

Cadillac Tax

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IRC Section 4980 I

- Added to the Internal Revenue Code (IRC) by the Affordable Care Act (ACA)
- Imposes a 40% excise tax on any “excess” health benefit provided to an employee
- As originally enacted, the Tax is not deductible for purposes of Federal income tax. However, a December, 2015 Amendment to the Code will change that and render the tax deductible.
- “Excess benefit” is defined as the excess (if any) of the “aggregate cost of the applicable coverage” for an individual over the “applicable dollar limit” for the employee (including retirees) for the month

To What Plans Does the Cadillac Tax Apply?

Group Health Plans sponsored by all employers, including:

- a.) private employers
- b.) governmental employers
- c.) non-profit employers
- d.) church-based employers

Applies to:

Fully Insured Coverage
Self-funded Coverage

PURPOSES

Different interests had differing purposes:

1.) reduce overly rich employer –
provided health benefit plan designs

a.) health coverage generally tax –
deductible- richer plans reduce
corporate

and personal taxes

b.) richer plans as a disincentive to
reducing
health care costs

2.) generate revenue to finance the
Affordable

Care Act (ACA) programs – particularly ,
the

STATUS

Originally Scheduled for Implementation in 2018

Implementation DELAYED until 2020 (by the Consolidated Appropriations Act, 2016)

- Regulations Have Not Been Issued
- 2 Notices issued by IRS in 2015 seeking input regarding the development of regulations
- Myriad of interests seeking repeal of the

STATUS (CONTINUED)

- In a largely “symbolic” vote taken in December, 2015 the Senate voted 90 - 10 to include a provision for the repeal of the Cadillac Tax in a larger bill gutting the Affordable Care Act.
- But no agreement on an alternative revenue source(s) for funding ACA programs

Aggregate Cost of the Applicable coverage includes:

HMO, PPO and indemnity coverage (includes Employer and Employee Contribution)

Health Flexible Spending Accounts (FSAs)

Health Savings Accounts (HSAs) (including employer contributions but excluding employee after-tax contributions)

Health Reimbursement Accounts (HRAs) (not specifically addressed in statute but IRS anticipates will be included)

On-Site Medical Clinics

Retiree Coverage

Certain coverage for specified diseases (if the cost of coverage is excluded from gross income)

Aggregate Cost of the Applicable Coverage

(Continued)

Does Not Include:

Stand alone dental or vision coverage
(Statute only references insured coverage as excludable but guidance suggests self-funded coverage will be treated similarly)

Cost of the Excise Tax, itself

FSA Cost Allocation

IRS considering safe harbor for calculating FSA costs (where non-elective flex credits are not available for use in the FSA) with regard to FSAs with a Carryover Option.

Proposed Safe Harbor:

Cost of FSA for plan year would be the amount of an employee's salary reduction without regard to amount actually expended. Carry-over amounts (\$s not used in that year) would be credited to the year funded by salary reduction and not to the year in which expended.

Above safe harbor
would not be
available where non-
elective flex credits
are available for use
in the FSA.

Determination of Cost of Applicable Coverage

Insured coverage – Actual premium expense

Self-Insured Coverage –

Similar to Determination of Applicable Premium under COBRA
i.e. cost of coverage for similarly situated individuals under the plan

Cost Calculated Separately For:

- 1.) Self-Only Coverage
- 2.) Other than Self-Only Coverage

Plan May Treat Pre-65 and Post-65 retirees as similarly situated individuals

**Guidance suggests that costs will be calculated separately for each benefit package
e.g. HMO v. PPO. “Excess benefit” will be based upon benefit package in which employee is enrolled (not plan(s) in which employee could have been enrolled.)**

Self-Insured Methods for Computing COBRA Applicable Premiums

- 1.) Actuarial Basis Method
- 2.) Past Cost Method:
 - 1.) based upon costs over preceding 12 month determination period
 - 2.) calculation includes costs of:
 - a.) claims
 - b.) stop-loss premium
 - c.) administrative expenses
 - d.) reasonable overhead expenses of employer

Applicable Dollar Limit

- Baseline Limits:

Self-Only Coverage - \$10,200.

Other Than Self-Only Coverage -\$27,500.

Inflation Adjustments

Possible 2018 Adjustment –

The above limits will be increased by the percentage by which the percentage increase between 2010 and 2018 to the:

Blue Cross Blue Shield standard benefit option under the Federal Employees health plan exceeds:

55%

Applicable Dollar Limit (cont.)

For calendar year 2019, the Applicable Dollar limits for 2018 shall be increased by the %age change to the Consumer Price Index (CPI) plus 1%

For calendar year 2020 and succeeding years – adjustment limited to %age increase to the CPI

The December, 2015 amendments indicate that, despite the delay in implementation of the tax, the above inflation adjustments for 2018 and 2019 will apply to the limits when the tax is implemented in 2020.

Other Adjustments

A. Age and Gender Adjustment –

Applies if the age and gender characteristics of an employer's workforce are different from those characteristics of the national workforce

The amount of the adjustment is determined by dividing:

(aa) the premium cost of the Blue Cross/Blue Shield standard benefit option under the Federal Employees Health Benefits Plan for the type of coverage provided such individual in such taxable period if priced for the age and gender characteristics of all employees of the individual's employer, by

(bb) that premium cost for the provision of such coverage under such option in such taxable period if priced for the age and gender characteristics of the national workforce.

Age And Gender Adjustment

The December, 2015 amendments require a review of the suitability of the use of the premium cost of the Blue Cross/Blue Shield standard benefit option under the Federal Employees Health Benefits Plan as a benchmark and recommendations for a more suitable benchmark for the age and gender adjustment

- No downward adjustments of the limits
- Adjustment determined separately for self-only coverage and other than self-only coverage
- Depends on the distribution of men and women in different age groups

Distribution in different age groups

- 1.) determine the age and gender characteristics of the national workforce. IRS considering use of BLS Current Population Survey.
- 2.) determine each employer's age and gender characteristics. IRS considering a requirement that each employer determine the age and gender of each employee as of the first day of the plan year.
- 3.) formulate and publish adjustment tables to facilitate and simplify the calculation of the age and gender adjustment.

Other Adjustments (cont.)

B. Adjustments for Qualified Retirees –

- a.) receiving coverage by reason of retiree status
- b.) age 55 or over
- c.) not eligible for benefits or enrollment under Medicare

Other Adjustments (cont.)

C. Adjustment for High Risk Professionals –

Adjustment for plans where the majority of covered employees are engaged in a high –risk profession or employed to repair or install electrical or telecommunication lines

“High-Risk Professions”

Police

Firefighters

**Ambulance/rescue
employees
(EMTs and first –
responders)**

**Individuals
employed in the
construction
industry NLC
lobbying IRS to
classify DPW
employees as
“employees within
construction industry”**

Problem:
High Risk Profession
Adjustment available
only if majority of
employees in the plan
are in high risk
professions.

IRS requested comments on:

- 1.) how an employer makes that
determination, and
- 2.) what the term “plan” means
in that context

\$ Adjustment for Qualified Retiree and High Risk Profession:

Self-Only Coverage \$1,650.

Other Than Self-Only Coverage \$3,450.

Cannot Double the Adjustment for Qualified Retirees
from High Risk Professions

Who Pays the Excise Tax?

- Answer: The “Coverage Provider”

Who is the Coverage Provider?

1.) insured coverage – the health insurance issuer

2.) Coverage under an HSA or an Archer MSA –
the employer

3.) all other applicable coverage – “the person
“ ” ”

Who is the “Person That Administers the Plan Benefits”?

- IRS proposes 2 possible approaches
 - 1.) the third party administrator (TPA)
 - 2.) the person with ultimate authority for administration of plan benefits

PROBLEM

Many strategies to address the Cadillac Tax require collective bargaining

(except for plan design changes permitted by M.G.L. c. 32B, Sections 21 and 22)

M.G.L. c. 32B, Sections 21 - 22

Establish a process for making plan design changes.

Permit a city-town to include in its health plans:

Co-payments,

Deductibles,

Tiered provider network copayments, and other cost-sharing plan design features that are no greater in dollar amount than those features offered in the GIC's plan with the largest subscriber enrollment.

Process involves the establishment of a Public Employee Committee (PEC) and negotiations with that Committee regarding the plan changes to be implemented as well as the sharing of savings that are generated by those changes

We have posted on the MIIA website at _____ the following documents:

- 1.) a Review of the provisions of the legislation that established Sections 21 and 22;
- 2.) an analysis of the regulations promulgated by the Secretary of Administration and Finance that deal with Sections 21 and 22, and
- 3.) a step-by-step guide to implementing the Section 21-22 process.

With Delay, Why be Concerned?

- Tax may not be repealed
- Legislation did not change benchmarks
 - As costs increase, amount owed in 2020 could be very significant
 - Takes time to implement initiatives to reduce costs of health care
- If Tax is repealed, health care cost increases remain unsustainable

Cost-lowering Strategies Requiring Union Negotiations

- Reduce richness of plan designs by increasing out-of-pocket payments (co-pays, deductibles, etc.)
- Limit or eliminate FSA, HSA and/or HRA contributions that count toward aggregate cost
- Eliminate high cost plans (e.g. PPO)
- Adopt limited network plans

Strategies Requiring Negotiations (cont'd)

- Create separate dental and vision plans
 - Dental and vision plans are not subject to Tax
 - Would reduce cost of health care plans subject to Tax
- Consider combining early and post-65 retirees
 - Reduces cost of active plans
 - Retirees have higher benchmarks
 - Check the math

Strategies without Union Negotiations

- Increase health and wellness initiatives
 - Long-term strategy, with potential for significant impact
 - Engaging enrollees is challenging
- Conduct eligibility audits
- Set contribution levels for early retirees at a lower level than active employees (floor is 50%)

Strategies without Union Negotiations

- Possibly create separate risk pools of similarly situated beneficiaries such as high-risk professionals
 - Entirely technical activity
 - Don't change coverage
 - IRS guidance if/when Tax implemented

A Door, Not a Barrier?

- Run projections to understand potential exposure under different scenarios
- Discuss realities of Tax with union representatives
 - Discuss options
 - Agree to open negotiations if Tax is implemented and municipality will exceed thresholds

Discussion

