

October 29, 2013

MA HEALTH CONNECTOR ANNOUNCES THE FATE OF THE MA SECTION 125 PLAN REQUIREMENT AND OTHER SUPPORTING PROVISIONS

The MA Health Connector has announced, in Administrative Bulletin 03-13, important policy decisions regarding four key components of the MA Health Reform law; three of which have been in place since 2007. The Bulletin is dated effective October 28, 2013 and its provisions should be considered effective immediately.

I. REPEAL

According to the Bulletin, the Patrick Administration plans to pursue legislation to repeal the following MA health reform provisions:

- Section 125 Plan requirement (956 CMR 4.00),
- Employer Health Insurance Responsibility Disclosure (Employer HIRD) report
- Free Rider Surcharge, and
- recently created Section 125 Notification requirement

The primary component is the Section 125 Plan requirement, which provides that employers with 11 or more full-time equivalent employees must offer a Section 125 plan as a way for non-benefits eligible employees to purchase non-group health insurance using pre-tax income and with no employer contribution. Under recent federal guidance discussed below, such pre-tax voluntary plans for non-group coverage will not comply with one or more of the ACA market reforms becoming effective in 2014.

The latter three components were all designed to support and enforce the MA Section 125 Plan requirement. Hence, the Health Connector wisely chose to seek repeal of these components as well.

II. NON-ENFORCEMENT BY HEALTH CONNECTOR

During the interim period while repeal is sought in the MA legislature the Health Connector indicates that it:

- will not enforce the Free Rider Surcharge,
- will take no further steps on the development of the Employer HIRD filing application (suspended since February 2013), and
- will not take any further steps regarding the recently created Section 125 notification requirement

III. RECENT FEDERAL GUIDANCE

New federal guidance was issued in September 2013 by the Department of Labor and the Internal Revenue Service via Technical Release 2013-03 and IRS Notice 2013-54, respectively. This guidance deals with the use of Section 125 plans, Health Reimbursement Arrangements, Flexible Spending Accounts and Employer Payment Plans under the Affordable Care Act (ACA). The guidance will not permit any employer contribution toward individual market coverage – whether purchased in a public exchange, private exchange, or direct from a carrier -- unless the employer’s contribution is taxable to the employee.

- Accordingly, this guidance is broad enough to include employee pay all pretax Section 125 plans and prohibits their use to purchase individual market health insurance
- However, Section 125 plans can continue to be offered to employees for the purchase of group health insurance or other benefits

A. “Employer Payment Plans” Include Employee Pay All Pre-Tax Section 125 Plans

The guidance creates a new term known as an “employer payment plan” -- a group health plan under which an employer reimburses an employee for some or all of the premium expenses incurred for an individual market health insurance policy, or an arrangement under which the employer uses its funds to directly pay the premium for an individual market health insurance policy covering the employee.

The reason the MA Section 125 Plan requirement is no longer viable under this guidance is that an employee pay all pretax Section 125 plan is considered an “employer payment plan.” Amounts deducted from employees’ pay under a Section 125 Plan election are treated as *employer* contributions for tax (but not ERISA) purposes. This is so because employee deferrals are made under a salary reduction agreement—the employee agrees to a reduction in salary in a specified amount and the employer agrees to contribute a like amount toward the purchase of qualified benefits (medical insurance, in this instance).

Therefore, any employee contributions made through the employer’s Section 125 plan will be treated as employer funds and the employer’s payment of individual market health insurance premium with those funds essentially creates an employer payment plan.

B. Transition Rule for Non-Calendar Year Plans

The guidance recognizes that some states have already established public Exchanges and employers in those states may have Section 125 Plans that allow employees to enroll in individual market health coverage through the Exchange on a pre-tax basis. (Perhaps the Health Connector was the prime example the regulators were thinking of when they issued the guidance.)

Therefore, the guidance created a special transition rule for fiscal year section 125 plans (but not for calendar year section 125 plans) that began in 2013. The transition rule provides that:

- IF an employer has a Section 125 plan with a fiscal plan year beginning in 2013, and
- IF the Section 125 plan permits the election of individual market coverage through an Exchange on a pre-tax basis,
- THEN the individual market Exchange coverage can continue to be paid under the Section 125 plan on a pre-tax basis beyond January 1, 2014
- BUT only until the 1st day of the section 125 plan's 2014 fiscal plan year.

NOTE: Employees benefiting from this transitional extension of pre-tax treatment through the end of the Section 125 plan's current plan year may not claim a federal advance premium tax credit for any month in which the individual is paying for the individual market coverage purchased through the Exchange on a pre-tax basis under the special transition rule.

There is no special transition rule for calendar year Section 125 plans.

IV. NEXT STEPS FOR EMPLOYERS

Employers should begin reviewing the terms of their written Section 125 plan documents to determine what, if any, amendments should be made to such documentation and the required timing for those changes.

Plan provisions related to the MA Section 125 plan requirement (including any references to the Health Connector and/or the Connector's voluntary plan program) should be removed effective as of January 1, 2014 for calendar year plans, or effective as of the 1st day of the 2014 plan year for non-calendar year plans.

Those employers that created separate Section 125 plan documents for non-benefits eligible employees should take whatever corporate action is necessary to terminate those plans following the timing in the preceding paragraph.

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Please contact me if you have any questions.

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