Affordable Care Act Compliance, New Type of Annuity Contract, and Taxation of Employer-Provided Parking

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WAITING PERIOD UNDER THE AFFORDABLE CARE ACT

A final rule has been issued by the Department of Labor, the IRS, and Health and Human Services ("Joint Agencies") with regard to the meaning of an orientation period for purposes of determining the maximum permissible waiting period for a group health plan under the Affordable Care Act. This rule was issued on June 25, 2014, at 79 Fed Reg 35942.

Under regulations previously finalized, the Joint Agencies stated that the maximum waiting period for a group health plan is 90 days. However these prior regulations stated that an employer could also utilize an employment-based orientation period of up to one month which would not count against the 90-day period. The earlier regulations issued proposed advice on what constitutes a permissible orientation period. The June 25, 2014, regulation constitutes a final regulation on a permissible orientation period.

A maximum one-month orientation period is determined by adding a calendar month to the first date of employment and subtracting one calendar date. There is no specific requirement as to what constitutes an orientation period. However, the regulation indicates it presumably covers items such as evaluation, orientation, and training.

This final rule generally permits an employer to delay enrollment under the group health plan until the completion of a one-month orientation period and a 90-day waiting period. However a "large employer" (one with 50 or more full-time employees—although an employer with at least 50 but no more than 99 employees is not considered a large employer until 2016) will be subject to a "shared responsibility excise tax" (commonly known as the "play or pay" tax) if coverage is delayed beyond the first day of the fourth full month of employment. Hence, such large employers, if using an orientation period, will have to make sure coverage starts by this deadline.

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The following is an example found in the preamble to the regulation on how the orientation period rules could cause a failure under the shared responsibility rules:

- An employee's first date of employment is January 6.
- Under the combined orientation period and waiting period rules, coverage must begin by May 6.
- For a large employer, under the combined orientation period and waiting period rules, coverage must begin the first day of the fourth full calendar month of employment (i.e., by May 1).

Hence employers with 100 or more employees in 2015 and 50 or more employees in 2016 need to seek advice to make sure the use of an orientation period does not cause the excise tax to be imposed.

IRS REITERATES ITS POSITION CONCERNING EMPLOYER REIMBURSEMENT OF INDIVIDUAL HEALTH POLICY PREMIUMS

Although the IRS in 2013 issued Notice 2013-54, which informed employers that they could not avoid the requirements of the Affordable Care Act by merely reimbursing an employee on a pre-tax basis for the employee's purchase of his or her own health insurance policy, confusion on the matter still existed. Hence the IRS posted on its Web site additional Q&As on May 13, 2014.

The IRS refers to such premium reimbursement by an employer as an "employer payment plan." Even though the purpose of the plan is to only reimburse an employee for the cost of individual health insurance, the IRS deems such a plan to be a group health plan subject to all the requirements of the Affordable Care Act. Given the nature of the reimbursement, it by itself could never meet the requirements of having no annual limit on essential health benefits and the requirement to provide preventive care without cost sharing. Hence an employer that attempts to satisfy its Affordable Care Act obligations by only reimbursing premiums paid by employees will be subject to a $100 per day excise tax per applicable employee under Internal Revenue Code Section 4980D.

The penalties discussed above apply to a group health plan under Internal Revenue Code Section 4980D. Therefore, there is no exemption from these rules for small employers.

NEW TYPE OF ANNUITY CONTRACT CAN BE OFFERED UNDER A DEFINED CONTRIBUTION PLAN

In the past, profit-sharing and 401(k) plans frequently offered an annuity contract as a choice for a form of distribution of benefits. That option is seldom seen these days due to both a lack of interest by participants (selection of an annuity often means, in the case of a death shortly after retirement, no benefits for survivors are payable—other than possibly a spouse if that option was elected) and fear on the part of the plan sponsor that a poor choice in the insurer providing the annuity could cause legal problems down the road if the insurer is financially unable to pay the full benefit. Since many profit-sharing and 401(k) plans currently offer only a lump sum, the IRS and Department of Labor have been concerned that retirees will outlive the assets represented by the lump sum.

In order to address this concern, the IRS issued final regulations on July 2, 2014, 79 Fed Reg 37633, to permit a new sort of hybrid annuity contract called a "qualifying longevity annuity contract" (QLAC). The purpose of this new QLAC is to allow a defined contribution retirement plan participant or IRA owner to purchase an annuity contract that has a deferred commencement date to provide some degree of protection against outliving retirement assets. To constitute a QLAC the following requirements must be met:

- The starting date of the QLAC can be no later than the first of the month following the month in which the plan participant reaches age 85.
- The contract cannot be a variable, indexed, or similar contract.
- The contract cannot have a cash-out feature but it can offer the option of a return of premium. The return of premium permits survivors to recoup from the insurer the balance of the amount the participant originally paid for the contract where the participant dies prior to receiving annuity payments equal to that amount.
- The maximum amount that can be used from the account balance is the smaller of 25% of the account balance or $125,000 (indexed for inflation).

There are additional rules with regard to survivor benefits under a QLAC that are beyond the scope of this article.

It is important to note how this new QLAC interacts with the Code Section 401(a)(9) rules commonly called the minimum distribution rules. Under the minimum distribution rules a plan participant must commence receiving payments from a qualified retirement plan upon reaching age 70½ unless he or she is still working for the plan sponsor and not an owner. A QLAC does not count for purposes of calculating the required minimum distribution, which, therefore, reduces the amount that must be distributed each year after age 70½. For example, if a participant with an account balance of $500,000 elects to receive a $125,000 QLAC, only $375,000 is used to determine the minimum distribution amount that must be paid out by the retirement plan.

No new relief has been granted under this regulation with regard to a plan sponsor's fiduciary obligations. Hence there is likely to still be a concern on the part of a plan sponsor that a poor choice of the annuity provider could result in fiduciary liability. Employers also still have a concern about recordkeeping obligations for the annuity contract until benefits commence. These concerns do not apply in the IRA marketplace, and more interest in a QLAC is expected in that area.

EMPLOYER-PROVIDED PARKING FOR EMPLOYEES IS NOT ALWAYS TAX-FREE

Due to apparent confusion among employers on the issue, the IRS issued guidance on employee parking and, in particular, whether such parking is tax-free or taxable. The guidance was provided in the form of *IRS Information Letter 2014-0017*, which was published May 13, 2014.

The IRS stated that all parking provided by an employer is taxable unless it meets the requirements of being qualified parking as defined in Internal Revenue Code Section 132(f)(2). The requirements are: (1) the parking must be on or very near the employer's premises; and (2) the employer must either own or rent the parking property or else directly pay or reimburse the employee for the parking. Qualified parking is never parking provided at or near the employee's home. Even meeting these requirements, the maximum exclusion is $250 per month in 2014. If the value of parking exceeds that amount, the excess is subject to all payroll taxes applicable to wages.

The above discussion is intended to briefly summarize certain recent legal developments in employee benefits, but is not intended to be legal advice and must not be relied upon as such. All readers are urged to raise any concerns they may have based on matters discussed in this column with experienced benefits legal counsel.