

REFORM *Update*

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ALERT FOR EMPLOYERS WITH RETIREE HEALTH PLANS

The White House issued a Fact Sheet with new information on the retiree reinsurance program that begins June 2010. This program has a fixed budget, so failure to act quickly could result in lost reimbursements. Health Reform Update #3 http://mcgrawwentworth.com/resources_reformupdate.html provides an overview and the last page of this Update provides a summary of the new Fact Sheet.

Our first five *Reform Updates* focused on changes that affect plan sponsors in the near term. For most plan sponsors, near term changes have tactical level implications with added cost and administrative burdens that will require relatively modest adjustments in 2011.

In our sixth *Reform Update*, we step back to review the new “employer responsibilities” and consider the potential implications on plan sponsors. The complexity and scope of these changes may, for some employers, completely alter the strategic direction of employee benefit programs when they take effect in 2014.

This *Update* provides an overview of the following new “employer responsibilities”:

- Employer “pay or play” provisions
- Plan “minimum essential coverage” rules
- Penalties for not providing coverage or not meeting certain standards
- Additional administrative requirements on plan sponsors

These new, complex “employer responsibilities” will need to be clarified through the regulation writing process and some aspects may be modified prior to January 1, 2014. This *Update* provides our best understanding at this time and should be used as a general guide and not a definitive interpretation.

Employer “Pay or Play” Requirements

The pay or play requirements apply to “large” employers – with an average of at least 50 full-time employees on business days in preceding calendar year. IRS controlled group rules will define an employer and the term employer will include any predecessor employer(s). The 50 employee threshold will be based on a two step calculation of full-time equivalents (“FTEs”). First, any employee working 30 or more hours each week will count as one FTE. Second, the number of hours worked by part-time employees (under 30 hours) during each month is divided by 120 to determine an additional number of FTEs. The total of these two numbers establishes the 50 employee threshold.

Example: As an illustration, we will look at ABC Company that has 800 full-time employees (30 or more hours) and 22 part-time employees in 2013. ABC offers a health plan with a \$1,500/\$3,000 deductible, \$2,500/\$5,000 out-of-pocket maximums, and the plan is expected to pay at least 60% of eligible expenses. ABC's plan has a net annual cost of \$9,000 per employee

If ABC Drops Coverage, What Is The Penalty?

If at least one of ABC's employees receives a credit to purchase coverage through the Exchange, ABC's penalty would be:

• Number of full-time employees in month	800
• Subtract first 30 employees	-30
• Equals number subject to penalty	=770
• Multiply times \$166.67 (\$2,000÷12 months)	\$128,336
• Annual Cost	\$1,540,031
• Plus loss of tax preference (assumed at 34%)	\$2,063,641

If ABC Drops Coverage, What Happens To Employees?

If ABC drops coverage, it may choose to provide pay increases to employees that will help them purchase coverage through the insurance Exchange. The challenge is that ABC must now pay the penalty and all dollars are now subject to taxation.

If ABC is willing to continue paying the same \$9,000 per employee cost, employees could expect the following:

• Per employee annual health plan value	\$9,000
• Less, penalty payment (\$2,063,641÷800 employees)	\$2,580
• Amount of gross increase to employee pay	\$6,420
• Less, individual income taxes (assumed at 25%)	\$1,605
• Equals, employee added earnings to purchase health plan	\$4,815
• Actual cost to purchase health benefits (need to wait on Exchanges)	????!

Employer Offers Coverage, But Coverage Does Not Meet Certain Standards

Even if an employer offers health plan coverage, it may be subject to a penalty if:

- At least one full-time employee opts out of employer's plan and receives either a premium tax credit to purchase coverage or a cost sharing reduction for coverage purchased through the Exchange; and
- Employer coverage is deemed unaffordable, as follows:
 - ▶ Required contribution to purchase lowest plan cost coverage available from employer exceeds 9.5% of employee's household income; **or**
 - ▶ Employer plan pays for less than 60% of eligible expenses.

An employer offering coverage may or may not be subject to this penalty when one or more employees choose to purchase benefits via the Exchange. Application of the penalty depends on the health plan offered by the employer and the household income of employees purchasing benefits via the Exchange.

The penalty requires two calculations and an employer would pay whichever calculation provides the lowest amount. Details on the frequency of payment have not been provided, but the penalty is to be calculated each month as follows:

- Number of full-time employees in month _____
 - Subtract first 30 employees -30
 - Equals number subject to penalty _____
 - Multiply times \$166.67 ($\$2,000 \div 12$ months) \$ _____
- or**
- Number of full-time employees in month subject to #1 or #2 above _____
 - Multiply times \$250 ($\$3,000 \div 12$ months) \$ _____

If ABC Offers Coverage, But Does Not Meet Standards

The answer here depends on many specifics, but we will assume that 5 of ABC’s employees take advantage of a premium tax credit to purchase coverage through the Exchange.

First, determine if ABC’s plan is “unaffordable” for any of these 5 employees:

- Is employer plan actuarially designed to pay more than 60% of covered expenses under the plan?
 - ▶ If no, penalty applies.
 - ▶ If yes, determine if plan costs more than 9.5% of any employees’ household income.
 - ✓ If lowest wage full-time employee has \$23,000 household annual income and ABC’s plan contribution for single coverage is \$1,200 per year, the contribution is 5.2% - no penalty.
 - ✓ If lowest wage full-time employee has \$23,000 household annual income and ABC’s plan contribution for single coverage is \$2,300 per year, the contribution is 10% - penalty applies.

If ABC’s plan is deemed unaffordable for 2 employees, the penalty would be the lesser of the amount calculated above (penalty for not offering coverage at \$1,540,031), or:

- Number of full-time employees in month subject to #1 or #2 2
- Multiply times \$250 ($\$3,000 \div 12$ months) \$500
- Annual Cost \$6,000
- Plus loss of tax preference (assumed at 34%) \$8,040

These simple examples based upon the details currently provided in the health care act demonstrate how the play or pay provisions will work. More guidance will be needed for employers to do a thorough evaluation of the impact of the pay or play provisions. Many questions will need to be answered, and more guidance is expected to clarify the situation over the next several years.

Additional Administrative Requirements

In order to administer the new Health Care Reform rules, a number of new administrative requirements have been established. These include several that require plan sponsor action including:

- Employers that do not offer coverage will need to file a return stating they do not offer coverage, the number of full-time employees, and other information required by the Secretary.
- Employers that offer coverage will be required to file a return with the following information:
 - ▶ Name of each individual they provide an opportunity to enroll for coverage.
 - ▶ The length of any waiting period.
 - ▶ The number of months that coverage was available.
 - ▶ The monthly premium for the lowest cost plan option.
 - ▶ The plan's share of covered health care expenses.
 - ▶ The number of full-time employees.
 - ▶ The number of months employees were covered.
 - ▶ Any additional information required by the Secretary.
- All employers will have a notice requirement that will apply in 2013 that will educate employees about the Exchanges and how they will operate.

Similar to so many aspects of Health Care Reform, additional guidance will be needed to understand exactly what action plan sponsors will need to take in order to fully comply with these requirements.

Concluding Thoughts

The "employer responsibilities" may change over the next several years, but employers will want to closely monitor developments and may revise how they provide health care benefits to their employees. The new insurance Exchange combined with relatively small penalties may lead some employers to drop coverage while others may decide to improve coverage to avoid penalties and establish a labor market edge. Much will depend on the specific employer situation, the cost of coverage through the new Exchanges, general economic conditions, and the myriad of yet to be issued regulations. Employers with historically weaker benefits (such as restaurant/retail) may face new penalties while employers with historically strong benefits (such as manufacturing) may look longingly on the possibility of turning health plan responsibility over to individual employees. Employers have already begun to lobby Congress for special exceptions and modifications to Health Care Reform.

Our next *Update* will cover the guidance that was just published to address the details to apply for retiree reinsurance program.

Additional Information Released on the Retiree Reinsurance Program

As noted in the page one, the White House issued a Fact Sheet last week on the reinsurance program that provided some new details on the program for employers that offer retiree coverage to pre-65 retirees. Based on our review of that document, we noted several interesting comments:

- Implies employers may use reinsurance payments to offset some of their expenses for providing the early retiree health care plan; this is more expansive than language in Health Care Reform that required reinsurance payments be used to offset expenses for the early retirees.
- \$15,000 claims threshold applies per individual; not retiree and dependents combined.
- Effective date for claims that can be reimbursed pushed up to June 1, 2010.
- Claims incurred on January 1, 2010 and after will count toward the accumulation of \$15,000 claim threshold.
- Only claims incurred after June 1, 2010 that exceed the \$15,000 threshold (accumulated since January 1, 2010) will be eligible for reimbursement.
- Application process expected to be ready by the end of June.
- Limited funds available under the reinsurance program, so interested employers may want to take action quickly to submit applications for reimbursement.

We expect more guidance to be issued in May and June regarding the retiree reinsurance program and we will keep you apprised of all the information released via future *Reform Updates*.

The actual text of the Fact Sheet can be found at <http://www.whitehouse.gov/the-press-office/fact-sheet-early-retiree-reinsurance-program>.

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