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# Rewards Policy Insider
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## IRS Announces End to Special Pandemic Rule for HSA Compatible HDHPs

High-deductible health plans can continue providing below-the-deductible coverage of COVID-19 diagnostic testing and treatment and still be compatible with Health Savings Account (HSA) eligibility rules, but only for plan years ending on or before December 31, 2024. According to IRS Notice 2023-37, the special relief that was extended at the start of the pandemic is no longer needed.

## Overview

In general, in order for an individual to be eligible to contribute to an HSA, they must be covered by a high-deductible health plan (HDHP) and no other health plan that is not an HDHP. Subject to certain exceptions, including one for preventive care, an HDHP may not provide any coverage below the minimum required deductible.

The Families First Coronavirus Response Act (FFCRA) and the Coronavirus Aid, Relief, and Economic Security (CARES) Act established certain mandates for group health plans regarding coverage of COVID-19 testing during the COVID-19 Public Health Emergency. In general, plans were required to cover COVID-19 tests and testing-related services without any cost-sharing, prior authorization, or other medical management requirements.

Separately, early in the pandemic the IRS issued Notice 2020-15 to establish a special, temporary rule permitting HDHPs to provide coverage for COVID-19 testing and treatment.

The coverage mandates ended when the Public Health Emergency ended, on May 11, 2023. The relief provided by Notice 2020-15, previously scheduled to remain in effect "until further guidance is issued," will no longer apply to plan years ending after December 31, 2024.

## Telehealth Safe Harbor

Also during the pandemic, Congress amended Code section 223 to provide a temporary safe harbor for HDHPs to cover telehealth services without a deductible. This special safe harbor has been extended twice and is currently set to expire for plan years beginning on and after January 1, 2025.

On June 7, 2023, the House Ways and Means Committee favorably reported a bill – the Telehealth Expansion Act (H.R. 1843) – that would extend the telehealth safe harbor permanently. It is not clear if, or when, the full House will act on the bill.

A companion bill (S. 731) has been introduced in the Senate.

# IRS Provides Guidance on Income and Employment Tax Treatment of Fixed-Indemnity Wellness Plan

A recent IRS Chief Counsel Memorandum (CCM) advises that a fixed-indemnity wellness plan that pays a $1,000 per month benefit to participants who participate in certain specific health and wellness activities, regardless of whether they incur any out-of-pocket medical expense, results in taxable income to the employee and wages for various employment tax purposes. The result is the same regardless of whether the employer funds the premiums or the employee pays them via a Code section 125 plan salary reduction election.

The CCM was issued almost exactly one month before the IRS published proposed regulations that would apply the same standard to all fixed-indemnity health plans, including hospital only and specified disease coverage. The proposed regulations will be discussed in more detail in the next Rewards Policy Insider.

## Overview

The fixed-indemnity wellness program ("Program") at issue charges a $1,200 per month premium that is funded either directly by the employer or by employee salary reduction contributions through a Code section 125 plan. Participation is voluntary and is available to employees regardless of whether they have other comprehensive group health coverage. The Program offers three categories of benefits:

- A $1,000 payment for each month the employee participates in certain health and wellness activities;
- Wellness counseling, nutrition counseling, and telehealth benefits; and
- A per diem benefit for each day the employee is hospitalized.

Covered employees can qualify for the $1,000 per month benefit by obtaining certain preventive services – such as vaccinations – that are fully paid for by other comprehensive group health coverage. In other words, the $1,000 monthly benefit is payable regardless of whether employees incur any out-of-pocket medical expenses.

The insurance company pays the wellness benefit to the employer, who then makes the monthly benefit payment to employees through its payroll system.

## Issues and Conclusions

The CCM specifically addresses only the following two questions:

- Are the Program's wellness indemnity payments includible in employees' gross incomes?
- If so, are these payments "wages" for purposes of the Federal Insurance Contributions Act (FICA) taxes, Federal Unemployment Tax Act (FUTA) taxes, and federal income tax withholding (FITW) – collectively "employment taxes"?

The answer to both questions, according to the CCM, is "yes." Although Code section 105(b) provides a gross income exclusion for employer payments to reimburse employees for "medical care" expenses, the CCM notes that the section 105(b) exclusion "does not apply to amounts which the taxpayer would be entitled to receive irrespective of whether the expenses are incurred for medical care."

In this situation, the Program does not require employees to actually incur any medical care expenses to qualify for the benefit payment. And even if an employee does incur some medical care expenses, there is no relationship between the amount of expenses incurred and the benefit payment amount.

The CCM also concludes that these benefit payments are "wages" for employment tax purposes because no statutory or regulatory exclusion would apply.

Note that the CCM does not address the income or employment tax consequences of the Program's hospital indemnity benefit or the free counseling and telehealth services.

### Implications

Previous CCM's and related IRS sub-regulatory guidance have addressed similar plan designs and reached the same basic conclusions. Nonetheless, the fact the IRS issued this CCM indicates that there continues to be insurers, brokers, and others promoting these types of products. Employers should remain vigilant and, if necessary, seek appropriate professional guidance whenever they are considering a health-related product that that is being marketed for its tax benefits.

## IRS Proposes Changes to the Corporate Bond Yield Curve Methodology for Defined Benefit Plans

The Internal Revenue Service ("IRS") is proposing changes to the method of developing the corporate bond yield curve, which is used in the calculation of minimum funding standards and lump sum distributions for qualified defined benefit ("DB") plans. The proposed changes would generally retain the current methodology but make some modifications to reflect changes in the bond market in recent years.

## Background

DB plans must meet minimum funding requirements described in section 412 of the Internal Revenue Code ("Code"). In addition to the rules under section 412, Code section 430 specifies rules for funding standards that apply to single-employer DB plans. Under section 430, the funding target of a plan in a plan year is the present value of all benefits accrued or earned under the plan as of the beginning of the plan year. Section 430 also contains rules for the interest rates to be used in connection with funding standards. These interest rates – called segment rates – are used to determine a plan's funding target and target normal cost for a plan year.

The corporate bond yield curve is used to determine the interest rates for calculating present value, as well as other calculations under a DB plan. The corporate bond yield curve is prescribed by the Treasury Department monthly and reflects the average of monthly yields on certain corporate bonds within a 24-month period. Instead of using segment rates, a plan sponsor can elect to use the interest rates set by the corporate bond yield curve to determine the plan's minimum required contribution. However, once this election is made it can only be revoked with the IRS's consent.

The methodology that the Treasury Department uses to develop the yield curve is provided in IRS Notice 2007-81. In general terms, the Notice provides that the yield curve is calculated by compiling market data on certain bonds and making adjustments based on a bond's credit rating.

## Proposed Changes

On June 23, 2023, the IRS released new proposed regulations to make modifications to the methodology used to develop the corporate bond yield curve. The proposed regulations generally continue to follow the existing methodology that is laid out in Notice 2007-81. However, the proposed regulations would make two key changes that take into account changes in the bond market since the release of Notice 2007-81.

First, the proposed regulations would apply a new adjustment factor to the existing factors used to determine spot rates (i.e., the current price at which an asset can be acquired for an immediate settlement). Spot rates are used in the calculation of the corporate bond yield curve. The new factor, called a "hump adjustment variable," would allow the yield curve to reflect the effect of a rate hump in spot rates that is often seen with bonds that are at 20 years' maturity.

Second, callable bonds (i.e., bonds that allow the issuer to redeem before the maturity date) would be included in the bond data set used to develop the corporate bond yield curve, provided that the call feature is exercisable only during the last year before maturity. In the proposed regulations, the Treasury Department explains that this type of call feature has become more widely used in recent years, and including these types of bonds in the yield curve will result in a larger pool of bonds that more accurately reflects the market for high quality corporate bonds.

The proposed regulations would also amend the existing regulations to reflect the addition of interest rate stabilization relief that was enacted by the American Rescue Plan Act of 2021, as well as to eliminate prior transition rules that do not apply anymore. Public comments on the proposal can be submitted through August 22, 2023.

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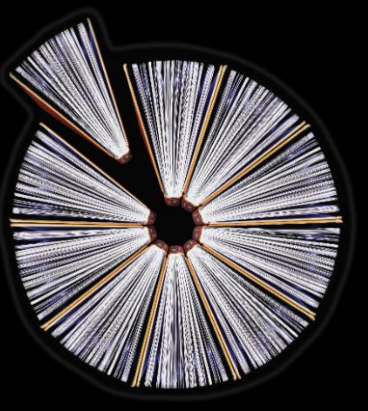

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