

# IRS STATES EMPLOYERS NOT EXPOSED TO ACA PENALTIES FOR MAKING CASH PAYMENTS IN LIEU OF HEALTH BENEFITS AS PERMITTED UNDER THE SERVICE CONTRACT ACT

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**Practices & Industries**

Employee Benefits

In June, the IRS issued an information letter indicating that federal contractors subject to prevailing wage laws will receive credit for making cash payments to employees who opt out of health insurance coverage when determining whether such health coverage is affordable. The IRS provided this clarification in response to an inquiry from a Congressperson on behalf of a constituent who was an applicable large employer for purposes of complying with the Affordable Care Act's (ACA) employer mandate, but was also subject to a Service Contract Act (SCA) prevailing wage determination.

The SCA requires federal contractors to comply with the terms of a DOL wage determination by providing specified wages and qualifying fringe benefits. The SCA permits federal contractors subject to such fringe benefit obligations to allow employees who opt out of health coverage to receive cash in lieu of health benefits.

The ACA provides that an applicable large employer's obligation to provide affordable health coverage limits the employer to receiving credit for contributions only if such amounts are exclusively used to pay for medical expenses. Hence, cash offered in lieu of health benefits is generally disregarded in computing the amount of an employer's contribution that may be included when calculating whether health coverage is affordable. As a result, the amount of cash-out payments to employees who opt out of coverage is added to the total premium price when determining whether the coverage is affordable.

The IRS letter restates the special transition rule from Notice 2015-87 allowing employers subject to the SCA to include employer cash-out payments as part of the employee's required contribution for purposes of determining the affordability of such coverage under Code Section 4980H(b). Thus, offering the choice of a cash-out payment to employees will not require an SCA employer to pay a greater share of the cost of coverage to avoid affordability penalties.

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Although IRS Notice 2015-87 applies this rule for coordinating the ACA and SCA for plan years before January 1, 2017, the IRS letter indicates that the executive order directing agencies to minimize the burden of ACA compliance allows the IRS discretion to continue applying the special treatment of SCA cash-out payments when determining compliance with the ACA's affordability mandate. *IRS Information Letter 2018-0013*.