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A TECHNICAL UPDATE FOR FLEXSYSTEM | REFERENCE NUMBER: FX083 **LAST UPDATED: 032314**

TOPIC: Non-Employer Sponsored Premium Cafeteria Plans

Regulatory Authority

A cafeteria plan may allow employees to use "tax free" dollars to pay for an individual accident or health plan. These premium payments are excludable from income under Code §106. In clarifying the point, the 2007 proposed §125 regulations specifically allow for the payment or reimbursement of "employees' substantiated individual health insurance premiums" as a qualified benefit under a cafeteria plan. The preamble to the proposed §125 regulations suggests that other individual accident or health insurance coverage (e.g., LTD or AD&D coverage) that satisfies Code §106 will also qualify under the cafeteria plan rules.

POINTS TO REMEMBER

- Potential compliance issues exist under ERISA, HIPAA and COBRA.
- Notice 2013-54 maintains the fact an individual health insurance policy is considered a qualified benefits plan.

This tax exempt status is limited to an employee's coverage under §106, and per IRS regulations, it does not reach tax free payments for a plan issued by another employer for a spouse. On the individual plan side, a plan covering a husband and wife does not make the distinction between "employee" and "dependent," each having similar rights under an individual plan.

In IRS Rev. Rul. 61-146, the IRS determined amounts employers paid for employee hospital and medical insurance were excludable from employee gross income (under §106). The employees were not covered by the employer's group policy and had individual insurance for which they paid the premium directly to the insurers. The employer paid a part of the premiums upon proof the insurance was in force and paid for by the employees.

The IRS consistently defines an individual health insurance policy as a "qualified benefits plan" under a Section 125 cafeteria plan, thus assigning it the same status as any other qualified benefits plan (such as major medical and dental plans). Notice 2013-54 specifically addresses "group health plans", clearly a Section 125 cafeteria plan is not a group health plan.

In sum, the Notice maintains the fact an individual health insurance policy is considered a qualified benefits plan. Further, an employer may offer a Section 125 cafeteria plan, even when the employer does not sponsor group health insurance. In addition, since this benefit is not a Flexible

Spending Account, the following contribution limits do not apply:

- The $2500 cap on employee salary reduction,
- The $500 limit on employer contributions,
- Employer contribution limits to individual plans (i.e. defined contribution).

Potential Compliance Issues

Compliance issues may arise under ERISA, HIPAA, and COBRA. The preamble to the proposed § 125 regulations specifically note that other laws such as ERISA, HIPAA, and COBRA may impose additional requirements. The key: whether the employer has endorsed the individual health plan, thereby making it subject to ERISA. This determination is based on the facts and circumstances of each case. Preparing adequate plan documents helps reduce this risk to employers.

Further, employment-related laws such as the Family Medical Leave Act (FMLA), Uniformed Services Employment and Reemployment Rights Act (USERRA), and federal anti-discrimination laws such as the Age Discrimination in Employment Act (ADEA) and Americans with Disabilities Act (ADA) may become applicable.

State Small Group Requirements may also be triggered as some states prohibit insurance companies from knowingly accepting premiums from small employers for individual plans.

In the event an individual health plan purchased by the employee is found to be subject to ERISA, the employer will be required as follows:

- file it on their IRS Form 5500s (unless the small plan exception applies);
- respond to Participant requests for documents;
- comply with general fiduciary obligations;
- follow DOL claims procedure and timing requirements;
- provide a plan document and summary plan description;
- provide COBRA; and
- apply HIPAA portability requirements including the prohibition on discrimination (underwritten plans could be an issue).

TASC has a solution backed by the TASC Audit Guarantee

- Use the TASC documents that clearly state the employer does not endorse the individual plan and further that any plan purchased by the employee is not subject to ERISA.
- Have the employee purchase the individual coverage directly from the carrier, the employee pays the premium directly to the carrier, the employee follows the TASC substantiation requirements for claims.

Patient Protection & Affordable Care Act (PPACA) and the Non-Employer Sponsored Premium Plan

Employers providing the Non-Employer Sponsored Premium Plan as an alternative to providing a group health plan may have to pay a penalty in 2014. PPACA requires employers to provide minimum essential coverage to their employees. (A Non-Employer Sponsored Premium Plan or a Health FSA are not considered minimum essential coverage.) Any employer with over 50 employees who fails to provide health coverage for employees must pay the PPACA penalty in 2015; currently this amount is $2,000 per full-time employee. At this time, employers with fewer than 50 employees are excluded.