



Insight

Health Reimbursement Arrangements Under the ACA

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Last month, the Internal Revenue Service (IRS) released a Question & Answer document disclosing potential penalties - up to \$36,500 a year per employee - for employers who do not offer insurance coverage, but instead seek to reimburse their employees for insurance purchased on the individual market. Specifically the IRS addressed how Health Reimbursement Arrangements (HRAs) would be treated for tax purposes under the Affordable Care Act (ACA). The IRS effectively stated that unless employers who offer HRAs also offer their employees an ACA-compliant group health plan, those employers will be subject to crippling tax penalties, even if their employees have access to affordable and comprehensive insurance through the individual market. Although information on how many HRA arrangements are connected with ACA-compliant coverage is not available, the IRS decision could result in many of the estimated ten million^[1] employees who receive HRA reimbursements from their employers losing those benefits.

HRAs allow employees to shop for and purchase an individual market insurance plan or *a la carte* health care services. Employees can then submit receipts to the employer who will reimburse the employee for these expenditures with tax-exempt dollars. This form of payment provides employees with the opportunity to make health care decisions that are most appropriate for them, while avoiding the threats of job-lock or pre-existing condition rejections that may result from tying health insurance to employment.

The justification for the IRS' decision to limit the availability of these plans is that while HRAs are considered "group plans" for purposes of the ACA, the health benefits offered (effectively none, because the employer offers only reimbursement) do not satisfy other requirements of the ACA; specifically, the IRS states that these plans violate the [Essential Health Benefits](#) provision of the ACA, as well as the prohibition on spending caps on these mandatory benefits.

The penalty for offering what the administration has deemed to be sub-standard insurance is a \$100 per day fine on each employee offered the HRA - totaling \$36,500 per year for each employee. Compared to the \$2,000 per year, per employee tax levied against employers who offer no insurance at all, this new rule is extremely punitive.

With a tax penalty of tens of thousands of dollars per employee looming, employers will inevitably exit the HRA system and either pay a smaller penalty to drop all coverage and dump their employees into the individual market, sans reimbursement, or shoulder the much larger burden of establishing an ACA compliant group plan or insurance arrangement. As employers make this shift, up to ten million Americans could lose their current insurance coverage and provider network.

Though the health policy community has been hearing about the \$2,000 employer fine for years, this \$100 fine is appearing in industry [talks](#) as of late. The \$100 fine, however, was already embedded in IRS code long before the ACA was passed, and the administration incorporated the tax regulation into ACA compliance guidelines. This incorporation was accomplished as follows:

- Group health plans are regulated under the [Public Health Service Act](#) (PHS, 42 USC), and the relevant enforcement requirements are codified in [Chapter 100](#) of the Internal Revenue Code (IRC). [Section 4980D](#) of the IRC states that the penalty for failure to comply with Chapter 100 is a \$100 per day per employee fine.
- When the Affordable Care Act was passed, parts of it were codified as part of the PHS Act, including new regulations of group plans. As a result, group health plan requirements of the ACA were to be enforced under Chapter 100 of the IRC.
- Then, in September 2013, the IRS published a [Notice](#) confirming earlier [projections](#) that HRAs are to be considered group health plans. In a recent [Q&A](#), the IRS clarified that since HRAs are group plans subject to the PHS Act, any HRA that lacks additional group primary health coverage with no annual limit is in violation of the ACA and will be taxed according to Chapter 100.

Employers will have a difficult choice to make in regards to the health insurance options for their employees. Employers will no longer be able to allow employees to make health care decisions that best fit their needs, and receive reimbursement for their choices. Instead millions of working Americans could see losses or changes in their current health insurance plans.

[1] Center for Health and Economy, [Annual Report](#) (January 2014); Amelia Haviland et al., Growth of Consumer Directed Health Plans to One-Half of All Employer Sponsored Insurance Could Save \$57 Billion Annually, 31 Health Aff. 5, 1009 (May 2012); Robert Wood Johnson Foundation, [State-Level Trends in Employer-Sponsored Health Insurance: A state-by-state analysis](#) (April 2013).