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Notice 2015-16

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STATE OF WASHINGTON  
**HEALTH CARE AUTHORITY**

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May 15, 2015

**TO:** Internal Revenue Service  
Karen Levin  
Office of Associate Chief Counsel (Tax Exempt and Government Entities)

**FROM:** Thuy Hua-Ly, Chief Financial Officer  
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Financial Services Division

**SUBJECT: STATE OF WASHINGTON COMMENTS TO IRS NOTICE 2015-16**

The attached document contains the Washington State Health Care Authority's comments to the proposed rulemaking detailed in IRS Notice 2015-16 (Excise Tax on High Cost Employer-Sponsored Health Coverage).

Attachment:

IRS Notice 2015-16 - Comments FINAL

❖ **Introduction:**

The Washington State Health Care Authority (HCA) is an executive branch agency, reporting to the Governor of the State of Washington (Washington). The HCA is responsible for the provision and administration of health and other insurance benefits for state employees, retirees from local school districts, and various other public employees in Washington. The HCA provides health insurance coverage to about 350,000 members, through both self-insured and fully insured plans. HCA also administers the joint federal-state Medicaid program within Washington State.

Below are Washington's comments to IRS Notice 2015-16.

❖ **Definition of Applicable Coverage - (III.)**

➤ **On-Site Clinics (III.E.)**

**A. Mobile (transitory) On-Site Clinics – (III.E.):**

- **Request:** Washington requests that mobile (transitory) on-site clinic services be excluded for the purposes of the excise tax. Alternatively, Washington requests the Department of the Treasury (Treasury) and the Internal Revenue Service (IRS) clarify reasonable regulatory limits on the frequency of, or services provided by, such on-site clinics.
- **Background:** Every year, Washington agencies contract with mobile on-site providers to provide certain preventative health care services, such as immunization clinics, mammograms, and diabetes screenings, to state employees. These services are only available for limited periods during the year and are provided by the staff of the mobile on-site clinic rather than state staff. Washington also requests that employee 'health fair' activities, focusing on wellness education, disease screening, and preventative care be excluded.

**B. De Minimis Services for Traditional On-Site Clinics:**

- **Request:** Washington requests that the Treasury and IRS clarify what services will be considered de minimis for purposes of the excise tax. Washington also requests including the following services as de minimis:
  - Immunizations
  - Screening tests
  - Biometric services
  - First Aid
  - Wellness and health education.

**C. Higher Education On-Site Clinic Definition:**

- **Request:** Washington requests the Treasury and IRS exempt hospitals or clinics associated with institutions of higher education from the definition of on-site clinic for the purposes of the excise tax. Alternatively, Washington requests the Treasury and IRS establish a special provision in the definition for on-site clinics so that certain employees will not be counted twice if they are employees of higher education institutions and receive free or low-cost health care services from clinics affiliated with their employers.
- **Background:** Many institutions of higher education in Washington State have affiliated hospitals and/or clinics that further the education of health care professionals, such as the University of Washington Medical Center. These hospitals and clinics may also offer the employees of the affiliated higher educational institution with low-cost or free health care services. Additionally, some institutions of higher education are considering establishing and/or expanding existing medical education programs. However, subjecting such hospital and clinic services to the excise tax could dis-incentivize the future creation or expansion of hospitals and clinics associated with higher education institutions.

➤ **Stand-alone dental and vision plans - (III.F.):**

- **Request:** Washington requests that limited scope dental and vision plans be excluded from the cost of coverage, regardless of whether the coverages are fully insured or self-funded.

➤ **HIPAA Incentives for Nondiscriminatory Wellness Programs in Group Health Plans:**

- **Request:** Washington requests the Treasury and IRS exempt wellness incentives from the excise tax. If wellness incentives were to be included, employers would be dis-incentivized from establishing wellness plans. Additionally, including wellness incentives would undercut the federal regulatory framework for wellness plans. Alternatively, if the Treasury and IRS do not exempt wellness incentives from the excise tax, Washington requests the Treasury and IRS set reasonable regulatory standards on the amount or type of wellness incentives employers may offer.
- **Background:** Washington has a HIPAA wellness plan for public employees that rewards subscribers who complete wellness activities or who do not use tobacco products. The reward can be a combination of a \$125 deductible reduction for employees in PPO/HMO products, a \$125 extra employer pre-tax health savings account deposit, and not paying a \$25 surcharge for tobacco use. These appear to be considered “benefits” for purposes of the excise tax.

➤ **Employee Assistance Program (EAP) - (III.G.)**

- **Request:** Washington requests that EAPs be excluded from the excise tax.
- **Background:** The Treasury has issued recent regulations adding EAPs that meet certain criteria to the list of excepted benefits. Washington requests the Treasury and IRS exercise their authority to also exclude EAPs from the definition of applicable coverage.

❖ **Determination of Cost of Applicable Coverage - (IV.)**

➤ **Contributions Under Cafeteria Plans:**

- **Request:** Washington requests employee contributions to flexible spending accounts be carved out from determining the cost of applicable coverage, as the current scheme would penalize employers for cafeteria plan-related contributions made by their employees. Washington also requests that employee contributions to health savings accounts be excluded for similar reasons.
- **Background:** IRS Notice 2015-16 and I.R.C. § 4980I indicate that contributions made by employees to health savings accounts and flexible spending accounts through a cafeteria plan count as employer contributions for purposes of determining the cost of applicable coverage for the excise tax. Washington offers its employees health savings accounts and flexible spending accounts so employees can take a more active role in controlling and determining their own health care costs. However, the more money employees choose to contribute to their health savings accounts and flexible spending accounts, the closer an employer will come to paying the excise tax, which will result in health care costs ballooning. This result would undermine the cost-saving policy bases for offering cafeteria plan benefits, as well as the cost-saving policy bases for the Patient Protection and Affordable Care Act itself.

➤ **Definition of “similarly situated” - (IV.C.1.)**

- **Request:** Washington requests the Treasury and IRS establish a definition for “similarly situated” that excludes group health plan members’ contributions to their flexible spending arrangement and health savings accounts. Alternatively, Washington requests the Treasury and IRS establish a definition for “similarly situated” that permits group health plans to calculate the average contribution to flexible spending arrangements and spread the average over all members in the group health plan.
- **Background:** Either requested option would eliminate the administrative burden of evaluating each group health plan member’s contributions individually.

➤ **Definition of “similarly situated” - Retirees (IV.C.1)**

- **Request:** Washington requests that all retirees who are younger than 65 or older than 65 be considered “similarly situated” if they are in the same group health plan.
- **Background:** The IRS has requested comment on § 4980I(d)(2)(A). Washington provides separate benefit plans to Medicare-eligible and non-Medicare-eligible retirees. The authority to consider these retirees as similarly situated would be useful to Washington, primarily if the Age 65/Medicare-eligible retirees could be treated separately from the under Age 65/Non-Medicare-eligible retirees. Washington also requests clarification on how to disaggregate non-Medicare-eligible retirees from active employees when they are all included in the same health plan and community risk pool but are charged different participant premiums.

➤ **Special Rule for Government Plans:**

- **Request:** Washington requests the Treasury and IRS clarify that I.R.C. § 4980I(d)(1)(E) does not replace but supplements the general definition of “applicable employer-sponsored coverage” for government plans.
- **Background:** I.R.C. § 4980I(d)(1)(E) is currently unclear as to whether it supplements or replaces the general definition of “applicable employer-sponsored coverage” in I.R.C. § 4980I(d)(1)(A)-(D) for government plans. Washington encourages the Treasury and IRS to adopt regulations stating that I.R.C. § 4980I(d)(1)(E) supplements the general definition of “applicable employer-sponsored coverage” for government plans rather than replaces it. Washington is concerned that if I.R.C. § 4980I(d)(1)(E) replaces the general definition of “applicable employer-sponsored coverage,” government group health plans will have to pay the excise tax for some forms of coverage, while private group health plans will not.

➤ **Definition of “employee” - (IV.C.1.)**

- **Request:** Washington requests clarification on who would be included in the definition for “employee.” Specifically, does the term “employee” include an ex-spouse or a child who is no longer eligible under the terms of the group health plan?
- **Background:** I.R.C. § 4980I(d)(3) provides that “the term employee includes any former employee, surviving spouse, or other primary insured individual.” The term “primary insured individual” is not defined elsewhere in statute.

➤ **Calculating Cost of Coverage - (IV.2.C.2.) and (VI.)**

- **Request:** IRS Notice 2015-16 proposes three separate methods for calculating the cost of coverage for the excise tax. Rather than adopting only one method, Washington requests the Treasury and IRS adopt all three methods and permit group

health plans to select a method. Washington also requests the flexibility to change from one method to another, at least for the first five years of the excise tax.

- **Background:** Group health plans are administered in different ways, and having only one means of determining the cost of applicable coverage may benefit some group health plans while unduly burdening others administratively. IRS Notice 2015-16 provides different means for determining the cost of applicable coverage using COBRA regulations. The notice also seeks input on other methods for determining this cost, such as comparing the cost of an employer's group health plan to other health plans. If group health plan administrators are permitted to choose which approach they may use, then administrators will have the ability to select the method most compatible with their group health plan, which will reduce administrative burden and ensure more accurate calculations. While recognizing the IRS's concerns about potential abuse through frequent switching between cost methods, Washington feels that locking group health plans into an inflexible, single method is too restrictive. Washington has occasionally experienced unusual plan situations, where an inability to switch from a past-cost method to an actuarial-basis method would have significantly overstated the ongoing plan cost, because of cost shifts between plan years. The most recent example occurred during Washington's Fiscal Year 2009. At that time, Washington's self-insured employee health cost trend nearly tripled from the previous year because of increased utilization by staff who anticipated reductions in force. The following year, however, the cost trend was nearly flat.

➤ **Taxes and Fees - (IV.A.2.(1.))**

- **Request:** Washington supports the Treasury and IRS language (Section 4980I(d)(2)(A)) that excludes all fees and taxes imposed by the Patient Protection and Affordable Care Act, and also requests that all applicable taxes imposed by state laws be excluded from the cost of coverage as well.
- **Background:** State and local tax regimes differ by locality. Excluding taxes collected by these government entities from the cost calculation would be equitable and more accurately reflect the actual cost of benefits.

➤ **COBRA Good Faith Compliance:**

- **Request:** If the Treasury and IRS mirror COBRA regulations for the process of determining applicable coverage, then Washington also requests the Treasury and IRS adopt the good faith compliance provisions in COBRA to allow for small technical errors in determining the cost of applicable coverage, or in calculating a group health plan's liability for the excise tax.

➤ **Retirees - (IV.A.2.(3.)) and (IV.C. 1., Permissive Disaggregation)**

- **Request:** Washington requests the Treasury and IRS adopt regulations for group health plans that pool retirees age 55-64 with their active employees, or establish a means by which group health plans can show that their costs are not entirely associated with the types of benefits offered. Washington also requests the Treasury and IRS issue more guidance specifically stating that retirees who are pooled with active employees can also have the early retiree threshold apply.
- **Background:** For Washington, group health plan costs vary for reasons beyond how rich the plan's benefits are. For example, under state statute, state and school district retirees, ages 55-64 are pooled with active employees. This pooling leads to higher costs for active employees but is not related to the richness of the benefits. The age and gender adjustment provided by I.R.C. § 4980I(b)(3)(C)(iii) only references active employees of the employer and thus disadvantages health plans that pool retirees age 55-64 with their active employees.

➤ **Aggregation of Tiers (Self-Only Coverage and Other-Than-Self-Only-Coverage) – (IV.C. 1.)**

- **Request:** Washington supports the proposal to allow other-than-self-only coverage tiers (employee plus one, employee plus two) to be aggregated for the purposes of calculating the cost of coverage.
- **Background:** Washington's cost structure does not differentiate the cost of full family coverage based on the number of covered individuals.

❖ **Applicable Dollar Limit – (V.A.)**

➤ **Geographic Adjustments:**

- **Request:** Washington requests the Treasury and IRS establish adjustment methods to account for differences in health care costs based on geographic regions.
- **Background:** Washington provides and administers benefits for employees throughout the State. A large number of employees reside in metropolitan areas, such as Seattle, Spokane, and Vancouver, where health care costs are notably higher than in other parts of the State. Employees in metropolitan areas receive the same types of benefits as employees in less-densely populated areas, but the benefits in metropolitan areas are generally more expensive. As a result, Washington faces a potentially significant burden in managing its exposure to the excise tax; even if Washington reduces all employees' benefits, the higher cost of benefits for employees living in certain geographic areas may still expose Washington State to the excise tax.

➤ **Qualified Retirees: Determination of Medicare Eligibility - (V.C.1.)**

- **Response:** The HCA does not directly determine whether or not plan participants are eligible for Medicare. Rather, the HCA has a Voluntary Data Sharing Agreement (VDSA) with the Center for Medicare Services (CMS). Under the VDSA, the HCA sends quarterly files to CMS of everyone who is enrolled in employee coverage in the HCA's system, with start dates and termination dates if applicable.

➤ **Third Party Administrators and Excise Tax:**

- **Request:** Washington requests guidance on what percentage of the excise tax, if any, is the responsibility of third party administrators.
- **Background:** Washington uses third party administrators to administer certain benefits offered under its cafeteria plan, such as its flexible spending arrangements and health savings accounts. The current statute requires employers to calculate the excise tax. The current guidance, however, does not indicate if third party administrators will have to pay a share of the excise tax for benefits they administer.

➤ **Composite Limits - (V. B.)**

- **Request:** Washington requests the Treasury and IRS allow for both methods of calculating the dollar limit when an employee simultaneously has self-only coverage and other-than-self-only coverage.
- **Background:** IRS Notice 2015-16 proposes two methods for calculating the dollar limit when an employee simultaneously has self-only coverage and other-than-self-only coverage. If group health plan administrators are permitted to choose which approach they may use, then administrators will have the ability to select the method most compatible with their group health plan, which will reduce administrative burden and ensure more accurate calculations.

➤ **Age and Gender Adjustments -(V.C.3)**

- **Request:** Washington requests the Treasury and IRS establish a 'safe harbor' adjustment for age and gender characteristics.
- **Background:** The excise tax on high cost employer-sponsored health coverage is applied to 'excess benefits' provided in health plans. While cost of the coverage is a general indicator of the richness of benefits provided, that cost also reflects factors that are unrelated to the benefits, notably age and gender. Washington makes a concerted effort to recruit and retain a diverse workforce, including legally protected classes, such as workers over age 40. An excise tax penalty that might be incurred based on the age or gender of the workforce, rather than the richness of the benefits, would undermine these efforts. Particularly helpful action would be establishing a relatively simple table providing differential thresholds for "high cost" based on

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average employee (or participant) age and gender. This action would help group health plans avoid additional costs for actuarial consulting service companies that would be needed in the absence of a 'safe harbor' adjustment.