Davis Wright Tremaine LLP
DEFINING SUCCESS TOGETHER

Health Care Reform:
What Hospitality and Lodging Businesses Need to Know

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Unique Challenges to Hospitality

- How will health care reform impact the hospitality/lodging industry?
- Unique aspects of the industry:
  - Part-time/seasonal/low-wage employees
  - Franchisor requirements
  - Multiple facilities with joint ownership

Overview

- 2010 Changes
  - Adult Children
  - Tax Credit
  - Early Retiree Reinsurance
- 2011 Changes
  - Cafeteria Plans
  - Adult Children Coverage
  - Changes to Grandfathered and Nongrandfathered Plans

Overview (continued)

- Later Changes
  - Medicare Tax Increase
  - Information Reporting
  - State Exchanges
  - Coverage/Cost Sharing Requirements
  - Play or Pay Penalties
  - “Cadillac” Plan Tax

Adult Children

- If employer provides coverage for dependents, must continue to cover child until age 26 (effective for plan years beginning on or after 9/23/10)
- Value of any employer-provided health insurance coverage or medical expense reimbursement for an employee's child is excluded from employee's income through the end of the taxable year in which child turns 26 (effective 3/30/10)

Adult Children (continued)

- Applies regardless of child's marital status, residency and support
- Same application to self-employed health insurance deduction
- No FICA or FUTA on health coverage for a child under 27
- IRS guidance on April 27 (Notice 2010-38)

Adult Children (continued)

- Applies even if employer is not required to provide coverage
- Tax benefit extends beyond extended coverage requirement

Tax Credit

- Small businesses can take a tax credit for contributions for employee health insurance
- Section 45R of the Internal Revenue Code

Tax Credit (continued)

- Full credit for employer with 10 or fewer FTE employees with average wages of not more than $25,000
- Phased-out credit for employer with up to 25 FTE employees with average wages of not more than $50,000
- Disregard for FTE if work less than 120 days
- Multiple facilities - if a person owns several properties, or several entities, must aggregate employees

Tax Credit (continued)

- STEP 1: Compute FTE
  - Total full-time (at least 40 hrs/week) +
  - Total hours of part-time/2080

Do not count owners or family members

Tax Credit (continued)

- STEP 2: Compute average annual wages; divide total wages by number of FTE computed in STEP 1.

Tax Credit (continued)

- Employer must contribute at least half of premium cost
- Nonrefundable credit; claim on employer's tax return; carryback one year and carryforward 20 years, except no carryback for 2010
- For tax-exempt organization, deduct from income tax withheld from employee wages and Medicare tax (both employer and employee)

Tax Credit (continued)

- Effective 2010 for coverage purchased from health insurance company any time in 2010
- For years beginning 2014, credit available only if insurance purchased through a state exchange; only take credit for two years

Tax Credit (continued)

- For years through 2013, credit is 35% (25% for tax-exempt organizations) of lesser of (a) employer contribution for health insurance, or (b) average premium payment for the small group market in the state (Rev. Rul. 2010-13)
- For years beginning 2014, credit is 50% (35% for tax-exempt organizations)
- Deduction for contribution reduced by credit

Early Retiree "Reinsurance": Effective 2010

- Temporary program from June 1, 2010 to 2014; $5 billion limit
- Reimburses plan for 80% of retiree costs within range of $15,000 to $90,000
- Must be age 55 but not Medicare eligible
- Plans must apply, similar to Part D subsidy; HHS application out already
- Reimbursement must be used to lower cost of plan or cover increased cost

Cafeteria Plans: Effective January 1, 2011

- Need to implement before 1/1/11
- Health FSAs cannot reimburse for OTC drugs, unless prescribed
  - Affects open enrollment for most plans
- Cafeteria plans should be amended by 12/31/10 for elections for adult children
  - Retroactive to when offered
- Also FSA limit of $2,500 in 2013

Immediate Health Plan Changes Effective for Next Plan Year

- Many changes effective for plan year beginning after 9/23/10
- Means 1/1/11 for many, but could be as early as 10/1/10, or later in 2011
  - Need to be prepared by enrollment period
- Requirements vary depending on whether plan is “grandfathered”

“Grandfathered” Plans

- Promise that employees can keep current coverage
- Plan must be in effect March 30, 2010
  - Adding new members does not affect it
  - Status can be lost due to changes to carriers, employee cost-sharing
- Not a complete exemption, but affects which changes apply and when

Mandatory Adult Child Coverage

- Applies to grandfathered plans
- If plan covers children, must cover until child turns age 26
- Student, dependency status no longer matter; does not matter if married
- For grandfathered plans, must not be eligible for other employer coverage (until 2014)
- Not required to cover grandchildren
- Temporary regulations issued

Other Immediate Plan Changes

- All affect grandfathered plans
- No lifetime limits on “essential benefits”
- Annual limits only as allowed by regs to be issued by HHS, until 2014
- No pre-existing condition exclusions for children up to age 19
- No rescission except for fraud

Additional Changes if Not Grandfathered

- First dollar coverage for preventive care
  - Includes immunization and well baby care
- Section 105(h) nondiscrimination rules apply to insured plans
- Choose any primary provider, no preauthorization for emergency or OB/GYN
- Adult child coverage even if child eligible for other coverage

Change that could take effect in 2010 or 2011

- Auto-enrollment required for employers with more than 200 employees
- Must enroll in lowest cost option, after plan waiting period
- Notice and opportunity to opt out required
- Tied to when regulations are issued rather than plan year

Uniform Explanation of Benefits and Coverage

- Max. four pages describing plan coverage, including cost sharing, exceptions and limitations on coverage and whether minimum essential coverage is provided
- Deliver to all participants at time of initial enrollment and at annual enrollment
  - Within 60 days of effective date of changes
- Administrator provides for self-insured plan; insurer for insured plan

Uniform Explanation of Benefits and Coverage (continued)

- Penalty for failure to provide – up to $1,000 per failure
- Also new penalty on employers up to $100 per day, per participant failure
- Distribution deadline – 24 months after 3/23/10 (by 3/23/12)
- Duplication of SPD and SMM disclosures

“Simple” Cafeteria Plans

- Effective for years beginning after 12/31/10
- Safe harbor available to employers with 100 or fewer employees during either of two preceding years
  - If have 100 or less employees for a year, treated as meeting that requirement in later years
  - Cannot employ 200 or more employees during a later year

“Simple” Cafeteria Plans (continued)

- Automatically treated as meeting nondiscrimination rules
  - Traditional plans can’t discriminate in favor of highly compensated employees or key employees
  - Also nondiscrimination rules applicable to dependent care FSAs and group term life insurance
- Applicable for cafeteria plans and certain components
  - Health FSAs
  - Dependent Care FSAs
  - Group Term Life Insurance

“Simple” Cafeteria Plans (continued)

- Employer must contribute to provide qualified benefits on behalf of qualified employees for an amount equal to:
  - Uniform percentage of employee’s annual compensation (not less than 2%) or
  - Not less than the lesser of 6% of employee’s annual compensation or twice the amount of the salary reduction contributions of each qualified employee

“Simple” Cafeteria Plans (continued)

- All employees with 1,000 hours of service in prior year must be eligible and each eligible employee must be able to elect any benefit under the plan
  - Can exclude employees under age 21 and collectively bargained employees

“Simple” Cafeteria Plans (continued)

- Watch out for predecessors
- Model plan?

Increased Penalty for Nonqualified Withdrawals from HSAs

- Effective January 1, 2011
- Penalty for withdrawals from a health savings account not used for qualified medical expenses increases
  - 10% to 20% of withdrawal amount

W-2 Reporting

- Must disclose the aggregate value of the employer health benefits provided to each employee on Form W-2
- Value is calculated using rules for COBRA premiums
- Effective 2011
- Does <u>not</u> make benefit taxable to employee

Corporate Information Reporting

- Payments made to for-profit corporations for goods and services must be reported on Form 1099 if exceed $600 during the year
- Effective 2012
- Requirement for goods reporting for all payees, not just for-profit corporations

Medicare Tax Increase

- Additional Medicare tax on employee for wages in excess of
  - $250,000 married filing jointly
  - $125,000 married filing separately
  - $200,000 all other
- Not indexed for inflation
- Employer must withhold on wages in excess of $200,000 (even if married)

Medicare Tax Increase (continued)

- 0.9% of wages in excess of threshold
- Employer's share is not increased
- Also applies to self-employment tax, but half of this tax is not deductible
- Effective 2013

Medicare Tax Increase Investment Income

- Additional 3.8% tax on net investment income if exceed threshold
- Not to exceed the amount the modified adjusted gross income (MAGI) exceeds the threshold
- AGI increased by foreign earned-income exclusion to reach MAGI
- Employers have no reporting or withholding obligations
- Effective 2013

Medicare - Example

Single taxpayer has net investment income of $100,000 and modified adjusted gross income of $220,000.

The 3.8% tax is imposed on $20,000, the difference between the $200,000 threshold and $220,000 income.

Healthcare Information Reporting

- Certain employers must comply with new reporting requirements
  - Employers required to offer full-time employees minimum essential coverage (50+ FTE)
  - Employers offering minimum essential coverage and paying portion of cost, but only if required employee contribution exceeds 8% of any employee's wages
- Information on employer's health insurance plan and employees covered by the plan
- Effective 2014

State Exchanges

- Federal government to give states funding to establish exchanges
  - Help employers purchase health insurance coverage
- Beginning in 2014, small employers may purchase health insurance through the exchange
  - 100 or fewer employees

State Exchanges (continued)

- Beginning in 2017, larger employers may also purchase coverage through exchange if permitted by the state
- Employees can pay for coverage on pre-tax basis through cafeteria plan if employer is a "qualified employer"
  - Small employer electing to make all full-time employees eligible for coverage through an exchange

State Exchanges (continued)

- Health plans offered through an exchange must be certified “qualified health plans”
  - Must include essential benefits, such as emergency services, hospitalization, mental health and substance abuse and prescription drugs
  - Must satisfy limits on cost sharing
  - Either platinum, gold, silver, bronze or catastrophic plan

Notice of State Exchanges

- By March 1, 2013
- Employers must notify employees at time of hiring of:
  - The existence of state exchange
  - That employee may be eligible for a subsidy under the exchange if the employer's share of total costs of benefits is less than 60%
  - If employee buys policy through exchange, may lose employer contribution to coverage
- Model notice?

Coverage/Cost Sharing Requirements

- Effective for plan years beginning on or after January 1, 2014
- No preexisting condition exclusions or limitations for anyone
  - Previously only applied to persons under age 19
  - Still need certificates of creditable coverage?

Coverage/Cost Sharing Requirements (continued)

- No annual benefit limits on essential health benefits
  - Previously could impose “restricted annual limit” as permitted by HHS
- No waiting periods in excess of 90 days
  - Override current rules for enrollment of newborns and adopted children?

Coverage/Cost Sharing Requirements (continued)

Wellness Programs

- Increases maximum reward amount from 20% to 30% of cost of coverage
- Regulations may increase amount to up to 50%
- N/A to grandfathered plans

Coverage/Cost Sharing Requirements (continued)

- Insured small group health plans must offer essential health benefits
  - Deductibles cannot exceed $2,000 for single coverage; $4,000 for family coverage
    - Indexed for cost of living changes
    - N/A to grandfathered plans
  - Cannot require employee out-of-pocket expenses in excess of health savings account limits
    - Currently $5,950 (single coverage); $11,900 (family coverage)
    - N/A to grandfathered plans

Vouchers for Qualified Employees

- Effective 2014
- Employers that offer minimum essential coverage and make a contribution must give “qualified employees” a voucher
- Voucher can be used to buy coverage under a state exchange
- Value of voucher is the employer contribution to its plan

Vouchers for Qualified Employees (continued)

- "Qualified employee"
  - Household income exceeds 100%, but not more than 400% of federal poverty level
  - Required employee contribution for coverage under the employer plan exceeds 8% of income (but not more than 9.8% of income)
  - Limits indexed after 2014
  - Does not participate in employer plan

Vouchers for Qualified Employees (continued)

- Vouchers excludable from income (if used to pay for health care) and deductible by employer
- If several benefit plan options offered, amount of voucher is based on the option for which the employer pays the largest portion

Play or Pay Penalties

- No requirement that employer must provide health insurance, but potential penalty if do not provide minimum essential coverage to all full-time employees and their dependents
- No penalty for employer with less than 50 FTE employees (work 30 hours or more per week)

Play or Pay Penalties (continued)

- Part-time employees count for determining FTE, but no penalty for part-time
- Temporary employees count only if work more than 120 days

Play or Pay Penalties (continued)

- Example: 12 employees work 12 hrs/wk and 45 employees work 30 hrs/wk

12 employees x 25 hrs/wk x 4 wks = 1200 hrs/mo

	1200/120 hours (30 hrs x 4 wks)	=	10 FTE
+	45 employees work 30 hours/wk	=	45 FTE
	TOTAL:		55 FTE

Play or Pay Penalties (continued)

- Multiple facilities: if a person owns several properties, or several entities, must aggregate employees

  Example: Franchisee owns two hotel properties with 25 employees each, even if each property owned through a separate entity; considered as having 50 employees

Play or Pay Penalties (continued)

- Penalty imposed if fail to provide 60% of the cost of care, cost for employee exceeds 9.5% of any employee’s household income, and any employee receives subsidy from state exchange
- “Excise tax” and not deductible (IRC 4980H)

Play or Pay Penalties (continued)

- If fail to provide coverage: penalty is \$2,000 per employee per year for all employees, but not for the first 30 employees, pro rata per month
- Example: 12 part-time/45 full-time

  45 employees – 30 = 15 x \$2,000 = \$30,000

  No penalty for 12 part-time

Play or Pay Penalties (continued)

- If provide coverage but at least one employee receives a state exchange subsidy or credit: $3,000 penalty per such employee per year (NTE $2,000/year penalty), pro rata per month
- No penalty if provide free choice voucher

Play or Pay Penalties (continued)

- Penalties indexed for inflation
- No deduction for penalties
- Effective 2014

“Cadillac” Plan Tax

- Pushed out to 2018
- 40% excise tax on value of employer-sponsored coverage in excess of:
  - $10,200 (single) or $27,500 (family coverage)
  - Adjusted for inflation (before 2018 if > expected)
- Tax is determined by employer, imposed on employer or insurer if fully insured plan
  - Shared pro rata in partly insured plan

“Cadillac” Plan Tax (continued)

- What counts as employer coverage for tax?
- COBRA premium for accident and health coverage, even if employee pays after-tax
- Include health FSA and HSA contributions, whether by employer or employee deferral
- Exclude vision, dental, AD&D, long term care, employee-paid hospital and specific disease coverage

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