



Opt-Out Arrangements: Employer Compliance Considerations

Employers are often looking for ways to manage rising health care costs. One common approach they may consider is offering an opt-out arrangement to their employees. In such an arrangement, an employer offers a financial incentive or an opt-out payment to employees who waive employer-sponsored group health coverage. Employers may implement an opt-out arrangement with the idea that the cost of the opt-out payment will be less than cost of covering the employee on the group health plan. If an employer is considering an opt-out arrangement as a plan design, they should be aware of the various compliance issues and laws affecting these arrangements.

Implementing the Opt-Out Arrangement

One of the first steps an employer should take when implementing the opt-out arrangement is to decide which employees will be eligible for the opt-out payment and the actual amount of the opt-out payment. In general, it is advisable for the opt-out payment to be a uniform amount available to all eligible employees. If the employer's aim is to only offer the opt-out payment to employees who have high-cost claims, they should know that this would be prohibited under a variety of laws, including HIPAA which prohibits discrimination based on health status.

Secondly, opt-out arrangements should only be offered under the employer's Section 125 plan, which will require inclusion in the plan document. Note, however, that while this payment is a feature of the employer's Section 125 plan, the payments are taxable and must be treated as taxable income. Also, because opt-outs are a feature of the Section 125 plan, the nondiscrimination rules should be considered.

Lastly, employers should not offer an opt-out payment to encourage employees to purchase individual insurance policies, on or off the Marketplace. Doing so may create a group health plan that has to comply with the full array of laws governing employer-sponsored group health plans.

Types of Opt-Out Arrangements and ACA Affordability

The employer must decide what type of opt-out payment to make to their employees. The IRS has outlined three types of opt-out payments. If an employer is an applicable large employer (ALE), they will need to structure their opt-out payment properly to avoid inclusion of the opt-out payment in their ACA affordability calculations. The three types of opt-out arrangements include:

(1) Unconditional Opt-Out Payments

Employees do not have to offer proof of other coverage (whether through documentation or attestation) when waiving group health plan coverage to receive the opt-out payment.

(2) Conditional Opt-Out Payments

Employees must provide substantiation of other coverage (not including individual market coverage) in order to receive the payment after waiving coverage.

(3) Eligible Opt-Out Arrangements

This is the **only** type of arrangement where the opt-out payment would not increase the employee's cost of coverage and would therefore not need to be added to the plan's ACA affordability calculation. In order for the conditional opt-out payment to be considered an eligible opt-out arrangement, two requirements must be satisfied:

- (a) The opt-out payment must only be available to employees who decline employer sponsored minimum essential coverage, and
- (b) The employee must provide **reasonable evidence** that they and their "expected tax family" have or will have minimum essential coverage (MEC) **other than individual market coverage** (e.g., under a spouse's employer's plan) during the plan year covered by the opt-out arrangement. Employees can have Medicare Part A, CHIP and most Medicaid and TRICARE plans.

It is important to note that "reasonable evidence" of other coverage can include the employee's attestation of other coverage for employee and expected tax family (other than individual market coverage). Also, there is no requirement that the employer require any proof except an attestation from the employee. The employee and expected tax family must

attest to not having other coverage annually and the attestation can be obtained during open enrollment or the employer can allow employees to provide proof after the start of the plan year.

The Medicare Secondary Payer (MSP) Rules

Employers who are subject to the Medicare Secondary Payer (MSP) rules are prohibited from offering employees or family members eligible for Medicare any financial or other incentives to not enroll in the employer-sponsored group health plan. This raises the question—can employers offer an opt-out payment under a Section 125 to employees who are entitled to Medicare? HHS has informally indicated that if the opt-out payment is *offered equally to all employees* (regardless of Medicare eligibility) under a Section 125 plan, the opt-out payment **will not** violate the MSP rules. Note, however, that there is language in a CMS enforcement manual that diverges from HHS' informal comments slightly, at least for employees without primary coverage other than Medicare. Additional guidance from CMS on this subject would be welcome.

Next Steps

Employers thinking about offering an opt-out arrangement as a benefit strategy will want to make sure they structure their opt-out carefully, with the following compliance considerations.

- If an opt-out is offered in combination with a fully insured plan, check with the carrier to confirm that the opt-out payment does not violate any contractual agreement with the carrier;
- If an opt-out arrangement is offered in combination with a self-insured plan, be aware of potential 105(h) nondiscrimination issues, especially if a high number of non-highly compensated employees decline coverage and receive the opt-out payment;
- Make sure that offering an opt-out does not discourage healthy employees from enrolling in the plan or lead to lower plan participation overall if that is not your intended outcome;
- Ensure that the opt-out payment is offered under a Section 125 plan and amend the written Section 125 plan accordingly;
- Make certain that opt-out payments are uniformly offered to all eligible employees;
- If you are an ALE, verify that the opt-out arrangement is an “eligible opt-out arrangement” so the opt-out payment does not count towards your ACA affordability calculation.



ADDITIONAL RESOURCES

[Notice 2015-87](#)

[2016 Proposed Regulations](#)

**[Waiver of Coverage and Certification of Other Medical Coverage
\(Eligible Opt-Out Arrangement\)](#)**