimbursement arrangements (HRAs).”¹² With regard to HRAs, the Executive Order directs the Secretaries of Treasury, Labor, and Health and Human Services to “consider proposing regulations or revising guidance, to the extent permitted by law and supported by sound policy, to increase the usability of HRAs, to expand employers’ ability to offer HRAs to their employees, and to allow HRAs to be used in conjunction with nongroup coverage.”¹³ The Executive Order further provides that “[e]xpanding the flexibility and use of HRAs would provide many Americans, including employees who work at small businesses, with more options for financing their healthcare.”¹⁴

As directed in the Executive Order 13813, on October 29, 2018, the Secretaries of Treasury, Labor, and Health and Human Services issued the Proposed Regulations to expand the use of HRAs, including allowing HRAs to be integrated with certain individual health insurance coverage.¹⁵

CHANGES IMPOSED BY THE FINAL REGULATION

The Proposed Regulations would expand the use of HRAs in two important ways. First, the Proposed Regulations remove the current prohibition against integrating an HRA with individual health insurance coverage under Section 2711 of the PHS Act.¹⁶ Instead, the Proposed Regulations permit an HRA to be integrated with individual health insurance coverage and be in compliance with the PHS Act, if certain conditions are met.¹⁷

Second, the Proposed Regulations would expand the definition of “limited excepted benefits” under Section 9832(c)(2) of the Code, Section 733(c)(2) of ERISA, and Section 2791(c)(2)(C) of the PHS Act, to recognize certain HRAs limited in amount and that are limited with regard to the types of coverage for which premiums may be reimbursed as limited excepted benefits if certain other conditions are met (an “excepted benefit HRA”). Under the proposed regulations, an employee would not have to enroll in the employer’s group health plan in order to participate in an excepted benefit HRA.¹⁸

INTEGRATION WITH INDIVIDUAL HEALTH INSURANCE

Under current guidance, HRAs that are not integrated with group health coverage violate the ACA’s prohibition against placing lifetime or annual limits on the dollar value of EHBs. The Proposed Regulations would provide an exception to this prohibition for HRAs that are integrated with

individual health coverage, including coverage offered on the Exchange, provided that certain requirements are met.

In order to integrate an HRA with individual health coverage, the HRA must require participants to enroll in individual health insurance that complies with the requirements of the PHS Act.¹⁹ For this purpose, all individual health insurance coverage, except for individual health insurance coverage that consists solely of excepted benefits (e.g., plans that cover only dental or vision benefits), is treated as being subject to and complying with the PHS Act.²⁰ Additionally, reasonable procedures must be established to verify that individuals whose medical care expenses are reimbursable by an HRA are, or will be, enrolled in individual health insurance coverage (other than coverage that consists solely of excepted benefits) during the plan year.²¹

Under the Proposed Regulations, an employer may offer an HRA integrated with individual health insurance coverage to a class of employees only if the employer does not also offer a traditional group health plan to the same class of employees.²² This means that an employer may not allow employees to choose between enrolling in an HRA integrated with individual health insurance coverage or a traditional group health insurance.²³ If such a choice was permitted under the Proposed Regulations, then employers may try to incentivize their employees with health conditions (“higher risk employees”) to accept the HRA and move to the individual market instead of enrolling in the employer’s traditional group health plan. If employers were able to steer their higher risk employees to the individual market through an HRA, then the individual market risk pool would worsen and could impact the selection on the individual market and raise premiums.²⁴

Further, an employer must offer this HRA on the same terms to all employees in the same employee class.²⁵ Permitted classes of employees include full-time employees, part-time employees, seasonal employees, employees in a particular collective bargaining unit, employees who have not met a waiting period, and employees who have not attained age 25.²⁶ When classifying employees, employers may choose to use the definitions from the nondiscrimination regulations that apply to self-insured plans under Section 105(h) or 4980H of the Code.²⁷ This rule also helps prevent employers from singling out higher risk employees and incentivizing them to enroll in individual coverage on the Exchange.

The Proposed Regulations would allow employers to design an HRA that allows the maximum dollar amount made available under an HRA to increase for participants within a class of employees as the age of a participant increases, provided that the same maximum dollar amount attributable to that increase in age is made available to all participants of the same age within the same class of employees.²⁸ Similarly, the Proposed Regulations would allow an HRA to be designed to allow the maximum dollar amount made available under an HRA to increase for participants within a class of employees as the number of a participant’s dependents who are covered under the HRA increases, provided that the

same maximum dollar amount attributable to that increase in family size is made available to all participants in that class of employees with the same number of dependents covered by the HRA.²⁹

Employers that sponsor an HRA must provide affected employees with a notice concerning the HRA.³⁰ This notice is designed to help these employees understand that being eligible to participate in an HRA may impact their eligibility to receive a premium tax credit for Exchange coverage.³¹ The notice must be provided at least 90 days before the beginning of each plan year and must describe, among other things,

- (1) The terms of the HRA,
- (2) The participant's right to opt out of the HRA and waive future reimbursements from it,
- (3) The potential availability of the premium tax credit for Exchange coverage if the participant opts out of the HRA and if the HRA is deemed not affordable,
- (4) A statement explaining that a participant's dependents may lose eligibility for premium tax credits for Exchange coverage for any month the participant is covered by the HRA,
- (5) The participant's obligation to inform the Exchange of the availability of the HRA when applying for a tax credit,
- (6) The participant's obligation to substantiate medical care expenses in order to be reimbursed by the HRA, and
- (7) A statement that it is the responsibility of the participant to inform the HRA if the participant or any dependent whose medical care expenses are reimbursable by the HRA is no longer enrolled in individual health insurance coverage.³²

The Proposed Regulations clarify that the individual health insurance coverage that is integrated with an HRA is not part of the employer's group health plan for purposes of the Employee Retirement Income Security Act of 1974 ("ERISA"), provided that

- (1) An employee's purchase of the individual health insurance coverage is voluntary,
- (2) The employer does not endorse any particular insurance coverage,
- (3) Reimbursement for nongroup health insurance premiums is limited solely to individual health insurance coverage,

- (4) The employer receives no consideration in the form of cash or otherwise in connection with the employee's selection or renewal of any individual health insurance coverage, and
- (5) The employer notifies the participant annually that the individual health insurance coverage is not subject to ERISA.³³

EXCEPTED BENEFIT HRAS

In addition to providing for a new HRA that is integrated with individual health insurance coverage, the Proposed Regulations would provide for a new excepted benefit HRA under which amounts newly made available for each plan year are limited to \$1,800 (indexed for inflation after 2020), provided that certain requirements are met.³⁴ Excepted benefit HRAs are exempt from certain ERISA and ACA requirements, which allows them to be offered on a stand-alone basis without being integrated with group or individual medical coverage.³⁵ However, even though an excepted benefit HRA does not need to be integrated with other coverage, in order to offer an excepted benefit HRA, an employer must offer its employees a group health plan that is not limited to excepted benefits and that is not an HRA.³⁶ The employees do not need to enroll in this group health plan, but it must be offered.³⁷ Not having to enroll in the employer's group health plan is a departure from traditional HRAs. Employee enrolled in an excepted benefit HRA could be reimbursed for any medical expense, other than premiums for individual health insurance coverage, group health plan coverage (other than COBRA, state, or other continuation coverage), or Medicare Parts B or D.³⁸ The excepted benefit HRA could be used to pay premiums for coverage that consists solely of excepted benefits.³⁹

CONSIDERATIONS FOR EMPLOYERS

If the Proposed Regulations are finalized in substantially its current form, certain employers may be tempted to offer an HRA integrated with individual health insurance coverage rather than a traditional group health plan. Such employers may hope to experience reduced administrative cost since such employers would no longer need to choose and manage health insurance plans or self-insured health benefits for their employees. If enough employers with higher risk employees offer HRAs integrated with individual health insurance coverage instead of traditional group health plans, then the increased risk in the individual market risk pool could impact the price and selection of individual coverage on the Exchange.

If the regulations are finalized as proposed, offering an HRA may be able to help applicable large employers (“ALEs”) (i.e., employers with 50 or more full-time equivalent employees) avoid having to pay the ACA’s “pay or play penalty.” In general, an employer will owe a payment under Section 4980H(a) of the Code if it fails to offer an eligible employer-sponsored plan to at least 95 percent of its full-time employees and their dependents and at least one full-time employee is allowed a premium tax credit for a month. An HRA is considered an eligible employer-sponsored plan. Therefore, if an ALE offers an eligible employer sponsored plan (including an HRA) to at least 95 percent of its full-time employees and their dependents, the ALE may not be liable for a payment under Section 4980H(a) of the Code for each month such an offer is made. However, such an employer may still be liable for a payment under Section 4980H(b) of the Code if at least one full-time employee is allowed a premium tax credit, which may occur if the eligible employer-sponsored plan offered was not affordable or did not provide minimum value, or if the employee was not offered coverage. The extent to which a full-time employee who was offered an HRA will be eligible for a premium tax credit depends on the rules proposed under section 36B of the Code.⁴⁰ The Treasury Department intends to issue guidance that describes a safe harbor for purposes of determining whether an employer that has offered an HRA integrated with individual health insurance coverage would be treated as having made an offer of adequate coverage for purposes of Code Section 4980H, regardless of whether the employee who received that offer declines the HRA and claims a premium tax credit.⁴¹

Additionally, if the regulations are finalized as proposed, smaller employers (i.e., employers with fewer than 50 full-time equivalent employees) are not subject to Section 4980H of the Code, so such employers can offer an HRA integrated with individual health insurance coverage without being concerned that such an offering is deemed affordable and provides minimum value.⁴²

An employer who wants to offer an HRA and does not want to require employees to substantiate their enrollment in individual health insurance coverage may find an excepted benefit HRA to be an attractive option. However, an employer should note that in order to offer an excepted benefit HRA, an employer must still offer a group health plan other than a separate HRA that is integrated with individual health insurance coverage.

CONCLUSION

The Proposed Regulations would allow HRAs to be integrated with individual health insurance coverage, provided certain conditions are met. Being able to offer an HRA integrated with individual health insurance coverage would provide all employers (i.e., ALEs and small employers) with more choices and opportunities to provide medical employee

benefits to their employees, if the regulations are finalized as is. However, if the regulations are finalized as proposed, it may be very disruptive to the health insurance market. Employers should reach out to their legal counsel to learn more about HRAs integrated with individual health insurance coverage and excepted benefit HRAs and how to incorporate them into their employee benefit packages for employees, including designing an HRA program that complies with the ACA and the proposed nondiscrimination rules.

Notes

1. *See* 83 Fed. Reg. 54420, 54420 (October 29, 2018).
2. *See id.*
3. *See id.* at 54421.
4. *See id.*
5. *See id.*
6. *See id.*
7. *See* The Patient Protection and Affordable Care Act, Public Law 111-148, enacted on March 23, 2010.
8. *See* 83 Fed. Reg. 54420, 54421.
9. *See id.*
10. *See id.*
11. *See id.* at 54422. The current regulations and guidance also provide that HRAs may be integrated with Medicare and TRICARE coverage if certain conditions are met.
12. *See* 82 Fed. Reg. 48385, 48385.
13. *Id.* at 48386.
14. *Id.* at 48385.
15. *See* 83 Fed. Reg. 54420, 54420.
16. *See id.* at 54427.
17. *See id.*
18. *See id.*
19. *See id.* at 54461.
20. *See id.*
21. *See id.* at 54434.
22. *See id.* at 54430.
23. *See id.*
24. *See id.* at 54428.

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25. *See id.* at 54430.

26. *See id.* at 54430-31.

27. *See id.* at 54430.

28. *See id.* at 54433. The Treasury Department intends to issue guidance to address the interaction of the nondiscrimination requirements under Code Section 105(h) and HRAs under which the maximum dollar amount may vary based on age.

29. *See id.*

30. *See id.* at 54434.

31. *See id.*

32. *See id.* at 54434-35.

33. *See id.* at 54441.

34. *See id.* at 54450.

35. *See id.* at 54425.

36. *See id.* at 54450.

37. *See id.*

38. *See id.*

39. *See id.*

40. *See id.* at 54440.

41. *See id.*

42. *See id.*

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