SIIA
SELF-INSURANCE INSTITUTE OF AMERICA, INC.
Protecting and Promoting Self-Insurance and Alternative Risk Transfer Since 1981.

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Submitted Electronically via Email: *Notice.comments@irscounsel.treas.gov*

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

To Whom It May Concern:

The Self-Insurance Institute of America, Inc. ("SIIA") respectively submits these comments in response to Notice 2015-52, which – similar to Notice 2015-16 – is intended to initiate and inform the process of developing regulatory guidance regarding the Excise Tax on High-Cost Employer-Sponsored Health Coverage (the "Excise Tax").

SIIA is a member-based association dedicated to protecting and promoting the business interests of companies involved in the self-insurance/alternative risk transfer marketplace. SIIA's membership includes self-insured employers, third party administrators, and stop-loss/reinsurance carriers, among other industry service providers.

Comments Relating to Notice 2015-52

1. Third-Party Administrators of Self-Insured Benefits Should Not Be the Entity Liable to Pay the Excise Tax

The Patient Protection and Affordable Care Act ("ACA") added section 4980I to the Internal Revenue Code ("Code"), imposing a 40 percent excise tax on employer-sponsored health coverage that exceeds $10,200 for individuals and $27,500 for families for tax years beginning on or after December 31, 2017.[1] A literal reading of new Code section 4980I provides that the Excise Tax liability is payable by an insurance company (in the case of fully-insured benefits), the entity that administers the plan benefits (in the case of self-insured benefits), and the employer (if, for example, certain contributions to a health savings account ("HSA") are made).[2] In the case of self-insured benefits, Notice 2015-52 indicates that the Department of Treasury ("Treasury") and the Internal Revenue Service ("IRS") are considering two approaches for determining who is the entity that "administers the plan benefits" for purposes of imposing the Excise Tax liability on that entity.

Under the first approach, the Excise Tax liability would be imposed on the entity "responsible for performing the day-to-day plan administration functions, such as receiving and processing claims for benefits, responding to inquiries, or providing a technology platform for benefits information." The Notice explains that Treasury and the IRS anticipate that this entity would be the third-party administrator ("TPA") for the self-insured

[1] Section 4980I(a), (b)(3)(C)(i), (c) of the Internal Revenue Code ("Code").
[2] *See* Code section 4980I(c)(1), (2).

benefits, except in rare circumstances where an employer administers its own plan (or owns a TPA performing these functions).

Under the second approach, the entity liable for paying the Excise Tax would be the entity "that has the ultimate authority or responsibility under the arrangement with respect to the administration of the plan benefits (including final decisions on administrative matters), as well as authority or responsibility over eligibility determinations, claims administration, and arrangements with service providers (including the authority to terminate service provider contracts)." In other words, it would appear that the employer would be responsible for paying the Excise Tax if Treasury and the IRS adopted the second approach.

For the reasons discussed below, SIIA believes that if Treasury and the IRS adopt the first approach – where the Excise Tax liability is imposed on the TPA – significant administrative burdens, complex contract negotiations, and disparate tax treatment among similarly situated TPAs would result. For these reasons, SIIA respectfully requests that Treasury and the IRS give due consideration to adopting the second approach – where the Excise Tax is *not* imposed on the TPA, but rather, the Tax is imposed on the employer sponsoring the self-insured benefits.

a. *Administrative Burdens In the Case of Multiple TPAs*

Due to the nature in which Congress structured the Excise Tax, an employer offering self-insured benefits to its employees is required to aggregate the cost of the entire package of health care coverage for each employee.[3] In other words, the self-insured employer will be required to determine – on an employee-by-employee basis – (1) the different types of health coverage for a particular employee, (2) the aggregate cost of that coverage, and (3) the amount, if any, that exceeds the Excise Tax's dollar thresholds for the year. If this calculation shows that there is an excess benefit subject to the Excise Tax, the self-insured employer is then required to (1) determine the amount of the Tax on the excess benefit and (2) apportion – on a pro rata basis – the Tax liability among the entities that are "administering" one or more self-insured benefits. The employer must notify each of these entities of the amount of the Tax owed,[4] and the employer must report the amount of the Tax payable by each entity – and also the employer, if applicable – to the IRS.[5]

The majority of employers that sponsor a self-insured health plan contract with a number of TPAs to administer the various benefits offered under the arrangement. For example, in cases where an employer offers prescription drug benefits, the employer may contract with a Pharmacy Benefit Manager ("PBM") to administer these benefits. In addition, where an employer offers a Health Flexible Spending Arrangement ("Health FSA) and/or self-funds a Health Reimbursement Arrangement ("HRA"), the employer will typically contract with a TPA to administer the Health FSA and/or HRA. This same employer may also contract with a company that specializes in "wellness" benefit offerings, and the employer may even offer on-site clinics, each of which may be administered by separate TPAs. And, an employer may contract with one TPA to perform enrollment functions, and another TPA to adjudicate medical claims.

As stated, in the event the aggregate cost of health coverage for a particular employee exceeds the Excise Tax's dollar thresholds for the year, the employer must

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[3] Code section 4980I(c)(4)(A)(i).
[4] Code section 4980I(c)(4)(A)(ii).
[5] *Id*.

calculate the amount of the Tax liability and then apportion the liability among the entities responsible for paying the Tax. If the TPA is considered the entity responsible for paying the Tax liability, this would mean that the employer would be required to make multiple calculations for the multiple TPAs the employer contracts with to administer its self-insured benefits. Then, the employer would be required to notify each particular TPA of the portion of the Tax liability the TPA must pay to the IRS. Requiring the employer to determine the portion of the Excise Tax liability allocable to these multiple TPAs will be time consuming and difficult to calculate. In addition, the burden of notifying each of the TPAs of the Tax liability owed – along with the burden of sending a separate notice to the IRS regarding the Tax liability for each TPA – will be significant. Imposing the Excise Tax liability on the employer, however, would eliminate these administrative burdens, thereby making it easier for the employer to calculate, assess, and pay the Tax, as well as making it easier for the IRS to collect any resulting Excise Tax liability.

b. *No Audit Procedures for TPAs*

If and when a TPA receives notice of any Excise Tax liability it is responsible to pay, the TPA will then perform its own audit to determine if the Tax liability apportioned to them was calculated accurately. If there are discrepancies in the apportioned Excise Tax liability amounts, the TPA and the employer would be required to reconcile their differences.

It is important to note that there are no "audit" procedures set forth in the statute or suggested in Notice 2015-16 and Notice 2015-52. The fact that TPAs will often times question the Tax liability the employer is suggesting that it is responsible to pay will strain the relationship between the TPA and the employer, and complicate future contract negotiations. By imposing the Excise Tax liability on the employer – instead of the TPA – Treasury and the IRS would eliminate the need to reconcile any differences in the assessed Tax liability amounts, and avoid complicating the business dealings between the employer and its TPA partners.

c. *TPAs Have No Control Over an Employer's Plan Design and the Overall Cost of the Applicable Health Coverage for the Calendar Year*

While some TPAs assist their self-insured employer clients with developing the design of the types of health care coverage that is offered, many other TPAs simply provide ministerial services such as enrollment functions, claims adjudication, and making benefit payments, all of which are generally governed by a "plan document," which is written by the employer (with the aid of legal counsel and/or outside benefit consultants). Because these TPAs have no control over plan design, these TPAs cannot control whether the cost of applicable health coverage offered to a particular employee exceeds the Excise Tax's dollar thresholds for a given year. Instead, the self-insured employer is essentially the only entity that can control the comprehensiveness of the health care coverage that is offered. In addition, a TPA cannot control the amount of tax-preferred contributions employees may make to a Health Flexible Spending Arrangement ("Health FSA") or a Health Savings Account ("HSA") made through a Code section 125 cafeteria plan, which may have the effect of pushing the overall cost of applicable coverage over the Excise Tax's dollar thresholds for the year.

Put simply, imposing the Excise Tax liability on the TPA is in no way equitable. Instead, a much more equitable result would be to impose the Excise Tax liability on the employer, considering the employer – and not the TPA – has the requisite control over whether the cost of applicable health coverage offered to a particular employee may trigger the Excise Tax or not.

d. *If TPAs Are Required to File Forms 720 With the IRS, New Precedent Would Be Set and Administrative Burdens Would Be Created*

Notice 2015-52 indicates that Treasury and the IRS are considering requiring the entities responsible for paying the Excise Tax to use IRS Form 720 for the payment of the Tax liability. The Form 720 is used to pay excise taxes for, among other things, violations of certain "group health plan" requirements. The Form 720 is also used to pay the Patient-Centered Outcomes Research Fee (i.e., the "PCORI" excise tax). In each case, the excise tax liability is the sole responsibility of the employer. As a result, TPAs are not required to complete a Form 720 because the TPA is not liable for any excise taxes associated with the self-insured benefits they administer. Imposing the Excise Tax liability on TPAs would set new precedent.

In addition, requiring the TPA to pay the Excise Tax would create administrative burdens by forcing TPAs to complete an IRS Form with which they have no familiarity with. These administrative burdens are further exacerbated if a TPA is required to complete multiple Forms 720 for the multiple self-insured employer clients that trigger the Tax in a given year. As stated, the TPA cannot control which of its self-insured employer clients trigger the Tax, and therefore, cannot control how many Forms 720 the TPA must complete and file with the IRS.

e. *Imposing the Excise Tax Liability on TPAs Creates a "Tax-Within-a-Tax"*

As is customary in a TPA service agreement with a self-insured employer, any resulting tax liability is passed through by the TPA to the employer. If the Excise Tax liability is imposed on the TPA, the TPA will respond in accordance with its current business practices and pass the Tax liability through to the employer. Importantly, because the Excise Tax liability is non-deductible, the Tax liability will effectively be higher than the 40 percent tax rate applied to the excess benefit. This means that the total amounts that would be passed through to the employer could be higher than if the employer paid the Tax liability directly (e.g., the variation of these amounts will depend upon the marginal tax rate for the TPA and the employer).

Treasury and the IRS have indicated that any amounts passed through to the employer will be taxable income to the TPA. In this case, the TPA will respond by "grossing up" the passed through amounts to cover the additional tax liability. This activity will, again, effectively increase the total Excise Tax liability that will be passed through, resulting in the employer paying a greater amount than the statutory 40 percent tax rate on the excess benefit. Congress never intended for this counterintuitive result when the drafters developed the Excise Tax provision.

f. *Treating Any Passed Through Excise Tax Liability as Taxable Income Will Produce Perverse Results*

In addition, given the variability in tax rates among for-profit TPAs – and especially non-profit TPAs (which in many cases are non-profit insurance carriers) – treating the "gross-up" amounts as taxable income to the TPA may put some TPAs at a competitive disadvantage as compared to other similarly situated TPAs solely on account of the TPA's marginal tax rate. This could lead to a market where TPAs are not competing with other TPAs on the level and quality of services they provide, but instead, the TPAs are competing on their marginal tax rate.

In other words, if a TPA's marginal tax rate is lower relative to other TPAs in the market, the TPA with the low marginal tax rate may reduce the price of their services solely because the amount of the Excise Tax liability – plus the "gross-up" amount – that is passed through to the employer is lower than the amounts passed through by their competitors. This issue is most acute in cases where a TPA is a non-profit organization (i.e., where the TPA's marginal tax rate is effectively zero). Here, the Excise Tax liability that is passed through to the employer would not produce any additional income tax liability, and therefore, the TPA would not be required to "gross-up" any amounts. As a result, this TPA could be more attractive from a price perspective because an employer would not be paying the "gross-up" amounts associated with the Excise Tax liability. This would effectively give non-profit TPAs a competitive advantage over for-profit TPAs, a result that Congress surely did not intend.

g. *Excluding the "Gross-Up" Amounts From the Cost of Applicable Coverage Is Complex and Will Produce Perverse Results*

Notice 2015-52 indicates that Treasury and the IRS will draft regulations excluding the passed through Excise Tax liability from the cost of applicable health coverage for the year. The Notice further suggests that some or all of the "gross-up" amounts should similarly be excluded for purposes of calculating the Tax liability for the year, but Treasury and the IRS are concerned whether making such a calculation is even administerable. If Treasury and the IRS do not impose the Tax on the TPA, then this issue is moot. As a result, the best way to limit undue complexity and difficulty in the case of determining the "gross up" amounts that may be excluded from the cost of applicable coverage is to clarify that the Tax liability is payable by the employer and not the TPA.

If, however, Treasury and the IRS conclude that the "gross-up" amounts can be determined (and thus excluded from the cost of coverage), Treasury and the IRS suggest that TPAs (and insurance carriers) utilize a formula commonly used to calculate "tax gross-ups" to determine the appropriate amount to be excluded. Treasury and the IRS further suggest two approaches for applying this formula. The first approach requires the use of the TPA's marginal tax rate. However, determining a TPA's marginal tax rate for a given year is typically determined months after the end of the coverage year (i.e., the applicable calendar year). If a TPA operates on a fiscal year, then additional complexities arise. This will create administrative difficulties for the IRS, the TPA, and the employer (which will be the entity ultimately bearing the cost of the "grossed-up" amounts).

Even if Treasury and the IRS adopt an approach that applies a "standard marginal tax rate" for applying this formula (under the second suggested approach), this would unfairly treat TPAs with varying applicable marginal tax rates differently. As stated above, if the Excise Tax is not imposed on the TPA, then this issue is moot. As a result, the best way to limit undue complexity and difficulty in this case is to clarify that the Tax liability is payable by the employer and not the TPA.

2. <u>The Suggested Determination Period May Result In Medical Claims Triggering the Excise Tax In a Given Year</u>

Notice 2015-52 suggests that the Excise Tax will be determined based on the calendar year. The Notice further suggests that an employer will determine the Tax liability soon after the end of the calendar year (so the employer can then notify the entities responsible for paying the Tax as soon as possible to ensure that these entities can pay the Tax liability in a timely manner). SIIA is concerned that Treasury's and the IRS's interest in determining the Tax liability soon after the end of the calendar year forces self-insured employers to determine its COBRA applicable premiums on a retrospective basis, rather than a prospective projection of expected claims and costs.

Typically, a self-insured employer will determine its COBRA applicable premiums prior to the start of a calendar year by making a prospective projection of expected claims (based on prior claims experience) and expected costs. These prospective projections allow the employer to determine the premium amounts for the major medical health plans offered to the employer's employees for the following year. According to Notice 2015-16, employers anticipated that these projected amounts would be counted as a component of the total aggregated cost of the health coverage offered to any particular employee during the applicable calendar year.

It appears, however, that Treasury and the IRS want employers to determine whether the Excise Tax is triggered for the applicable calendar year based on "actual" costs of the plan, which is determined by looking back at the medical claims submitted during the applicable calendar year, along with claims submitted during a subsequent run-out period after the end of that year. If this is the approach Treasury and the IRS are suggesting, adverse medical claims – which are out of the control of the employer – will unfairly drive whether the employer's health coverage triggers the Excise Tax during the applicable calendar year. Congress never intended medical claims to determine whether or not the Excise Tax is triggered in a particular calendar year. Instead, it appears that Congress intended to base any Excise Tax liability on the COBRA applicable premiums – which are traditionally determined on projected costs – and do not include an adjustment for actual experience if the plan runs higher than expected claims in any given year.

It is also important to note that COBRA applicable premiums may be determined on a "plan year" basis, as opposed to a "calendar year" basis, which may result in two sets of rates for an applicable calendar year. In addition, the COBRA applicable premiums estimated by the employer may include the risk transfer costs (e.g., stop loss insurance premiums) the employer has engaged for the sole purpose of limiting unforeseen, catastrophic claims. This is done so the costs of the COBRA applicable premiums are predictable during the ensuing calendar year. However, if full catastrophic claims incurred during the applicable calendar year must be taken into account, then the cost of the plan that the employer designed and budgeted to stay under the Excise Tax thresholds may exceed these thresholds solely on account of a high number of, for example, motor vehicle accidents or premature births, which are out of the direct control of the employer. Put simply, an "actual" cost approach would set new precedent.

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Thank you in advance for considering these comments. Please do not hesitate to contact me if you have questions, or if members of SIIA can serve as a resource on this very important issue.

Sincerely,

Mike Ferguson
President & CEO
Self-Insurance Institute of America, Inc.