ACA COMPLIANCE BULLETIN

Fixing the Family Glitch—Premium Tax Credit Eligibility

On Oct. 11, 2022, the IRS released a final rule that changes the eligibility rules for the premium tax credit (PTC) for family members beginning with the 2023 tax year. The PTC lowers monthly premiums for eligible individuals who purchase health insurance coverage through an Exchange. Individuals are not eligible for the PTC if they have access to affordable employer-sponsored health coverage.

Prior to 2023, the affordability of employer-sponsored coverage for family members was determined based on the lowest-cost self-only coverage available to the employee rather than the cost of family coverage. This "family glitch" made it more difficult for family members to receive a PTC. The final rule fixes the family glitch by basing the affordability of employer-sponsored coverage for family members on the cost of family coverage.

In connection with the final rule, the IRS issued Notice 2022-41 to expand permitted midyear election changes for Section 125 cafeteria plans. Beginning in 2023, employers may permit employees to revoke their elections for family coverage to allow one or more family members to enroll in an Exchange plan if certain requirements are met.

Impact on Employers

Beginning in 2023, more family members will likely be eligible for the PTC for coverage purchased through an Exchange. However, the affordability rules for employees continue to be based on the employee's required contribution for self-only coverage. This means that an employer's health coverage may be unaffordable for a family member even though it is affordable for the employee. Due to this change, employers may see some employees move from family coverage to self-only coverage.

In addition, employers that decide to expand their cafeteria plan's midyear election change events based on the IRS' new guidance should amend their plan documents by the applicable deadline.

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Highlights

- Beginning in 2023, the IRS changed the rules for determining if family members are eligible for the PTC for Exchange coverage.
- The new rules fix the "family glitch" for family members by basing the affordability of employer-sponsored coverage on family coverage instead of self-only coverage.
- The IRS also expanded the midyear election change rules for cafeteria plans to correspond with the new rules for family members.

Other ACA Rules

The new IRS guidance on the PTC does not affect:

- The ACA's "play or pay" rules for applicable large employers (ALEs)
- An ALE's use of affordability safe harbors under the "pay or play" rules
- ACA reporting under Internal Revenue Code (Code) Sections 6055 and 6056

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Premium Tax Credit

The premium tax credit, also known as PTC, is a refundable credit that lowers monthly premiums for eligible individuals who purchase health insurance through an Exchange. The amount of an eligible individual's PTC depends on his or her household income for the year, as estimated on the Exchange application. Eligible individuals can elect for advance payment of the PTC, where the Exchange sends the PTC directly to the insurance company, lowering how much eligible individuals pay each month in insurance premiums.

Individuals must meet certain eligibility requirements to qualify for the PTC. Individuals are not eligible for the PTC if they have **access to affordable employer-sponsored health coverage** that provides minimum value.

Affordability Determination

Employer-sponsored coverage is considered affordable if the employee's cost for self-only coverage does not exceed 9.5% (as adjusted annually) of the employee's household income for the tax year. For 2023, the adjusted affordability percentage is **9.12%**.

Fixing the Family Glitch

Before 2023, the affordability determination for employees and their family members was based only on the cost of self-only coverage. The cost of family coverage for family members was not considered, which made fewer family members eligible for reduced monthly premiums through an Exchange. Under the prior rules, if the cost of self-only coverage was no more than 9.5% (as adjusted annually) of the employee's household income, family members were not eligible for the PTC, even if family coverage costs more than 9.5% of household income. This eligibility issue was commonly referred to as the "family glitch."

Effective for 2023 and future tax years, the IRS revised the PTC eligibility rules for family members to fix the family glitch. Under the new PTC eligibility rules, an employer-sponsored plan is affordable for family members if the portion of the annual premium the employee must pay for family coverage (that is, the employee's required contribution) does not exceed 9.5% (as adjusted annually) of household income. Thus, for 2023, family members may be eligible for the PTC if the cost of family coverage is more than 9.12% of household income.

Impact on Employers

Because the family glitch has been fixed, more family members will likely be eligible for the PTC for coverage purchased through an Exchange. The affordability determination for employees continues to be based on the cost of self-only coverage. This means that, in some situations, an employer's health coverage may be unaffordable for family members even though it is affordable for the employee. Beginning in 2023, employers may see some employees move from family coverage to self-only coverage because family members are newly eligible for the PTC.

This new guidance does not affect the ACA's "pay or play" penalties for ALEs. Under the ACA's pay or play rules, ALEs (that is, employers with 50 or more full-time employees, including full-time equivalents) must offer affordable, minimum-value health coverage to their full-time employees or pay a penalty. These penalties are triggered only when an employee receives a PTC, not a family member. Thus, the PTC eligibility change for family members does not require ALEs to make any changes to the cost of family coverage.

The IRS has also confirmed that ALEs may continue to use the affordability safe harbors (federal poverty line, rate of pay and Form W-2) to determine whether self-only coverage is affordable to employees under the pay or play rules.

In addition, according to the IRS, this new guidance also does not impact an employer's reporting requirements under Code Sections 6055 and 6056. The IRS does not intend to revise Forms 1095-B or 1095-C to require any new data elements related to the new guidance.

Section 125 Cafeteria Plans—Midyear Election Changes

In tandem with fixing the family glitch, the IRS released Notice 2022-41 to expand the situations in which individuals can change their health coverage elections midyear under a Section 125 cafeteria plan. In general, employees' elections for pre-tax benefits are irrevocable during the plan year, unless an IRS exception applies. This new guidance, which is effective for elections made on or after Jan. 1, 2023, allows employees to revoke their elections for family coverage under employer-sponsored health plans so that one or more family members can enroll in an Exchange plan.

To qualify for the midyear election change, family members must qualify for a special enrollment period to enroll in an Exchange plan, or they must enroll during the Exchange's annual open enrollment period. Also, the employee's election to drop family coverage must correspond with the family member's Exchange enrollment. The Exchange coverage must be effective no later than the day immediately following the last day of the original revoked coverage. If the employee does not enroll in an Exchange plan, the employee must elect self-only coverage (or family coverage including one or more already-covered related individuals) under the group health plan. An employer may rely on the reasonable representation of an employee that the employee and/or family members have enrolled (or intend to enroll) in an Exchange plan within the required timeframe.

Employers that want to allow this new midyear election change event must update their cafeteria plan documents. In general, plan amendments must be adopted on or before the last day of the plan year in which the elections are allowed. However, for plan years beginning in 2023, the amendment may be adopted at any time on or before the **last day of the plan year that begins in 2024**.