



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF THE CHIEF COUNSEL

September 22, 2014

Number: **2014-0037**
Release Date: 12/26/2014

CONEX-130604-14

UIL: 105.00-00

The Honorable Bob Goodlatte
Member, U.S. House of Representatives
70 North Mason Street
Harrisonburg, Virginia 22802

Attention:

Dear Congressman Goodlatte:

I am responding to your inquiry dated August 11, 2014, on behalf of your constituent, . He wrote about the ability of employers under the Affordable Care Act to reimburse medical expenses of employees with pre-tax dollars under section 105 of the Internal Revenue Code (Code).

Prior to the Affordable Care Act, an employer could reimburse employees for the medical expenses of the employee and the employee's family and exclude those amounts from the employee's income and wages under section 105(b) of the Code.

The Affordable Care Act has not changed the tax treatment of the reimbursement for employee medical expenses. However, these arrangements are considered to be group health plans and must satisfy the market reform rules enacted for them as part of the Affordable Care Act.

One of the requirements for group health plans, is that they cannot impose an annual or lifetime dollar limit on essential health benefits under section 2711 of the Public Health Service Act. An agreement by the employer to reimburse medical expenses up to a fixed amount is a group health plan under which there is an annual limit on essential health benefits. This fails to comply with the prohibition on annual limits under section 2711 of the Public Health Service Act.

If an employer offers a group health plan that satisfies the market reform rules by providing coverage for essential health benefits without annual limits in addition to a separate arrangement to pay for other medical expenses, the guidance we provided in Notice 2013-54 (2013-40 I.R.B. 287) allows the group health plan and the separate

arrangement to be combined to determine if together it satisfies the market reforms. If the employer does not offer the employee a group health plan and the employee obtains other coverage, such as when the employee is covered by an individual health insurance policy or Medicare, the separate arrangement cannot be combined with that other coverage to determine if it satisfies the market reform rules for group health plans.

Moreover, the coverage under a group health plan that does not satisfy the market reforms will generally disqualify the individual from receiving the premium tax credit under section 36B of the Code. This is because the Affordable Care Act generally does not allow an individual to receive both the benefits of pre-tax coverage under an employer-sponsored group health plan and the premium tax credit.

I hope this information is helpful. If you have any questions, please call me at _____, or _____ at _____.

Sincerely,

Harry Beker, Chief
Health and Welfare Branch
Office of Division Counsel/ Associate
Chief Counsel (Tax Exempt and
Government Entities)



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September 22, 2014

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CONEX-132278-14

UIL: 105.00-00

The Honorable Danie Lipinski
U.S. House of Representatives
Washington, DC 20515

Attention:

Dear Mr. Lipinski:

I am responding to your inquiry dated August 26, 2014, on behalf of a nonprofit organization in your district. The organization asked for guidance on reimbursing employees for the premiums they paid for individual health insurance policies. As we understand the inquiry, the organization previously reimbursed the premiums with pre-tax funds (so that the arrangement did not result in any taxable income to the employees).

Prior to the ACA, an employer could reimburse employees for the medical expenses of the employee and the employee's family and exclude those amounts from the employee's income and wages under section 105(b) of the Code. The ACA has not changed the tax treatment of the reimbursement for employee medical expenses. However, these arrangements, under the ACA, are considered to be group health plans and must satisfy the market reform rules for them.

One of the requirements for group health plans, is that they cannot impose an annual or lifetime dollar limit on essential health benefits under section 2711 of the Public Health Service Act. An agreement by the employer to reimburse medical expenses up to a fixed amount is a group health plan under which there is an annual limit on essential health benefits and thus fails to comply with the prohibition on annual limits under section 2711.

If an employer offers a group health plan that satisfies the market reforms by providing coverage for essential health benefits without annual limits and in addition offers an arrangement to pay for other medical expenses, Notice 2013-54 (2013-40 I.R.B. 287) allows the group health plan to be combined with the arrangement to determine if it satisfies the market reforms. However, if the employer does not offer a group health plan, such as when the employee is covered by an individual health insurance, the

arrangement to pay the premiums cannot be combined with any other coverage to determine if it satisfies the market reforms.

The guidance that we provided in Notice 2013-54 did not change the tax results described in Revenue Ruling 61-146. This ruling says that under certain conditions if an employer reimburses an employee's substantiated premiums for individual health insurance policies, the payments are excluded from the employee's gross income under section 106 of the Code. This exclusion also applies if the employer pays the premiums directly to the insurance company. Section 106 excludes these payments as payments by an employer under a group health plan, because the reimbursement arrangement itself is treated as a group health plan. As a group health plan, the arrangement must meet market reform rules for group health plans, including not providing a limit on the annual or lifetime benefits that the employee may receive under the arrangement (such as a reimbursement limit equal to the premiums paid).

Employers that do not want to provide group health insurance coverage but want to help their employees with the purchase of health coverage can provide the employee additional compensation to do so. The additional compensation would not be excluded from the employee's income under section 106 and would be reported with other income and wages on the Form W-2. This is because the additional compensation would not be restricted to the payment of medical expenses.

I hope this information is helpful. If you have any questions, please call me at _____, or _____ at _____.

Sincerely,

Harry Beker, Chief
Health and Welfare Branch
Office of Division Counsel/ Associate
Chief Counsel (Tax Exempt and
Government Entities)