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Individual Coverage HRAs

Highlights from the Final Rule

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The Departments of Labor, Health and Human Services, and the Treasury (collectively, “the Departments”) finalized rules creating two new Health Reimbursement Arrangement (HRA) options available to employers beginning January 2020. These final rules generally follow the proposed guidance (issued in October 2018) with some notable changes.

This article addresses individual coverage HRAs. Excepted benefit HRAs are discussed in a separate update.

Briefly, beginning with the first plan year on or after January 1, 2020, employers are permitted to offer an individual coverage HRA. This is an arrangement where the employer integrates individual health insurance coverage with an HRA when other traditional group health plan coverage is not offered, subject to certain conditions.

While individual coverage HRAs may not be a benefit strategy for all employers, some employers may want to consider this new option as part of their 2020 renewal planning.

The following highlights some of the key provisions of the final rules, including notable changes from the proposed guidance. The final rule is lengthy and dense and includes numerous examples. Employers interested in pursuing an individual coverage HRA should review the final rule and supporting guidance and work with their benefits consultant and third-party administrators to understand the various requirements.

HRA Integrated With Individual Health Insurance Coverage

Generally, pre-2020, existing law barred most employers from offering (and paying for) individual health insurance policies. However, these final rules create a mechanism by which employers may, in lieu of traditional group health insurance coverage, offer an HRA to reimburse individual health insurance premiums for employees (an individual coverage HRA).

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The following six conditions must be met in order to offer an individual coverage HRA:

1. Participants (and dependents) must be enrolled in permitted individual health insurance coverage to receive benefits under the HRA.

2. No traditional group health plan may be offered to a classification of employees that is also offered an individual coverage HRA.

3. Individual coverage HRAs must be offered on the same terms to all participants within a classification, except where deviation is permitted by the rules.

4. There must be an opportunity for eligible participants to opt-out and waive future reimbursements each year.

5. Reasonable procedures must be in place to substantiate individual health insurance coverage.

6. Employers must provide and comply with notification requirements.

Each of these conditions are discussed below.

1. Permitted Individual Health Insurance Coverage.

The final rule generally mirrors the proposed rules requiring every individual covered by an Individual Coverage HRA to enroll in individual health coverage to receive the benefits.

For this purpose, an individual coverage policy qualifies regardless of whether it is purchased inside or outside the federal or a state-based Exchange (also called "the Marketplace").

The final rule differs from the proposed in that catastrophic coverage, Medicare Part A, B, or C and fully insured student health insurance coverage also qualify as permitted individual health coverage, if certain conditions are met (discussed below).

However, the following are not considered individual health insurance coverage and cannot be integrated with an individual coverage HRA:

- coverage consisting solely of excepted benefits,
- short-term limited duration insurance,
- other non-HRA group coverage,
- self-funded student health coverage,
- healthcare sharing ministries, and
- TRICARE.

2. Permitted Classifications, Minimum Size Rule

A plan sponsor that offers an individual coverage HRA to a class of employees must offer such coverage on the same terms to each participant within the class (with limited exceptions).

Permitted classifications.

The final rule modifies the proposed classifications by adding new categories and removing a proposed "under age 25" classification. Per the final rule, the following classifications are permissible:

- Full-time;
- Part-time;
- Employees working in the same geographic locations (generally the same insurance rating area, state or multi-state region);
- Seasonal employees;
- Employees in a unit of employees covered by a collective bargaining agreement;

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- Employees who have not satisfied a waiting period;
- Non-resident aliens with no U.S.-based income;
- Salaried workers **(new)**;
- Non-salaried workers (such as hourly workers) **(new)**; or
- Temporary employees of staffing firms **(new)**.

Note regarding definition of Full-Time, Part-Time and Seasonal Employees.

For purposes of defining "full-time employee," "part-time employee," and "seasonal employee," the rule requires the use of either:

- The definitions under the employer mandate (Code Section 4980H); or
- The definitions as used in the nondiscrimination rules for self-insured health plans (Code Section 105(h)).

The elected definition must be included in the HRA plan document and consistent across all classifications (i.e., if the 4980H definition is used for full-time employees, it must be used for part-time and seasonal employees).

Additionally, the definition used should be established prior to the start of the plan year to which the definition will apply and be applied consistently throughout the year. The final rule clarifies that mid-plan year adjustments to the definitions used to identify the classes of employees for this purpose **are not permitted**.

Minimum size rule.

Additionally, the final rule takes further steps to prevent adverse selection by imposing a minimum class size rule. This rule applies when a plan sponsor offers a traditional group health plan to one class of employees and an individual coverage HRA to at least one other class of employees and the following classifications are used (or any combination that includes one of these classifications):

- Full-time;
- Part-time;
- Salaried;
- Non-salaried; or
- A class is based on a geographic location smaller than a state.

The minimum class size is based on the number of employees in the classification eligible for the individual coverage HRA at the beginning of the plan year.

- Fewer than 100 employees – class size must be 10 employees or greater
- 100-200 employees – class size must be ten percent (10%) of the total number of employees
- More than 200 employees – class size must be 20 employees or greater

For example, an employer with 100 employees offers a traditional group health plan to full-time employees and an individual coverage HRA to part-time employees. To meet the minimum class size rule, there must be at least 10 part-time employees eligible for the individual coverage HRA at the start of the plan year (regardless of how many enroll).

Special new hire rule.

The final rule permits employers to offer newly hired employees an Individual Coverage HRA, while grandfathering existing employees in a traditional group health plan, subject to certain conditions.

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3. Same Terms & Permitted Variation

If an employer offers an individual coverage HRA to a permitted classification of employees, the HRA must be offered on the same terms to all participants within the classification, with limited exception.

Generally, there is no federal cap on the maximum amount that can be contributed to an individual coverage HRA. Employers may contribute as little or as much as they want. However, employers generally must make the same dollar amount available to all participants in the individual coverage HRA unless an exception exists. Permitted exceptions include different contribution amounts based on family size, the participant's age, and eligibility date.

Permitted variations.

- **Variation due to number of dependents.** The final rule retains the proposed rule guidance permitting variance in the HRA contribution based on the number of dependents a participant enrolls in the individual coverage HRA so long as the amount attributable to the increase in family size is available to all in the same class with the same number of participants.
- **Variation due to age.** Both the proposed and final rules permit an employer to offer more individual coverage HRA dollars to participants based on the age, as individual health insurance premiums generally increase based on age. However, the final rule includes a limitation:
  - The maximum dollar amount made available under the terms of the HRA to the oldest participant cannot be **more than three times (3x) the maximum amount available to the youngest participants.**
  - While varying contributions by age is permitted, variations must be applied equally to all participants who are the same age.
- **New Hires:** These rules also permit employers to vary HRA contribution amounts based on eligibility. Specifically, an employee eligible mid-year may receive prorated amounts based on the number of months they are eligible for the HRA. The method used to determine this prorated amount must be the same for all participants in the same classification.

4. Opt-Out Provisions

Employers offering an individual coverage HRA must allow employees an opportunity to opt-out or waive enrollment every year. Even if an individual opts out of the individual coverage HRA, the employer may be shielded from incurring ACA penalties under 4980H if the coverage meets affordability and minimum value standards. See the ACA discussion below.

5. Substantiation of Coverage

The final rules require employers to establish reasonable procedures to verify that participants and dependents are (or will be) enrolled in individual health insurance coverage for the plan year before releasing HRA funds and that the expenses are not otherwise reimbursed. Employers may rely on either:

- documentation from a third-party that the individuals covered by the HRA had coverage (e.g., EOB or insurance card), or
- an attestation from the participant of coverage through an individual policy. A model form has been provided for this purpose. For the model attestation visit: https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB87/individual-coverage-model-attestation.docx

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The final rules clarify that an employer may rely on the participant's assertions about having individual coverage based on the documentation or attestation, unless the employer has actual knowledge that the individual covered by the HRA is not (or will not be) enrolled in individual health insurance coverage for the plan year or the month, as applicable.

6. Notice Requirements

The final rules require employers to provide written notice to all employees (including former employees) who are eligible for the individual coverage HRA.

This notice must be provided at least 90 days prior to the start of the plan year and must meet content requirements outlined by the regulation. The notice includes, among other items:

- a description of the HRA,
- contact information,
- the maximum dollar amounts available,
- opt-out and waiver rights,
- effect of the coverage on availability of any premium tax credit,
- reimbursement rules, and
- the substantiation rules.

This notice must be distributed in a manner reasonably calculated to ensure actual receipt by participants. For new HRAs established less than 120 days prior to the beginning of the first plan year, the notice may be provided no later than the date on which the HRA will first take effect for the participant. For individuals that become eligible after the beginning of the plan year, the notice must go out no later than the effective date of the coverage.

The Departments issued a 6-page model notice that can be used to meet this requirement. For the model notice, visit: https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/completed-rulemaking/1210-AB87/individual-coverage-model-notice.docx.

Other Considerations for Individual Coverage HRAs

ERISA.

The final rules clarify that ERISA will generally apply to the HRA, but not to the underlying individual health insurance coverage. Therefore, the HRA (but not the individual coverage) remains subject to all ERISA requirements (including reporting and disclosure requirements and COBRA). To prevent ERISA applicability to the underlying individual coverage, an employer must:

- provide annual notice that ERISA Title I does not apply to the individual coverage;
- ensure enrollment is voluntary,
- not endorse, select, or limit the options available to employees (providing general information about or educational information is not endorsing), and
- not receive any consideration in the form of cash or otherwise in connection with the employee's selection or renewal of any individual health insurance coverage.

IRS 105(h)Nondiscrimination.

While the flexibilities that permit employers to vary contributions for certain employees may give rise to discrimination issues under current IRS Code Section

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105(h) rules, the IRS is expected to provide safe harbor guidance to alleviate the discrimination issue.

ACA Employer Mandate and Affordability.

An offer of an individual coverage HRA counts as an offer of Minimum Essential Coverage ("MEC") under the employer mandate. An employer must contribute sufficiently to an individual coverage HRA for the MEC to be considered affordable. The final rule provided further details on how affordability should be calculated for individual coverage HRAs. Generally, the coverage will be affordable for an employee if the employer's annual HRA contribution is large enough to allow the employee to obtain the lowest cost silver plan on the Exchange without having to contribute monthly toward the premium in an amount greater than the following:

(Participant's household income X current affordability percentage) ÷ 12

The Affordability percentage changes annually. In 2019, plans are considered affordable if the employee's share of the contribution does not exceed 9.86% of their household income.

Future guidance is expected from the IRS to assist Applicable Large Employers (ALEs) in calculating the ACA's affordability and minimum value standards. This guidance is expected to extend the existing affordability safe harbors (W-2, Rate of Pay, and Federal Poverty Level) to employers offering an individual coverage HRA.

An individual who is offered an individual coverage HRA that is affordable and meets minimum value will not be eligible for a Premium Tax Credit (PTC) on the Exchange.

The IRS is expected to provide more information on how the employer mandate applies to individual coverage HRAs.

COBRA.

An HRA is a group health plan generally subject to the COBRA continuation coverage requirements. If an individual elects COBRA continuation coverage, the employer must provide for the continuation of the maximum reimbursement amount for an individual at the time of the COBRA qualifying event and by increasing that maximum amount at the same time and by the same increment that it is increased for similarly situated non-COBRA beneficiaries. The final rules do not modify these long-standing IRS rules.

Medicare.

The individual coverage HRA may reimburse individuals for Medicare premiums, but may not limit other reimbursements to only expenses not covered by Medicare. Individual coverage HRAs may limit reimbursement only to premiums or non-premium medical care expenses (e.g., cost-sharing), or may decide which particular medical care expenses will be reimbursable (and which will not) under the terms of the plan. Unlike the proposed rules, the final rules allow employers to offer an individual coverage HRA to participants that are otherwise Medicare eligible without violating the Medicare Secondary Payer (MSP) rules and anti-duplication rules.

The individual coverage HRA (as the group health plan) will be the primary payer and Medicare will be the secondary payer. Generally, most group health plans are subject to MSP rules which prohibit offering Medicare-eligible individuals financial incentives to decline enrolling in the group plan because it causes Medicare to become the primary payer. However, the final rules clarify that offering an individual coverage HRA does not violate MSP rules because the HRA is the group health plan. Note, the final rules do not permit an employer to create an employee classification based solely on Medicare

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eligibility, but Medicare-eligible employees within a classification must be offered the same HRA benefits as other employees.

HHS intends to issue additional guidance clarifying this coordination of benefits and the associated reporting requirements.

State Law.

Some state insurance laws (such as Oregon and Texas) may bar employers from purchasing (directly or indirectly) health insurance coverage from the individual market on behalf of employees. The final rules confirm that the states' authority to regulate individual insurance markets remain unaffected. Therefore, prohibitions at the state level remain valid and may limit this HRA option in certain areas.

Employer Action

Employers may consider whether individual coverage HRAs may be a viable option for their employee benefit plan strategy for 2020 or beyond.

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