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On July 8, 2016, the Internal Revenue Service (IRS) issued proposed regulations that, among other things, address affordability determinations for individuals who are eligible for employer-sponsored health coverage. This proposed rule builds on earlier guidance, Notice 2015-87, describing the effect an opt-out payment has on affordability. This latest guidance likely signals the direction the IRS will take in their final rule with respect to the affordability of employer-sponsored health plans.

According to this guidance, the IRS anticipates issuing final regulations on opt-out arrangements and affordability prior to the end of 2016.

For employers that qualified for limited relief (defined below), this guidance is not effective until the issuance of final regulations. For employers that did not qualify for relief (as described later in the article), these requirements currently apply.

Background

Applicable large employers (“ALEs”) may be subject to the Employer Penalty if any full-time employee (“FTE”) receives a Premium Tax Credit (“PTC”) to purchase Exchange coverage. There are two penalties, “A” and “B.” The “B” Penalty can apply when the ALE offers at least 95% of FTEs and their dependent children minimum essential coverage (“MEC”) but the coverage is not affordable, does not provide minimum value, or excludes 5% or fewer FTEs and an FTE receives a PTC.

The concept of affordability is significant as it affects:

- whether an employer is subject to a “B” Penalty assessment;
- how an employer reports the affordability of any group health plan coverage offered to FTEs on Form 1095-C (Line 15); and
- how the affordability safe harbor is used for those who waive coverage (Line 16).

Under a cafeteria plan, an employer may offer an employee a “cash option,” a taxable amount that is available if the employee declines coverage under the employer’s health plan (also referred to as an “opt-out bonus” or “opt-out arrangement”).

On December 16, 2015, the IRS issued Notice 2015-87 where it specified situations that would affect the determination of affordability by either increasing or decreasing the employees cost of self-only coverage. The Notice discussed opt-out arrangements, but requested public comments to issue proposed regulations.

Opt-Out Arrangements

The proposed regulations specify when an opt-out arrangement affects the cost of coverage and therefore, affordability.

- **Rule:** A conditional opt-out payment does NOT affect affordability. To qualify as a conditional opt-out payment, the employee must:
 - decline the employer sponsored coverage, and
 - provide reasonable evidence that the employee and the expected tax family have MEC, other than individual coverage (whether or not obtained in the Marketplace).

For this purpose, the “expected tax family” is composed of the individuals for whom the employee can claim a personal exemption on his/her tax return.

Reasonable evidence includes an attestation that the employee and the expected tax family have MEC or other reasonable proof of coverage. Such documentation must be furnished by the employee at least annually and within a reasonable amount of time prior to the start of the plan year. Providing documentation during the annual open enrollment period would be reasonable.

If an opt-out arrangement meets the requirements above, the payment will not affect the cost of coverage.



- **Rule:** An unconditional opt-out payment affects affordability. For example, if an employee declines coverage and receives a taxable payment with no other conditions, this is not a conditional opt-out payment and the amount of that payment is added to the employee's cost of coverage when determining affordability.

If an employer determines its opt-out arrangement does not meet these requirements, the employer should consider amending the opt-out arrangement requirements to meet eligibility. Otherwise, employers will have to consider the opt-out in their affordability calculation.

Effective Date

Employers that qualified for relief contained in Notice 2015-87 (generally those employers with opt-out arrangements in effect or communicated prior to December 16, 2015) are not required to include unconditional opt-out payments into the cost of coverage for purposes of affordability until final regulations are issued; this delay includes reporting the employee contribution amount on line 15 of the 1095-C.

Employers that implemented opt-out payments on or after December 16, 2015 are currently subject to these requirements and will report the amount including the unconditional opt-out bonus on line 15 of the 1095-C.

Collectively Bargained Plans

The proposed rule clarifies and expands the relief provided under Notice 2015-87 for opt-out arrangements provided under collective bargaining agreements in effect before December 16, 2015. Until the later of (1) the beginning of the first plan year following the expiration of the collective bargaining agreement in effect before December 16, 2015, or (2) the applicability date of these regulations with respect to the employer mandate and applicable reporting, employers participating in the collective bargaining agreement are not required to increase the amount of an employee's required contribution by amounts made available under an opt-out arrangement.

Employer Action

Employers should review any opt-out arrangements in place and determine if the arrangement meets the conditional opt-out arrangement requirements. If so, the employer should ensure proper disclosure to employees of the arrangement and annual collection of proof of other coverage.