EMPLOYERS COUNCIL ON FLEXIBLE COMPENSATION

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Exempt Individuals' Contributions to HSAs and FSAs from the Excise Tax

What is the Excise Tax?

The Affordable Care Act (ACA) created a new excise tax, commonly referred to as the Cadillac Tax, on certain high-end health care plans. The purported purpose of this tax was to discourage employers from offering health insurance plans with excessively rich benefits. Unless repealed, the tax will be applied starting in 2018, and is equal to 40 percent of the value of any coverage in excess of $10,200 for an individual and $27,500 for a family. The tax, required to be paid by the health plan itself (or in some cases the employer sponsoring an arrangement or its plan administrator), applies to current and retired employees and includes "any applicable employer-sponsored coverage." To determine whether these cost thresholds are exceeded, an overly broad net is cast including many employer sponsored arrangements that actually promote efficient health care such as wellness program incentives and consumer-directed coverage arrangements such as flexible spending arrangements (FSAs), health reimbursement arrangements (HRAs), and health savings accounts (HSAs). It is these latter arrangements that we seek to exclude from the Cadillac Tax. ***In particular, the statute is being interpreted to require the contributions made by individuals into their HSAs and FSAs to be deemed as if they were provided by the employer for purposes of calculating the tax.***

Impact of the Tax on the Marketplace:

Statistics show the structure of the tax will eventually result in penalizing employers offering ANY health coverage and these penalties will likely be passed on to employees. Preliminary analysis shows that 48 percent of employers are likely to trigger the tax in 2018, and 82 percent could hit the threshold by 2023.[1] Instead of having a tax that discourages overly generous health benefits, the tax will actually hit the majority of employer-sponsored health plans that average Americans receive.

With 42 percent of employers increasing employee cost sharing, employees will face serious increases in their out of pocket exposure. To offset this exposure, the time is **NOW** to foster, not stunt, the growth of consumer directed arrangements.[2]

According to an American Health Policy Institute survey using data of large employers collected in June and September of 2015, the excise tax is already having, and will continue to have a significant impact:

- Almost 90 percent of large employers are taking steps to try to prevent their company from having a plan that triggers the excise tax in 2018;
- Over 30 percent of large employers said they would have at least one plan impacted by the excise tax in 2018;
- Almost half of the employers that did not have plans hitting the excise tax in 2018 said they would have a plan that would be impacted by 2023;
- Among employers who are going to reduce the values of their plans as a result of the excise tax, 71 percent of employers said that they probably would not provide a corresponding wage increase; 16 percent said they would.[3]

With regard to HSAs and FSAs, the American Health Policy Institute survey found:

- Almost 19 percent of large employers were already curtailing or eliminating employee contributions to flexible spending accounts (FSAs) in order to avoid triggering the excise tax;
- Almost 13 percent were already curtailing or eliminating employee contributions to health savings accounts (HSAs).[3]

[1] "2014 Health Care Changes Ahead Survey Report", Towers Watson, September, 2014. http://www.towerswatson.com/en-US/Press/2014/09/nearly-half-us-employers-to-hit-health-care-cadillac-tax-in-2018-with-82-percent-by-2023.

[2] Trevi D. Troy and D. Mark Wilson, *The Impact of the Health Care Excise Tax on U.S. Employees and Employers*, American Health Policy Institute, 2014.

[3] Trevi D. Troy and D. Mark Wilson, *ACA Excise Tax: Cutting Family Budgets, Not Health Care Budgets*, American Health Policy Institute, 2015.

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A 2015 Kaiser Family Foundation study predicted that:

- More than a quarter of employers face tax liability in 2018, and more than 40 percent by 2028; among large employers (>200 employees), 46 percent in 2018 and 68 percent by 2028 will have to pay the tax.
- The tax could reduce plan offerings, limit employee choice, and restrict use of consumer-directed health care accounts (*e.g.*, HSAs and FSAs).[4]

Impact of the Tax on Consumer Directed Health Accounts (HSAs and FSAs):
According to Internal Revenue Service (IRS) Notice 2015-16, the tax applies to employer and employee contributions to FSAs, employer contributions to HRAs, and employer and employee pre-tax employee contributions to HSAs. Including these contributions in the tax calculation will undermine the very options created to make health care more affordable, manageable, and predictable for American families. In an effort to avoid hitting the tax threshold, employers will be less likely to offer such benefits, which help employees pay for their increasing share of out-of-pocket healthcare costs.

Importance of FSAs and HSAs to Consumers:
A majority of employers currently sponsor consumer-directed arrangements for their employees. ECFC member companies assist in the administration of such arrangements for over 33 million employees and dependents. Approximately 103.5 million Americans benefit from consumer-directed accounts, which include HSAs, FSAs and HRAs.[5]

Many more employers are moving toward higher deductible health plans or plans that increase the amount of cost sharing borne by employees.[6] In addition, employers are taking action to reduce the costs of their health coverage, yet protect employees from higher out of pocket costs by moving to account-based, consumer-directed arrangements.[7] This trend is seen on both state-and federally-facilitated exchanges, where much of the coverage available will have high deductibles and higher cost-sharing.[8] Consequently, consumer-directed benefit arrangements, such as FSAs and HSAs, are of increasing importance to American workers and their families.

These tools provide a means of financing health care costs incurred under health plans, particularly under high deductible health plans, and help many Americans afford critical health care procedures that might otherwise force them into bankruptcy.

Companies are increasing enrollment by 20 percent or more to their Consumer Directed Health Accounts. Over the last year, they report average cost trends of only 2 percent over that period.[9] This is likely in part because participants in these accounts are more likely to exhibit cost-conscious behaviors and participate in wellness programs.[10] According to a 2014 survey conducted by Visa, Inc., 43 percent of the responders said they would probably/definitely cut back on medicines and treatments if they didn't have an FSA.[11] The type of treatments they

[4] Gary Claxton and Larry Levitt, *How Many Employers Could be Affected by the Cadillac Plan Tax?* Kaiser Family Foundation: Health Costs, August, 2015.

[5] FSA counts extrapolated from U.S. Census Bureau statistics on number of employed, number of employers who offer FSAs, average enrollment statistics, and Visa research (conducted by C+R Research, July 2012). HRA statistics based on "U.S. Consumer-Driven Healthcare: Health Benefit Account Market Sizing," Aite Group, November, 2013. HSA statistics from "2014 Year-End Devenir HSA Research Report," February, 2015 (http://www.devenir.com/research/2014-year-end-devenir-hsa-market-research-report/). These counts aggregated and multiplied by 2.35, (HHS PCORI fee multiplier that determines the average number of lives covered under the plan for the plan year [169 Treas. Reg. §§ 46.4376-1(c)(2)(iv)(B) and (C)].

[6] National Business Group on Health, "Large Employers' 2015 Health Plan Design Survey", August 13, 2014. According to this survey 42 percent of employers are increasing employee cost-sharing.

[7] National Business Group on Health, "Large Employers' 2015 Health Plan Design Survey", August 13, 2014. According to this survey, 57 percent of employers are implementing or expanding account-based consumer-directed arrangements.

[8] Kev Coleman, *Deductibles, Out-Of-Pocket Costs, and the Affordable Care Act,* HealthPocket.com. (December 12, 2013). http://www.healthpocket.com/healthcare-research/infostat/2014-obamacare-deductible-out-of-pocket-costs#.

[9] "2014 Health Care Changes Ahead Survey Report", Towers Watson, September, 2014.

[10] "Findings from the 2014 EBRI/Greenwald & Associates Consumer Engagement in Health Care Survey", Employee Benefit Research Institute, December, 2014

[11] Visa Annual Consumer Survey on Behaviors, Perceptions, and Attitudes of FSAs, 2014.

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would cut back on, in order of most to least, includes: doctor visits, vision, dental, over-the-counter (OTC) medicines, prescriptions, and sick doctor visits. The study also indicated that the cut-backs are higher for people in lower to middle income brackets compared to those in higher income brackets.

Users of FSAs and HSAs are middle class families. On average, they earn roughly $57,000 per year, which is less than 300% of the federal poverty level (FPL). For comparison, when the ACA was passed, income-based subsidies were made available on the exchanges to any family of four earning less than 400% of FPL.

ECFC Recommendation:
It is clear that the excise tax will have an adverse impact on millions of American businesses and consumers. Action must be taken now to counteract the unintended consequence of this provision. Consumer directed arrangements such as FSAs, HRAs, and HSAs help keep healthcare costs down and therefore should be exempted from this tax if it is not repealed. **The tax should be repealed given its impact on consumers, employers and all consumer directed arrangements. However, at a minimum it should be corrected to remove individuals' contributions to their HSAs or FSAs from the calculations.**

Legislation to repeal the excise tax has already been introduced in the House of Representatives and has bipartisan support. We encourage support of H.R. 879 (Ax the Tax on Middle Class Americans' Health Plans Act) and H.R. 2050 (Middle Class Health Benefits Tax Repeal Act of 2015) and support introduction of legislation to repeal the tax or reform the tax to exclude consumer directed accounts in the Senate. **<u>However, to provide immediate relief we ask that legislation be considered to make clear individuals' contributions to their HSAs and FSAs should be exempted from calculations.</u>**