Benefit Minute

October 2022

IRS Addresses the ACA Family Glitch

Since 2014, eligibility for ACA Marketplace premium tax credits for all family members of an employee has been determined based on whether the cost of employee-only coverage is affordable (i.e. not more than 9.61% of household income for 2022) and provides minimum value coverage to the employee. This is regardless of the additional cost to cover an employee's family members, which sometimes results in uninsured family members, a consequence referred to as the ACA family glitch. This will change in 2023 due to a new regulation issued by the Treasury Department and Internal Revenue Service. The change is viewed as "family-friendly" because it is more likely to provide all family members with access to affordable health coverage.

Overview of the Final Regulation

This situation where employee-only coverage is affordable, but family coverage is not affordable, is fairly common. While most employers offer family coverage, many do not subsidize it at the same level as employee-only coverage, which keeps the cost high for employees who cover family members. The final regulation states that eligibility of an employee's spouse and dependent children to receive ACA premium tax credits will be based on the affordability of the offer of family coverage through the employer group health plan. Family coverage includes any applicable tier other than employee-only.

Although the ACA requires an employer to offer coverage to an employee's children to the end of the month in which the child turns age 26 regardless of the dependency status of the child, the final regulation specifies that the cost of providing coverage to non-dependent children is not considered when determining affordability. This will be applicable when the coverage tiers are tied to a specific number of dependents (employee + one, employee + two, etc.) and a non-dependent child is covered.

Clarification of Minimum Value

In addition to the affordability test, the final regulation also makes a similar change to the rules for determining whether employer coverage provides minimum value. The coverage offered to an employee's spouse and dependent children must provide minimum value (in addition to being affordable at the appropriate coverage tier) to disqualify the family members from eligibility for a Marketplace premium tax credit. A health plan provides minimum value if the plan's share of the total allowed costs of benefits provided is at least 60% and the plan provides substantial coverage of inpatient hospital services and physician services.

Impact on ACA Employer Mandate and Reporting

The final regulation does not expand an employer's obligations under the employer mandate. An employer is not required to make an offer of affordable minimum value coverage to family members to avoid ACA penalty exposure. As long as an employer offers at least one group health plan that provides minimum value and is affordable based on the cost for employee-only coverage, an employer will continue to be insulated from ACA employer mandate penalties.

For now, there is no change to an employer's ACA reporting obligation on Form 1095-C. The employer will continue to report the monthly cost of employee-only coverage for the lowest cost minimum value plan offered. While the employee cost of the applicable coverage tier will be used to determine family members' eligibility for Marketplace premium tax credits, it will be the responsibility of those individuals to provide the cost of employer-sponsored coverage for the family to the Marketplace.

New Section 125 Election Change Option

In conjunction with the expanded Marketplace premium tax credits that will be available as of January 1, 2023, the IRS has issued guidance that permits an additional election change opportunity. A section 125 cafeteria plan may allow an employee to make a mid-year election change to drop a covered spouse and/or dependent children so they can enroll in Marketplace coverage. This includes Marketplace enrollment at open enrollment or due to a special enrollment opportunity. The family members must enroll in Marketplace coverage. This new election change is optional, not required. Employers with non-calendar year cafeteria plans should consider adding this election change opportunity so that an employee's family members can enroll in Marketplace coverage during the current open enrollment period.

To allow the new permitted election change, the cafeteria plan must be amended. An employer must adopt the amendment on or before the last day of the plan year in which the new election change is allowed, and the amendment may be retroactive to the first day of that plan year. However, for 2023, an employer may amend the cafeteria plan at any time on or before the last day of the plan year that begins in 2024.

How Will This Affect Enrollment in Employer-sponsored Plans?

There is uncertainty about the rule's impact on enrollment in employer-sponsored plans, but it is not expected to be significant. One estimate indicates that the number of individuals with subsidized Marketplace coverage could increase by about one million. This includes both uninsured individuals and dependents moving from employer-sponsored coverage to Marketplace coverage. Not all family members are expected to enroll in subsidized Marketplace coverage simply because it is available. Many employees might prefer to have all family members remain on a single plan rather than have the family split between employer-sponsored coverage and Marketplace coverage. Enrollment in two separate plans means separate premiums, deductibles, out-of-pocket maximums, and provider networks that might also be expensive or unwieldy for a family to navigate.

Some employers with lower wage workers may still be inclined to dramatically increase the cost of dependent coverage to drive spouses and dependent children to the Marketplace. However, such an increase would likely have to apply to employees at all compensation levels because doing this only for low wage employees (who would more often benefit from the end of the family glitch) could result in a contribution strategy that is discriminatory under IRS rules.

For employers that want to communicate this change to their employees during open enrollment, the federal government intends to provide outreach materials that will be accessible to individuals and employers. However, it is unlikely that these materials will be available to employers in advance of their open enrollment period for January 1, 2023.

Effective Date

Absent legal challenges in the interim, the final regulation is effective December 1, 2022. This means that the enhanced premium tax credits will be available for Marketplace coverage as of January 1, 2023. Marketplace open enrollment for 2023 begins on November 1, 2022.