

Health Promotion Program Legal Update: Q2 – 2021 (April 21, 2021)

Barbara J. Zabawa, JD, MPH

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CENTER FOR
HEALTH AND
WELLNESS LAW,
LLC

Wellness Incentives and Taxes, Cafeteria Plans and HSAs

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Agenda

Tax Laws and Health and Wellness

Nondiscrimination Rules (Health Plan Contributions)

- Cafeteria Plans
- Noncafeteria Plans

Case Examples

Q&A

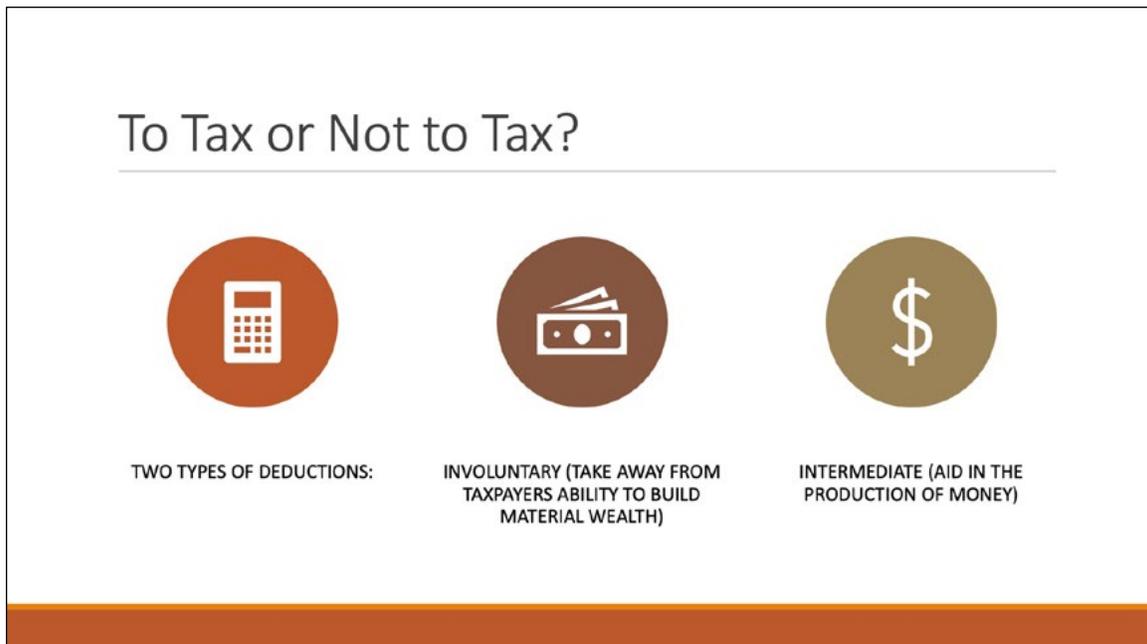
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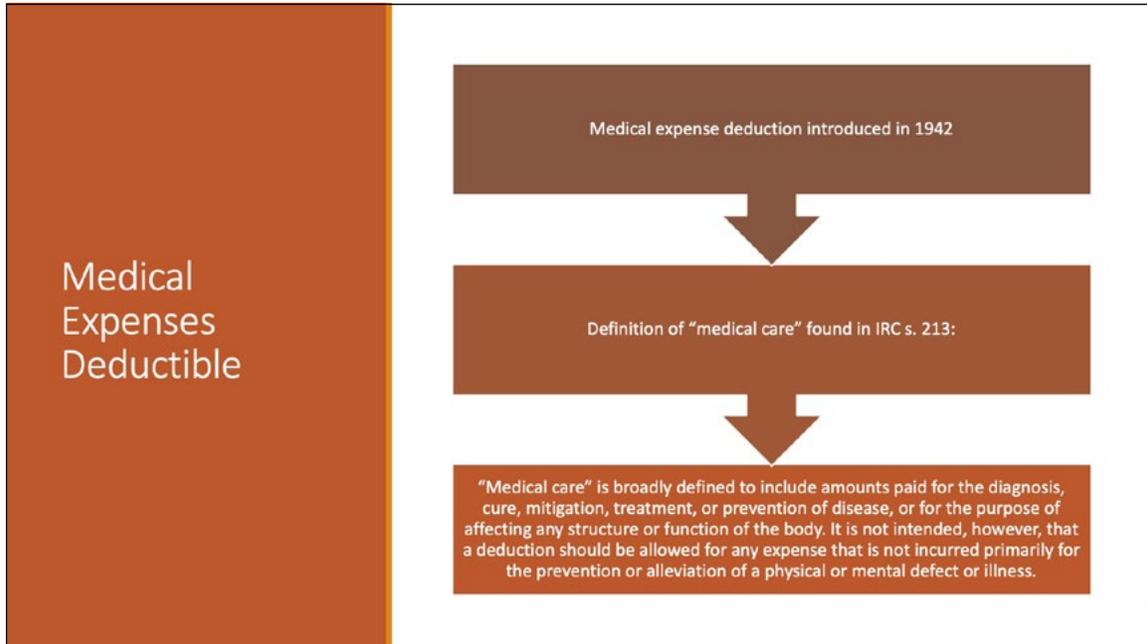
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Medical Expenses Deductible

Employer reimbursements of:

- health club dues
- costs of weight loss or nutrition programs

generally subject to tax.

Treat the reimbursement as income and add the fair market value of the wellness expense to Box 1 on Form W-2.

Such expenses may be tax deductible if taxpayer can show that expense was to treat a specific disease, prescribed by physician and would not have been incurred but for the disease.

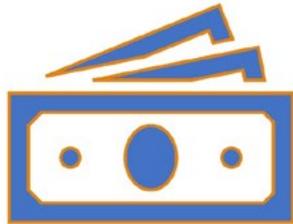
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What About *Preventing Disease?*

IRS has stated:

"Expense qualifies as medical care as preventing disease only if a *present existence or an imminent probability* of developing a disease, physical or mental defect, or illness exists."

Adopting healthy lifestyles to stave off illness or disease that may occur in the far distant future, NOT MEDICAL CARE.



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De Minimis Benefits Not Taxable

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Cash or Cash Equivalents Always Taxable

Gift cards = Cash

Cash can never qualify as de minimis

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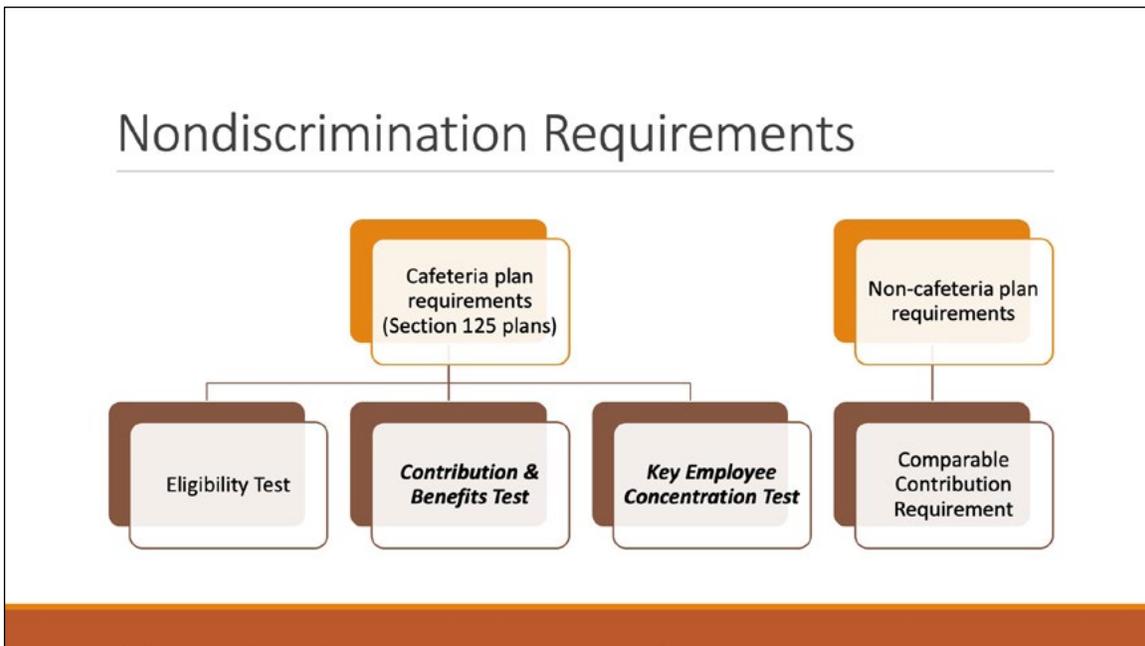
Health Coverage Contributions

Employer contributions:

- FSAs
- HRAs
- HSAs

Can be excluded from income tax BUT must comply with nondiscrimination requirements

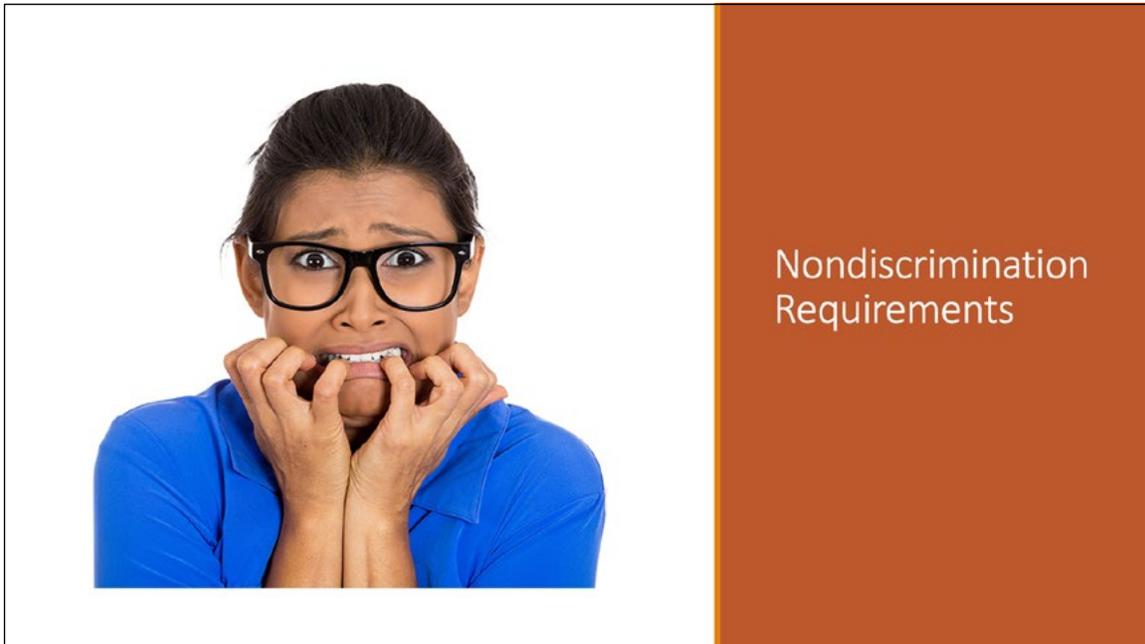
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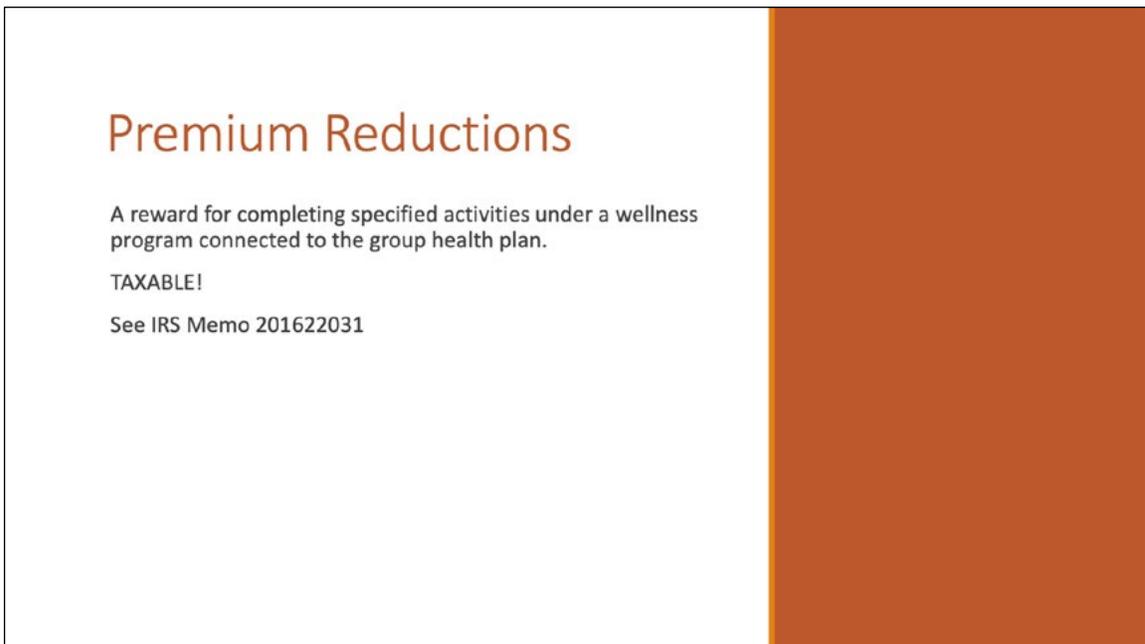
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Tax Withholding Responsibility

Where a third party (such as a health insurer for an insured group health plan) administers (in more than a “ministerial way”) a wellness program that provides a taxable incentive (e.g., cash or a gift card), the third party may be deemed the “statutory employer” for purposes of complying with related income and employment tax withholding and Form W-2 reporting responsibilities (in contrast to the general rule that imposes these obligations upon the common law, or “true,” employer).

- See IRC s. 3401(d).

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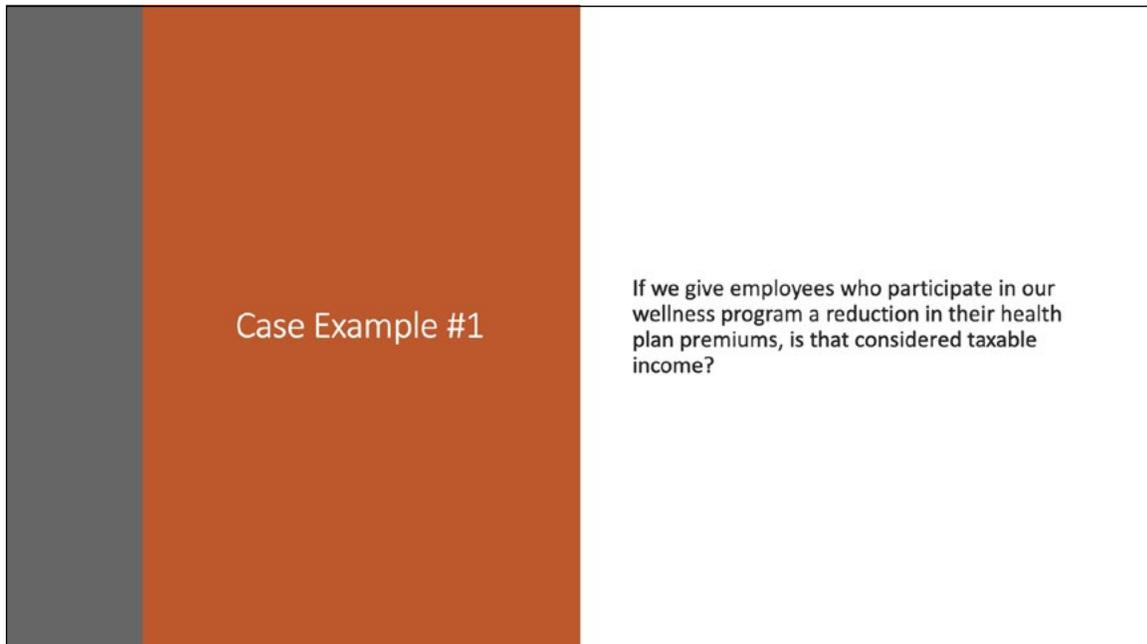
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Case Examples

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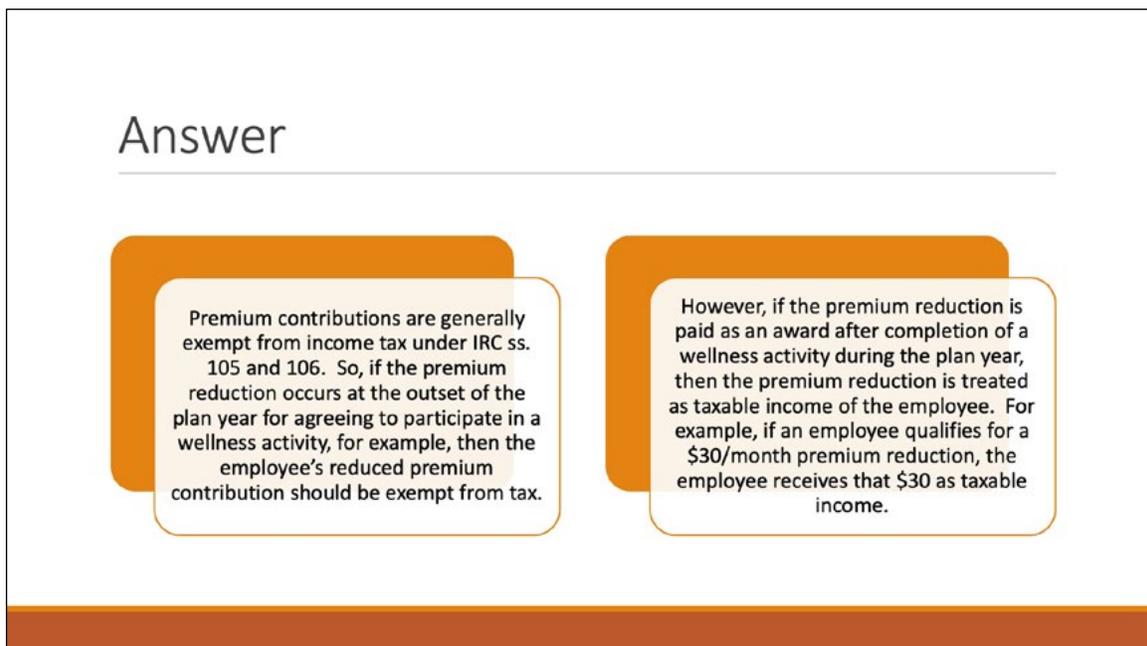
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Case Example #1

If we give employees who participate in our wellness program a reduction in their health plan premiums, is that considered taxable income?

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Answer

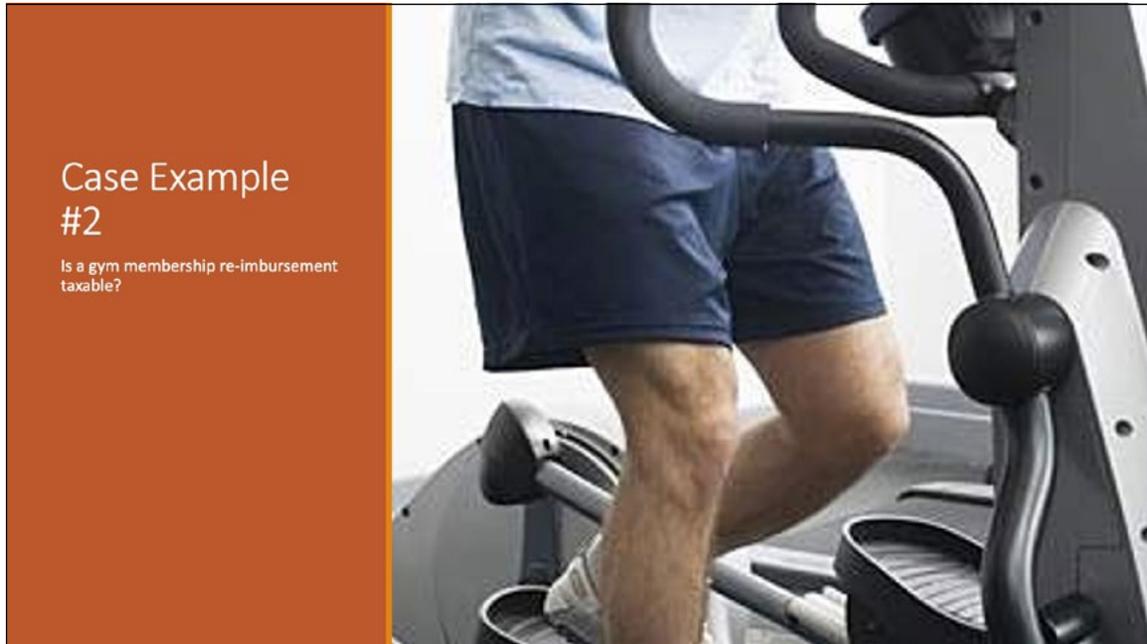
Premium contributions are generally exempt from income tax under IRC ss. 105 and 106. So, if the premium reduction occurs at the outset of the plan year for agreeing to participate in a wellness activity, for example, then the employee's reduced premium contribution should be exempt from tax.

However, if the premium reduction is paid as an award after completion of a wellness activity during the plan year, then the premium reduction is treated as taxable income of the employee. For example, if an employee qualifies for a \$30/month premium reduction, the employee receives that \$30 as taxable income.

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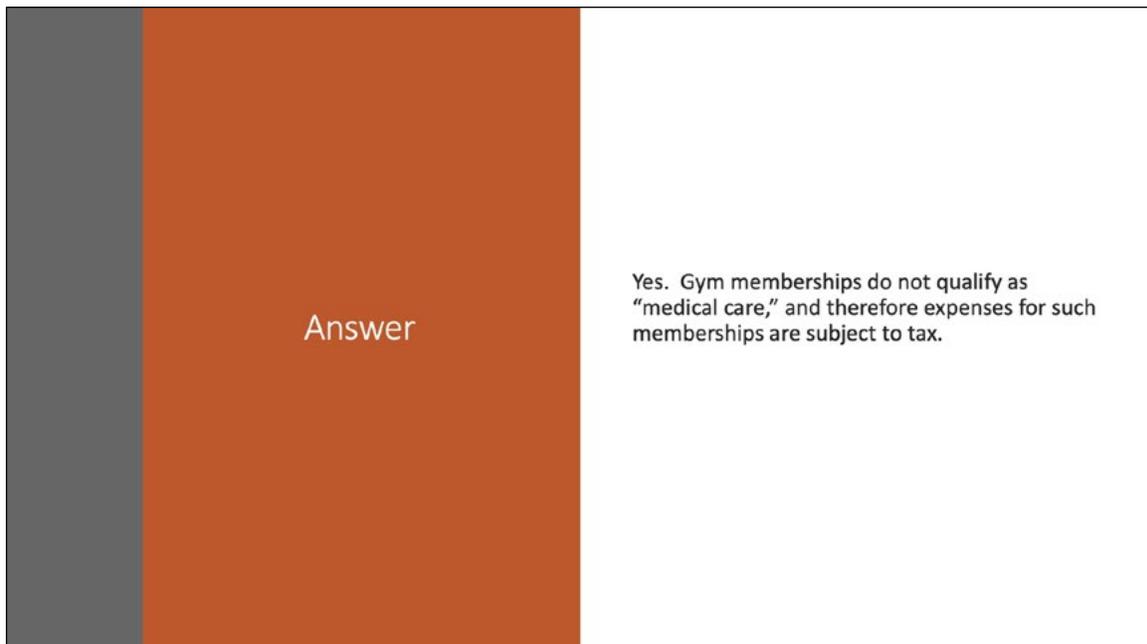
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Case Example
#2

Is a gym membership re-imbusement taxable?

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Answer

Yes. Gym memberships do not qualify as “medical care,” and therefore expenses for such memberships are subject to tax.

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	<h2>Case Example #3</h2>	<p>How can you tax incentives earned if the employee has been termed from the company?</p>
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	<h2>Answer</h2>	<p>Individuals who earn income on their own, such as wellness incentives, should report that income on their taxes. See https://www.irs.gov/uac/reporting-miscellaneous-income.</p>
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Case Example #4

My insurance carrier offers incentives for completing various task. The incentives are available via a catalog. I've utilized those incentives and I've never been taxed. Some of the items are well over \$100. Should I be taxed on some of those incentives?

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Answer

Yes, it sounds like some of those items should have been subject to tax because the items are not de minimis fringe benefits. See <https://www.irs.gov/government-entities/federal-state-local-governments/de-minimis-fringe-benefits>

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Case Example #5

An employee completes a reasonable alternative standard during the plan year and therefore earns a reward through the wellness program, which is a reduction in premium. Is an employer with a section 125 plan prohibited from making premium changes during the year?

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Answer

Perhaps prospectively. Under 26 CFR s. 1.125-4(f)(2), "if the cost of a qualified benefits plan increases or decreases during a period of coverage and, under the terms of the plan, employees are required to make a corresponding change in their payments, the cafeteria plan may, on a reasonable and consistent basis, automatically make a prospective increase or decrease in affected employees' elective contributions for the plan." Thus, prospective changes to an employee's premium payment seem to be allowed. As for retroactive rewards/premium reductions, IRS Memorandum No. 201622031 states that employers may reimburse employees for all or a portion of the premiums paid by salary reduction, however that reimbursement from the employer is taxable and must be included in the employee's gross income.

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Case Example #6

As a reward for completing a menu of wellness activities, an employer with a cafeteria plan makes a contribution to the employee's HSA equal to 1% of the employee's salary. Is this contribution taxable? Is it permissible?

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Answer

No, it is not taxable. It may not be permissible, however, if the cafeteria plan nondiscrimination rules are violated. At issue may be the key employee test, which is failed if key employees receive more than 25% of the aggregate nontaxable benefits under the cafeteria plan. Because this reward is set up as a percentage of income, those employees with higher incomes (and most likely to be "key employees") may receive more than 25% of the aggregate nontaxable benefits under the cafeteria plan. A flat amount may be a safer option.

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Case Example #7

An employer wants to contribute to an employee's HSA that is not part of a cafeteria plan. Employees would earn the contribution if they complete certain wellness activities. Can the employer structure its wellness incentive this way?

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Answer

No. Because the HSA is not part of a cafeteria plan, the employer must follow the non-cafeteria plan nondiscrimination rules, which are "comparable contribution" requirements. To satisfy those requirements, the employer would need to make the same contribution amount on behalf of all "comparable" employees (i.e., all employees who are full-time, or part-time, as examples), regardless of whether they participated in the wellness program. This effectively negates the "incentive" aspect of the wellness program.

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Case Example #8

InsureU offers to ABC Company a defined benefit wellness program for which employees pay premiums, pre-tax via salary reduction. The premiums are paid to participate in the employer's wellness program, not to purchase other insurance. These premiums are excluded from employees' wages, reducing employment and income taxes. The wellness plan then pays employees a cash reward for participating in wellness activities like health screenings, healthy eating programs, exercise programs, and meeting with a health coach. Are the rewards for participating in the wellness activities taxable?

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Answer

Yes. The reimbursement is for the pre-tax premiums the employees paid, and this is taxable according to Rev. Ruling 2002-3 and IRS Memo 2016-22031.

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Case Example #9

ABC Manufacturing offers health insurance to its employees through InsureYou Health Insurance Company. InsureYou offers an employee wellness program that issues cash incentives to group health plan employees who complete certain wellness activities. InsureYou decides which employees qualify for the incentives and issues those incentives once earned. ABC Manufacturing is not involved in the program at all. Does InsureYou have any tax withholding and Form W-2 reporting responsibilities with regard to ABC Manufacturing group health plan employees?

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Answer

Very likely. InsureYou is doing more than ministerial administration of the wellness program. Rather, it decides who earns the reward and distributes the reward.

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Q&A REMINDER

The following Q&A session does NOT constitute legal advice and should not be used as such. It is for educational purposes only.

WELCOA Members should retain legal counsel to obtain definitive answers.

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Questions?

For more information, contact:

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