Notice 2015-16



May 15, 2015

CC:PA:LPD:PR (Notice 2015-16)
Room 5203
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Dear Sir or Madam,

Subject: Internal Revenue Service Notice 2015-16

Aon Hewitt appreciates the opportunity to provide comments to the Internal Revenue Service (IRS) pursuant to IRS Notice 2015-16 regarding the excise tax on high cost employer-sponsored health coverage (the "excise tax") under Section 4980I of the Internal Revenue Code of 1986, as amended (the "Code").

Under Notice 2015-16, the IRS requested comments on the implementation of various aspects of the excise tax that will be addressed in future regulations. Aon Hewitt is providing comments on the specific questions for which comments are being solicited, as well as additional considerations pertaining to employer-sponsored group health plans.

## Who We Are

Aon plc (NYSE: AON) is the leading global provider of risk management, insurance and reinsurance brokerage, and human resource solutions and outsourcing services. We have 66,000 colleagues worldwide. Aon unites to empower results for companies in over 120 countries via innovative and effective risk and people solutions and through industry-leading global resources and technical expertise.

Aon Hewitt, a business unit of Aon, empowers organizations and individuals to secure a better future through innovative talent, retirement and health solutions. We advise, design and execute a wide range of solutions that enable companies to cultivate talent to drive organizational and personal performance and growth, navigate retirement risk while providing new levels of financial security, and redefine health solutions for greater choice, affordability and wellness. Aon Hewitt is the global leader in human resource solutions, with over 30,000 professionals in 90 countries serving more than 20,000 companies worldwide.

**Aon Hewitt** | Consulting | Health and Benefits
4 Overlook Point | Lincolnshire | IL | 60069
t +1.847.442.3247 | f +1847.575.3629 | aon.com

## Comments on Excise Tax

Aon Hewitt commends the IRS for its initiative in reaching out to the employer community to obtain its feedback and input on the development of regulations to implement the excise tax. As of 2014, employer-sponsored group health plans, both fully insured and self-insured, provided health care coverage for 55% of the pre-age 65 population in the United States. Thus, Aon Hewitt believes it is critical that the implementation of the excise tax be accomplished in a manner that encourages employers to continue to offer comprehensive health care coverage to employees, retirees, and their dependents.

With that in mind, Aon Hewitt submits the following comments for your consideration:

## Definition of Applicable Coverage

Section 4980I(d)(1)(A) of the Code defines "applicable employer-sponsored coverage" as coverage under any group health plan made available to the employee by an employer which is excludable from the employee's gross income under Code Section 106, or would be so excludable if it were employer-provided coverage (within the meaning of such Code Section 106). As discussed more fully below, Aon Hewitt supports excluding the value of after-tax Health Savings Account (HSA) contributions, self-insured limited scope dental and vision benefits, and employee assistance programs from the definition of "applicable employer-sponsored coverage." In addition, Aon Hewitt supports the IRS's adoption of the statutory exclusions from the definition of "applicable employer-sponsored coverage" under Code Section 4980I(d)(1)(B).

### HSAs

Aon Hewitt supports excluding employee after-tax HSA contributions from the excise tax calculation. As discussed in Notice 2015-16, such contributions are not excludable from gross income as employer contributions under Code Section 106, but rather are deductible by an employee from gross income under Code Section 223. Since employee after-tax contributions to an HSA are not employer contributions, they should not be included in "applicable employer-sponsored coverage" under Code Section 4980I. Employers who offer qualifying high deductible health plans (HDHP) with an HSA often do so to control the employer's health care costs and encourage employees/participants to take responsibility for their own health and use health care coverage appropriately. The employer will be required to include the employer's contribution to the HDHP as "applicable employer-sponsored coverage" for purposes of the excise tax.

### Limited Scope Dental and Vision Benefits

Similarly, Aon Hewitt supports excluding self-insured limited scope dental and vision coverage that qualifies as an excepted benefit under Treasury Reg. Section 54.9831-1(c)(3) from the excise tax calculation. Regarding dental and vision benefits, Code Section 4980I(d)(1)(B) provides as follows:

> the term applicable employer-sponsored coverage shall not include ... any coverage under a separate policy, certificate or contract of insurance which provides benefits substantially all of which are for treatment of the mouth (including any organ or structure within the mouth) or for treatment of the eye.

From the standpoint of tax policy, we see no reason for excluding fully insured limited scope dental and vision benefits from the calculation of the excise tax, while at the same time including self-insured dental and vision benefits in the calculation of the excise tax. There exists sufficient basis under the statute to exclude limited scope dental and vision benefits, regardless of how they are funded, from the excise tax calculation. We note that for purposes of reporting coverage on IRS Form W-2 under Notice 2012-9, limited dental and vision benefits that qualify as "excepted benefits" are excluded. In promulgating that guidance, the IRS relied on the fact that the statutory language that refers to cost of coverage for purposes of reporting on IRS Form W-2 cross-references the excise tax language. Thus, the IRS has already interpreted this language broadly enough to implement the exclusion consistently in the excise tax calculation.

## Determination of Cost of Applicable Coverage

As outlined in Code Section 4980I, the 40% excise tax is based on the excess, if any, of the aggregate cost of the applicable coverage of an employee for a month over the applicable dollar limit for the month. Code Section 4980I(d)(2) defines cost of coverage for excise tax purposes by reference to COBRA, as follows:

> The cost of applicable employer-sponsored coverage shall be determined under rules similar to the rules of section 4980B(f)(4), except that in determining such cost, any portion of the cost of such coverage which is attributable to the tax imposed under this section shall not be taken into account and the amount of such cost shall be calculated separately for self-only coverage and other coverage. In the case of applicable employer-sponsored coverage which provides coverage to retired employees, the plan may elect to treat a retired employee who has not attained the age of 65 and a retired employee who has attained the age of 65 as similarly situated beneficiaries.

Employers would prefer maximum flexibility when determining the cost of coverage so as not to complicate the administration of group health plans and the annual calculation of the excise tax.

In addition, we note that the Treasury and IRS "anticipate that to the extent guidance under § 4980I provides improved methods for determining the cost of applicable coverage, consistent rules may be issued for purposes of § 6051(a)(14)" (the Form W-2 reporting). Aon Hewitt recommends that Treasury and the IRS adopt, to the maximum extent permissible, consistent rules for both purposes in order to simplify plan administration and reporting.

## Aggregation by Benefit Package

Aon Hewitt supports the concept of aggregating coverage by "benefit package" set forth in Notice 2015-16 and suggests giving employers maximum flexibility in aggregating benefit packages and populations. For example:

- The excise tax regulations should permit employers to aggregate benefit packages for purposes of calculating the cost of applicable coverage if an employer offers the same benefit package to active employees and retired employees.
- The excise tax regulations should permit employers to aggregate benefit packages for purposes of calculating the cost of applicable coverage, regardless of whether the benefit package is offered under a separate group health plan and regardless of whether the benefit package is offered to different populations (actives and retirees). In this regard, Aon Hewitt suggests the excise tax regulation allow employers the maximum flexibility in aggregating populations. For example, an employer should be permitted to aggregate a benefit package offered to actives, pre-65 retirees and post-65 retirees, regardless of whether the benefit package is offered under one or more group health plans and regardless of whether one or more benefit packages coordinate with Medicare. In addition, for purposes of aggregating two or more benefit packages, any difference in value among such benefit packages should be ignored to the extent such difference is less than 2% determined on an actuarial basis.
- Aon Hewitt supports the suggestions in IRS Notice 2015-16 that employees would be grouped only by the benefit packages in which they are enrolled rather than the benefit packages in which they are offered. This approach would be helpful in achieving timely and orderly implementation of the regulations. Many employers offer several benefit packages to employees and retirees and performing the excise tax calculations on the basis of the benefit package in which the employee or retiree is enrolled would ease the administrative burden of compliance.

Notwithstanding the foregoing, Aon Hewitt recommends that employers should be able to aggregate data across multiple benefit packages in order to determine the applicable cost of coverage, as is commonly done in developing COBRA rates. Such flexibility should not be restricted, even in the event of aggregation by benefit packages.

## Permissive Aggregation Within Other-Than-Self-Only Coverage

Aon Hewitt supports permissive aggregation of benefit packages with other-than-self-only coverage for purposes of determining the cost of applicable coverage. The statute only addressed mandatory disaggregation between self-only and other-than-self-only coverage. Permitting employers to aggregate coverage tiers within other-than self-only coverage would give employers more flexibility in administering the excise tax while abiding by the statutory language of Code Section 4980I. For example, an employer that maintains three coverage tiers (employee-only, employee plus one, and family) would be permitted to permissively aggregate the cost of coverage for participants enrolled in the employee plus one coverage tier and the family coverage tier to determine the cost of applicable coverage (even if the actual cost of coverage varied between the employee plus one and family coverage tiers) for purposes of determining whether the applicable dollar limit for other-than-self-only coverage has been exceeded.

## Permissive Disaggregation

Aon Hewitt supports the suggestion for the application of a broad standard when determining whether employee and retiree populations may be disaggregated, for example, bona fide employment criteria, job categories, location, and business units. This would permit easier collection of data at locations and allow employers greater flexibility in administering the excise tax calculations.

## Self-Insured Methods—Actuarial Basis Cost Method

Aon Hewitt supports allowing an actuarial projection of expected costs to be used for the purposes of excise tax calculation for self-funded plans. Since actuarial methods are used to set premium rates for fully insured plans, allowing similar actuarial methods for self-funded plans would ensure the reasonability, flexibility, and appropriateness of the excise tax across funding types and minimize disruption.

Actuarial methods would generally consider and control for several factors:

- Credibility of group experience;
- Impact of large claims and statistical outliers;
- Antiselection between benefit options;
- Data quality and other issues; and
- Demographic changes.

Since an actuarial determination of plan costs requires technical proficiency and industry experience and is a Statement of Actuarial Opinion as defined by the American Academy of Actuaries, Aon Hewitt recommends that any actuary attesting to projected plan costs for the purposes of the excise tax calculation meet the Qualification Standards of the American Academy of Actuaries.

# Health Reimbursement Arrangement (HRA)

## HRA as "Applicable Coverage"

While the nature of an HRA suggests that the best regulatory approach would be to exclude the value of an HRA from the cost of applicable coverage, Aon Hewitt suggests that, at a minimum, the value of an HRA be excluded from the cost of applicable coverage if the sole use to which the HRA can be applied is the funding of the employee contribution. Such an approach would avoid the possibility of double-counting the HRA and the cost of applicable coverage under the plan being funded. In addition, the value of an HRA that funds, either totally or partially, "excepted benefits" should also be excluded from the cost of applicable coverage.

## Determining Cost of Applicable Coverage Under an HRA

Aon Hewitt does not recommend that the cost of applicable coverage under an HRA be determined based on the amounts made newly available to a participant each year. As noted above, calculating the cost of applicable coverage in that fashion for an HRA would overvalue the HRA and would fail to take into account that HRA amounts might never be fully used or forfeited upon death or termination of employment. Aon Hewitt suggests that the cost of applicable coverage be based on an actuarial projection of future HRA costs, as is used in determining the COBRA premium for an HRA.

# Applicable Dollar Limit

Code Section 4980I (b)(3) sets forth two separate dollar limits—one limit for an employee with self-only coverage (for 2018, a baseline of $10,200, as adjusted) and another limit for an employee with other-than-self-only coverage (for 2018, a baseline of $27,500, as adjusted). Aon Hewitt suggests the following with respect to the application of the higher threshold in the case of an individual who is a Qualified Retiree or who participates in a plan sponsored by an employer the majority of whose employees covered by the plan are engaged in a high-risk profession or employed to repair or install electrical or telecommunications lines.

## Adjustments for Qualified Retirees

A Qualified Retiree is an individual who (A) is receiving coverage by reason of being a retiree, (B) has attained age 55, and (C) is not entitled to benefits or eligible for enrollment under the Medicare program under Title XVIII of the Social Security Act. For ease of employer administration, Aon Hewitt suggests that employers be permitted to assume that any retiree who has not attained age 65 is "not entitled to or eligible for enrollment under the Medicare program ..." While Aon Hewitt understands that a retiree could be eligible for Medicare due to disability or end stage renal disease, it would be administratively burdensome and costly to require employers to make such a determination on an annual basis. Even working with the Centers for Medicare and Medicaid Services to make this determination would require a cumbersome process that neither employers nor the federal government are prepared to implement and would only serve as a disincentive to employers to

maintain retiree health coverage. In addition, the higher threshold should apply to coverage for any dependents of a Qualified Retiree, such as a spouse, provided that the Qualified Retiree is enrolled in other-than-self-only coverage, to avoid the anomaly of a Qualified Retiree who covers dependents not being eligible for the higher threshold.

## Adjustments for High Risk Professionals/Individuals Employed to Repair or Install Electrical or Telecommunications Lines

Code Section 4980I(b)(C)(iv) provides for higher thresholds for an individual who participates in a plan sponsored by an employer, the majority of whose employees covered by the plan are engaged in a high-risk profession or employed to repair or install electrical or telecommunications lines. The Treasury and IRS requested comments on the process of determining whether the majority of employees covered by the plan are engaged in a "high-risk" profession, what the term "plan" means in this context, and how an employer determines that an employee was engaged in a high risk profession for at least 20 years (the rule for retirees in this category).

Aon Hewitt requests flexibility in this category. Even if these employees participate in a collectively bargained plan, such a "plan," as defined under ERISA, often contains multiple benefit packages and covers collectively bargained employees in a variety of jobs (e.g., a call center that assists employees in the high risk profession or installation of electrical or telecommunications lines). Even if the term "benefit package" is used in lieu of "plan," it's unlikely that employers would be able to take advantage of these higher thresholds.

Instead, Aon Hewitt suggests that a plan that covers participants who are or were engaged in a high-risk profession or employed to install electrical or telecommunications lines be given the benefit of a higher threshold. Aon Hewitt believes that this higher threshold was enacted so that plans covering these types of employees were not immediately subject to the excise tax. As a practical matter, it will be administratively cumbersome and onerous to identify such employees so as to satisfy the "majority" requirement. Alternatively, if the Treasury and IRS believe such flexibility is not warranted, then the legal definition of "plan" under ERISA should be used and employers should be permitted to restructure the benefits under the plan to create two separate mirror image benefit packages in each ERISA plan.

## Age and Gender Adjustment

Aon Hewitt supports the development of 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. Based on Code Section 4980I(b)(3)(C), the use of age and gender adjustments would increase the dollar thresholds for Qualified Retirees and individuals who participate in a plan sponsored by an employer, the majority of whose employees covered by the plan are engaged in a high-risk profession or employed to repair or install electrical or telecommunication lines. Aon Hewitt recommends that a separate, higher safe harbor adjustment be applied to Qualified Retirees and that a weighted average dollar limit be applied to the whole group (pre- and post-65).

Aon Hewitt supports the development of 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.

Developing population-specific adjustment factors requires significant amounts of exposures that would not normally be available for most employers. Actuaries typically rely on aging assumptions developed from normative data. Examples of normative data that actuaries have used to calculate age and gender adjustments include:

- The table produced by the Bureau of Labor Statistics that counts national workforce participants by age and gender.
- The table of age and gender factors developed for the Society of Actuaries in June 2013, which reflects national data for the commercial market that is held by the Health Care Cost Institute.

Aon Hewitt suggests the Treasury and IRS publish a set of age-banded factors, separate for single coverage and other than single coverage, that can be relied on for developing threshold adjustments and will produce stable results over time and over employers in different circumstances.

For ease of administration, Aon Hewitt recommends that the age and gender adjustment to thresholds be based on all employees of the employer, regardless of how plans are aggregated or disaggregated when calculating the tax. This approach seems most consistent with the language in the statute that refers to "age and gender characteristics of all employees of the individual's employer." Aon Hewitt recommends that the employer's population include all active employees whether enrolled or not, COBRA primary insureds, retired employees and surviving spouses, and any other primary insureds.

Aon Hewitt believes it is appropriate to include retirees in developing the employer's age and gender adjustment to reflect the difference in age-related costs between retirees and the national workforce. This is consistent with the definition of "employee" in the statute and avoids penalizing employers who continue to provide coverage to retirees and thereby reduces the government's exposure to non-Medicare retirees receiving subsidies through the state Exchanges. Aon Hewitt recommends excluding actual dependent demographics for this purpose since employers may not have easy access to this data. The impact of dependents would instead be captured by the "other than single coverage" aging factors published by the Treasury and IRS.

## Double Taxation

Aon Hewitt requests that any proposed or final regulations eliminate the possibility that a self-insured employer could become liable for paying more than the cost of the excise tax. Under Code Section 4980I(c)(2)(C), the third party administrator (TPA), as the party who administers the plan benefits for a self-insured group health plan, could be deemed liable for paying the excise tax. As a business matter, an employer sponsoring a self-insured group health plan could be liable for reimbursing that TPA for the excise tax and for grossing up such payment so that the TPA is made whole after taxes.

This result would be avoided if liability for the payment falls on the self-insured plan sponsor, who would then pay any tax directly to the IRS and avoid liability for grossing up reimbursements to the TPA. Code Section 4980I(c)(2)(C) supports the interpretation that the "administrator" is the "Plan Administrator," which means the employer-sponsor under ERISA.

## Closing

Aon Hewitt applauds the efforts of the IRS to create workable, flexible rules that encourage the design, establishment, and operation of employer-provided group health plans that help employees, retirees, and dependents pay for their health care expenses and reduce the cost and burden of those expenses on individuals, government, employers, and society. Aon Hewitt believes that the above recommendations will facilitate those objectives and help achieve the goal of affordable health care for all Americans.

Thank you for your consideration.

Sincerely,

Hewitt Associates LLC, an Aon Hewitt company

John D. Piro, Jr.
Senior Vice President

Molly B. Iacovoni
Senior Vice President

Paul L. Koch
Vice President