



P4P “Preparing for PPACA”

**Session #31: 40% Excise Tax  
on High-Cost Health Coverage**

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# Overview

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- Background
- Effective Date
- How Is the Cadillac Tax Determined?
- Annual Limitation
- How to Value Coverage?
- What Employers Are Subject?

# Overview

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- Whose Coverage Gets Counted?
- What Coverage Gets Counted?
- What Coverage Does Not Get Counted?
- Who Calculates and Pays the Tax?
- Is the Tax Deductible?
- Is the Tax ERISA Trust Chargeable?

# Background

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- Nondeductible 40% excise tax located in new IRC Section 4980I
- Tax applies to “applicable employer-sponsored coverage” in excess of statutory thresholds
  - Base thresholds: \$10,200 for self-only; \$27,500 for family
- Revenue raiser to pay for other aspects of the ACA (such as IRC section 36B subsidies)
- Also intended to address perceived over-consumption of health care coverage
- Very complicated and hard-to-administer excise tax
- No regulations or other agency guidance; many questions remain

# Effective Date

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- Effective beginning January 1, 2018
- Applies on a calendar year basis
  - Thus, if have fiscal year plan, will need to look to plan years that span the given calendar year in measuring compliance with the thresholds
- Employers are forecasting compliance
  - Collective bargaining
  - Developing compliance strategies
  - Establishing a “glide path” to avoid relatively significant benefit reductions in 2018

# How Is the Cadillac Tax Determined?

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- 40% of the “excess benefit” of applicable employer-sponsored coverage in excess of the “annual limitation”

# Annual Limitation

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- Base: \$10,200 for self-only, \$27,500 for family
- Certain additional adjustments permitted
  - Certain health inflation
  - Qualified retirees
  - Participants in certain plans covering employees engaged in certain high-risk professions or employed to repair or install electrical and telecommunications lines
  - Age
  - Gender
  - **Note:** No express adjustments permitted for geographical differences or high claims individuals

# Annual Limitation

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- Based on enrolled or offered coverage?
  - Statute is not entirely clear (although we believe IRS/Treasury is focusing on enrolled)
  - Uncertainty is because of somewhat conflicting statutory language



# Annual Limitation

## (a) Imposition of tax

If—

- (1) an employee is covered under any applicable employer-sponsored coverage of an employer at any time during a taxable period, and
- (2) there is any excess benefit with respect to the coverage,

there is hereby imposed a tax equal to 40 percent of the excess benefit.

**VS**

## (b) Excess benefit

For purposes of this section—

### (1) In general

The term “excess benefit” means, with respect to any applicable employer-sponsored coverage made available by an employer to an employee during any taxable period, the sum of the excess amounts determined under paragraph (2) for months during the taxable period.

# Annual Limitation

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- Base: \$10,200 for self-only, \$27,500 for family
  - What about employee + 1, etc.?
    - No tiers – either self-only or family
    - An employee is treated as having self-only coverage unless (i) the employee is enrolled in coverage that provides minimum essential coverage (MEC) to at least one other beneficiary, and (ii) benefits do not vary based on whether any covered individual is employee or another beneficiary

# Annual Limitation

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- Base: \$10,200 for self-only, \$27,500 for family
  - Example. In 2018, Employee A and his family are enrolled in self-insured employer-sponsored coverage with an aggregate annual cost of \$33,000. Neither Employee A nor his family is enrolled in other applicable employer-sponsored plans. Assuming no adjustments are made to the annual dollar limitations specified above, the plan administrator with respect to the employer-sponsored coverage would be liable for a Cadillac Tax for 2018 equal to \$2,200 ( $40\% * (\$33,000 - \$27,500) = \$2,200$ ).

# Annual Limitation

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- Adjustment for participants in certain plans covering employees engaged in certain high-risk professions or employed to repair or install electrical and telecommunications lines
- Employees engaged in high-risk professions is defined as certain individuals:
  - Engaged in law enforcement,
  - Engaged in fire protection activities,
  - Providing out-of-hospital emergency medical care,
  - Whose primary work is longshore work,
  - Engaged in the construction, mining, agriculture (not including food processing), forestry, and fishing industries.
- The term also includes an employee who is retired from a high-risk profession (described above), if such employee satisfied the requirements of the preceding sentence for at least 20 years during employment.

# Annual Limitation

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- Adjustment for participants in certain plans covering employees engaged in certain high-risk professions or employed to repair or install electrical and telecommunications lines
  - Allows for an increase in the base threshold of \$1,650 for self-only coverage and \$3,450 for family coverage
  - Only applies if the “majority” of plan participants are high-risk professionals
    - Unclear how to determine “plan” here given the coordination/stacking of coverages

# Annual Limitation

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- Adjustment for Qualified Retirees
  - Defined as any individual who (i) is receiving coverage by reason of being a retiree, (ii) has attained age 55, **and** (iii) is not entitled to benefits or eligible for enrollment under the Medicare program under title XVIII of the Social Security Act.
    - Appears to only encompass retirees age 55 through age 64
  - Allows for an increase in the base threshold of \$1,650 for self-only coverage and \$3,450 for family coverage
    - Unlike with high-risk professionals, majority of plan participants need not be qualified retirees

# Annual Limitation

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- Adjustment for age and gender

**Amount of  
Adjustment**



Premium cost of standard BCBS FEHBP coverage of same type provided to individual, BUT priced for the age and gender characteristics of all employees of the employer



Premium cost, based upon procedures determined by the Treasury Secretary, for the same coverage if priced for the age and characteristics of the American workforce

# Annual Limitation

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- Adjustment for age and gender
  - Example: For an employee with individual coverage in 2019, if standard FEHBP coverage priced for the age and gender characteristics of the workforce of the employee's employer is \$11,400 and the Secretary estimates that the premium cost for individual standard FEHBP coverage priced for the age and gender characteristics of the national workforce is \$10,500, the threshold for that employee would be increased by \$900 (\$11,400 less \$10,500).
- Source: Technical Explanation of the Revenue Provisions of the 'Reconciliation Act of 2010,' as Amended, in Combination with the 'Patient Protection and Affordable Care Act' ("JCT Report")



# Annual Limitation

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- Adjustment for pre-2018 inflation
  - Provides that the base thresholds are multiplied by the “health cost adjustment percentage” (HCAP)

$$\text{HCAP} = 100 \% \times$$

Percentage by which the per employee cost for providing coverage under the Blue Cross/Blue Shield standard benefit option under the FEHBP for plan year 2018 (determined by using the benefit package for such coverage in 2010) exceeds such cost for plan year 2010

$$- 55 \%$$

# Annual Limitation

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- Adjustment for pre-2018 inflation
  - Example: If the growth in the cost of health care during the period between 2010 and 2018, calculated by reference to the growth in the per employee cost of standard FEHBP coverage during that period (holding benefits under the standard FEHBP plan constant during the period) is 57%, the threshold amounts for 2018 would be \$10,200 for individual coverage and \$27,500 for family coverage, multiplied by 102% (100% plus the excess of 57% over 55%), or \$10,404 for individual coverage and \$28,050 for family coverage.

Source: JCT Report

# Annual Limitation

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- Adjustment for inflation in 2019 and beyond
  - For 2019 – Base limitations are indexed using CPI-U, plus one percentage point, rounded to the nearest \$50
  - For 2020 and beyond – Base limitations are indexed using CPI-U, rounded to the nearest \$50

# How to Value Coverage?

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- Cost of coverage is determined using rules “similar to the rules of section 4980B(f)(4)” of COBRA
  - “[E]xcept that in determining such cost, any portion of the cost of such coverage which is attributable to the tax imposed under this section shall not be taken into account”
  - IRC section 4980B(f)(4) generally looks to the cost of the coverage for “similarly situated” beneficiaries
  - Special rule for retirees
    - Permits employers to treat pre-65 and post-65 retirees as similarly situated
    - Because many post-65 retirees are limited to Medicare supplemental coverage, should help employers avoid or minimize the Tax on their pre-65 retiree population

# What Employers Are Subject?

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- Applies to all employers subject to the excise tax provisions of the IRC, including:
  - Private, for-profit employers regardless of size
  - Tax-exempt entities
  - Governmental entities

# Whose Coverage Gets Counted?

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- Coverage of “employees”
  - Statute then defines “employee” very broadly to mean:
    - Active employee
    - Former employee
      - Note: No retiree-only plan exception; the excise tax is distinct from the ACA market reforms
    - Surviving spouse
      - But what about other surviving beneficiaries, such as surviving children?
    - “Other primary insured” (which is undefined)

# What Coverage Gets Counted?

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- Applies to “applicable employer-sponsored coverage”
  - Generally **any** group health plan made available to an employee by an employer which is excludable from the employee’s gross income under Code section 106, or would be so excludable if it were employer-provided coverage (within the meaning of Code section 106)
    - **Be careful – No blanket exception for HIPAA-excepted coverage**

# What Coverage Gets Counted?

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- Applies to “applicable employer-sponsored coverage”
  - Encompasses self-funded and insured coverage
  - Encompasses coverage whether paid:
    - By an employer directly
    - By an employee via salary reduction through a Code section 125 cafeteria plan
    - By an employee with after-tax dollars (such as through payroll deduction)



# What Coverage Gets Counted?

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- Applies to “applicable employer-sponsored coverage”
  - Picks up most contributions to medical savings accounts:
    - HRAs (Employer contributions)
    - Health FSAs (Employee’s contributions via salary reduction and employer flex credits)
    - HSAs (Employer contributions as well as pre-tax contributions by accountholder via salary reduction; appears to not encompass after-tax contributions by accountholder where deducted on his Form 1040)
    - EPPs (Employer premium payments or reimbursements)

# What Coverage Gets Counted?

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- Applies to “applicable employer-sponsored coverage”
  - Statute suggests self-insured dental- and vision-only coverage **is** subject coverage
    - Statute expressly excepts dental and vision coverage where offered under a “separate policy, certificate, or contract of insurance”
    - Hopefully regulators will clarify in future rulemaking that self-insured coverage is also excepted from the Tax

# What Coverage Does **NOT** Get Counted?

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- Coverage described in Code section 9832(c)(1):
  - Coverage issued as a supplement to liability insurance
  - Liability insurance, including general liability insurance and automobile liability insurance
  - Workers' compensation or similar insurance
  - Automobile medical payment insurance
  - Credit-only insurance
- **NOTE:** Statute makes clear that on-site medical clinics are NOT excepted from the Tax
  - JCT suggests clinics that provide only a de minimis amount of coverage are excepted

# What Coverage Does **NOT** Get Counted?

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- Coverage for “long-term care”
  - Neither the statute nor the JCT Report defines the term. Thus, unclear whether only applies to qualified long-term care insurance

# What Coverage Does **NOT** Get Counted?

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- The following coverages, but only if paid for with after-tax dollars:
  - IRC section 9832(c)(3) specified disease
  - IRC section 9832(c)(3) hospital or fixed indemnity

# What Coverage Does **NOT** Get Counted?

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- What about retiree-only coverage?
  - The statute does **NOT** except such plans from the Cadillac Tax
  - As noted above, however, the annual limitation is subject to upward adjustment for “qualified retirees”
  - Also, statute allows employers to treat pre-65 and post-65 retirees as “similarly situated” when valuing coverage

# Who Calculates and Pays the Tax?

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- The sponsoring employer is required to determine the total amount of any Cadillac Tax due with respect to a given employee
- Once the employer has determined the amount of any Tax owed, it must allocate the amount among all entities liable for paying their share of the Tax
- If the employer fails to correctly calculate the Tax attributable to each responsible entity, and as a result the entity pays too little tax, the employer is on the hook for:
  - A penalty equal to 100% of the error amount
  - Underpayment interest

# Who Calculates and Pays the Tax?

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- By statute, the Tax is allocated among the following entities on a pro rata basis (based on the extent of coverage):
  - Health insurance issuer with respect to insured coverage
  - Employer plan sponsor with respect to HSA/MSA contributions
    - Presumably excludes after-tax contributions by an employee
  - “In the case of any other applicable employer-sponsored coverage, the person that administers the plan benefits”
    - Will this be the TPA or the ERISA plan administrator?



# Is the Tax Deductible?

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- No. The statute makes clear that the 40% excise tax is not deductible
  - Effectively increases the economic costs for the paying entities

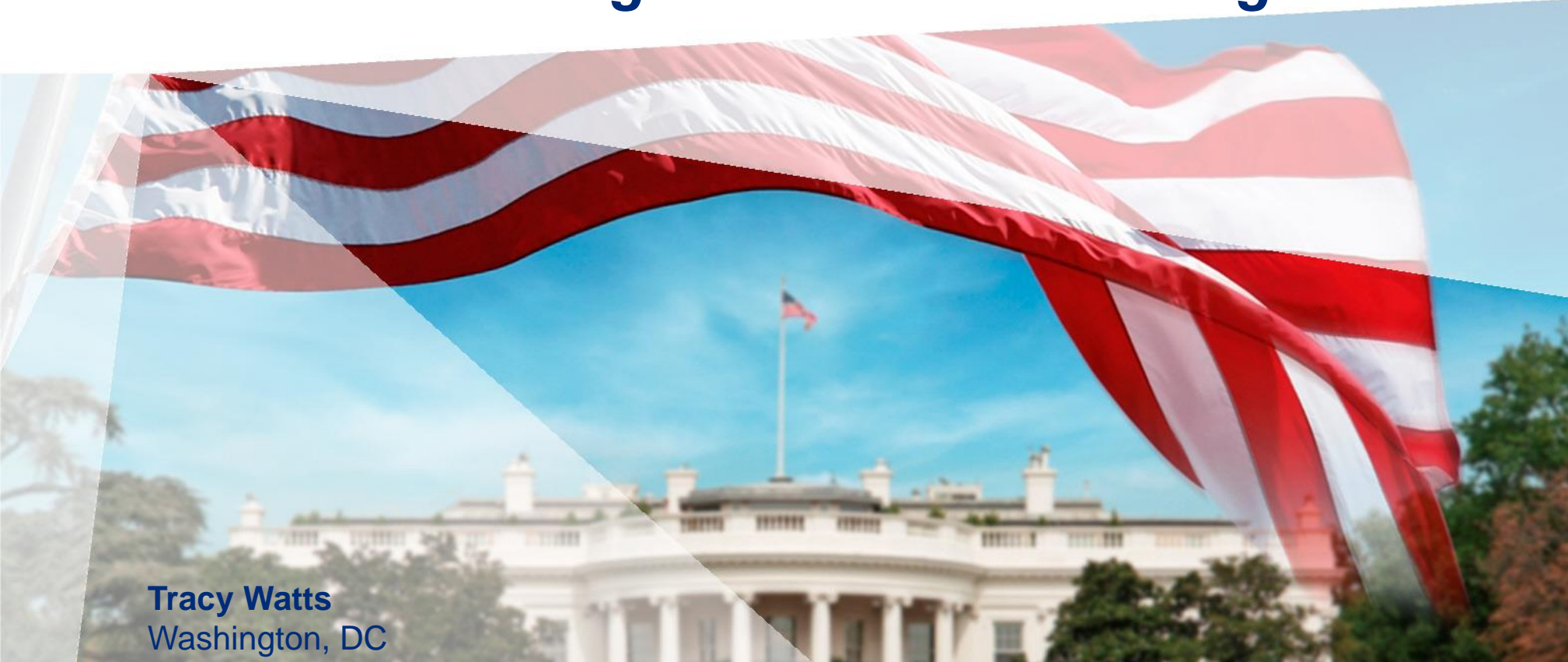
# Is the Tax ERISA Trust Chargeable?

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- Unclear, but unlikely
  - For insured coverage, however, Tax liability is likely to be forecasted into current premiums and/or recouped by future-year premiums
    - Is that the basis for the language in IRC section 4980I(d)(2)(A)?
  - For employer sponsor liability, ERISA rules do not require that these amounts be charged back to an ERISA plan
    - Also, see PCORI Fee
  - For “person that administers the plan benefits” – unclear
    - Note that with respect to the TRP Fee, the Fee ran to the “group health plan” itself by statute

# **American Benefits Council**

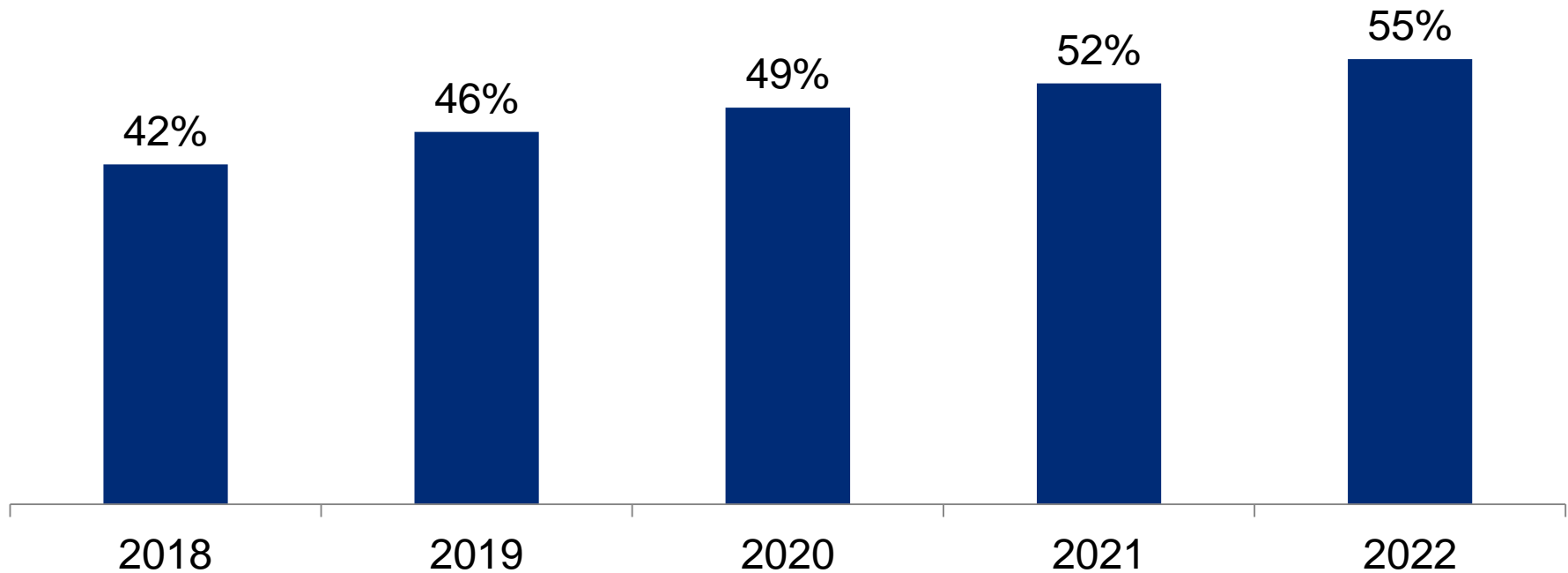
## ***Preparing for PPACA: Excise Tax on High-Cost Health Coverage***



**Tracy Watts**  
Washington, DC

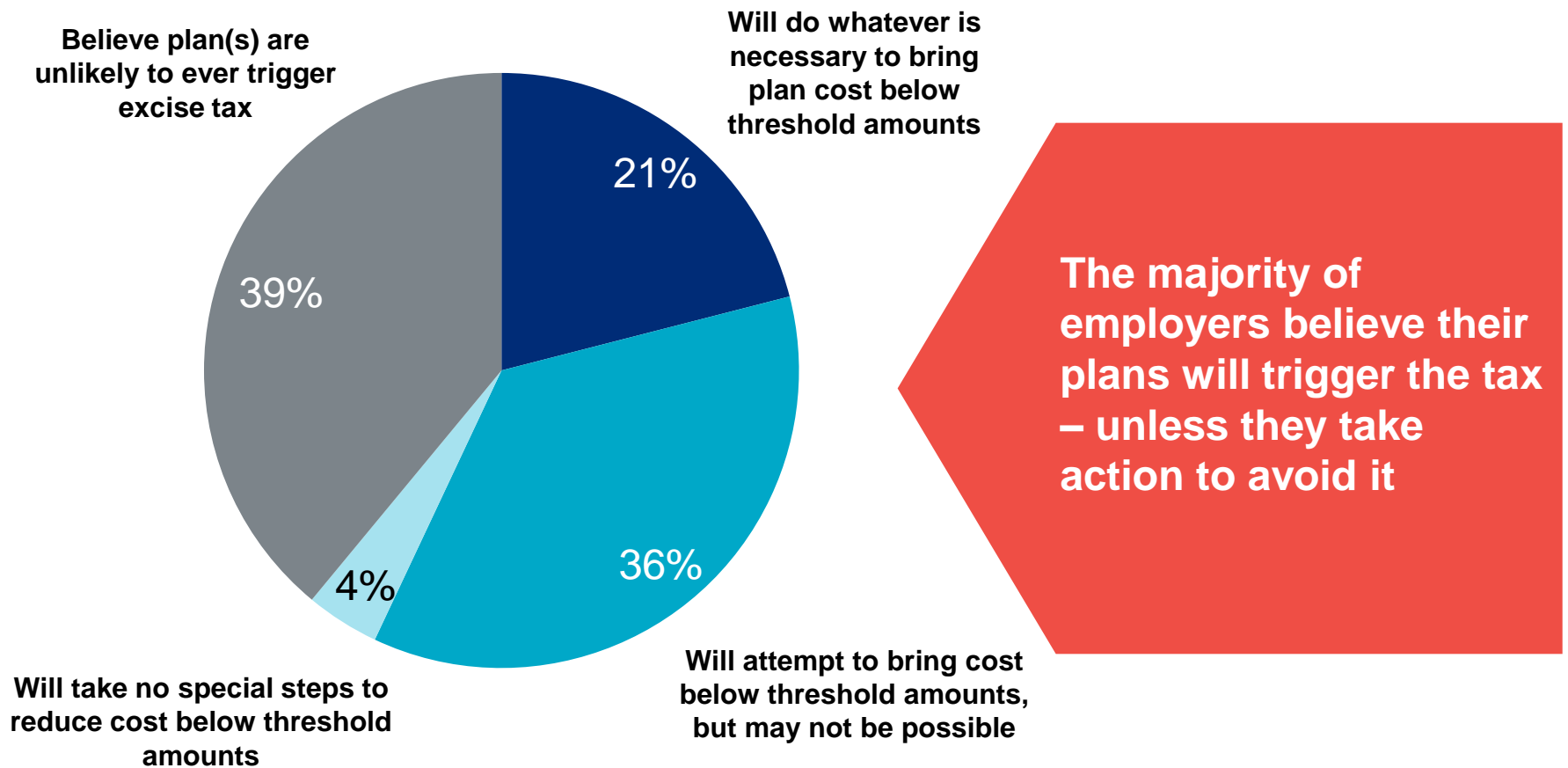
# Excise Tax in 2018: Is It a Big Deal to Employers? Our Initial Estimate in 2011...

Percent of employers that would be subject to the excise tax  
*if they made no changes to their current plan...*



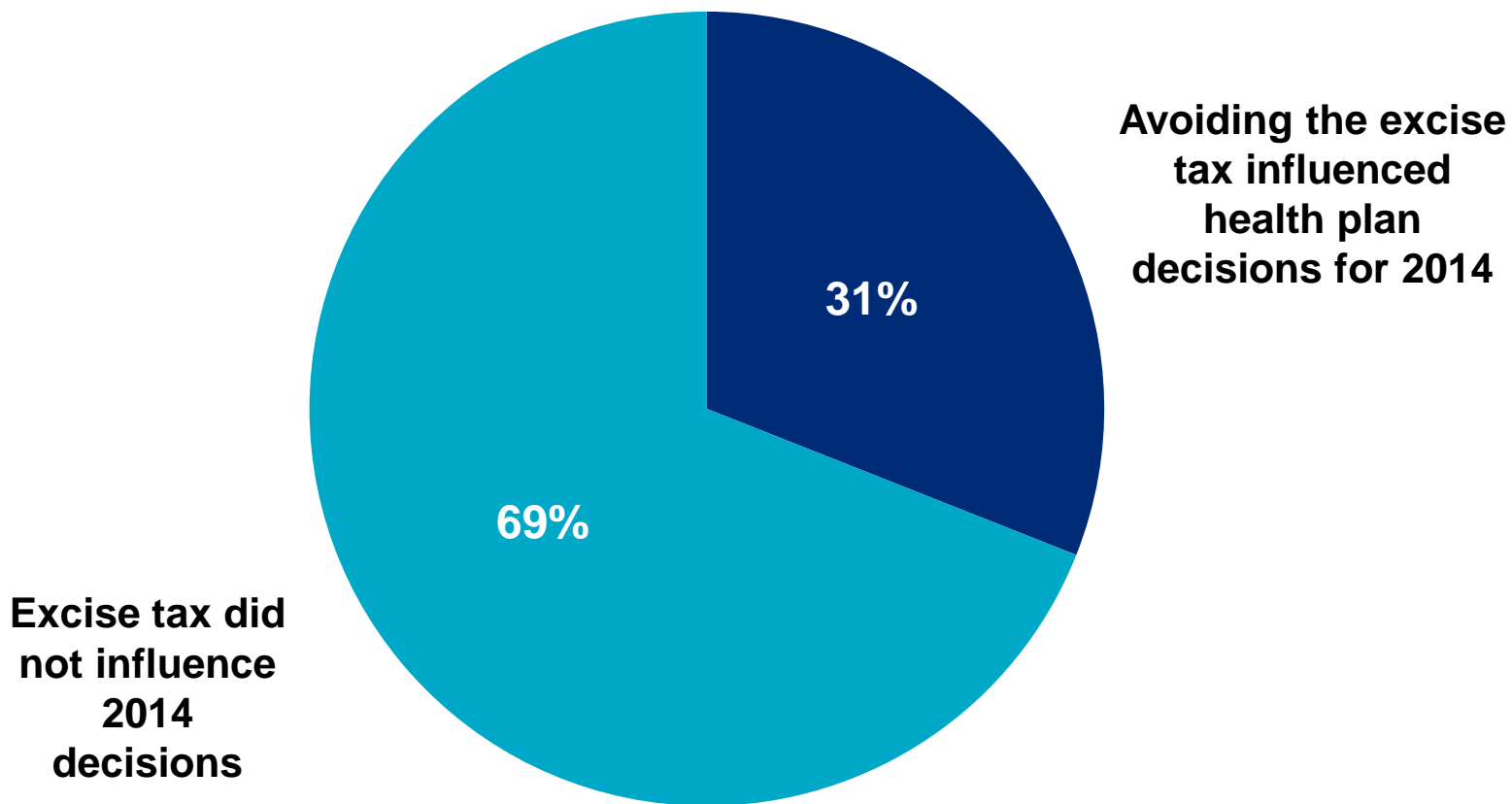
Source: 2011 National Survey of Employer-Sponsored Health Plans

# Consistently the #1 Concern of Employers Since ACA Passed



Source: 2011 National Survey of Employer-Sponsored Health Plans

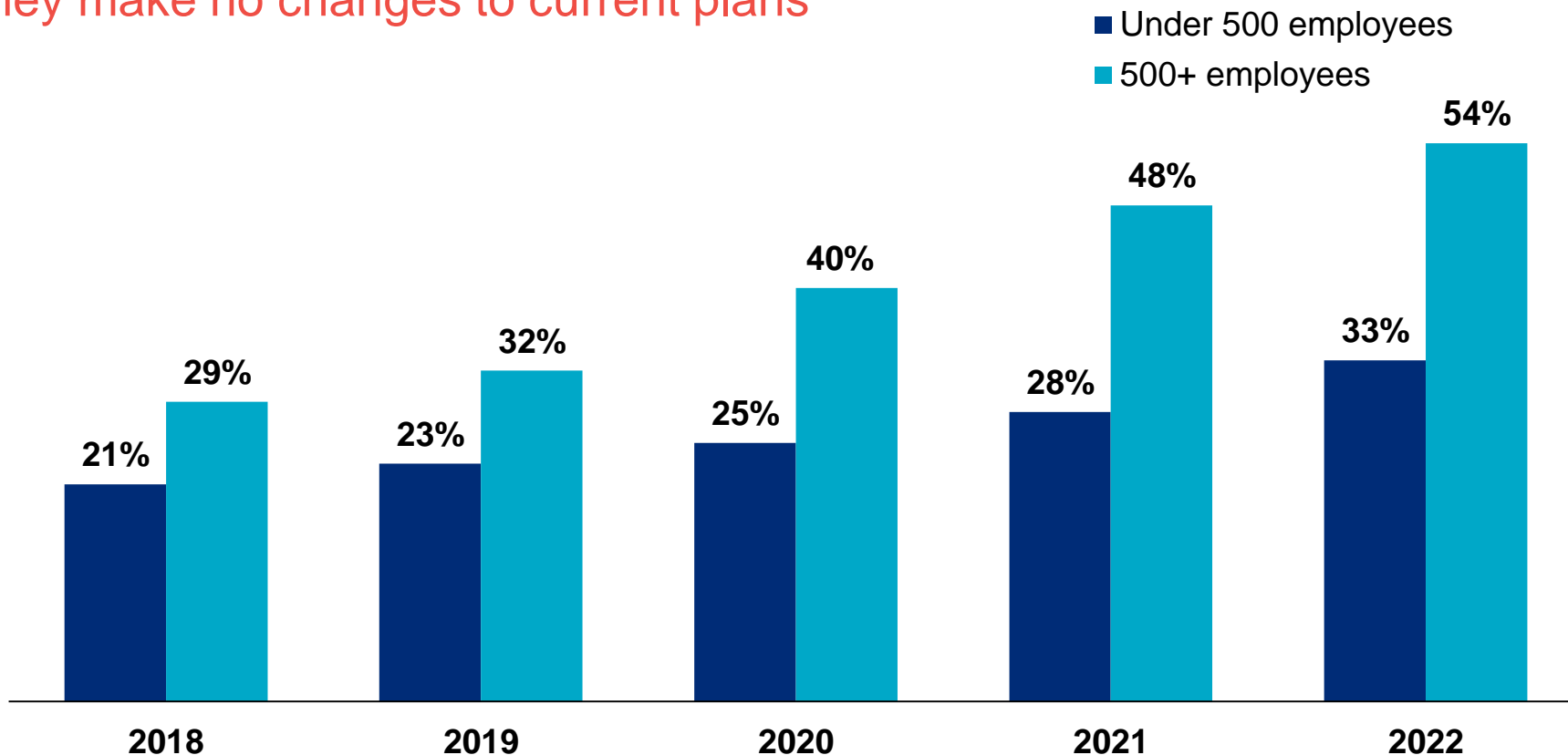
## Almost a Third Said Avoiding the Tax Influenced 2014 Health Plan Decisions



Source: Mercer's Survey on Health Care Reform, 2013

# Is It Still a Big Deal to Employers? More Recent Estimate...

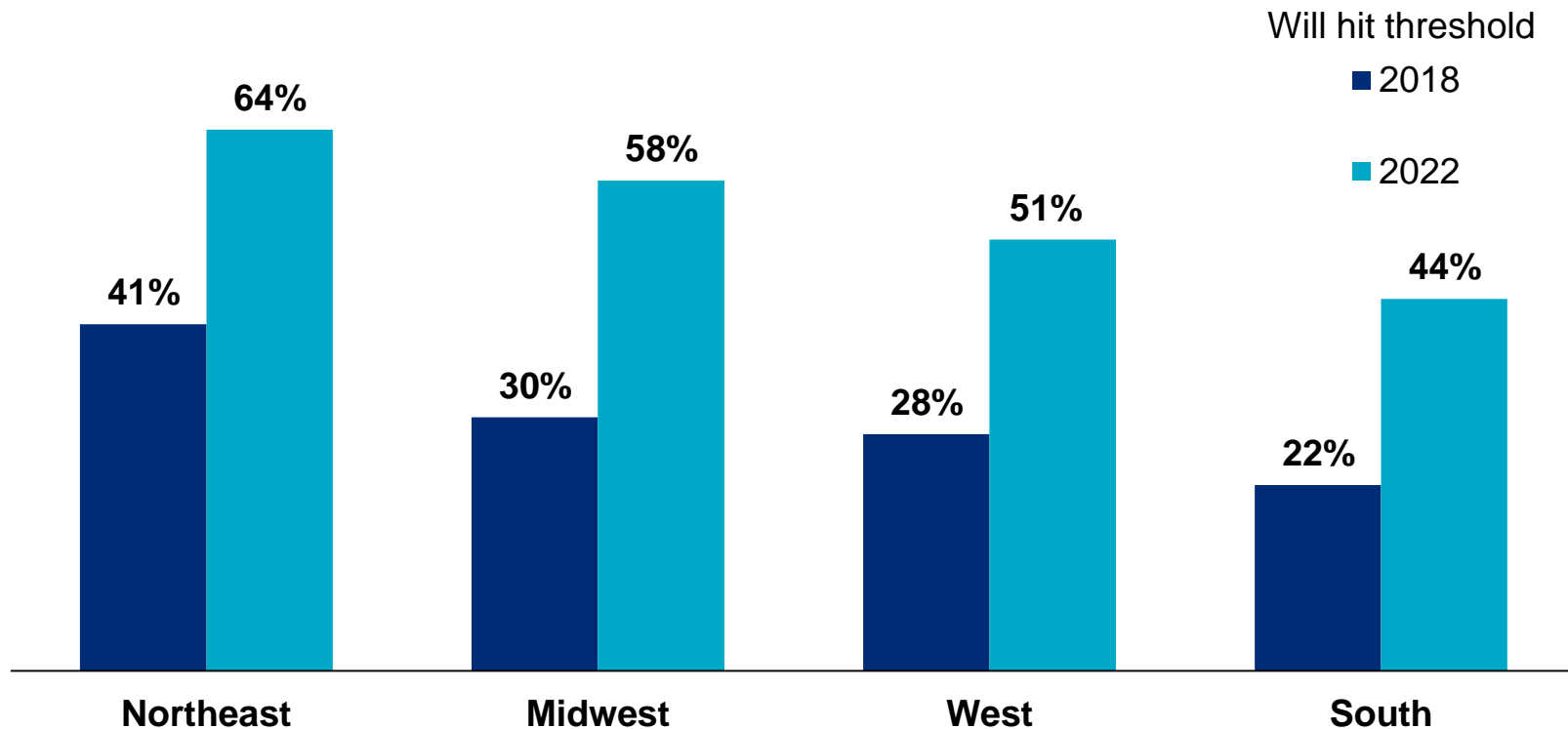
Percent of employers that will be subject to tax if they make no changes to current plans



Estimates based on data from Mercer's National Survey of Employer-Sponsored Health Plans 2013; premium trended at 6%, tax threshold trended at 3% (CPI + 1%) in 2019 and 2% for future years

# Location, Location, Location

Whether you're subject to the tax depends on where you are  
Percent of large employers subject to the tax...



Estimates based on data from Mercer's National Survey of Employer-Sponsored Health Plans 2013; premium trended at 6%, tax threshold trended at 3% (CPI + 1%) in 2019 and 2% for future years



## Not so “Cadillac” After All...

### Employers with high-cost plan\*

### Employers not offering high-cost plan

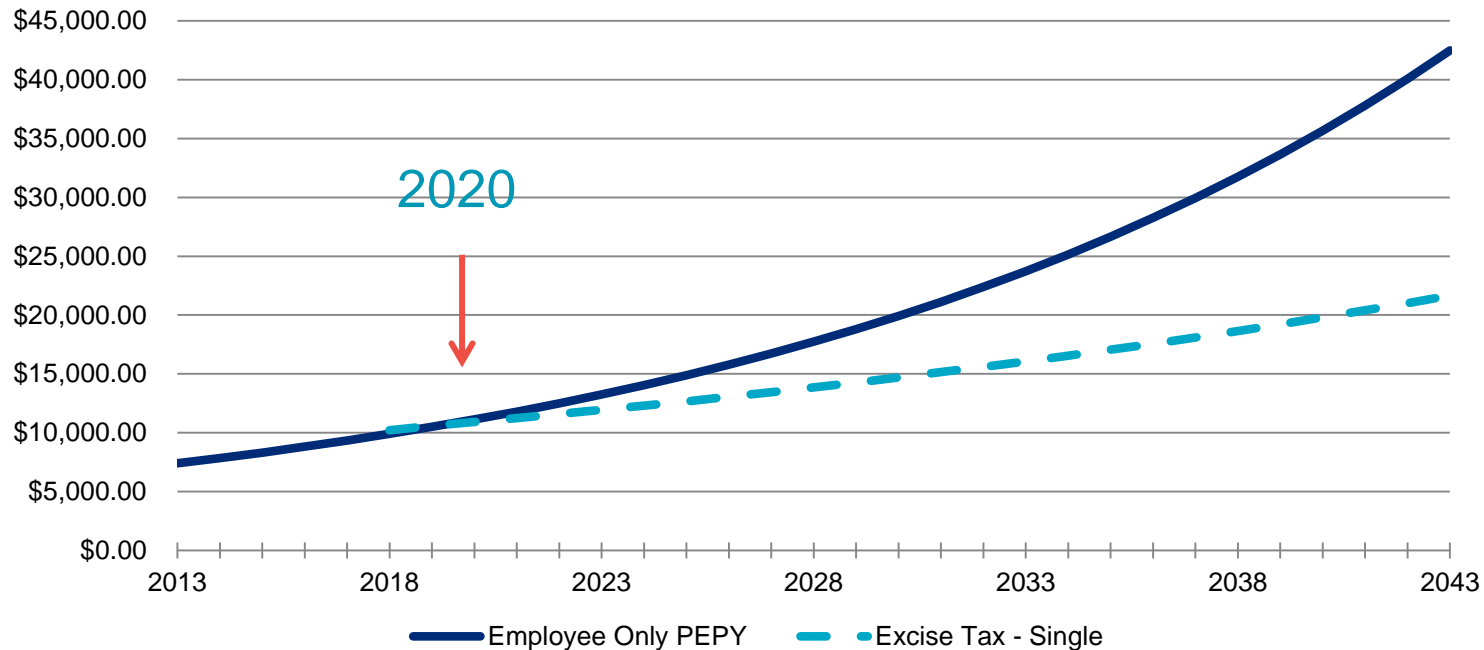
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Average salary	\$45,360	\$45,609
Average PPO deductible		
- Small employers	\$1,313	\$1,729
- Large employers	\$640	\$712
Average age	44	40
Average % of employees in unions among large employers	23%	13%

\* Plan cost estimated to hit threshold by 2018

# When Will FEHBP Standard BCBS Plan Hit the Threshold?

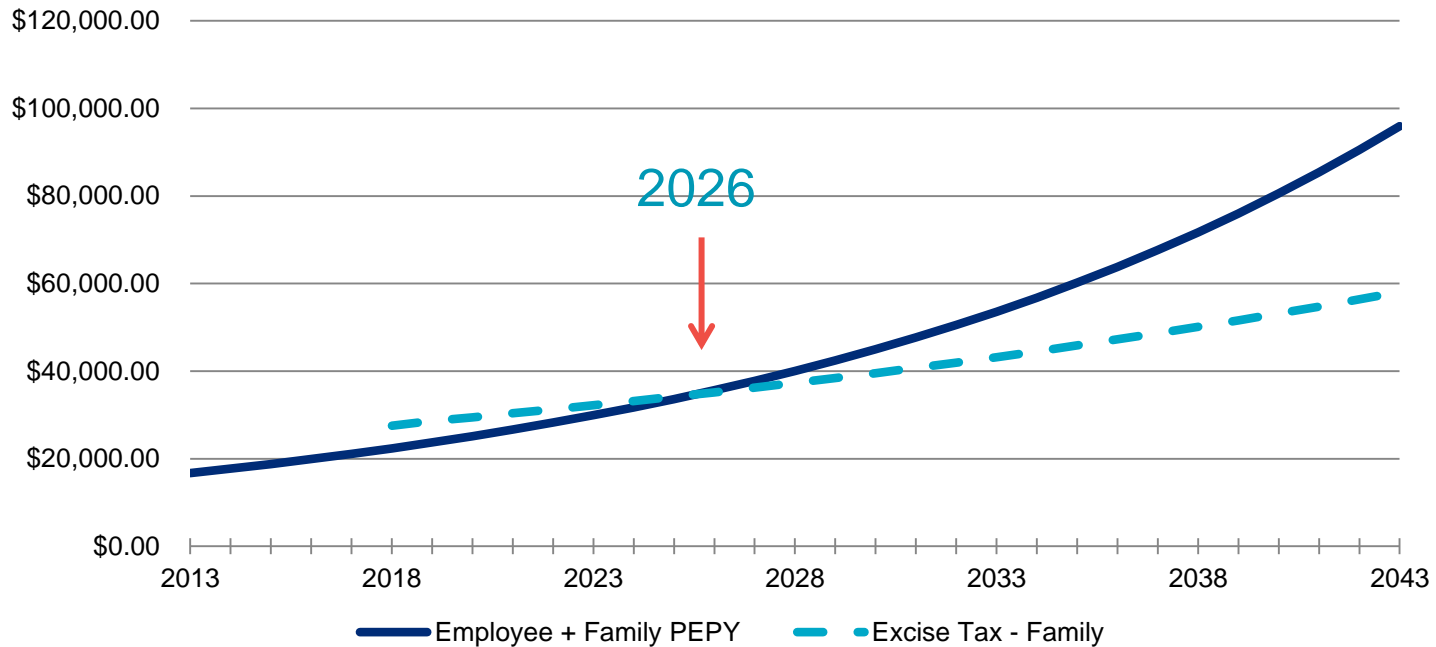
## 2014 FEHBP - BCBS Standard Option Plan vs. Excise Tax Employee Only \$7,397 in 2014



FEHBP premium trended at 6%, tax threshold trended at 4% for 2019; 3% thereafter.

# When Will FEHBP Standard BCBS Plan Hit the Threshold?

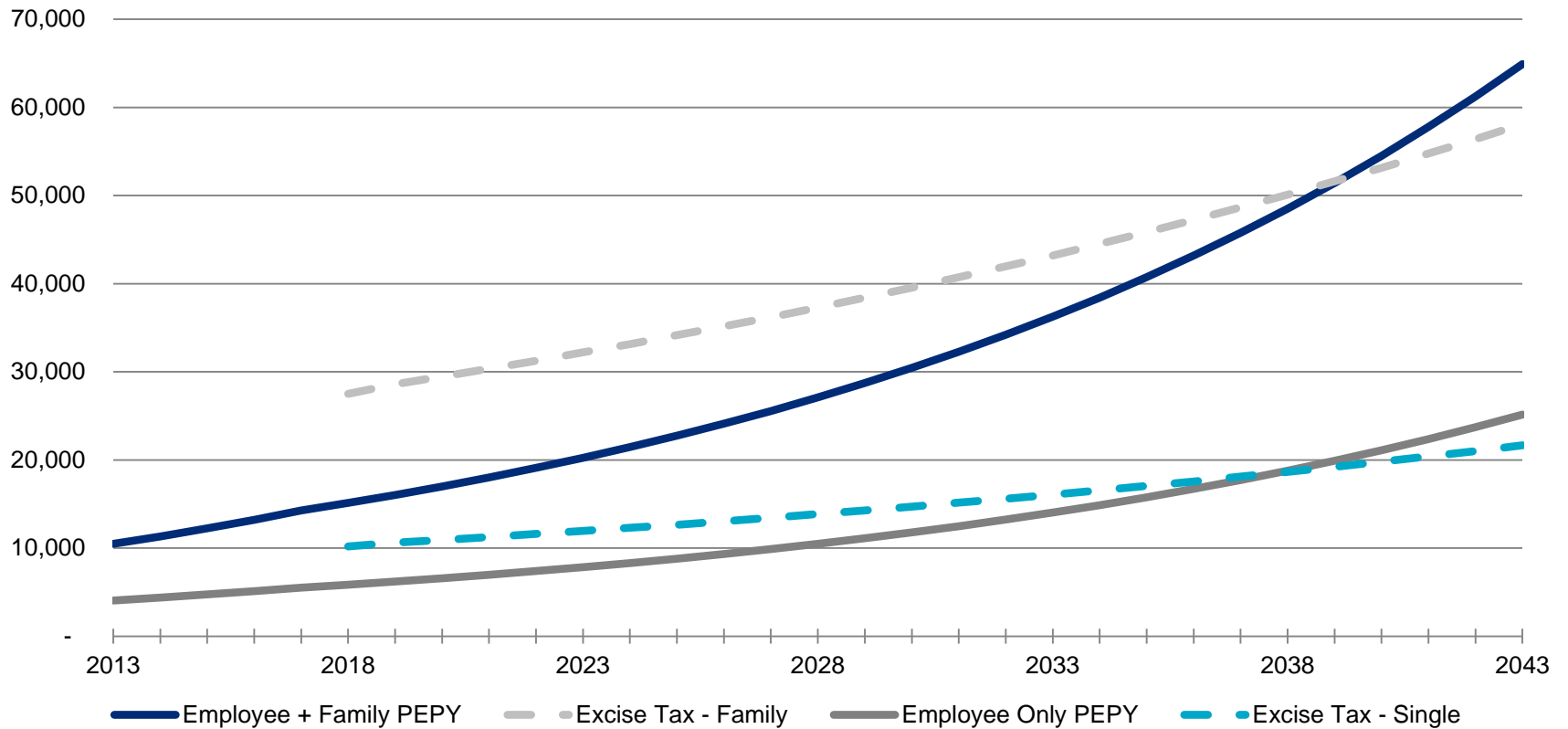
## 2014 FEHBP - BCBS Standard Option Plan vs. Excise Tax Employee + Family \$16,708 in 2014



FEHBP premium trended at 6%, tax threshold trended at 4% for 2019; 3% thereafter.

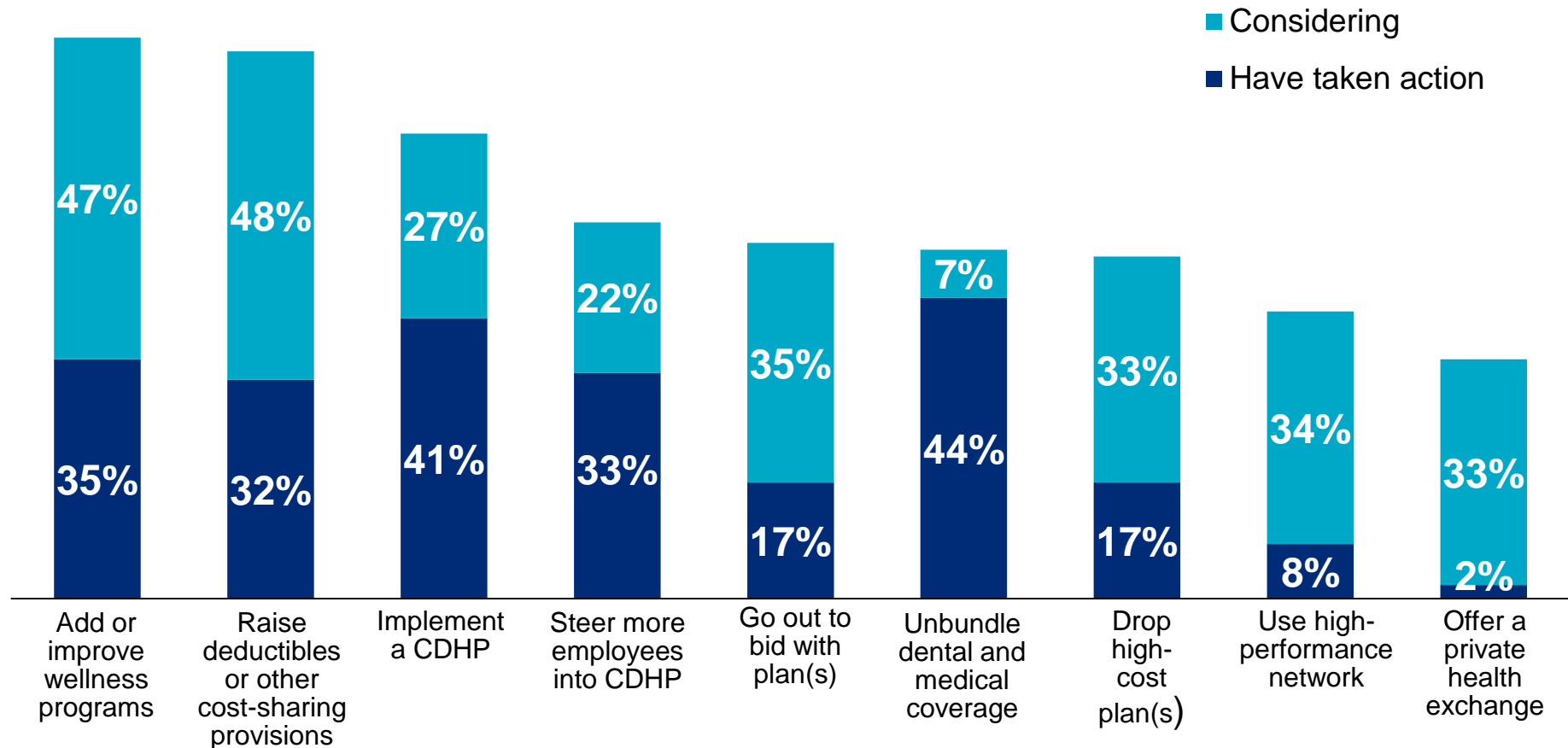
# When Will a 60% Plan Hit the Threshold?

## Average PPO Plan - 60% plan value



Estimates based on data from Mercer's National Survey of Employer-Sponsored Health Plans 2013; premium trended at 6%, tax threshold trended at 4% for 2019; 3% thereafter.

# What are employers doing, or considering, to minimize the impact of the excise tax on high-cost plans?



Source: Mercer's Survey on Health Care Reform, 2014

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This is for informational purposes only - not intended to be used as legal advice.

## Excise Tax: Things to Keep in Mind...

Lots can happen between now and 2018.

We do not have any guidance yet.

Still need to plan as if it will happen.

Advance planning especially required for union plans where employers may lock in commitments for 2018 in the very near future.

These are smart strategies – and we already are (or will be) doing them even without the threat of the excise tax in 2018.

