



October 1, 2015

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

Re: IRS Notice 2015-52, Excise Tax on High Cost Employer-Sponsored Health Coverage

Dear Sir or Madam:

The Los Angeles County Employees Retirement Association ("LACERA") submits these comments in response to IRS Notice 2015-52 (the "Notice") which describes potential approaches to implementing the Excise Tax on High Cost Employer-Sponsored Health Coverage (the "Excise Tax") under Internal Revenue Code section 4980I ("Section 4980I"). The Excise Tax is a 40% tax that applies to any "excess benefit," meaning the excess of the aggregate cost of an employee's applicable coverage over the applicable dollar limit. Section 4980I requires each "coverage provider" to pay the excise tax on its applicable share of the excess benefit. LACERA understands the challenges posed by Section 4980I, and appreciates the diligent and collaborative rulemaking process in which the Treasury Department and Internal Revenue Service ("IRS") are engaged, particularly in the context of identifying the "coverage provider" responsible for the Excise Tax. LACERA is concerned that the Excise Tax may have unintended consequences for retirees and for public pension systems that facilitate retiree health benefits—benefits that, although modest, often cost more because of their older population. LACERA offers these comments to highlight the unique and limited administrative role that many public pension systems play in facilitating health benefits for fixed income pensioners, and to urge the Treasury Department and IRS to avoid harming pensioners by any inadvertent application of the Excise Tax to public pension systems.

1. Background

LACERA is one of the largest public pension systems in the United States, with over 150,000 members and over \$48 billion in assets. An independent governmental entity, separate and distinct from its plan sponsors, LACERA is responsible for managing and administering pension benefits for employees of Los Angeles County ("County") and certain other participating employers. Secondly, under written agreements with the County, it facilitates¹ retiree health benefit coverage, primarily

¹ In this letter, in order to avoid confusion, we use the word "facilitate," rather than "administer," to refer to the limited administrative functions performed by LACERA which we believe are materially different from the more substantive administrative functions encompassed by Section 4980I's reference to "the person that administers the plan benefits."

through fully-insured group health insurance plans. These benefits consist of indemnity plans, HMO plans, a Medicare Supplement Plan, Medicare Advantage Prescription Drug HMO plans, and dental and vision plans, all of which are fully-insured and offered through large health insurance issuers.²

LACERA's role with respect to these benefits is limited.

Although LACERA is commonly referred to as the plan administrator for the retiree health benefits being provided, it does not perform the functions that would typically be performed by a third party administrator. Most significantly, LACERA has no role in claims processing or adjudication, and is not responsible for coordination of benefits, subrogation, pre-certification, medical necessity determinations or other similar matters that are generally handled with claim processing. LACERA also does not provide a technology platform with a member's individual benefit or claim information. Rather, LACERA's administrative functions are more akin to those that would typically be performed by the benefits unit within a large Human Resources Department that handles general program management for an insured group health plan but does not administer any individual member's specific benefits and claims once coverage is established. For example, LACERA collects premiums from retirees by deducting their monthly pension checks, and it collects premium subsidies from the County.³ It then forwards these amounts to the health plans. 91% of premium payments are subsidized by the County, with the remaining 9% paid for by retirees. LACERA also enrolls retirees into the health plans, determines eligibility for enrollment, determines whether any waiting periods have been met, determines the County's share of the premium based on the retiree's years of service, and provides a call center to respond to participant questions on purely administrative issues rather than coverage or claim handling or processing.

2. Liability for the Excise Tax

Section 4980I provides that the health insurance issuer will be liable for the Excise Tax in all cases where coverage is provided by insured group health plans. In fact, the Excise Tax appears to have been intended to be primarily a tax on insurers.⁴

² A limited number of LACERA members participate in the Los Angeles County Fire Fighters Local 1014 Health and Welfare Plan, which offers its own self-administered medical plan and insured dental and life plan to retirees of the Los Angeles County Fire Department. Premiums are subsidized by the County. LACERA's limited role with regard to this plan is collecting premiums from retirees by deducting their pension checks, and determining eligibility for the County subsidy and collecting the subsidies from the County for covered retirees, and then forwarding these amounts to the plan administrator. LACERA has no independent authority or financial liability for this plan.

³ Because LACERA is responsible for paying monthly pension checks to retirees, it is in the best position to deduct health premiums from those checks.

⁴ See Senate Finance Committee, *America's Healthy Future Act of 2009, Report to Accompany S. 1796 on Providing Affordable, Quality Health Care for all Americans and Reducing the Growth in Health Care Spending, and for Other Purposes Together with Additional and Minority Views*, S. REP. NO. 111-89,

This makes sense because the health insurance issuer underwrites the risk and is ultimately liable for the cost of coverage.⁵ As such, it is in the best position to control the cost of coverage, and the benefit payment stream upon which the tax is ultimately determined. In short, where coverage is provided through insured group health plans, there is no need to look beyond the health insurance issuer for liability with respect to the Excise Tax. Accordingly, the coverage providers responsible for any related Excise Tax will be the large health insurance issuers with whom LACERA contracts.⁶

Only in the absence of a health insurance issuer does it become necessary to look elsewhere for the Excise Tax. In the case of an HSA or Archer MSA (neither of which is part of the retiree health care program facilitated by LACERA), Section 4980I provides that the employer is responsible for the Excise Tax. This is because under these plans, the employer stands in place of the insurer as the party liable for the cost of coverage. Reports issued by the Senate Finance Committee and the Joint Committee on Taxation confirm this, noting that “if an employer contributes to an HSA or an Archer MSA, the employer is responsible for payment of the excise tax, as the insurer” (emphasis added).⁷ By standing in the shoes of the insurer, the employer assumes liability for the cost of coverage, and is in the best position to control that cost.

Where coverage is not provided under an insured group health plan, or by way of an HSA or Archer MSA, Section 4980I provides that the coverage provider is “the person that administers the plan benefits.” The Treasury Department and IRS are considering two approaches for determining the identity of the person that administers the plan benefits. Before commenting on these two approaches, we emphasize that determining the identity of the person that administers the plan benefits is only necessary when the coverage is not provided under an insured group health plan, or by way of an HSA or Archer MSA. In LACERA’s case, where all coverage is insured, Section 4980I makes explicit that the health insurance issuers are responsible for any

October 19, 2009, at 325 [Senate Finance Committee Report]; Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions of the “Reconciliation Act of 2010,” as amended, in combination with the “Patient Protection and Affordable Care Act”* (JCX-18-10), March 21, 2010, at 62 [Joint Committee on Taxation Technical Explanation]; Joint Committee on Taxation, *General Explanation of Tax Legislation Enacted in the 111th Congress* (JCS-2-11), March 2011, at 305 [Joint Committee on Taxation General Explanation].

⁵ In using the phrase “cost of coverage,” LACERA is referring to the bundle of costs associated with providing coverage that include more than premium costs. Consistent with IRS Notice 2015-16, LACERA recognizes that the cost of coverage includes administrative expenses and overhead expenses, in addition to the cost of claims.

⁶ As noted above, the Los Angeles County Fire Fighters Local 1014 Health and Welfare Plan provides its own self-administered medical coverage and insured dental and life coverage.

⁷ Senate Finance Committee Report, *supra* at 325; Joint Committee on Taxation Technical Explanation, *supra* at 62; Joint Committee on Taxation General Explanation, *supra* at 305.

Excise Tax, not LACERA. Notwithstanding this, LACERA is concerned that regulations defining the person that administers the plan benefits may inadvertently overreach and apply to entities that perform only minimal administrative functions, such as LACERA. To that end, in that LACERA does not “administer the plan benefits” in the sense referred to in Section 4980I, LACERA offers the following comments:

- Bearing in mind that the Excise Tax was intended to be a tax on insurers, the person that administers the plan benefits should be the entity that functions most like the health insurance issuer in terms of controlling the cost of coverage. Hence, the person that administers the plan benefits should be the entity performing those functions that most directly impact the cost of coverage, and would otherwise be handled by the health insurance issuer if the coverage were insured. Any other result would be illogical because it would separate the Excise Tax from the benefit payment stream upon which it is ultimately determined, and as a result, the entity liable for the Excise Tax would not actually control the cost of coverage.
- Under either approach, the person considered to be administering the plan benefits should be an entity with an independent source of funds with which to pay the Excise Tax and one that is also liable for funding the benefits (e.g., a health insurance issuer or, in the case of a self-insured plan, the employer). The person considered to be administering the plan benefits should not be an entity, like LACERA, that is merely a conduit of funds, and has no fund source from which to pay the Excise Tax. The purpose of Section 4980I can best be achieved if the Excise Tax is levied against a party that is financially invested in the cost of coverage.⁸
- LACERA encourages use of the second approach proposed by the Treasury Department and IRS which would define the person that administers the plan benefits as the entity that has ultimate authority or responsibility with respect to the administration of plan benefits. Of particular importance, this should be the entity with authority or responsibility at the level at which benefits are provided, such as authority over arrangements with health care providers. This entity is in the best position to impact the cost of coverage because it selects health care providers and networks, and determines the amounts they will be paid for health care services. This function is qualitatively different from negotiating premium rates with an insurer. Employers and plan sponsors frequently negotiate premium rates, as do systems like LACERA on behalf of employers like the County, but they generally (as with LACERA) lack control over (and even information about) health care provider arrangements, and therefore are not meaningfully positioned to influence the cost of coverage in the way the insurer can by determining the amounts paid for claims as well as administrative and overhead expenses. Likewise, the person that administers the plan

⁸ In LACERA's case, the purpose of Section 4980I could be frustrated if LACERA were deemed the coverage provider because it does not have a source of funds upon which to draw to pay the Excise Tax, and it would be unlawful to use pension assets for this purpose.

benefits should have ultimate authority over claims adjudication insofar as claims adjudication also directly impacts the cost of coverage. Hence, responsibility for health care provider contracts and claims adjudication should take precedence over responsibility for functions that are not at the provider level, such as premium collection and enrollment activities.

- LACERA recommends against defining the person that administers the plan benefits as the person responsible for performing day-to-day administrative functions. In many instances, it will be difficult to identify a single entity as being responsible for day-to-day administrative functions. In the case of LACERA, as with many large plans, several entities play administrative roles. For example, LACERA collects premiums, enrolls retirees in the health plans, determines eligibility, and provides call center services, but it does not perform other more substantive functions, such as claims processing. The role played by entities such as LACERA is necessary to facilitating the provision of insurance benefits (particularly since LACERA pays the monthly pension checks from which premiums are deducted), but it is not the type of activity, nor does it demonstrate the type of control over the cost of coverage, that should trigger liability for the tax.
- Alternatively, if the person that administers the plan benefits is defined as the person responsible for performing the day-to-day administrative functions, then the functions should be specifically and narrowly defined to require the administrative functions that are at the level at which benefits are provided, have the most direct impact on the cost of coverage, and would otherwise be handled by the health insurance issuer if the coverage were insured. For example, it should require responsibility for coverage and provider network design, claims adjudication, coordination of benefits, subrogation, pre-certification, medical necessity determinations, utilization review, and handling referrals and second opinions.⁹ It should not include administrative functions that would typically be performed by a sponsor of an insured group health plan, such as premium collection, enrollment processing and preliminary eligibility determinations.
- Lastly, in determining the person that administers the plan benefits, consideration should be given to the uncertainty as to whether it would be constitutional to impose the Excise Tax on public pension systems insofar as the federal government is generally precluded from directly taxing the States and their instrumentalities. LACERA asks that the Treasury Department and IRS avoid any application of the Excise Tax that could be deemed unconstitutional.

⁹ To the extent these functions include providing a “technology platform,” as referenced in Notice 2015-52, that term should be defined. Specifically, it should refer to a *benefits* technology platform that includes such things as participants’ claims and benefit information. It should not be confused with a technology platform that is more akin to a human resources platform that collects general enrollment information (e.g., addresses, names of dependents, etc.), but does provide a platform once coverage is established or otherwise provide a mechanism for handling claims.

3. Age and Gender Adjustment of the Dollar Limit

LACERA supports adjustments that would provide for an increase in the dollar limits based on age and gender characteristics and thereby decrease the impact of the Excise Tax. As you know, retiree health plans have specific actuarial features based on the older-than-average age of their participants that cause costs to go up, even when benefit levels are comparable to plans that include active employees. Health insurance issuers with whom LACERA contracts indicate that retiree health care costs are as much as 50% to 100% higher than costs for active employees. LACERA supports, and believes it would be appropriate, to make adjustments even greater than those mentioned in the Notice. LACERA looks forward to further guidance on this issue.

4. Excise Tax Reimbursement

The Notice recognizes that the coverage provider liable for the Excise Tax may pass through that amount to the employer, and that reimbursement of the Excise Tax may create additional tax events. LACERA is concerned that the Excise Tax could be passed off by way of increased premiums, to the detriment to retirees. LACERA is also concerned that insurers may increase premiums to pass through income tax incurred as a result of any Excise Tax reimbursement. LACERA is further concerned that an insurer's increased administrative costs of compliance associated with the Excise Tax and reimbursement of the Excise Tax will result in additional premium increases. To the extent these costs are passed off through premium increases, it will negatively impact LACERA's retiree members. Increased premiums also mean an increase in the cost of coverage, and, in turn, the Excise Tax. LACERA believes it is important that Excise Tax reimbursements, related income tax reimbursements, and administrative costs of compliance be excluded from the cost of coverage so that they do not artificially increase the Excise Tax. LACERA looks forward to more guidance on this issue, specifically as to how the amounts would need to be billed.

LACERA appreciates the opportunity to comment on these important issues, and urges the Treasury Department and IRS to take into account the unique needs of retirees, and the pension systems that facilitate their health care benefits, during this rulemaking process. Ensuring that health care remains affordable for fixed income pensioners requires thoughtful consideration of these issues. If you have any questions or comments, please call Cassandra Smith, Director, Retiree Health Care, at (626) 564-3621, or csmith@lacera.com.

Sincerely,



Gregg Rademacher
Chief Executive Officer

GR/SR/dd

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