# The “Cadillac Tax” is Rollin’ In!

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When healthcare reform was rolled out in 2010, there was a provision included in the law imposing a tax on healthcare benefits provided to employees that exceed a threshold cost. This tax has been referred to as the “Cadillac tax” since it is aimed at “high cost” health plans. The unfortunate impact of this tax is that many employers will have to actually reduce the level of health benefits that they provide to employees in order to avoid the tax.

The tax, scheduled to come into play in 2018, equals 40% of any “excess benefit” provided to an employee. Excess benefit is the cost of the “applicable coverage” of the employee for the month over the “applicable dollar limit” for the employee for the month. Recently, the IRS issued Notice 2015-16 seeking comments from the public regarding the details of this tax.

**What is Applicable Coverage?**

Applicable coverage means any plan of an employer or an employee organization that provides health care to the employees, former employees, the employer, others associated or formerly associated with the employer in a business relationship, or their families. The IRS expects that this would include the following types of plans:

- Medical plans
- Health Flexible Spending Arrangements (FSAs)
- Archer Medical Savings Accounts (MSAs)
- Health Savings Accounts (HSAs)
- Health Reimbursement Arrangements (HRAs)
- Governmental plans
- On-site medical clinics – with a possible exception for on-site medical clinics that provide only limited medical care
- Retiree health coverage
- Multiemployer plans
- Coverage for a specific disease or illness, and hospital indemnity or other fixed indemnity insurance, unless paid for with after-tax dollars
- Executive physical programs

The IRS is currently considering whether stand-alone dental and vision plans, and Employee Assistance Plans (EAPs), would be considered applicable coverage.

**How is the Cost of Applicable Coverage Determined?**

The cost of Applicable Coverage is determined under rules similar to those that apply for purposes of determining COBRA premiums. So, the cost would generally be based on the average cost of providing coverage to those employees under the plan who are similarly situated. It looks at both the employer’s cost and the employee’s cost. For example, if an insured medical plan has a premium equal to $800 per month, and the employer pays $300 of that premium, the cost of the coverage that would be used for the tax calculation would be the full $800. Since all plans do not have easily determined premiums, there are special rules being considered for self-insured plans, HRAs, and other types of plans.

The law requires that the cost of Applicable Coverage be calculated separately for self-only coverage and other-than-self-only coverage. Any coverage under a multiemployer plan will be considered other-than-self-only coverage. In addition, the law allows the plan to treat retired employees who have not reach age 65 and retired employees age 65 and older as

similarly situated participants.

**What is the Applicable Dollar Limit?**

There are actually two annual Applicable Dollar Limits for 2018 – $10,200 for an employee with self-only coverage, and $27,500 for an employee with other-than-self-only coverage. The determination of what type of coverage the employee has is based on the coverage that is provided to the employee as of the beginning of the month. In some cases, an employee may have both types of coverage simultaneously – such as family coverage under the employer's medical plan and self-only coverage under the on-site medical clinic. The IRS is considering how to handle this situation, but is proposing either using the coverage that accounts for the majority of the cost, or using a composite dollar limit determined by pro-rating the dollar limits for each employee according to the ratio of the cost of the self-only coverage and the cost of the other-than-self-only coverage provided to the employee. For multiemployer plans, all coverage is subject to the $27,500 limit since the coverage is automatically considered to be other-than-self-only coverage.

There are adjustments to these limits for certain factors. An additional amount is added to the dollar limit for "qualified retirees," which are any individuals who are receiving retiree coverage, are at least age 55, and are not entitled to, or eligible for, Medicare. An additional amount is also added to the dollar limits of individuals (including retirees) who participate in a plan sponsored by an employer, the majority of whose employees covered by the plan are engaged in high-risk professions, or employed to repair or install electrical or telecommunication lines. High-risk professions include police officers, fire fighters, paramedics and first-responders, longshoremen, and workers in the construction, mining, agriculture, forestry and fishing industries. Finally, the dollar limits may be increased by an employer for age and gender adjustments if the age and gender characteristics of an employer's workforce are different from those of the national workforce.

**Who is Responsible for Paying the Tax?**

Each "coverage provider" is responsible to pay its applicable share of the tax on the excess benefit. The employer is required to calculate the tax and determine what the applicable share is for each coverage provider. If the employer calculates the tax incorrectly or allocates the tax incorrectly to the coverage providers, the employer will be subject to a penalty of 100% of the error amount and underpayment interest.

To determine who the coverage provider is, you must look at the type of coverage: for fully insured coverage, it is the health insurance issuer; for HSA and MSA contributions, it is the employer; and for all other coverage, it is the person that administers the plan benefits. It is unclear from the law whether this means the ERISA plan administrator, or the third-party administrator. Keep in mind that taxes imposed on the health insurance issuer or a third-party administrator are likely to be passed on to the employer through increased premiums and fees.

**What Should You do Now?**

Although the tax on excess benefits does not go into effect until 2018, you should start looking at what health plans you have that will be included in the calculation. If it looks like the cost of these plans will exceed the stated thresholds, then you should start thinking about ways to reduce the cost, with ample time to implement changes and to inform employees how their coverage may be changing.

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