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May 15, 2015

VIA ELECTRONIC MAIL

CC:PA:LPD:PR (Notice 2015-16)
Courier's Desk
Internal Revenue Service
1111 Constitution Avenue NW
Washington, D.C. 20044

Re: Comments to Notice 2015-16

To Whom It May Concern:

Pursuant to Notice 2015-16, 2015-10 I.R.B. 732 (the "Notice"), American Fidelity Assurance Company ("American Fidelity") respectfully submits the following comments with regard to regulatory guidance implementing the excise tax on high cost employer-sponsored health coverage under Section 4980I of the Internal Revenue Code of 1986, as amended (the "Code"). American Fidelity appreciates the opportunity to comment on the Notice and would welcome the opportunity to meet with the Internal Revenue Service (the "IRS") and the Treasury Department to discuss these comments in greater detail or answer any questions that you may have.

Founded in 1960, American Fidelity is one of the largest private, family-owned insurance companies in the United States. American Fidelity provides supplemental health insurance benefits and financial services to education employees, automobile dealerships and associations, health care providers, and municipal workers across the United States, serving more than 1 million customers in 49 states.

Determination of Aggregate Cost of Applicable Coverage

For taxable years beginning on or after January 1, 2018, Code Section 4980I(a) imposes a 40% excise tax on any "excess benefit" provided to an employee, if (i) an employee is covered under any applicable employer-sponsored coverage ("applicable coverage") of an employer at any time during the taxable year, and (ii) there is any excess benefit with respect to that coverage. For this purposes, Code Section 4980I(b) defines "excess benefit" as the excess of (i) the aggregate cost of the applicable coverage of the employee for the month, over (ii) an amount equal to one-twelfth of the annual limitation for the applicable calendar year (the "statutory dollar limit").

The Notice indicates that the aggregate cost of the applicable coverage of an employee will be calculated based on the particular benefit package in which the employee is actually enrolled, without taking into account any coverage offered to the employee "but in which the employee does not enroll." Notice, Section IV.B. The Notice further proposes to determine the cost of applicable coverage for each particular benefit package by aggregating the experience of all employees covered under that benefit package, subdividing the employees into those who are

enrolled in self-only coverage versus other-than-self-only coverage (*i.e.*, mandatory disaggregation), and permitting further subdivision based on other factors (*i.e.*, permissive disaggregation). Notice, Section IV.C.1. Stated another way, where an employer offers its employees multiple benefit packages under a group health plan – *e.g.*, a PPO, HMO, and indemnity option – the Notice would purport to require the cost of each such benefit package to be calculated independently, based on the population of employees enrolled in that particular benefit package only.

This proposed, siloed approach is based on certain statutory references to “coverage,” which the IRS and the Treasury Department have interpreted to mean the particular benefit package in which the employee is enrolled. Notice, Section IV.B. But as the Notice acknowledges, the statute also refers to coverage “made available” to the employee. This seems to support calculating the cost of coverage for each benefit package based on a broader category of “similarly situated” employees that refers to all enrolled employees to whom the same benefit packages are *offered* (regardless of the particular benefit packages in which those employees choose to enroll for the year). See Code Sections 4980I(b)(1) (defining “excess benefit” by reference to applicable coverage “made available” to employee), 4980I(c)(4)(B) (noting special rules for applicable coverage “made available” through a multiemployer plan) and 4980I(d)(1) (defining applicable coverage for each employee, in relevant part, by reference to “coverage under any group health plan made available to the employee”).

Given the uncertainty as to the proper measurement base, we respectfully request that the determination of the cost of applicable coverage be based on the aggregate experience of employees enrolled in all benefit packages offered by the employer. Adjustments then would be made to account for differences in the actuarial value for each benefit package (*e.g.*, based on the covered benefits and cost-sharing provisions), before disaggregating the coverage into self-only and other-than-self-only groups, and perhaps applying other permissive disaggregation factors. We believe that this recommended approach comports with the statute, is consistent with the methodology that self-funded plan sponsors use to design and price their plans, and will reduce uncertainty and volatility from year to year.

Employers that offer multiple benefit package options typically work with their actuaries to evaluate the overall cost of all the benefit packages they offer, and then determine the cost (and required employee contribution) for each option based on differences in the relative actuarial value between them. As a result, the differences in the actuarial value and costs between benefit packages are based, objectively, on distinctions in the benefits and cost-sharing requirements for each option, rather than enrollment variations that can change from year to year. By contrast, determining the cost of coverage independently for each benefit package, based solely on the experience of those employees who actually enroll in it, could distort the value of the benefit package in certain scenarios due to a lack of sufficient headcount or “credibility,” adverse selection (*i.e.*, a greater number of high-cost claimants choosing a more generous option), or other factors that are tied to the characteristics of the enrolled population. Therefore, even if the underlying benefits did not change at all, fluctuations in the enrollee population, in and of themselves, could cause a great deal of volatility in the cost of coverage from year to year, potentially resulting in some coverage options being subject to the excise tax in one year but not in the following year (and vice versa).

As a result, determining the cost of applicable coverage based on the coverage that is “made available” to each employee would not only be consistent with the statutory language, and comport with the methodology that most self-funded plan sponsors use today, it would also ensure a more reliable and consistent measurement base. By reducing or eliminating the impact

of year-to-year changes in enrollee population trends in calculating the cost of coverage, this approach would increase the predictability and stability of the cost calculation, ultimately leading to less volatility in employee contribution rates from year to year.

Use of Employer Overhead Costs, Taxes and Fees in Determining Cost of Applicable Coverage for Self-Insured Plans

Code Section 4980I(d)(2)(A) provides that the cost of applicable coverage is determined “under rules similar to the rules of section 4980B(f)(4)” regarding the calculation of “applicable premiums” for COBRA continuation coverage. Code Section 4980B(f)(4)(B) permits self-insured plans to use one of two methods to compute a COBRA applicable premium: the actuarial basis method or the past cost method.

The Notice states that the IRS and the Treasury Department anticipate that proposed regulations will describe the costs to be taken into account under the past cost method, including claims, premiums for stop-loss or reinsurance coverage, administrative expenses, and “reasonable overhead expenses (such as salary, rent, supplies and utilities) of the employer, with those reasonable overhead expenses being ratably allocated to the cost of administering the employer’s health plans.” Notice, Section IV.C.2.c.ii. The Notice further requests comments as to whether the IRS and the Treasury Department should adopt a presumption that reasonable overhead expenses will be reflected in a plan’s third-party administrator fee (if applicable), and/or whether a safe harbor should allow self-administered, self-funded plans to use a defined percentage of claims as a proxy for reasonable overhead expenses. *Id.*

American Fidelity opposes the inclusion of any overhead expenses under the past cost method. Employers typically do not consider such expenses in developing the required employee contribution rates for self-funded plans, but rather take into account claims, stop-loss or reinsurance premiums, and perhaps certain plan administrative expenses. Moreover, an employer generally would incur the same expenses for salaries, rent, supplies, utilities, or other overhead costs regardless of whether or not it offered the self-funded plan at issue. Requiring the employer to take into account a ratable amount of those expenses, therefore, would increase the cost of the coverage arbitrarily and artificially, thereby making the coverage more likely to be subject to the excise tax. This could serve as a significant deterrent to employers that otherwise wish to offer (or continue offering) a self-funded plan, as opposed to utilizing a different funding mechanism, or ceasing to offer coverage altogether. Accordingly, we recommend that future guidance exclude from the past cost method any amounts attributable to an employer’s overhead expenses.

In addition, American Fidelity respectfully requests that future guidance clarify that the cost of applicable coverage need not take into account any amounts attributable to transitional reinsurance program contributions under Section 1341 of the Patient Protection and Affordable Care Act (“ACA”), the patient-centered outcomes research fee under Code Section 4376, or any other federal or state taxes or fees imposed upon self-funded group health plans (or plan sponsors). Such guidance would be consistent with the statutory approach relating to costs that are attributable to the excise tax under Code section 4980I. See Code Section 4980I(d)(2)(A); Notice, Section IV.C.2.c.ii.

Determination of Cost of Coverage Under an HRA

The Notice notes that the IRS and the Treasury Department “anticipate that future guidance will provide that an HRA is applicable coverage under [Code Section] 4980I.” Notice, Section

IV.C.3. *See also* Notice, Section III.B. For purposes of determining the cost of coverage under an HRA, the Notice provides that the IRS and Treasury Department are considering making such determination “based on the amounts made newly available to a participant each year” (i.e., current-year HRA contribution amounts). Notice, Section IV.C.3. American Fidelity supports the use of such a methodology, as a matter of administrative convenience, and agrees with the observation in the Notice that this methodology will “provide employers with greater certainty as to the cost of applicable coverage under an HRA from year to year.” *Id.*

If the IRS and the Treasury Department consider alternative methodologies in an effort to make a more accurate determination of the cost of applicable coverage under an HRA, American Fidelity respectfully submits that such cost should be determined based on the amount that the employer actually reimburses the employee from an HRA for the year at issue, regardless of whether such reimbursement is made from amounts initially made available in the current year or carry-over amounts from prior years (other than carry-over amounts initially made available prior to January 1, 2018).

Further, American Fidelity supports the recommendation in the Notice that the IRS and the Treasury Department should consider that the cost of applicable coverage of an HRA be based on only those funds that are expended (or available to be extended) for qualified medical expenses other than the payment of an employee’s contribution towards group health plan coverage to avoid any “double counting” associated with such contribution for excise tax purposes. *Id.*

Determination Period

Section 4980B(f)(4)(c) provides that the determination of any COBRA applicable premium must be made, in advance, for a 12-month period. As a result, the employer must elect the method for calculating the COBRA applicable premium prior to the determination period for which that applicable premium will apply. The Notice provides that for purposes of the excise tax, “it is contemplated that under similar rules the method for calculating the cost of applicable coverage would be elected prior to the determination period for which the cost is determined.” Notice, Section IV.D. Stated another way, the employer would need to elect its cost calculation method (i.e., actuarial basis or past cost) prior to the beginning of the determination period, and at least if the employer elected the past cost method, the amount of any excise tax liability for a given taxable year, under Code Section 4980I, generally would be known as of the *beginning* of the year. The Notice requests comments on whether the COBRA rules should apply for purposes of the excise tax, and the “feasibility of a method for determining the costs of applicable coverage using actual costs” for the year at issue. *Id.*

We recognize that there are benefits in using the same calculation rules for purposes of COBRA applicable premiums and the excise tax, in general, such as allowing employers to account for expected plan-related changes or enrollment trends. However, we respectfully request that the IRS and the Treasury Department ensure that plan-related changes or enrollment shifts that occur mid-year are taken into account properly in determining the cost of coverage, even if the employer generally is required to elect the cost calculation method – and, where the past cost method is used, will generally know its potential excise tax liability for the year – in advance of the determination period.

For example, if an employer were to amend its plan mid-year in an effort to reduce its cost and avoid or mitigate the impact of the excise tax, then such mid-year changes should be taken into account in determining the plan’s cost for that year. This could be accomplished by allowing

employers to determine the cost of coverage using the actual costs that end up being incurred throughout the entire year at issue, perhaps as an alternative methodology. Such an approach would provide greater flexibility to employers in controlling health care costs and reducing their potential excise tax exposure, the savings from which ultimately may be passed through to participating employees.

As the Notice states, the feasibility of an alternative methodology based on actual costs for the year could depend on the required timing for filing a return and paying the excise tax. The Notice notes that these (and other) procedural issues will be addressed in future guidance. Notice, Section IV.D. We recommend that such future guidance provide sufficient time for an employer to collect all the relevant data for the entire year at issue (*i.e.*, after the close of the plan year), including claims incurred during but paid after the end of the year, prior to the due date for filing the excise tax return.

Application of Statutory Dollar Limit to Employees with Both Self-Only and Other-Than-Self-Only Applicable Coverage

American Fidelity supports the approach suggested in the Notice to clarify the application of the statutory dollar limit when an employee simultaneously has both self-only coverage and other-than-self-only coverage under different group health plan or benefit package options. Notice, Section V.B. Specifically, American Fidelity supports as a matter of administrative convenience an approach based on a determination of the employee's primary coverage/major medical coverage using a "majority" of aggregate cost test.

If the IRS and the Treasury Department consider alternative methodologies, in an effort to provide further administrative simplification, American Fidelity respectfully submits that the other-than-self-only dollar limit simply could apply to each employee who is enrolled in one or more other-than-self-only coverage options (regardless of whether he or she is also enrolled simultaneously in one or more self-only coverage options).

Age and Gender Adjustment to Statutory Dollar Limit

As noted above, the excise tax under Code Section 4980I applies where the cost of applicable coverage exceeds the statutory dollar limit. This limit will be revised annually and subject to a number of potential adjustments, including an "age and gender adjustment" as provided by Code Section 4980I(b)(3)(C)(iii). This adjustment is based on a comparison of the premium cost of the Blue Cross/Blue Shield standard benefit option under the Federal Employees Health Benefit Plan using (i) the "age and gender characteristics of all employees of the individual's employer" (referred to in the Notice as the "employer's workforce"), and (ii) the "age and gender characteristics of the national workforce." *Id.* For this purpose, an employee includes "any former employee, surviving spouse, or other primary insured individual." Code Section 4980I(d)(3).

The scope of "employees of the individual's employer" is not entirely clear. The statute does not specify whether or not that phrase might include, for example, enrolled current or former spouses (other than surviving spouses), children, domestic partners, or other dependents enrolled in COBRA continuation coverage ("Other Parties"). In addition, the term "other primary insured individual" in the definition of an "employee" is not specifically defined. We respectfully request that future guidance clarify the definition of "employee" for purposes of the age and gender adjustment, recognizing that although employers typically collect age and gender information for each employee, they may be limited in their ability to access such demographic

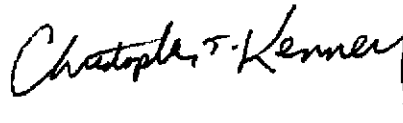
information for Other Parties. In particular, we respectfully request that the IRS and the Treasury Department either clarify that the term "employee" excludes all Other Parties for purposes of the age and gender adjustment or, alternatively, if the age and gender information of certain Other Parties will be considered, provide an appropriate mechanism to account for an employer's potential lack of reliable demographic information for those Other Parties.

The Notice requests comments as to "whether it would be desirable and possible to develop safe harbors that appropriately adjust dollar limit thresholds for employee populations with age and gender characteristics that are different from those of the national workforce." Notice, Section V.C.3. We would support a safe harbor to account for the potential lack of reliable demographic information for Other Parties, provided that such a safe harbor should not be based on a plan's actuarial value. The statute requires this adjustment to apply based on the actual age and gender of the plan's enrollee population, which would not be correlated in any way with the plan's actuarial value. Therefore, any proposed safe harbor that might apply based on a plan's actuarial value would not comport with a plain reading of the statute. Accordingly, we recommend that any safe harbor be limited in application to certain age and gender thresholds (e.g., where a specified percentage of the employee population is a particular gender and/or falls within a particular age range). Plans failing to satisfy such safe harbor thresholds (again, based exclusively on age and gender) would compute any age and gender adjustment based on the general, statutory calculation described above.

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American Fidelity appreciates the opportunity to comment on the Notice, and would welcome the opportunity to meet with the IRS and the Treasury Department to discuss these comments in greater detail or answer any questions that you might have. Please do not hesitate to contact us with any questions or if there is any additional information that you would find useful.

Respectfully submitted,

A handwritten signature in black ink that reads "Christopher T. Kenney". The signature is written in a cursive, flowing style with a long, sweeping tail on the final letter.

Christopher T. Kenney
General Counsel and Corporate Secretary