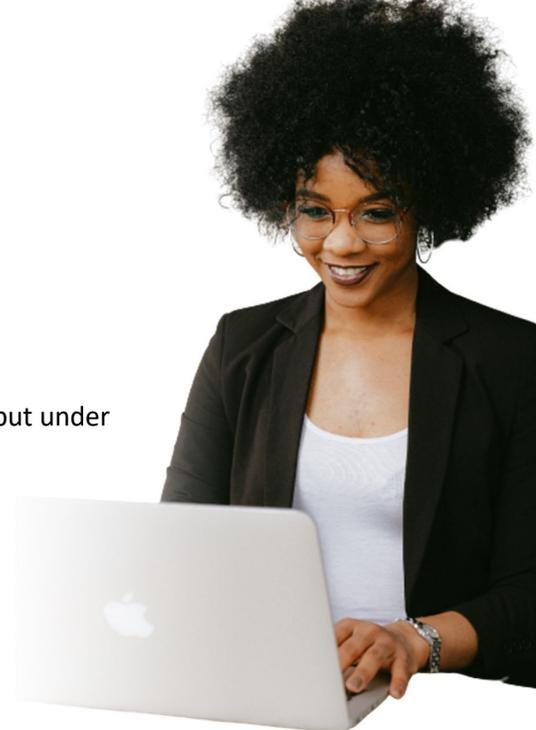


You asked, I'm happy to answer!
I love researching this topic!



The other day you asked me this question:

I need an answer for the below for a company that employs over 50 employees but under 100: Employees electing health insurance this year would not receive a pay increase but would see a savings in health insurance coverage. Employees waving health insurance coverage would see an increase applied to their base rate. Is it legal for a company in PA of this size to pay employees in this manner?

I did some research and here's what I came up with:

For employees waiving health coverage, the employer cannot specifically increase their base rate. By incenting employees to waive health coverage, the employer has created a cash in lieu or opt out credit plan under Section 125.

The employer can't tie base compensation to health care enrollment. Employees can and will have mid-year health coverage changes which would make it difficult to reduce hourly rate. Instead, the employer can utilize the cash in lieu provision and pay taxable compensation more like a bonus (without affecting the regular hourly rate). If the employee enrolls mid-year in health coverage, the cash in lieu credit is removed.

More information:

An employer can incentivize or reward an employee for waiving the employer plan. The arrangement must be written in the employer's Section 125 plan and the compensation is taxable compensation. For an employer subject to the ACA Employer Shared Responsibility Provision, the opt out amount must be added to the employee contribution to determine affordability unless the employer complies with rules that the employee provides evidence there is other group coverage. More information on this is below.

Offering cash if an employee waives coverage is considered to be a "cash in lieu" or "opt out" credit. It would be additional taxable compensation. The employer can gross up the employee's salary to cover taxes.

The only way that an employer may offer an employee compensation for waiving coverage is through a "cash in lieu" provision which is part of the employer's Section 125 plan. These types of payments are also often known as waiver credits or opt out credits. When offered compliantly through a Section 125 plan, these payments must be taxed.

Example: Employee has a choice of electing Medical Plan A or receiving \$100/month cash (in addition to wages). If employee elects the cash, it is subject to all ordinary income taxes and employment taxes.

An established cafeteria plan must be created in accordance with IRS regulations (e.g., written plan; elections made prior to start of coverage period; no mid-year changes other than certain change-in-status events; nondiscrimination rules). For a cash in lieu provision, the employer cannot restrict the use of cash, i.e. they cannot say it must be used for benefits, etc. Additionally, in order to be valid, the option must be offered to all benefit eligible employees equally.

1.125-2: Cafeteria plans; elections.

- (a) *Rules relating to making and revoking elections—(1) Elections in general.* A plan is not a cafeteria plan unless the plan provides in writing that employees are permitted to make elections among the permitted taxable benefits and qualified benefits offered through the plan for the plan year (and grace period, if applicable). All elections must be irrevocable by the date described in paragraph (a)(2) of this section except as provided in paragraph (a)(4) of this section. An election is not irrevocable if, after the earlier of the dates specified in paragraph (a)(2) of this section, employees have the right to revoke their elections of qualified benefits and instead receive the taxable benefits for such period, without regard to whether the employees actually revoke their elections.

Section 125 2007 Proposed Regulations: <https://www.federalregister.gov/documents/2007/08/06/E7-14827/employee-benefits-cafeteria-plans#sectno-citation-%E2%80%891.125-2>

Applicable Large Employers subject to ACA Employer Shared Responsibility Provision:

Part of the ACA Employer Shared Responsibility Provision on providing affordable coverage (to not be possibly subject to a penalty) requires that a cash-in-lieu benefit (i.e., cash option under a cafeteria plan for employees that waive or opt out of health coverage) is counted as an additional employee cost for purposes of determining “affordability.” E.g., if self-only contribution is \$100 and cash-in-lieu benefit is \$50, the employee’s contribution is deemed to be \$150.

There was additional guidance on July 8, 2016 concerning the ACA affordability rules and opt-out (cash in lieu) credits. This information supplements [IRS Notice 2015-87](#) and can be relied on as of January 1, 2017. The opt-out credit amount does not have to be added to the employee only premium amount for the affordability calculation if the employee provides reasonable evidence that they have other minimum essential coverage (has to be a group plan, not individual plan).

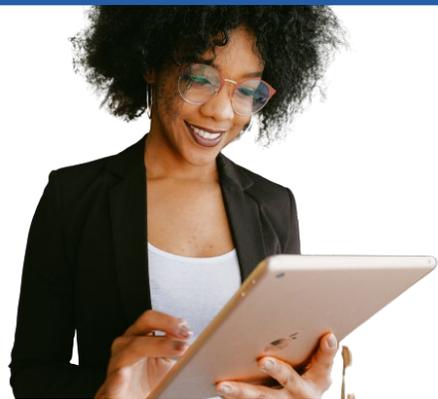
In [these proposed regulations](#), the IRS said when an employee waives medical coverage and receives an opt out credit if the employee provides reasonable evidence that they have other minimum essential coverage under a group plan (not individual coverage), this would eliminate the need to add the opt-out credit amount to the cost of employee self-only coverage to determine if the plan is [affordable](#). The proposed regulations are listed below.

If the plan does not follow the requirements to be a “eligible opt-out arrangement”, then the cash in lieu amounts are added to the employee only premium to determine affordability.

[July 8, 2016 proposed regulations \(page 44575\):](#)

Concerning reasonable evidence:

1. Employee provides “reasonable evidence” that the employee (and family members on employee’s tax return) have or are expected to have minimum essential coverage (MEC) during the period for which the opt-out is offered;
2. MEC can be group coverage, and most types of governmental coverage (e.g., Medicare), but cannot be individual coverage;
3. “Reasonable evidence” can be the employee’s attestation;
4. Reasonable evidence must be provided at least annually;
5. Reasonable evidence must be provided within a reasonable period (e.g., open enrollment, or after plan year starts); and
6. Employer cannot pay the opt-out benefit if employer knows or has reason to know that employee or family does not have/will not have MEC.



I do my best to make sure YOU are protected!
I always like to ask:

1. Have you and your employees taken *harassment prevention and diversity* training this year?
2. When was the last time you updated your *employee handbook*?

[Let's chat about it!](#)