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VIA E-MAIL (Notice.comments@irsounsel.treas.gov)

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

Re: Comments on IRS Notice 2015-52

Dear Sir or Madam:

This firm represents a client that sponsors a health reimbursement arrangement (“HRA”) that is integrated with its group health plan and allows participants to carry forward their unused notional account balances year-to-year (even after a termination of employment). On behalf of our client, we would like to comment on Notice 2015-52 (the “Notice”) regarding the forthcoming regulatory guidance on the excise tax that will apply to high cost employer-sponsored health coverage under Section 4980I of the Internal Revenue Code of 1986, as amended (the “Code”), commonly known as the “Cadillac Tax.” Specifically, we would like to address (1) the manner in which “person that administers the plan benefits” should be interpreted; (2) the way in which “taxable period” should be interpreted; and (3) how unused amounts retained in a notional HRA account should be considered when determining the Cadillac Tax.

I. Executive Summary

As mentioned in our comments that were submitted with regard to Notice 2015-16 and again in Section III below, HRAs are clearly different from health FSAs and HSAs. Neither health FSAs nor HSAs accomplish some of the most important goals of the Affordable Care Act (the “ACA”)—decreasing moral hazard and incentivizing employees to utilize funds wisely and participate in wellness programs—all of which help contain rising health care costs and promote healthier and longer lives.

Unlike HRAs, health FSAs actually encourage employees to spend health care dollars in a potentially unwise manner since the funds must generally be utilized by the end of the plan year. In addition, the different rules that apply to HSAs allow them to be utilized as tax-free investment vehicles



for retirement rather than the reimbursement of eligible medical care expenses. For these reasons, we urge Treasury and the IRS to exempt all HRA contributions from the Cadillac Tax calculation because HRAs actually help minimize rising health care costs and promote employee enrollment in wellness programs. The inclusion of HRA contributions in the Cadillac Tax calculation will force our client, and other employers, to either eliminate their HRAs entirely or severely restrict them to a point that their benefits become nominal and the cost of administration outweighs the intended benefit.

If all HRA contributions are not exempted from the calculation of the Cadillac Tax, we urge Treasury and the IRS to consider exempting HRAs sponsored by not-for-profit entities since those employers do not receive any tax incentive to contribute to HRAs and there is no loss of revenue to Treasury.

If HRA contributions are not exempted, we strongly urge Treasury and the IRS to clarify that the “person that administers the plan benefits” is the ERISA plan administrator and not the third party administrator.

In addition, if HRA contributions are not exempted, we strongly urge Treasury and the IRS to interpret the “taxable period” as a plan year and exempt from the calculation of the Cadillac Tax unused amounts in participants’ notional HRAs that have been saved by such participants and rolled over each plan year due to their wise health care decisions.

II. Definition of Applicable Coverage

While Code Section 4980I generally applies to all employer-sponsored coverage that is excludable from taxation by an employee under Code Section 106, it also specifically addresses health FSAs, Archer MSAs, and HSAs and provides that they constitute applicable coverage. The statute does not, however, explicitly indicate that HRAs are to be considered applicable coverage and included when calculating the Cadillac Tax. As such, it is unclear whether Congress’ intent was to specifically exclude HRAs from the Cadillac Tax. It seems probable that HRAs should be excluded because including them in the Cadillac Tax calculation (1) increases moral hazard; (2) defeats the purpose of consumer-directed health care; and (3) disincentivizes employee participation in wellness programs. Unlike health FSAs and HSAs, a properly designed HRA achieves the essential goals of health care reform.

III. HRAs Are Dissimilar from Health FSAs and HSAs

Health FSAs and HSAs do not accomplish all of the foregoing goals of health care reform (*i.e.*, decreasing moral hazard, achieving the purposes of consumer-directed health care, and incentivizing participation in wellness programs) because they are distinctly different forms of health savings accounts.

A. Health FSAs

Due to the “use-it-or-lose-it” rule, which generally requires unspent funds at the end of the plan year to be forfeited, health FSAs do not encourage participants to accumulate funds in their account and spend their money wisely. However, employees still receive the immediate tax benefit of decreasing their taxable compensation and paying for medical expenses on a pre-tax basis. In contrast to HRAs,

health FSAs are not subject to the Medicare Secondary Payer (“MSP”) rules. This means that health FSAs do not have to comply with the complex MSP rules, while HRAs must comply.

B. HSAs

HSAs provide greater benefits than just the ability to reimburse medical expenses. The rules and regulations applicable to HSAs allow individuals to not only accumulate funds for the payment of medical expenses in later years, but they also allow individuals to (1) invest the funds; (2) utilize them as emergency savings accounts; and (3) convert them into retirement plans.

With HSAs, an individual can pay for his or her out-of-pocket medical expenses with current income, save his or her receipts, and withdraw the funds as reimbursements years later. As such, an HSA can easily be utilized as an emergency savings account. HSAs are also “tax advantaged” because the funds that were originally contributed on a pre-tax basis will accumulate on a tax-free basis and any investment growth will be distributed tax-free if utilized for medical expenses. This means that HSA contributions will accumulate and individuals will pay no taxes on medical expenses and only income taxes (no penalty) on non-qualified withdrawals after age 65. In addition, individuals can avoid income taxes on traditional Individual Retirement Account (“IRA”) assets by directly transferring them to an HSA. As long as the money is utilized for qualified medical expenses, the individual will avoid ever having to pay taxes on that IRA money. Thus, an HSA is different from an HRA because it can be utilized as an additional tax-free savings vehicle for retirement.

Furthermore, unlike HRAs, medical expenses that are reimbursed from HSAs are not adjudicated by a plan sponsor. This means that an ineligible HSA reimbursement is only discovered if, and when, an individual is audited and the examiner discovers that ineligible expenses were reimbursed. Also, an individual is permitted to withdraw funds from an HSA so long as the tax penalties are paid. However, an HRA notional account may only be used for eligible medical expenses and may not, as an HSA may, distribute cash without proof of purchase of eligible medical products and service expenses. Finally, like health FSAs, HSAs do not have to comply with the complex MSP rules.

For the enumerated reasons listed in this Section III, we urge Treasury and the IRS to clarify in future guidance that HRAs are excluded from applicable coverage and the calculation of the Cadillac Tax.

IV. Person That Administers the Plan Benefits

Code Section 4980I(c)(1) provides that each “coverage provider” is liable for, and must pay, its applicable share of the Cadillac Tax. However, the identity of the coverage provider depends on the type of coverage that is being provided to employees. While Code Section 4980I(c)(2) specifically addresses insured group health plans and HSAs and Archer MSAs, it provides that for all other applicable coverage, the coverage provider that must pay the applicable Cadillac Tax is the “person that administers the plan benefits.”

Code Section 4980I does not define the term “person that administers the plan benefits.” Instead, Code Section 4980I(f)(6) provides that the term shall include the plan sponsor if the plan sponsor administers benefits under the plan, which indicates that the plan sponsor of a self-insured arrangement may be, but is not always, the “person that administers benefits under the plan.” Section

4980I(f)(7) provides that the term “plan sponsor” has the meaning given such term in Section 3(16)(B) of the Employee Retirement Income Security Act of 1974 (“ERISA”).

As mentioned in the Notice, such term is not used anywhere else in the Code, ERISA, the ACA, or in the Public Health Service Act; therefore, Treasury and the IRS have requested comments on two alternative approaches that are currently being considered. The first approach would make an employer’s third party administrator the person responsible. However, such an entity has no authority or control over the plan benefits that an employer offers to its employees. Most employers offer multiple types of employer-sponsored benefit plans, such as medical, health flexible spending accounts, HRAs, and HSAs, etc., and some employers may offer dental, vision, and other “excepted benefits.” A third party administrator typically would have no idea if an ERISA plan sponsor set up such plans, and even if it did, it has no way of requiring the employer to reimburse it for any excise taxes imposed on it other than through contract / litigation.

As plan sponsor, with the authority to revise / modify its employer-provided benefit plans, the plan sponsor should be responsible for the Cadillac Tax, if any—not the third party administrator. Third party administrators and pharmacy benefit managers (“PBMs”) merely manage and administer the benefits provided under employer-sponsored benefit plans and have no ability to change the design, which affects cost. The Cadillac Tax should be imposed on the entity responsible for plan design.

We urge the Treasury and the IRS to clarify that the “person that administers the plan” is the ERISA plan administrator—the person that has the ultimate authority or responsibility under the plan with respect to the sponsorship, design, and administration of the plan, including final decisions on all matters, regardless of that person’s day-to-day functions—and not the TPA.

We request that Treasury and the IRS provide guidance on this issue and clarify that the ERISA plan administrator is the “person that administers the plan benefits” and not the third party administrator.

V. Taxable Period

Code Section 4980I(f)(8) generally provides that the “taxable period” is the “calendar year or shorter period” as the Secretary of the Treasury may prescribe. Since many plan sponsors elect non-calendar plan years for their group health plans, it would be preferable if such plan sponsors could determine the Cadillac Tax, if any, based upon the twelve-month fiscal plan year (*e.g.*, February 1 – January 31, etc.). This would allow them to plan accordingly and not have to calculate the Cadillac Tax using two different calendar years’ (not plan years’) data and cost valuations.

A plan sponsor with a non-calendar year plan should be permitted to utilize the Code Section 4980I(b)(3) annual limitations with respect to the applicable taxable period, which would include all twelve months of coverage for the plan’s plan year. For example, if a plan sponsor has a twelve-month plan year that begins on February 1, 2019, then it would apply the 2018 dollar thresholds for measuring the value of coverage and determining any Cadillac Tax liability for the entire taxable period, which would end January 31, 2020. Alternatively, the Cadillac Tax liability for non-calendar year plan sponsors could be allocated to each applicable month, so that the dollar limits could switch mid-plan year.

We strongly suggest that the IRS and Treasury adopt such a rule to assist plan sponsors, with non-calendar year plans, in reducing administrative burden and in planning for compliance with the Cadillac Tax. For example, the IRS and Treasury should allow plan sponsors that have non-calendar year plans to use any twelve-month taxable period in order to calculate the Cadillac Tax.

VI. Certain Amounts Should Be Excluded When Valuing Coverage

The contemplated approach in Notice 2015-52 for valuing the cost of applicable coverage may be helpful and useful to many plan sponsors because the cost of coverage for purposes of Code Section 4980I with respect to their group health plan or medical savings account would be equal to the annual contributions that were made. However, this approach does not assist plan sponsors of HRAs that have outstanding notional accounts (in many cases, from years ago) that were carried forward year after year by plan participants who elected to wisely spend their health care funds.

HRAs by their very nature are neither fixed nor certain—except as to the time and place that the HRA participant elects to utilize the funds for eligible medical expenses. To impose the Cadillac Tax on HRA accounts set up by employers would impose the Cadillac Tax on a notional HRA account balance that, as mentioned, is neither fixed nor certain. If the Cadillac Tax were to apply to employer contributions to the HRA, which may not be utilized for years, then employers would be forced to severely limit the use of HRAs as important consumer and wellness-directed health care tools that minimize moral hazard. Accordingly, in order to preserve HRA notional account balances, it is important to exempt HRAs from the Cadillac Tax calculation.

We strongly recommend that the IRS and Treasury exclude unused amounts in HRA participants' notional accounts when valuing coverage for the Cadillac Tax. These types of HRAs were designed to encourage participants to save and make informed decisions as to how to utilize the funds for medical care. Since these types of HRAs encourage less than 100% utilization each year (*i.e.*, by allowing participants to utilize the funds in future years), even after a termination of employment, carry over amounts should be excluded from the calculation of the Cadillac Tax.

VII. Conclusion

As discussed above, Health FSAs and HSAs are clearly different from HRAs because they do not accomplish some of the most important goals of the ACA—decreasing moral hazard and incentivizing employees to utilize funds wisely and participate in wellness programs—all of which help contain rising health care costs and promote healthier and longer lives.

Unlike HRAs, health FSAs actually encourage employees to spend health care dollars in an unwise manner since the funds must generally be utilized by the end of the plan year. In addition, the rules that apply to HSAs allow them to be utilized as tax-free investment vehicles for retirement rather than for the reimbursement of eligible medical care expenses. Finally, an HRA is notional in nature and does not become fixed and certain for tax purposes until a participant elects to utilize such account to purchase eligible medical products and services. For these reasons, we urge Treasury and the IRS to exempt all HRA contributions from the Cadillac Tax calculation because HRAs minimize rising health care costs and promote employee enrollment in wellness programs. The inclusion of HRA contributions in the Cadillac Tax calculation will force our client, and other employers, to either eliminate their HRAs

entirely or severely restrict them to a point that their benefits become nominal and the cost of administration outweighs the intended benefit.

If Treasury and the IRS include HRA contributions in the calculation of the Cadillac Tax, we urge them to consider exempting HRAs sponsored by not-for-profit entities since those employers do not receive any tax incentive to contribute to HRAs and there is no loss of revenue to Treasury.

In addition, we request that Treasury and the IRS provide guidance clarifying that the "person that administers the plan benefits" is the ERISA plan administrator and not the third party administrator.

Finally, if HRA contributions are not exempted, we strongly urge Treasury and the IRS to interpret the "taxable period" as a plan year and exempt from the calculation of the Cadillac Tax unused amounts in participants' notional HRAs that have been saved by such participants and rolled over each plan year-to-plan due to their wise health care decisions.

We appreciate this opportunity to comment regarding the excise tax on high cost employer-sponsored health coverage under Section 4980I of the Code in connection with the Notice. If you have any questions, or if we can be of any assistance in your consideration of the issues summarized above, please do not hesitate to contact me at (904) 598-6106 or lcarrasco@srglaw.com.

Sincerely,



Lisa Rhein Carrasco