The Internal Revenue Service (IRS) issued final regulations under the Patient Protection and Affordable Care Act (Affordable Care Act) on the federal premium tax credit for individuals who purchase health insurance through an Exchange beginning in 2014. The regulations, which were issued on May 18, 2012, impact individuals who enroll in a qualified health plan (QHP) through an Exchange and claim the premium tax credit, employers that sponsor group health plans, and Exchanges that will make QHPs available.

This Aon Hewitt bulletin discusses:

- An overview of the federal premium tax credit;
- Eligibility for the premium tax credit;
- How employer-sponsored coverage relates to the premium tax credit; and
- How the premium tax credit is calculated.

Overview of the Federal Premium Tax Credit

One of the federal subsidies available to individuals who enroll in a QHP under an Exchange is a health insurance premium tax credit. (Another federal subsidy takes the form of a cost-sharing reduction to help with deductibles and copayments.) The premium tax credit is designed to financially aid individuals who purchase health insurance in an Exchange, provided their household income does not exceed four times the federal poverty level (FPL) and they are not eligible for minimum essential coverage (MEC). In determining eligibility for the premium tax credit, an individual is eligible for MEC under an employer group health plan only if the plan is both affordable and provides a minimum actuarial value.

The regulations provide that the premium tax credit can be claimed by eligible individuals who enroll in a QHP through an Exchange. The premium tax credit is refundable and payable in advance directly to the insurance carrier.

In the preamble to the final regulations, the IRS states that the tax credit will be available to an individual who enrolls in a QHP offered by an Exchange, regardless of whether the individual purchases the QHP on a state Exchange, regional Exchange, subsidiary Exchange, or the federal Exchange that is established in states that have not created an Exchange by 2014. Commentators had suggested that the credit would only be available if an individual enrolled in a state Exchange, thus raising the possibility that, in states that have not established an Exchange by 2014, individuals who enroll in QHPs made available on the federal Exchange would not be entitled to the credit.
Eligibility for the Premium Tax Credit

To be eligible for the premium tax credit, the “Applicable Taxpayer” or a member of the taxpayer’s family: 1) must be enrolled in a QHP through an Exchange; and 2) cannot be eligible for MEC other than coverage in the individual market.

Who Is an Applicable Taxpayer?

An Applicable Taxpayer is an individual who is eligible for the premium tax credit. To meet this requirement, such individual must have household income that is at least 100%, but not more than 400%, of the FPL. “Household income” generally is defined as the modified adjusted gross income of all members of the household who are required to file an income tax return. Individuals, other than lawfully present aliens, with household income below 100% of the FPL generally are not eligible for the premium tax credit because they are eligible for Medicaid. Further, a married individual, to be an Applicable Taxpayer, must file a joint return for the taxable year and cannot be a tax dependent of another taxpayer.

What Is Minimum Essential Coverage?

The Affordable Care Act generally defines MEC as:

1. An eligible employer-sponsored health plan;
2. Government programs, such as Medicare, Medicaid, CHIP, TRICARE For Life, the veteran’s health care program, and a health plan for the U.S. Peace Corps volunteers;
3. Grandfathered health plans; and
4. Such other coverage designated by the Department of Health and Human Services (HHS).

Government Programs

The guidance generally indicates that an individual is eligible for government-sponsored MEC on the first day of the first month in which the individual may receive benefits. Therefore, a taxpayer would not lose eligibility for the premium tax credit upon enrollment, if benefits have not commenced. However, an individual who is eligible for a government program but fails to complete the requirements for enrollment by the last day of the third full month following the event that establishes eligibility will be treated as eligible for the coverage on the first day of the fourth month.

Example: A taxpayer turns 65 on June 3 and becomes eligible for Medicare. The taxpayer fails to enroll in Medicare by September 30. The taxpayer is considered eligible for MEC on October 1, the first day of the fourth month following the taxpayer turning 65.

Additional situations and related examples are set forth in the regulations.
How Does Employer-Sponsored Coverage Relate to the Premium Tax Credit?

An individual is eligible for MEC through an eligible employer-sponsored plan if the individual had the opportunity to enroll in coverage that is affordable and provides minimum actuarial value. An individual that is offered such coverage from an employer is not entitled to a premium tax credit.

The regulations clarify the following:

1. **Waiting Periods**—An individual will not be treated as eligible for MEC during a plan’s waiting period.

2. **Enrollment in Employer-Sponsored Coverage**—An individual that is enrolled in (not just eligible for) an eligible employer-sponsored plan will not be eligible for the premium tax credit even if the plan is unaffordable or does not provide minimum value. An individual who enrolls in a plan and who later disenrolls from the plan during the plan year will be treated as eligible for MEC only for the months the individual was actually enrolled in the plan. This might occur, for example, if the individual did not realize upon initial enrollment that the plan is unaffordable or does not provide minimum value.

   **Automatic Enrollment Exception to Enrollment Rule**—However, an individual who is automatically enrolled for a plan year will not be treated as eligible for MEC if the individual terminates the coverage before the later of the first day of the second full calendar month of the plan year or the last day of any opt-out period provided by the plan or specified in guidance issued by the Department of Labor (DOL) relative to the Affordable Care Act’s automatic enrollment requirement. According to the preamble to the regulations, this could also encompass an automatic enrollment due to an administrative error or automatic re-enrollment for a subsequent plan year.

Affordability

The affordability test for the premium tax credit for an employee is based on the cost of self-only coverage. An employer-sponsored plan is affordable if the employee’s required contribution for self-only coverage under the plan does not exceed 9.5% of the Applicable Taxpayer’s household income for the taxable year. The IRS has reserved for future regulations the issue of how to calculate affordability for related individuals, such as family members of an employee.

Note: The final regulations define affordability for purposes of an individual’s ability to receive the premium tax credit. However, the Treasury and IRS have described and expect to issue, for purposes of determining whether an employer will owe an assessable payment, a safe harbor allowing employers to use an employee’s Form W-2 wages in lieu of household income in determining whether coverage is affordable. The Treasury and IRS have requested and received comments on the safe harbor. Please see IRS Notices 2011-73 and 2012-17, found in the Resources section.

The preamble to the regulations makes the following observations:

1. Employer contributions to a health savings account (HSA) will not affect the affordability of employer-sponsored coverage because HSA contributions generally may not be used to pay health insurance premiums.
2. Amounts available under a health reimbursement arrangement (HRA) that may only be used to reimburse medical expenses and that may not be used to reimburse the employee's share of the cost of employer-sponsored coverage will not affect the affordability of employer-sponsored coverage. Further guidance may be issued to address how other HRAs are treated for this purpose.

3. The impact, if any, of wellness incentives on affordability will depend on the employee’s certainty that he or she will qualify for the incentive when being evaluated for eligibility for advance credit payments of the premium tax credit. Comments are requested on how amounts available under a wellness incentive program may affect the affordability of employer-sponsored coverage.

The regulations provide a number of examples for determining the affordability of MEC, such as how the affordability requirement applies if it is discovered that an employer-sponsored plan is unaffordable at year-end or if it is subsequently discovered that an employer-sponsored plan is affordable following an initial determination that the plan was unaffordable.

**Minimum Actuarial Value**

An employer-sponsored plan provides minimum actuarial value only if the plan’s share of the total allowed costs of benefits provided under the plan is at least 60%. The regulations defer the determination of minimum actuarial value for an employer-sponsored plan pending issuance of further guidance.

**Calculating the Premium Tax Credit**

A taxpayer’s premium assistance amount is the lesser of:

1. The premiums for the month for one or more QHPs in which a taxpayer or a member of the taxpayer’s family enrolls; or

2. The excess of the adjusted monthly premium for the applicable benchmark plan over 1/12 of the product of a taxpayer’s household income and the applicable percentage for the taxable year. The applicable benchmark plan generally is the second lowest cost silver plan offered at the time an individual enrolls in a QHP through the Exchange. The applicable percentage is derived from a table provided in the regulations of household income expressed as a percentage of the FPL.

The regulations provide a number of examples for calculating the premium for a QHP, such as how to factor in a premium paid for a stand-alone dental plan that provides pediatric dental benefits when the QHP does not include such benefits or how to exclude a portion of a premium paid for benefits in addition to essential health benefits that are required by a state to be covered by a QHP.

**Effective Date and Comments**

The regulations become effective May 23, 2012 and are applicable for taxable years ending after December 31, 2013. Comments on certain aspects of the regulations must be submitted by August 21, 2012.
Resources


In October 2011, Aon Hewitt submitted comments to the IRS in an effort to clarify the impact of the regulations on employers who offer health coverage. The Aon Hewitt comment letter is available at: http://www.aon.com/human-capital-consulting/thought-leadership/leg_updates/healthcare/reports-pubs_comments-premium-tax-credit.jsp


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