



EMPLOYEE BENEFITS

County of Riverside Human Resources

VEBA Post Employment Health Savings Plan

County of Riverside Human
Resources Services Department
P.O. Box 1569
Riverside, CA 92502
(951) 955-4981

Third-party Administration (TPA)
Service Provider
REHN & Associates
PO Box 5433
Spokane, WA 99205-0433
1-800-832-2101

CC:PA:LPD:PR (Notice 2015-52)
Room 5203
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station, Washington, DC 20044

Re: Notice 2015-52

Dear Sir or Madam:

On behalf of the County of Riverside, California Voluntary Employees' Beneficiary Association Post-Employment Health Savings Plan Trust (County of Riverside VEBA HSP), we offer comments with respect to § 4980I of the Internal Revenue Code (Code), which provides for an excise tax on high cost employer sponsored health coverage (the "Excise Tax"), and the potential regulatory guidance to be issued under § 4980I. The County of Riverside, California Voluntary Employees' Beneficiary Association Post-Employment Health Savings Plan Trust was established in December of 2002 by the County of Riverside in order to administer the County's Health Savings Plan (a post-retirement, funded health reimbursement arrangement). Currently, the County of Riverside Plan provides HRA benefits to more than 1,675 participants and their families and holds more than \$27.8 million in plan assets.

Attached for your more convenient reference is a copy of our prior response to Internal Revenue Service (IRS) Notice 2015-16 ("Prior Comments"). In our Prior Comments, we offered specific comments as requested in Notice 2015-16, but we also requested the IRS and Treasury consider delaying implementation of regulations in light of the significant issues relating to its ultimate effect and implementation, as reflected in many of the comment letters submitted by individual taxpayers, employers, and industry groups. Additionally, we asked that Treasury and the IRS advise Congress regarding these issues for further evaluation of a repeal of or amendments to § 4980I. Finally, we urged Treasury and the IRS not to include HRAs as a form of "applicable coverage" under the Excise Tax for the reasons set forth in our Prior Comments. Many of the comments and much of the factual information incorporated into our Prior Comments are applicable to the analysis of the issues identified in IRS Notice 2015-52. We ask that the Treasury and IRS continue to consider these Prior Comments as they develop implementing regulations.

In addition, to assist the IRS and Treasury in identifying reasonable and flexible methods for determining the cost (or COBRA applicable premium) of funded HRA plans, we offer the attached "Facts about Funded HRAs," which identifies many of the unique features of funded HRA plans that would affect the determination of their cost as applicable coverage for purposes of the Excise Tax.

Finally, we offer our specific comments on several issues addressed in IRS Notice 2015-52 relating to (1) who the “coverage provider” should be in the context of funded HRA plans and other self-insured plans, (2) the allocation of annual or other one-time HRA contributions, and (3) the notice, payment, and coverage provider allocation issues related to the Excise Tax liability. Throughout this Comment Letter, we identify some of the significant challenges presented by provisions of § 4980I that require payment of the tax by various third parties who have no control over the selection and aggregation of multiple types of applicable coverage that are subject to the tax.

For your convenience, the following is a brief summary of the main points and concerns we will address throughout this letter:

- For funded HRAs and other self-insured plans, the regulations should designate the employer as the “coverage provider” or allow plans the flexibility to designate the “coverage provider” in adoption and plan documents for purposes of the Excise Tax.
- Any income tax associated with the reimbursement of the Excise Tax should be excluded from the cost of applicable coverage.
- HRA contribution amounts do not accurately reflect the applicable cost of coverage of an HRA plan benefit.
- The actuarial and/or past-cost determination methods, as applied under §4980B(f)(4), most accurately reflect the applicable cost of coverage for HRA plans.
- HRA funding methods are unique and often consist of large one-time, lump-sum contributions upon termination from service based on *several* years of service, which are intended to provide benefits over a period of numerous years (*i.e.* these are not true *annual* contributions).
- Notice and payment provisions must allow for time and flexibility to accommodate any coordination among vendors, data collection needs, tax calculations, and collection of pass-through expenses.

I. Persons Liable for the Excise Tax.

A. Coverage provider as the “person that administers the plan benefits” for HRAs and certain other types of self-funded coverage.

We appreciate the efforts of the Treasury and the IRS in proposing alternative approaches to the issue of who is ultimately responsible and liable for the payment of the Excise Tax in self-insured arrangements, such as funded HRAs. In the Notice, the Treasury and IRS outline two potential regulatory approaches in dealing with the “coverage provider” issue for self-insured plans. In contrast to these definitional approaches, we propose that regulations designate the employer as the “person who administers the benefits,” or alternatively, regulations should permit the plan to identify the “person who administers the benefits” in the plan or adoption documents

for purposes of the Excise Tax. These two alternatives would result in a more efficient and predictable regulatory and payment scheme for self-funded plans that utilize a third-party administrator or that are governed by an independent board of trustees. Below we provide for your consideration comments on the two approaches proposed in Notice 2015-52 and on the two alternative approaches we propose.

1. First definitional approach: The person responsible for day-to-day functions that constitute administration of plan benefits.

Under the first solution offered in Notice 2015-52, “the person that administers plan benefits” would be defined as the person responsible for day-to-day functions that constitute administration of plan benefits. Although many health plans engage the services of a third party administration service provider (TPA) for assistance with day-to-day functions, these entities very rarely have the control and authority necessary to justify imposing the payment liability for an Excise Tax on excess benefits upon such entities. For example, TPAs do not have control over contribution amounts, level of benefits, coverage of dependents, or benefit exclusions or limitations for the plan it directly administers, much less over plans provided by the employer through other coverage providers for which the TPA does not provide administration services. As a result, TPAs generally will not possess the critical information needed to understand the potential tax liability, which will vary among each employer (and also among different employee groups covered by the same employer), and is dependent upon the proper cost determination of the employer’s other applicable coverage. This lack of information will make it improbable or impossible for the TPA to budget for and allocate monetary resources to its potential tax liability, unless the regulatory process allows for a reimbursement of the Excise Tax from the employer before the date the tax payment becomes due. Even under those circumstances, the process places a significant financial risk on TPAs.

In addition to the substantive reasons against the use of this approach, the impracticality of this approach is highlighted in circumstances where the plan has engaged numerous, un-related entities to provide different aspects of plan administration. For example, for many plans it is not uncommon for one entity to provide claims-adjudication services, while another entity handles inquiries and customer service, and yet a third provides the technology platform for record-keeping and reporting on behalf of the plan. Under the first approach proposed in Notice 2015-52, it would be very difficult to identify which of these entities should be liable for the tax. The alternative to identifying one entity would be to allocate to each service provider a pro-rata share of the plans’ pro-rata share of the Excise Tax. In either case, imposing the tax liability on these parties in these scenarios would increase the layers of complexity, administrative burden, and ultimately the number of parties impacted by the tax. The likelihood of error, non-payment risk, and increased administrative cost and burden is significantly greater under such circumstances with inevitable efforts to pass-through the tax to employers.

2. Second definitional approach: The person who has ultimate authority or responsibility under the plan or arrangement with respect to the administration of plan benefits (including final decisions with respect to administration matters).

Under the second approach proposed in Notice 2015-52, “the person who administers the benefits” would be the person who has ultimate authority or responsibility under the plan or arrangement with respect to the administration of plan benefits (including final decisions with respect to administration matters). In most cases for single-employer plans, this will be the employer. However, for multiple- and multi-employer plans, this will often be an independent board of trustees who jointly serve (often on a volunteer basis and without compensation) as the plan administrator. Boards who jointly serve in the capacity of plan administrator generally have authority (and final decisions) over establishment of rules, policies and procedures relating to operation of the plan, and compliance with applicable law. This authority may also include the ability to engage of one or more third-party service providers to operate the plan or provide services, such as claims payment, compliance, record-keeping, and reporting services. However, like the independent TPAs discussed above, these entities very rarely have the necessary control and authority over plan benefit decisions that would justify imposing the payment liability for an Excise Tax on these parties. Like TPAs, governing boards who service as plan administrators have no influence or control over the factors that directly affect the cost of benefits, such as (i) the frequency or amount of contributions an employer makes to the HRA, (ii) the funding sources for the employer’s HRA contributions, (iii) the choices employers make or negotiate regarding other unrelated benefits (including group insurance plans, HSAs, FSAs, etc.), or (iv) each employee’s spending or use of plan benefits. In addition, in many cases the trust agreement for funded plans, as well as federal regulations under ERISA and § 501(c)(9) (if using a voluntary employees’ beneficiary association (VEBA) trust), would prohibit reversion of plan assets or payment of certain taxes and expenses from plan assets in order to pay the Excise Tax liability. Imposing the Excise Tax liability on these independent boards would place an undue financial burden and risk on parties who have no independent source of revenue and no control over benefit decisions. Even if the ultimate regulations allow for a pass-through of this liability to the employer, any pass-through arrangement would place the risk of error or non-payment on these parties, unless the regulations provided some relief in those circumstances.

3. For self-funded plans, regulations should provide that the “person that administers the plan benefits” is the employer, or alternatively, the person/entity designated as such in plan or adoption documents.

a. This approach most effectively achieves the intended goals of the Excise Tax legislation.

For self-funded plans utilizing a third-party administrator or that are governed by an independent board of trustees, regulations should designate the employer as the “person who administers the benefits,” or, in the alternative, regulations should permit the plan or adoption documents to designate the employer as the “person who administers the benefits” for purposes of the Excise Tax. First, the employer is the party who is in direct control over many of the decisions that drive the cost of individual coverage and most, if not all, decisions that drive the aggregate benefit cost. Second, the employer is the one party among the possible parties liable for the tax

who has the broadest scope of information concerning the types of benefits and the cost of or amount contributed to each benefit, in order to reasonably project and budget for any Excise Tax liability. In addition, requiring the employer to pay the tax is the most direct way to incentivize employers to carefully evaluate benefit costs and options in considering current and future benefit decisions. It is also notable that Notice 2015-52 acknowledges that in most cases, the employer will ultimately bear the cost of the Excise Tax through the pass-through of the tax, plus the employer will bear the additional costs of any income tax pass-through resulting from the coverage provider's reimbursement of the tax from the employer. If regulations were to place the payment responsibility on the employer, either directly or permissively in plan documents, it would eliminate many of the administrative burdens, difficulty in determining the appropriate party responsible for payment, and additional costs and expenses associated with the determination, payment, and reimbursement of the Excise Tax.

b. This approach reduces administrative burdens for all parties, while eliminating potential unnecessary costs that would ultimately be borne by the employer and its employees.

A regulatory and administrative scheme that requires a back-and-forth exchange of information and a pass-through of the tax liabilities among providers, employers, and third-party administrators or trustee boards creates administrative burdens for all parties, a drag on timing of Treasury's receipt of the revenue, and the potential for layers of errors and disputes among all parties involved. Such a tax payment and pass-through structure is administratively challenging at best, but will likely prove to be unworkable for many self-insured plans, such as funded HRA plans that utilize an independent TPA or that are governed by an independent board of trustees. Moreover, the additional expense and administrative complications will force many employers and plan sponsors to abandon the health benefits they have previously provided to these plan participants as the overall cost to provide the benefits rises, not only due to the Excise Tax itself, but also due to the additional expenses associated with paying the Tax. Aside from placing a 40% excise tax upon the cost of applicable coverage that exceeds the annual threshold, the implementation of this tax will undoubtedly create additional costs via the expenses associated with income taxes imposed due to pass-through needs, the cost of consultants and actuaries in determining the cost of applicable coverage, fees from TPAs and other service providers associated with determining the cost, consultant or brokerage fees associated with finding alternative healthcare plans, legal fees for compliance, and many other unintended or unexpected expenses. In the end, it is the employer that will bear the additional expenses associated with making healthcare "available" to employees, effectively reducing the benefits employees receive or even resulting in an increase in the share of the financial burden borne by employees. This was not Congress's intent in enacting the Excise Tax.

c. This approach reduces financial risk for unrelated administrators that have no control over the aggregate cost of employer provided coverage.

Importantly, in Notice 2015-52, the Treasury and IRS point out that, "[i]t is expected that, if a person other than the employer is the coverage provider liable for the excise tax, that person may pass through all or part of the amount of the excise tax to the employer in some instances." This observation demonstrates a recognition that the appropriate party to bear the cost of the Excise

Tax is the employer, as the employer is the one party with the necessary control over most, if not all, of the factors and decisions that affect the aggregate cost of its employer-provided coverages. The Notice goes on to observe, “[c]overage providers generally will not know the amount of any excise tax due with respect to applicable coverage provided for a taxable period (discussed in section V.A above) until after the end of the taxable period. As a result, the Treasury and IRS expect that, as a practical matter, the coverage provider generally will be unable to bill for the excise tax reimbursement or the income tax reimbursement until the excise tax is paid by the coverage provider.” This observation begs the most important question for the independent TPA or board of trustees who might be deemed a “coverage provider” – how to budget and identify resources to pay for the tax if the provider will “[g]enerally not know the amount of any excise tax due with sufficient time to bill [the employer] for the reimbursement.” For third-party administrators or boards of large, multi- or multiple-employer plans, the potential Excise Tax liability could easily exceed millions or even tens of millions of dollars for which these unrelated parties have no independent source of funds to pay. Accordingly, we strongly encourage the Treasury and the IRS to designate the employer as the coverage provider for funded HRAs or allow funded HRAs and other self-insured plans the flexibility to designate the employer as the “coverage provider” in its plan documents. This approach will provide for clarity in streamlining this process, while avoiding additional administrative burdens, financial risk, unintended expenses, and potential for dispute that would otherwise exist.

II. Cost of Applicable Coverage: Exclusion of Income Tax Reimbursement and Allocation of Contributions.

A. Exclusion of Income Tax Reimbursement

Regulations placing the payment responsibility on the employer, either directly or permissively in plan documents, would largely mitigate the Treasury’s and IRS’s concerns regarding additional income taxation and the pass-through of such amounts. However, should the ultimate regulations result in an administrative scheme that creates additional taxable income on the Excise Tax reimbursement, we urge the Treasury and IRS to exclude it from the cost of applicable coverage amounts attributable to the Excise Tax. The Excise Tax itself is expected to cause a reduction of employer provided health benefits for a majority of employers, while negatively impacting high and middle-income employees alike within just a few years of its implementation. We hope the Treasury and IRS will recognize that counting the additional income tax reimbursement amount in the cost of applicable coverage is adding insult to injury and was not an intended consequence contemplated by Congress. The Excise Tax is just one additional, yet significant, component of the Affordable Care Act that will ultimately cost the citizens of the United States by making employer-sponsored healthcare less affordable. As such, we ask that the IRS and Treasury help prevent or remove any additional expenses associated with the implementation and administration of this Excise Tax, wherever possible.

B. Allocation of Contributions.

In Notice 2015-52, the Treasury and IRS indicated their awareness that contributions to HSAs, Archer MSAs, FSAs, and HRAs made annually or less frequently than monthly may need to be allocated on a pro-rata basis over the coverage period. The Notice asked for comments

regarding this issue and any other issues under §4980I. We appreciate and applaud the Treasury and IRS for taking particular note of this issue for account-based plans that may have only annual or less frequent contributions. The Excise Tax implications relating to this issue are of significant concern for many employers and participants of plans that involve less predictable contribution funding methods, and we feel it is important to inform the IRS and Treasury regarding these issues as they contemplate regulations regarding the determination of the cost of applicable coverage for funded HRAs.

First and foremost, we strongly suggest that the determination of the cost of applicable coverage for an HRA be based upon actuarial or past-cost methods contemplated in IRS Notice 2015-16 and currently applied under §4980B(f)(4), even if final regulations allow for a pro-rata allocation of large, one-time contributions to the extent such an allocation method benefits the cost determination. The actuarial and past-cost determination methods take into account factors that best reflect the true usage or cost of the benefits of HRAs for a given coverage period by taking into account actual claims experience, or in the case of the actuarial method, age, claims eligibility or other benefit limitations, demographics, and other valuation factors, to more closely reflect a monthly premium similar to group medical coverage. The contribution amount a participant receives typically does not correlate with the amount of money that individual will necessarily require or use for healthcare expenses in that year, or even over the course of several years. Unlike major medical plans, funded HRA plans are designed to incentivize wise consumerism in order to preserve account balances for future health care needs when employer-provided medical coverage is no longer available. As such, HRA plans should be valued on a claims experience basis rather than on the dollar amount of contributions in order to continue to allow for this advantageous health benefit that helps mitigate healthcare expenses and drives individuals to make more educated healthcare decisions.

To elaborate on this point further, we would like to make the Treasury and IRS aware that many public employers contribute large, lump-sum cash-out contributions at retirement or separation from service, which may be based upon unpaid sick or vacation leave or retirement incentives or years of service. These contributions could, in many cases, exceed the annual thresholds established for the Excise Tax, but are only one-time contributions. In that case, pro-rata allocation over a one-year coverage period would not alleviate or spread-out the tax burden. To base the cost of applicable coverage of an HRA plan on the actual contribution amount (especially for these large, lump-sum cash-out contributions) rather than basing it on claims experience, could unfairly punish an employee whose prior behavior was driven by the promise of that one-time HRA contribution, thereby causing a significant negative impact on his or her financial planning and healthcare coverage needs after separating from service. Such employees would be punished for making the decision to forego paid-time-off or continued employment (in the case of a retirement incentive) in exchange for a contribution to a funded HRA that is intended to bridge the gap of healthcare costs between separation and Medicare eligibility. Put differently, the Excise Tax on termination payments prorated only over the calendar year would penalize and dis-incentivize the good behavior that was negotiated between the employee and employer. In addition, many of these employees have negotiated these termination benefits prior to the enactment of the Affordable Care Act and will now be significantly impacted unless they rush to separate from service prior to 2018. Here again, such result was not among the intended consequences complemented by Congress in enacting the Excise Tax.

Again, we urge the Treasury and IRS to implement one or both of the past-cost or actuarial methods as the basis for determining cost of applicable coverage for funded HRAs, rather than determining the cost of coverage based upon the annual contribution amount. In any event, however, additional allocation alternatives should be included or permitted in regulations to the extent it would benefit the unique cost determination issues presented by plans with varying contribution formulas and methodologies (such as single annual or lump-sum termination contributions). Providing for the flexibility to pro-rate HRA contributions over more than the course of just one year is critical. As one possible solution or alternative, we ask the Treasury and IRS to consider a pro-rata system for lump-sum HRA contributions based on the years of service to the extent years of service is a factor in determining the contribution amount. Alternatively, a pro-rata allocation based upon years between separation and Medicare eligibility might be another viable allocation approach. By affording HRA plans this flexibility, the Treasury and IRS would be allowing for individuals to continue to negotiate for and use HRA plans in a manner that promotes thoughtful decisions and planning with regard to healthcare decisions and positive workforce behavior, such as lower absenteeism. Otherwise, the feasibility and affordability of HRAs, along with the funding mechanisms permitted by the Internal Revenue Code will be severely diminished.

This issue is of particular importance for post-separation or retiree-only plans, for which participants cannot access their HRA funds until after they have separated from service or retired from their position with that employer. Just like integrated HRA accounts that provide in-service benefits, retiree-only plan contributions are a part of the employees' compensation package and are intended to assist with their healthcare needs. However, what is unique about these post-separation or retiree-only plans, is that the contributions tend to be much larger one-time contributions provided as employers are attempting to assist with healthcare expenses that their employees face during retirement. For many employers, these contributions are in lieu of major medical plan coverage that was once provided to retired employees when such a benefit offering was more affordable to employers. Many employees have factored these HRA contributions into their financial planning for retirement and rely upon those funds in making retirement feasible. To impose the Excise Tax on these contributions amounts in the form of a benefit calculation would be to penalize both these employers and their participants in their attempts to be financially responsible and proactive in planning for retiree healthcare needs. Many participants will feel the need to rush into retirement prior to the Excise Tax's implementation or otherwise be required to work longer than anticipated to help compensate for the depletion of available funds by the Excise Tax.

III. Notice and Payment

The notification and payment issues associated with implementing the Excise Tax are particularly problematic in that the employer is the entity (1) driving benefit cost decisions, (2) required to calculate the aggregate cost of coverage and the Excise Tax liability, and (3) responsible for allocation and reporting of each coverage provider's share of the Excise Tax. Meanwhile, the "coverage provider" is the entity that (1) possesses the individual cost of coverage information needed by the employer to calculate the aggregate cost of coverage and the allocation percentages, (2) must rely on the employer and other coverage providers to deliver the requisite

information before the tax payment can be submitted, and (3) bears the financial risks associated with the determination, payment and, reimbursement processes. For a self-funded plan administered by an independent TPA or board of trustees, the required flow of information among the various providers, along with the pass-through of tax reimbursements will likely need to precede the actual due date for payment of the tax, thus affecting the determination period and timing of required notifications and payments of the tax.

For self-funded plans, such as a funded HRA, § 4980I provides that the cost of applicable coverage is to be determined using rules “similar to the rules of Section 4980B(f)(4)” regarding the determination of the COBRA premium. For self-funded plans that are administered by independent TPAs or boards of trustees, it will likely be the plan administrator or other service providers who will have the information needed, and be in the best position to calculate the cost of coverage for each of the employer’s coverage groups. Regulations should provide for procedures and dates by which employers can obtain from third-party service providers any usage, demographics, account balances, and other information needed to determine the cost of coverage. In the alternative, the regulations should provide for enough time so that the third-party administrators may determine the cost of coverage for each employee group and report back to the employers. The determination period must take into account the timing needed to allow for this information to be reported to the employer in addition to a reasonable amount of time for the employer to (1) assimilate the information from all coverage providers, (2) calculate the individual, aggregate, and excess benefit amounts, (3) determine the allocations, and (4) report this information to the coverage providers and the IRS.

Absent regulations that would allow for or require an employer to pay the entire Excise Tax liability directly, regulations should incorporate timeframes allowing for coverage providers to invoice the tax reimbursement (and reimbursement of the income tax compounded on top of the tax reimbursement) prior to the due date for the Excise Tax payment. As explained above, independent TPAs and boards of trustees for multi- or multiple-employer plans will not possess the critical information needed to project their potential tax liability, which will certainly vary among each employer (and also among different employee groups covered by the same employer). Therefore, it is improbable or impossible for TPAs and plan administrators (including governing boards) to accurately budget for and allocate monetary resources toward the potential tax liability, unless the regulatory process allows a reimbursement from the employer to occur prior to the date the tax payment becomes due. Even under those circumstances, this process places significant financial risk on independent plan administrators who have no control over the decisions affecting the aggregate benefit costs of individual employers, as they will have to incorporate some sort of right to review or audit of the Excise Tax and allocation calculations, and they will ultimately bear the risk of non-payment of the tax reimbursement from employers.

Toward that end, regulations should allow for an employer to submit its reimbursement of the Excise tax liability to each coverage provider at the time it is required to report the coverage provider’s allocable share of the Excise Tax. This reporting and simultaneous reimbursement of the tax liability to the coverage provider can serve as separate invoicing of the reimbursement amount as contemplated by Notice 2015-52, but will eliminate the concern of independent TPAs and boards of trustees regarding how they should budget for and identify monetary resources to pay a tax for which the liability will be unknown until they receive the Excise Tax allocation

notification from the employer. The Excise Tax reimbursement will be delivered by the employer prior to its payment due date from the coverage provider. Then, the income tax reimbursement, relating to the taxable income on the Excise Tax reimbursement (if applicable), could be billed separately and paid at the time such income tax becomes due in the calendar year following its receipt of the income.

It is our hope that the IRS and Treasury will recognize that the reporting and payment provisions of § 4980I are unworkable. These additional layers of administrative complexity and the burden of additional costs to be borne by employers and coverage providers in calculating the cost of applicable coverage and paying additional taxes on the reimbursements passed-through to the employer were not intended by Congress or well-thought-out in the statutory language. In our view, Congress granted the Secretary of Treasury broad discretionary authority to implement regulations calculated to achieve the *intended goals* of the Excise Tax, while minimizing the administrative complexity, burden, and cost to all parties impacted by its implementation. More specifically, we urge the IRS and Treasury the use this broad authority and discretion to deem the employer as the “coverage provider,” or alternatively, allow the employer the right to pay the tax directly. This approach will be the most effective solution to minimize the adverse impact to service providers, employers, and employees, and is more tailored to achieve Congress’ intended goals with respect to the Excise Tax.

Signature Page to Follow

Respectfully submitted,

Stacey M. Beale

STACEY M. BEALE
Human Resources Division Manager
The County of Riverside VEBA HSP

**Signature Page to County of Riverside, California
Comments re: Notice 2015-52**



COUNTY OF
Riverside
HUMAN RESOURCES

County Administrative Center

4080 Lemon Street, P.O. Box 1569 • Riverside, CA 92502 • (951) 955-3500
44-199 Monroe Street, • Indio, CA 92201 • (760) 863-2670

MICHAEL T. STOCK
ASST. COUNTY EXECUTIVE OFFICER
HUMAN RESOURCES DIRECTOR

May 14, 2015

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

Re: Notice 2015-16

Dear Sir or Madam:

On behalf of the County of Riverside, California Voluntary Employees' Beneficiary Association Post-Employment Health Savings Plan Trust (County of Riverside VEBA HSP), we offer comments with respect to § 4980I of the Internal Revenue Code (Code), which provides for an excise tax on high cost employer sponsored health coverage (the "Excise Tax"), and the potential regulatory guidance to be issued under § 4980I. The County of Riverside, California Voluntary Employees' Beneficiary Association Post-Employment Health Savings Plan Trust was established in December of 2002 by the County of Riverside in order to administer the County's Health Savings Plan (a post-retirement, funded health reimbursement arrangement). Currently, the County of Riverside Plan provides HRA benefits to more than 1,675 participants and their families and holds more than \$27.8 million in plan assets.

Initially, we advocate a repeal of the Excise Tax and replacement of the tax with alternative legislation that would further similar goals with a more efficient, less burdensome effect. We acknowledge that the IRS and Treasury have no authority to repeal the Excise Tax, but request that they advise Congress to do so in light of the significant issues relating to its ultimate effect and implementation, as reflected in many of the comment letters submitted by individual taxpayers, employers, and industry groups. We also request that Treasury and the IRS consider delaying implementation of regulations, and advise Congress regarding these issues for further evaluation of amendments to §4980I or alternative legislation. Alternatively, we urge Treasury and the IRS not to include health reimbursement arrangements (HRAs) as a form of "applicable coverage" under the Excise Tax for the reasons set forth below. Finally, we offer our specific comments on several issues addressed in Internal Revenue Service (IRS) Notice 2015-16 (the "Notice") relating to the potential approaches for determining the cost of coverage for HRA plans for purposes of determining the Excise Tax.

I. The Excise Tax should be repealed and replaced with alternative legislation that is more tailored to accomplish the intended goals of reducing healthcare spending and increasing federal revenue.

When originally conceived and advocated, the Excise Tax was hailed as a tax on insurance companies that would affect only insurers and wealthy executives, and its most frequently stated goals were to raise federal revenue and reduce or eliminate excessive healthcare spending. However, in its final form and through its proposed implementation, the tax will impact a much broader group, including many middle class workers. In addition, the tax will reduce or eliminate many employer-sponsored benefits, including many forms of employer-sponsored benefits that do not produce the same excessive healthcare spending and inefficiency that the envisioned “Cadillac” insurance plan generates. In order to accomplish the two primary goals more effectively, what is really needed is a repeal of the ill-advised Excise Tax and replacement with more sensible, cost-effective legislation. Several alternatives that were originally considered should be revisited and implemented in lieu of the Excise Tax. These alternatives include a number of possible ways to cap the personal income tax exemption for employer-sponsored insurance (based upon the value or cost of the insurance, employee income, or some combination of the two) or converting the exemption to an individual income tax deduction or even an income tax credit. Absent that, we urge the IRS and Treasury to use their authority under § 4980I(g) to implement an overall regulatory scheme that is more narrowly tailored to accomplish the stated goals for the Excise Tax, while streamlining the administrative burdens that will almost certainly (without significant overhaul) increase healthcare costs, reduce the level of benefits provided for the middle class and wealthy alike, and generally reduce the availability of the types of account-based benefits that do incentivize a healthier lifestyle and cost-conscious decision-making regarding healthcare.

II. Health reimbursement arrangements (HRAs) should be excluded as a form of “applicable coverage” for purposes of the Excise Tax.

As discussed below, HRAs should be excluded as “applicable coverage” under the Excise Tax for a variety of reasons. The design, unique features, and wide-ranging usage of HRAs present significant challenges in selecting and applying any method of cost determination contemplated under the proposed regulatory scheme. Moreover, the payment provisions of the Excise Tax should be more flexible and should permit or require employers to pay the tax for coverage that is administered by an unrelated third party who has no mechanism for passing liability through to employers or covered individuals. Finally, to include account-based plans, such as HRAs, as applicable coverage under the tax would run counter to one of the primary goals of the tax (restraining healthcare costs), ultimately leading to a significant reversal in the recent growth of consumer-driven healthcare decisions.

A. HRAs are not among the forms of healthcare coverage that led to the inefficiency and overutilization in America’s healthcare system that Congress intended to address with the Excise Tax.

An HRA is not insurance. In contrast, it is a form of account-based, defined-contribution coverage that is limited to a finite account balance. As such, HRAs do not pool risk of all covered individuals to provide specified benefit coverages that could potentially far exceed the dollar-amount contributed, as is the case with the potential benefit coverages available under defined-benefit insurance plans as compared to premiums paid or contributed. Rather, HRAs provide reimbursement (up to the account limit) for actual out-of-pocket costs incurred by the

covered individual due to deductibles, co-pays, co-insurance amounts, or expenses not covered by other medical plans. Accordingly, HRAs incentivize consumerism and efficiency in order to preserve account balances for future healthcare needs. This results in covered individuals taking more ownership in their use of healthcare resources, selection of providers, comparison of relative value and cost, evaluation of the necessity of medical care treatments, and careful budgeting of healthcare expenses.

HRAs may be either funded or unfunded by an employer. Unfunded HRAs consist of a promise by the employer to reimburse medical expenses incurred during the plan year up to a certain amount. Funded HRAs typically consist of an employer contribution made into the HRA account, where the contribution amount is made available either immediately or upon the satisfaction of certain conditions (vesting requirements and/or retirement, for example). The employee may then use his or her funded HRA account to reimburse current or future medical expenses for the employee or the employee's spouse and dependents (available benefits are permitted to carry over from year to year). In addition, funded HRAs typically include an investment component allowing employee-participants to direct the investments of their HRA accounts. Because funded HRAs are a *defined contribution* plan with carry-over and investment features, many HRA participants use funded HRAs to "save for a rainy day" when future health care needs present more of a financial burden. Thus, all HRAs, but particularly funded HRAs combined with an investment component, incentivize individual ownership, which drives improved healthcare planning and consumerism. In contrast, monthly or annual premiums paid to insurance companies are forgone money, unless the insured utilizes the benefits provided under the insurance plan. Accordingly, the incentive under a *defined benefit* insurance plan is to use the benefits or lose the value of premiums-paid. These defined benefit plans often fail to incentivize the careful planning and consideration experienced with defined contribution plans like HRAs.

The intention behind the Excise Tax (also known as the "Cadillac Tax") is to reduce inefficiency and overutilization in the healthcare system caused by overly-generous group insurance plans. These types of plans shield or hide costs and incentivize providers to recommend (and insureds to use) more services, which ultimately drives up the overall cost for medical care. In contrast, the nature and design of an HRA generates more careful management of available resources and encourages the saving of account balances for long-term healthcare needs. One of the government's stated goals in imposing the Excise Tax (in addition to increasing federal revenue) is to prompt employers to offer more cost-effective plans, with some shift of risk to employees along with mechanisms to help employees spend healthcare dollars wisely. HRAs are the very type of plan that are helping accomplish this goal, they are not the type of plan that Congress intended to cover, and they should be preserved by an exclusion in the definition of "applicable coverage" under the Excise Tax. Including HRAs in the definition of "applicable coverage" would be contrary to Congress' intent in promulgating the Excise Tax.

B. Funded HRAs have unique features and complexities that were not contemplated by the current language of § 4980I or the currently contemplated regulations.

Contributions to funded HRAs are most often held within single-employer or multi- or multiple-employer irrevocable trusts. These trusts frequently impose prohibitions on reversion of assets to the contributing employer and inurement to the employer or other third parties. In addition, these funded HRA plans and trusts are most frequently administered by independent third-party administrators or an independent board of trustees who jointly serve as the plan administrator. This adds a layer of complexity and special considerations in the administration

and payment of the Excise Tax that are not properly contemplated under § 4980I or the currently anticipated regulatory scheme, as discussed in more detail under Parts III and IV below.

C. The wide- range of HRA design types, features, and usage choices present significant challenges and the likelihood of inconsistency in the determination of cost or valuation of HRAs for purposes of the Excise Tax.

The potential benefit and claims-eligibility design features of HRAs can vary widely on an employer-by-employer and employee-by-employee basis. For example, an employer may offer an integrated HRA plan (with in-service claims eligibility) for employees who are enrolled in a qualified group health plan and a retiree-only (or post-separation claims-eligibility) HRA for those who are not. Vesting requirements may also affect timing for claims-eligibility. In addition, some plans reduce, or offer employees an election to reduce, benefit coverage under their HRA plan for several reasons, including eligibility for HSA contributions, Medicare coordination, or eligibility for the premium tax credit. Finally, the use of (or spending under) HRAs varies widely based upon the unique family and healthcare needs, as well as the long-term savings desires of each employee. These factors make determination of the cost or value of an HRA unique to each individual, or at least each different type or class of employees, and present significant challenges to employers and plan administrators in the calculation of the HRA's overall benefit valuation (cost).

D. An Excise Tax on HRAs will deplete account balances accumulated from HRA contributions, which are often negotiated in lieu of salary increases or other benefits or compensation as a means of providing long-term savings for post-retirement, pre-Medicare healthcare needs.

The tax-advantaged structure of HRAs that are funded in tax-exempt trusts, such as Section 115 trusts for governmental employers or VEBAs, are often designed to allow HRA participants to self-direct the investment of their account balance. This feature encourages employees to save unused amounts by investing those dollars on a tax-exempt basis and making available to the participant increased amounts of healthcare dollars during his or her retirement years. Many employee groups have previously negotiated for these HRA benefits in lieu of salary increases as a means of saving to help bridge the gap between retirement and Medicare eligibility. However, because § 4980I does not include a specific exemption for HRAs, or more specifically retiree-only HRAs, many of these funded HRA balances (which were negotiated many years ago in exchange for forgone salary increases or other benefits) will deplete if the Excise Tax must be withheld and paid by the plan administrator from plan assets. The result would work to counter one of the stated goals of the Excise Tax (encouraging more efficient and considered planning for health care expenditures) and would thereby reduce the primary effect of the Excise Tax to nothing more than generation of federal revenue.

III. In lieu of an exemption for HRAs from the Excise Tax, the regulatory implementation of the Excise Tax should be more narrowly tailored to reduce the administrative complexities presented by the overbroad language of § 4980I

All of the factors described above present unique and significant challenges in the valuation of HRA plans, as well as in the administration and payment of the Excise Tax. If Treasury and the IRS decline to use their authority under § 4980I(g) to exempt HRAs as applicable coverage for purposes of the Excise Tax, then we urge the IRS and Treasury to implement an overall regulatory scheme that is narrowly tailored to accomplish the stated goals

of the Excise Tax and streamlines the administrative burdens associated with compliance with § 4980I and its regulatory framework. Regulations relating to the determination of an HRA's value (cost) should afford employers and plan administrators the needed flexibility to choose the method that best fits their circumstances from a plan design, benefits usage, and administrative cost standpoint, all of which is further discussed in Part IV below.

IV. Specific comments and recommendations relating to determination of cost issues raised in Notice 2015-16.

A. Because plan design, claims-eligibility, and use of benefits vary significantly from employer to employer and employee to employee, employers or plan administrators should be afforded flexibility in determining cost of coverage for an HRA.

Limiting the cost-of-applicable-coverage determination to only one method could penalize some covered individuals while benefiting others unfairly. The Notice points out that providing only one method to determine cost of applicable coverage would minimize administrative complexity. However, the administrative complexity involved in determining the cost of coverage for an HRA will be borne by the employer (or in some cases the plan administrator as discussed further in Part V). Accordingly, Treasury and the IRS should afford those entities the choice of selecting one or more methods of determining cost (even if more complex or burdensome) if the entity determines such method or methods best take into account the factors affecting the cost of their coverage.

Various methods of determining cost for HRA coverage may make more or less sense depending on (i) the factors that affect valuation (such as claims-eligibility and scope of benefits), (ii) the administration and cost to make the cost determination, and (iii) the impact the valuation will have on the excess benefit calculation. For example, many retiree-only HRAs are funded with a lump-sum contribution upon separation from service. This one-time contribution can include one or more sources, including accrued sick and vacation pay, early-retirement incentive payments, or other mandatory contributions negotiated between employers and employee groups. In these cases, using a method based upon amounts newly made available for determining cost would unfairly disadvantage employees who receive a one-time, lump-sum contribution upon termination as compared to employees who receive monthly or annual contributions to their retiree-only HRAs prior to separation from service. In addition, for a retiree-only plan that is utilized to pay premiums, some participants (whether purchasing from the private market or the exchange) may choose much higher insurance coverage than others after separation from service, thereby using their HRA balances more quickly than others and driving up the cost determination for the overall HRA plan. Perhaps for these types of plans the determination of cost should be based upon the actual premium reimbursement amount for each participant. Alternatively, for HRA plans with very limited design options and elections, and consistent contribution methodology and history, benefit levels and usage may be very consistent. In these cases, the past-cost method would not only be the most accurate cost determination, but would also result in a fairly inexpensive method of determining cost. Finally, many employers have found with other types of self-insured coverage that the actuarial method is not always the most accurate predictor, and it is likely the most expensive method for determining cost. However, in cases where complexities in benefit usage, claims-eligibility, and contribution history will affect the cost determination, the actuarial method may be the best method to take all of these factors into account.

B. HRAs that are not yet claims-eligible should be excluded as applicable coverage or grouped separately for purposes of the cost determination.

The entity making the cost determination should be afforded the ability to exclude coverage under an HRA for which the participant is not yet claims-eligible. Many retiree-only HRAs and HRAs that are subject to vesting or other eligibility requirements or limitations should be excluded as applicable coverage under the Excise Tax prior to the account's claims eligibility. In many cases, funded retiree-only HRAs are not intended to be supplementary to the in-service group insurance coverage provided by the employer. Instead, these HRAs are often designed as a means of accumulating funds to bridge the gap for employees between retirement and Medicare-eligibility when they are no longer receiving employer-sponsored insurance coverage and must purchase coverage in the private market or from the exchange. Aggregating this coverage for purposes of the Excise Tax *prior to* the time the participant can utilize the benefits will significantly disadvantage these participants by either depleting accruing balances or driving employers to reduce contributions prior to retirement in order to avoid liability under the Excise Tax.

If HRA coverage for participants who are not yet claims-eligible status cannot be excluded as applicable coverage, then at the very least, those participants who are not yet claims-eligible should be treated as a separate group for purposes of making the cost determination. First, usage and benefit amounts available to claims-eligible participants will unfairly increase the cost determination for HRA participants who cannot utilize their benefits due to separation, vesting, or other eligibility requirements. In addition, HRA participants who are not yet claims-eligible may choose a higher-cost medical plan, with greater benefits or a lower deductible, than participants who are claims eligible and are able to use their HRA benefits to supplement their group insurance coverage. In this scenario, the cost of HRA coverage for the non-claims eligible participants will be artificially high (based upon usage of the claims-eligible participants) and will be combined with the higher premium associated with the greater benefits selected under the medical plan. As a result, the aggregate benefit for non-claims-eligible participants will be skewed higher than the claims eligible participants who have elected reduced benefits under the medical plan. This result can be reduced or eliminated if the non-claims-eligible participants can be treated as a separate group.

C. Any cost determination adjustments to be incorporated based upon geography should apply to all applicable coverage, including account-based coverage such as HRAs, HSAs, FSAs.

Many commentators have recommended that a cost adjustment based upon geography should be added, similar to the adjustments for gender, retiree-status, and high-risk professions. The increased premium cost based upon ZIP code that exists for insured plans is driven by higher costs for medical care in those areas due to a combination of factors including cost of living, limited access, less competition, etc. These same factors also drive up usage (or reimbursement amounts) under account-based plans, such as HRAs, which in turn will correlate to a higher cost determination. For this reason, any geographical adjustment incorporated into the Excise Tax regulations should be applied to account-based coverage as well as insurance coverage.

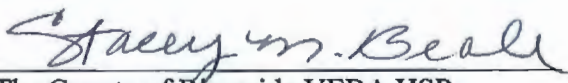
D. Governmental employees who are in high-risk professions, such as fire, public safety, and first-responders, should be treated as a separate group even if enrolled in the same coverage of other governmental employees.

The regulations applying the adjustment for high-risk professions should allow for fire and public safety officers enrolled in governmental plans to be treated as a separate group or to receive the adjustment regardless of whether the majority of all employees covered by the plan are in high-risk professions. Many fire, public safety, and first-responder employees are employed and participate in plans sponsored by a state or local government entity that provides benefits for all of its employees as a single group. In these cases, the majority of governmental employees covered by the plan will not be in a high-risk profession, thereby depriving the high-risk professional of the benefit of the higher-dollar-limit adjustment. Regulations should apply the higher dollar-limit adjustment for these employees without requiring the governmental employer to go to the expense of creating a separate plan.

E. The determination of cost for HRA plans should disregard contributions and balances accumulated prior to the 2018 effective date for the Excise Tax.

As mentioned above, one of the primary purposes for the Excise Tax is to reduce excessive insurance benefits and encourage consumer driven decision-making by penalizing insurers and employers who provide lavish health care benefits commencing in 2018. However, many HRAs (which were implemented to encourage healthcare savings and consumer driven decision-making) have funded balances that have accumulated from contributions made prior to 2018 and even prior to the enactment of the Excise Tax. These prior balances and their historical usage should be excluded from the cost determination for amounts accumulated prior to 2018. Instead, the determination of cost for HRAs should be based upon factors such as contributions amounts, accumulated balances, and prior and anticipated usage *beginning in 2018*, the effective date of the Excise Tax. To include balances accumulated prior to 2018 for purposes of making the cost determination for HRAs would not only present an additional layer of complexity to the already difficult actuarial and cost-determination process, but it would also work to contradict Congress's intent in enacting the Excise Tax.

Respectfully submitted,


The County of Riverside VEBA HSP

Facts About Funded HRAs

This is a list of some unique characteristics regarding funded health reimbursement arrangements (HRAs) that may assist in your contemplation of Excise Tax regulations.

Governance Features

- Often governed by independent boards of trustees who jointly serve as plan administrator with authority over plan terms, policies, procedures, and compliance
- Employers retain control over eligibility, contribution levels and methods, and scope of benefits for each employee and employee group (often collectively bargained)
- Costs and fees associated with the plan are sometimes borne by the participants, and not guaranteed or reimbursed by the employer or other third party

Funding Features

- Funding decisions and control generally retained by each employer
- Plan funding options include:
 - Available employer benefit dollars
 - Unused vacation leave cash-out
 - Unused personal leave cash-out
 - Unused sick leave cash-out
- Employees often forego other forms of compensation in exchange for an HRA contribution via collective bargaining or employer benefit policy changes, such as:
 - Exchange salary or bonuses (on a group mandated basis)
 - Exchange termination payments such as sick or vacation leave cash outs (on a group mandated basis)
 - Exchange continued employment for retirement incentive contribution
- Often funded with large one-time contributions relating to multiple years of service and intended to cover *several* years of benefits (as opposed to HSA and FSA employer contributions which are generally designed to fund benefits for the one current plan year)

General Design Features

- Designed akin to savings accounts as a defined-contribution plan with carry-over and investment features
- Typically held within single-employer, multi-employer, or multiple-employer irrevocable trusts that impose prohibitions on reversion of assets to the contributing employer(s)
- Frequently paired with a high deductible health plan (often a non- HSA qualified HDHP) in an effort by employers to make healthcare costs more manageable and offset increasing deductibles and co-insurance

Retiree-only HRA Design Features

- Claims eligibility is subject to separation from service for reimbursement of medical care expenses and premiums incurred after separation
- Claims eligibility is often subject to vesting requirements, which can result in forfeiture if not satisfied
- Used primarily to bridge the retiree cost gap between separation and Medicare eligibility
- Can be funded with contributions during employment and/or upon or after separation from service