

New Employee Benefit Rules Expand Health Reimbursement Arrangement Options for Employers

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June 19, 2019

On June 13, 2019, the Internal Revenue Service (IRS), Department of Labor and Department of Health and Human Services (HHS) issued a new regulation that is intended to increase the use of tax-favored health reimbursement arrangements (HRAs) as a means of expanding access to health insurance in the individual insurance market. One likely effect of the new regulation, which will take effect on January 1, 2020, is to make it more likely that small employers will be able to offer greater health insurance options to their employees. Announced with some fanfare at a White House event on June 14, 2019, the Administration expects that as many as 800,000 employers will be able to take advantage of the expanded options made available under the rule.

Background: HRAs

An HRA is an account funded solely by employers – they cannot be funded via a salary reduction arrangement through a cafeteria plan. Contributions made by the employer are excluded from the employee's gross income. In addition, amounts spent from an HRA are also excluded from gross income if they are used to pay qualified medical expenses. Finally, any unused amounts in an HRA can be carried forward, used for qualified medical expenses in a subsequent year, and remain tax free.

HRAs grew in popularity as an employee benefit in the 1990s as a means of allowing employees to pay for expenses not covered under a traditional health insurance plan (such as co-payments, wellness benefits, and prescription eyeglasses). In 2002, the IRS formally defined and clarified the tax status of health reimbursement arrangements in two guidance documents (Notice 2002-45, 2002-2 CB 93 and Rev. Rul. 2002-41, 2002-2 CB 75). These two guidance documents set forth, for the first time, the operational rules for HRAs.

The enactment of the Affordable Care Act in 2010 caused the IRS and the Departments of Labor and HHS to re-visit some prior HRA guidance. For example, although the IRS had always taken the position that HRA funds could be used to pay for health insurance premiums, in Notice 2013-54, 2013-40 I.R.B. 287, the IRS limited that position. Specifically, the IRS said that "an employer-sponsored HRA cannot be integrated with individual market coverage." Thus, HRA funds could not be used to pay for premiums on a plan sold in the individual market – even a qualified health plan sold on an Affordable Care Act Exchange.

The new regulation generally reverses this policy, and creates two new types of HRAs that, if a series of requirements are satisfied, would permit HRA funds to be used to pay for premiums for plans sold on the individual market.

Individual Coverage HRAs

An Individual Coverage HRA is an HRA that can be integrated with a health plan sold on the individual market, including on one of the ACA Exchanges. The following requirements apply to Individual Coverage HRAs:

- The employee must be enrolled either in individual market coverage (regardless of whether purchased on an ACA Exchange) or in Medicare;
- The employee must not be enrolled in short-term, limited duration insurance or insurance that consists only of excepted benefits;
- The HRA option cannot be offered to employees for whom the employer offers traditional group health plan coverage;
- Employers must offer the HRA on the same terms to all workers within a given class of employees, except that employers may

increase the amounts offered in the HRA for older workers or workers with more dependents; and

- The enrollee would need to substantiate their coverage in the individual market.

Excepted Benefit HRAs

This more limited type of HRA allows employers to reimburse employees' medical expenses that are not covered by insurance, including co-pays, deductibles, and medical care, on a pre-tax basis. The following requirements apply to excepted benefit HRAs:

- The HRA cannot be used to reimburse individual health plan (or Medicare) premiums, but may be used to reimburse premiums for dental, vision, short-term limited duration health plans, and other limited benefit insurance plans;
- Employers must offer their employees a traditional group plan in conjunction with the Excepted Benefits HRA. However, unlike with a traditional HRA, the employee may decline to participate in the group plan, and still enroll in the Excepted Benefits HRA;
- Contributions to the HRA are capped at \$1,800 per year (indexed for inflation); and
- Employers must make the HRA available to all similarly situated individuals.

Interaction with ACA Provisions

The final regulation also clarifies the interaction between the new policies and the requirements of the Affordable Care Act. On the employee side, an individual who uses an HRA to pay premiums for coverage in a plan sold in the individual market cannot then claim the advance premium tax credit enacted under the ACA. However, if an individual is offered the HRA option, but declines it, the individual may be able to qualify for the credit if the HRA, when combined with individual market coverage, is unaffordable. The final rule uses the lowest cost silver plan for self-only coverage available through the ACA Exchange in the region in which the employee resides to determine whether an Individual Coverage HRA is "affordable."

On the employer side, the final regulation specifies the interaction between the HRA policies and the employer coverage mandate. Under the ACA, employers with at least 50 full-time employees are generally required to offer affordable "minimum essential" coverage to their full-time employees, or pay a penalty to the IRS. The Individual Coverage HRA can constitute minimum essential coverage in certain circumstances. If the employer contributes a sufficient amount to the HRA to render the employee's individual insurance coverage "affordable," then the mandate is satisfied, and the employer does not need to pay the penalty to the IRS. However, the final rules leave some uncertainty about how Individual Coverage HRAs interact with the employer mandate, and the Treasury Department and the IRS are planning to propose new rules on this topic.

Employers that offer an Individual Coverage HRA must notify eligible employees regarding the availability of the HRA and how participating in the HRA impacts their eligibility for the premium tax credit. Employers are also obligated to substantiate that Individual Coverage HRA enrollees and their families are enrolled in individual health insurance (or Medicare).

Conclusion

The new rule will provide employers – especially small employers – an important health insurance coverage option for their employees. Foley Hoag attorneys have been advising clients on the development of the final rule for the past year and are available to respond to questions from clients who wish to explore their employee benefit options in light of the new policies.

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