

# IRS Guidance Expands Access to ACA Premium Tax Credit, Allows Cafeteria Plan Sponsors to Permit Employees to Revoke Family Coverage Mid-year

by Karen K. Hartford on November 29, 2022

## Final Regulations under Section 36B of the Internal Revenue Code

On October 11, 2022, the Internal Revenue Service (IRS) issued Final Regulations under Code Section 36B relating to eligibility for the Affordable Care Act's ("ACA's") premium tax credit ("PTC" or "subsidy"). The Final Regulations expand eligibility for the PTC to certain family members of employees who were previously ineligible. Under Regulation Section 1.36B-1(d), an employee's "family" includes the employee's spouse filing a joint return with the employee and the employee's tax dependents.

Under the ACA, individuals generally will not qualify for a PTC if they are offered health coverage through an employer ("employer-based coverage"). Employer-based coverage may be offered by the individual's own employer or may be available to the individual on account of an individual's relationship to the employee, such as a spouse or child of the employee. There is an exception, however, that allows individuals to qualify for the PTC if their employer-based coverage is not "affordable." Prior to the issuance of the Final Regulations, employer-based coverage was deemed affordable provided the employee's premium cost for *self-only* coverage did not exceed 9.5 percent (adjusted annually for inflation) of the employee's household income. In other words, the determination of whether each covered individual's employer-based coverage was affordable was based on the employee's self-only cost, even if the employee elected higher cost family coverage and the cost for such coverage exceeded 9.5 percent (as adjusted) of household income. This methodology for determining the affordability of employer-based coverage for related individuals could result in the employee's family members being ineligible for a PTC, because often, while the cost of self-only coverage was affordable, the cost of family coverage was not. As a result, families in this situation found themselves being financially stretched or with family members going uninsured.

Beginning in 2023, the Final Regulations repair this so-called "family glitch" by basing the affordability of employer-based coverage for a family member on the cost of family coverage, rather than the cost of employee-only coverage, thereby making it possible for family members who are offered unaffordable family coverage to qualify for the PTC through the Health Insurance Exchange ("Exchange"). Stated another way, going forward employer-based coverage will be affordable for covered family members

only if the employee's cost for family coverage does not exceed 9.5 percent (as adjusted) of household income. Importantly, the affordability of coverage for employees will continue to be determined based on the cost of self-only coverage.

The Final Regulations are applicable to taxable years beginning after December 31, 2022.

### **IRS Notice 2022-41**

Companion guidance, in the form of [IRS Notice 2022-41](#), was also published on October 11, 2022. Notice 2022-41 permits sponsors of Code Section 125 cafeteria plans to amend their plans to permit employee-participants to revoke an election for group health plan family coverage mid-year and make a new election to drop one or more family members on a prospective basis, provided the following conditions are met:

(1) the dropped family member(s) are eligible to enroll in the Exchange, either during the annual enrollment period or a special enrollment period, and

(2) the employee-participant represents that the dropped family members have either already enrolled in Exchange coverage or intend to enroll in Exchange coverage immediately.

In 2022, the annual enrollment period for Exchange coverage begins November 1, 2022 and ends January 15, 2023. Special enrollment periods occur outside of that period on account of certain life events, which include, but are not limited to: losing other health coverage, getting married, having a baby or adopting a child.

Of note, the Notice states that this new mid-year election change opportunity is *not* available with respect to flexible spending arrangements.

When initially issued, Notice 2022-41 limited the application of this change to non-calendar year plans, but on November 9, the Notice was revised to remove the non-calendar year restriction; therefore, any cafeteria plan, regardless of plan year, may be amended to include the new mid-year election change event. For example, an employee who elected family coverage through their employer's calendar year cafeteria plan in December 2022, but learns in early January that their spouse and dependent children could elect Exchange coverage with a premium subsidy that would be less costly than the employer coverage, could make an election to drop the employer-based family coverage and instead elect single coverage, thereby permitting their family members to elect the more affordable Exchange coverage — all assuming the employer amends its cafeteria plan to permit this new mid-year election change.

As with all [IRS-approved mid-year Section 125 election change events](#), this new event is optional. In our experience, many plan sponsors choose to include all permissible mid-

year election change events in their plan documents to afford their employees maximum flexibility. Pursuant to Notice 2022-41, plan amendments are generally required by the end of the plan year in which the new election change event becomes operational, but there is a special rule for the 2023 plan year. For changes that affect a plan year beginning in 2023, amendments are not required until the last day of the first plan year that begins on or after January 1, 2024. For example, a plan with a plan year ending June 30 need not be amended until June 30, 2025. In all cases, amendments may be retroactive to the start of the plan year, so long as the plan is operated in accordance with the change and informs plan participants of the amendment. In no event, however, may participants revoke coverage on a retroactive basis.

We expect some employers may experience cost savings by allowing this mid-year change to drop family members, whether due to administrative savings resulting from fewer participants or due to claims savings. However, it is also possible that participants who found employer-based coverage for family members unaffordable simply never enrolled their family members, and employers will see no cost savings. In any case, it does seem that including this new mid-year election change opportunity in employer cafeteria plans is another step to help ensure that as many Americans as possible can enroll in health care at a reasonable cost.

Plan sponsors with questions about the Final Regulations or who wish to amend their cafeteria plan to permit this new election change event may contact any member of Verrill's Employee Benefits and Executive Compensation Group for assistance.



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