KISTLER TIFFANY BENEFITS

Plan Designs

Medical Opt-out Payments

Some employers control health care costs by offering their employees a cash incentive to waive health care coverage. These arrangements, known as "opt-out payments" or "cash in lieu of benefits," are often aimed at employees with working spouses who are eligible for group health coverage through another employer. The employer benefits by avoiding the cost of paying for its share of the premiums while the employee receives the extra cash.

If an employer gives its employees a choice between health care coverage and taxable compensation, it must be done through a **cafeteria plan** under Section 125 of the Internal Revenue Code. The opt-out arrangement must be included under a cafeteria plan that meets IRS requirements in order to avoid taxation of participants who elect health care benefits. To be valid, a cafeteria plan must be established in a written plan document.

While medical opt-out payments are still permissible, there are various legal issues that impact the design of these arrangements, including Affordable Care Act (ACA) compliance concerns. *Before offering a health plan cash-out option, employers should consult with their advisors to confirm that the arrangement complies with applicable laws and insurance contract terms.*

Legal Issues under the ACA

A common design for medical opt-out payments is to require a certification or other form of proof that the employee has health coverage through another source, such as through a spouse's employer. This type of design should be carefully implemented due to ACA compliance concerns. Conditioning the availability of the cash incentive on an employee's purchase of an individual insurance policy likely creates an employer payment plan that violates the ACA's market reforms.

Also, effective for 2015, the ACA's shared responsibility rules for applicable large employers (ALEs) require certain ALEs to provide employees with an effective opportunity to decline health plan coverage. This requirement applies to ALEs whose health plan coverage does not meet the ACA's affordability and minimum value requirements. Employers may require employees to provide proof of other group health plan coverage to obtain a cash-out payment, but ALEs that do not offer affordable, minimum value coverage cannot require employees to provide this proof to decline the ALE's group health coverage.

In addition, to avoid potential penalties under the shared responsibility rules, ALEs must offer affordable, minimum value health coverage to substantially all full-time employees. In general, the affordability of an employer's offer of health coverage depends on whether the employee's required contribution for self-only coverage exceeds a certain percentage of the employee's household income. The Internal Revenue Service (IRS) released Notice 2015-87 and proposed regulations to provide guidance on how **medical opt-out payments impact the affordability calculation**. In general, until final regulations are issued, medical opt-out arrangements that were adopted before Dec. 16, 2015, will not increase the cost of employer-provided health coverage.

The IRS' guidance groups medical opt-out arrangements into two general categories:

- *Unconditional medical opt-out payments* – An arrangement where the opt-out payments are conditioned solely on an employee declining coverage under an employer's health plan and not on an employee providing proof of other coverage. According to Notice 2015-87, it is generally appropriate to treat unconditional opt-out payments as increasing an employee's contribution for health coverage beyond the amount of the employee's salary reduction contribution. For example, an employee whose required self-only contribution for health coverage is $200 per month, but who is eligible for a cash payment of $100 per month if coverage is waived would be treated as having a required contribution of $300 per month when determining if the coverage is affordable. Until the proposed regulations are finalized, this guidance applies to unconditional opt-out arrangements that are adopted after **Dec. 16, 2015**.
- *Conditional medical opt-out payments* – An arrangement where the opt-out payments are conditioned on an employee declining coverage under an employer's health plan and providing proof of other coverage. According to the proposed regulations, these payments would increase an employee's salary reduction contribution when determining the health plan's affordability, unless the arrangement qualifies as an "eligible opt-out arrangement." An eligible opt-out arrangement is one where the opt-out payments are available only to employees who decline employer-sponsored coverage and provide reasonable evidence that they and their expected tax dependents have or will have minimum essential coverage other than individual market coverage during the plan year. However, payments under conditional opt-out arrangements will not be treated as increasing an employee's required contribution until the proposed regulations are finalized.

Other Legal Concerns

Offering opt-out incentives only (or primarily) to employees who have a history of high health claims may violate HIPAA's nondiscrimination rules. Depending on how an employer defines eligibility for the opt-out incentives, other federal laws, such as the Americans with Disabilities Act (ADA) or the Age Discrimination in Employment Act (ADEA), could be implicated.

In addition, before offering a cash-out option for an insured plan, an employer should confirm that the cash-out does not violate minimum participation requirements or other insurance contract terms.

The following is an example of a waiver-of-health-coverage form that can be used in a medical opt-out program. It requires customization.

Sample Waiver-of-Health-Coverage Form

ABC Company

Medical Plan Waiver Form

Plan Year Jan. 1, 2017 – Dec. 31, 2017

Name: ____

Address: ____

____________ I decline coverage through ABC Company's group health plan for the Plan Year beginning on Jan. 1, 2017, and ending on Dec. 31, 2017.

I understand that, by declining health coverage through ABC Company, I authorize participation in the ABC Company Section 125 Cafeteria Plan. I also understand that I cannot revoke or change this election during the Plan Year unless I have a qualifying change in family and/or job status and that change is consistent with my change of election. I may then revoke my prior election and sign a new Agreement if a change in election event occurs. In exchange for my waiver of health care coverage, ABC Company will deposit $ per pay period (24 pay periods per plan year) into the cash benefit component of my cafeteria plan account for the Plan Year of Jan. 1, 2017, through Dec. 31, 2017, for a total annual deposit of $. I agree to accept $ each pay period from my cafeteria plan as ordinary income.

Signed: ____ Date: _________________