

5 ROADS FOR  
**HEALTHCARE  
REIMBURSEMENTS**  
BY CHURCHES  
AND MINISTRIES



FEBRUARY 2015

*Enhancing Trust*



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**HEALTHCARE  
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*The purpose of this publication is to present highly focused information on the healthcare reimbursement aspects of the Affordable Care Act (ACA) based on the information available as of the date of this publication (February 1, 2015). This text is provided with the understanding that ECFA is not rendering legal, accounting, or other professional advice or service. Professional advice on specific issues should be sought from an accountant, lawyer, or other professional.*

*ECFA expresses sincere appreciation to attorneys Danny Miller and Allison Gardner of Conner & Winters, LLP for their valued assistance in reviewing the information included in this resource.*

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# INTRODUCTION

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By now, most smaller churches and ministries across America are probably aware they are exempt from the employer mandate of the Affordable Care Act (ACA) because they have fewer than 50 full-time equivalent employees (FTEs).<sup>1</sup> That's the good news.

The bad news: Without even knowing it, many of these same organizations may be subjecting themselves to **penalties of up to \$100 per employee, per day** for making voluntary healthcare payments on behalf of employees (i.e., for individual policy premiums or other out-of-pocket medical costs) that do not comply with ACA market reforms. These onerous penalties became effective for health plan years beginning on or after **January 1, 2014**, so care must be taken now to understand and follow the existing guidance.

## *Background*

For decades, it has been the common practice of many smaller churches and ministries that are unable to offer group health insurance coverage to assist employees with the cost of their individual health insurance coverage (see page 3) and/or other out-of-pocket medical expenses (see page 4). Employers would pay these costs directly on behalf of employees or provide employees with reimbursements after incurring the expenses. If certain formalities were followed, generally these arrangements were blessed by the IRS and even allowed on a tax-free basis for employees.

That all changed recently as the result of the issuance of certain guidance relating to the ACA market reforms. When the ACA guidance was initially issued related to reimbursements,<sup>2</sup> it was clear that the tax-free reimbursement of individual healthcare insurance premiums would trigger an excise tax of \$100 per employee, per day. However, many people interpreted the initial guidance as permitting the employer to avoid ACA excise tax problems if they reimbursed the individual healthcare insurance premiums on a post-tax basis.

A year later, the government issued additional guidance<sup>3</sup> clarifying (changing its position) that an employer is not permitted to reimburse individual healthcare insurance premiums on either a pre- or post-tax basis. That means employers who adjusted their practices to align with the initial guidance by paying after-tax reimbursements may have incurred excise tax liability and should discontinue these payments or reimbursements on either a pre- or post-tax basis.

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1 Or less than 100 FTEs through 2015.

2 IRS Notice 2013-54 published on September 13, 2013.

3 "FAQs about Affordable Care Act Implementation (Part XXII)" prepared jointly by the Departments of Labor (DOL), Health and Human Services (HHS), and the Treasury published on November 6, 2014.

## ***Excise tax liability***

Smaller churches and ministries are most likely to be impacted by these penalties. This is because employers with 100 or more full-time equivalent employees (FTEs) are subject to the ACA mandate to provide qualified group coverage to employees beginning with their 2015 health plan year. Similarly, employers with 50 FTEs must provide group health coverage beginning in 2016.

Employers subject to excise taxes under the market reform rules are required to self-report on IRS Form 8928. Employers have the option to enter “0” for the excise tax due if they believe the failure to comply was due to reasonable cause and not due to willful neglect, and the failure was corrected during the 30-day period beginning on the first date anyone liable for the tax knew, or exercising reasonable diligence would have known, that the failure existed.<sup>4</sup>

Organizations that may be affected by these penalties should consult with their professional advisors immediately for guidance on any potential liability for past noncompliant reimbursements and to properly structure future healthcare plans and payments.

## ***Exceptions***

For employers without a group healthcare plan, there are still a few exceptions to the general rules discussed above. The following types of employer healthcare payments/reimbursements on behalf of employees remain exempt from the ACA market reforms:

- One-participant<sup>5</sup> health plans
- Accident-only coverage
- Disability income
- Certain limited-scope dental and vision benefits
- Certain long-term care benefits
- Benefits under an employee assistance program, if the program does not provide significant benefits in the nature of medical care treatment and satisfies certain additional requirements

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4 While employers may avoid the full excise tax penalties due to reasonable cause, the government may still demand some type of minimum tax payment from the employer under Internal Revenue Code Section 4980(D) depending on the circumstances. Organizations should consult with their professional tax advisors before filing Form 8928.

5 The exact language from the IRS guidance is a “group health plan that has fewer than two participants.” The IRS has informally indicated that an employer could not set up a separate health plan for each of its employees and fall within the exception. In addition, an employer with more than one employee that limits coverage under the reimbursement arrangement to one employee may violate certain nondiscrimination requirements applicable to group health plans.

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## ROAD 1: Employer Pays for Individual Health Insurance Coverage

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The payment/reimbursement of individual health insurance policy premiums was a very popular option in the past for smaller churches and ministries that desired to help employees with rising health care costs but could not afford group coverage.

Now, unless an exception applies (see page 2), individual health insurance coverage payments or reimbursements are generally subject to the ACA market reform excise taxes of up to \$100 per employee, per day.

*Example 1:* A church with more than one employee does not offer group health insurance coverage to its employees. Instead, the church reimburses the policy premiums incurred by its pastors and other staff members. Regardless of whether the reimbursements have been made on a pre- or post-tax basis, the church must stop the reimbursements immediately because they do not comply with the market reforms of the ACA and may be subject to penalty taxes of up to \$100 per employee, per day.



*Example 2:* The same facts as Example 1, except the church has only one employee, so it falls within an exception to the ACA market reforms. The reimbursements of the individual health insurance policy premiums would be tax-free to the employee and not result in excise tax penalties to the organization.



### **Summary**

If church and ministry employers have been paying or reimbursing the cost of individual health insurance policy premiums for employees (on a pre- or post-tax basis), they should STOP immediately and consult with their professional tax advisors on appropriate next steps. Not only would payments under these plans presumably constitute taxable income to employees, but even more importantly, they may subject the organization to significant tax penalties for noncompliant reimbursements. (Note: This represents a major shift from what has been common practice at many smaller employers over the last several decades.)

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## ROAD 2: Employer Pays Out-of-Pocket Medical Expenses (Not in Conjunction with Group Coverage)

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Some churches and ministries may suggest the idea of simply reimbursing the out-of-pocket medical expenses (e.g., doctors' fees, prescriptions, over-the-counter medical items, deductibles, co-pays, etc.) that their employees incur throughout the year instead of providing health insurance coverage. Unfortunately, the ACA market reforms also preclude this sort of arrangement from being a viable alternative (unless an exception on page 2 applies).

Payments/reimbursements of out-of-pocket medical expenses are not permitted unless an employer sponsors a formal health reimbursement arrangement (HRA) or health flexible spending account (FSA) *in conjunction with* a qualified group healthcare plan that meets ACA requirements (see page 8).

*Example 1:* A church with more than one employee does not offer group health insurance coverage to its employees. Instead, the church has been reimbursing the out-of-pocket medical expenses incurred by its pastors and other staff members throughout the year. Regardless of whether the reimbursements have been made on a pre- or post-tax basis, the church must stop the reimbursements immediately because they do not comply with the market reforms of the ACA and may be subject to penalty taxes of up to \$100 per employee, per day.

*Example 2:* The same facts as Example 1, except the church has only one employee. Reimbursements of the out-of-pocket medical expenses may be tax-free to the employee and may not result in excise tax penalties to the organization. Organizations should consult with their professional tax advisors for guidance.



### **Summary**

If church and ministry employers have been paying or reimbursing out-of-pocket medical expenses of their employees without a formal plan offered in conjunction with qualified group health insurance coverage, they should STOP immediately and consult with their professional tax advisors on appropriate next steps. Not only would payments/reimbursements of out-of-pocket medical expenses presumably constitute taxable income to employees, but even more importantly, they may subject the organization to significant tax penalties for noncompliant reimbursements. (Note: This represents a major shift from what has been common practice at many smaller employers over the last several decades.)

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## ROAD 3: Employer Makes No Healthcare-Related Payments

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A perfectly acceptable alternative for smaller churches and ministries is to make no healthcare-related payments whatsoever for their employees because they are not within the reach of the ACA's employer mandate,<sup>6</sup> which would otherwise require them to offer group coverage or pay a tax penalty.<sup>7</sup>

Some employers that have stopped making payments or reimbursements for individual health insurance coverage (see page 3) or out-of-pocket medical expenses (see page 4) that were allowed before the ACA may be able to offset the economic reality of the discontinued reimbursements to employees by increasing overall taxable compensation without tying the raise to required payments for health care.

For instance, an employer could tell all eligible employees that they are discontinuing any healthcare-related payments and increasing all eligible employees' pay by \$X per month. Employees are then free to use (or not to use) this money to purchase individual coverage on the Marketplace (perhaps qualifying for a subsidy) or through a private health insurance provider. However, offering that \$X per month only to those who buy coverage would be prohibited.

Employees could also set aside a portion of the additional taxable compensation to help pay for their other out-of-pocket medical costs incurred throughout the year and itemize medical expenses on Schedule A of their tax returns if these expenses exceed 10% of adjusted gross income for the year.

*Example:* A ministry with more than one employee that was previously reimbursing individual health insurance policy premiums for its staff has discontinued these payments to avoid penalties for noncompliant reimbursements under the ACA market reforms. To help offset the economic reality of these discontinued reimbursements to employees, the ministry chooses to increase taxable compensation without tying these raises to required payments for healthcare. The ministry's actions should not result in excise tax penalties based on the latest ACA market reform guidance.



### **Summary**

Increasing overall taxable compensation to employees without tying the raises to healthcare-related payments may be attractive to some smaller employers as a way to avoid penalties associated with noncompliant reimbursements and to offset the economic burden to employees who are no longer allowed to receive reimbursements (taxable or tax-free) for healthcare-related costs.

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<sup>6</sup> Employers with 50 to 99 full-time equivalent employees (FTEs) must fulfill certain reporting obligations concerning health coverage beginning in 2015; however, they have until 2016 to comply with the coverage requirements or pay tax penalties.

<sup>7</sup> Notwithstanding, individual employees would still need to comply with the individual mandate.

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## ROAD 4: Employer Pays for Group Health Insurance Coverage

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Even though smaller churches and ministries are not subject to the employer mandate, they may still continue to offer group healthcare coverage for their employees.<sup>8</sup> Group coverage can be obtained through the Small Business Health Options Program (SHOP) Marketplace or through a private insurer.

While this option may be too cost prohibitive for some organizations, it also comes with some of the best tax advantages for employers and employees. Additionally, employers may be entitled to a health care tax credit to offset the cost of providing group coverage if certain conditions are met (see [Health Care Tax Credits for Smaller Churches and Nonprofits](#) in the ECFA Knowledge Center for more information).

The tax benefits of offering group health insurance coverage to employees<sup>9</sup> include the following:

- Employers do not face penalties for noncompliant reimbursements.
- Payments of group premiums do not represent taxable income to employees.
- Once group coverage is offered, employers also have the option to establish tax-advantaged health care payment arrangements, such as HRAs and health FSAs.



### ***Health Flexible Spending Accounts (FSAs)***

An employer can sponsor a formal health FSA, funded on a pre-tax basis from employee compensation, without being subject to the ACA market reform rules and penalties if provided in conjunction with a qualified group healthcare plan that meets ACA requirements.

### ***Health Reimbursement Arrangement (HRA)***

An employer can sponsor a formal HRA without being subject to the ACA market reform rules and penalties if provided in conjunction with a qualified group healthcare plan that meets ACA requirements.

*Example:* A ministry offers qualified group health care coverage to its employees. The payments are tax-free to employees and do not result in severe ACA excise tax penalties to the ministry. The ministry may also offer a health FSA or an HRA that is properly integrated with its group health insurance plan.

### ***Summary***

Providing qualified group health insurance coverage to employees offers the most tax advantages of all the options, but it also may be too cost prohibitive for some smaller churches and ministries, depending on coverage needs and availability.

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<sup>8</sup> This discussion assumes the coverage represents a qualified group health plan meeting the requirements of the ACA.

<sup>9</sup> Some churches and ministries may not offer group coverage to their own employees but instead reimburse the cost for employees to participate in a group plan offered through the spouse's employer.



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## ROAD 5: Non-Insurance Arrangements: Health Care Sharing Ministries

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Finally, some churches and ministries may consider a non-insurance arrangement: participation by their employees in health care sharing ministries. One of the most attractive features of health care sharing ministries is that they provide participants with an exemption from the individual mandate and its related penalties.

However, there are a few other important considerations for employers and employees to keep in mind with respect to this approach.

- Payments/reimbursements for employees' participation in health care sharing ministries may constitute taxable compensation to employees because the arrangements do not meet the traditional definition of qualified group health insurance coverage.
- Similarly, employers may be unable to pair HRAs or FSAs with health care sharing ministries because they do not meet the traditional definition of qualified group health insurance coverage.
- Finally, it is also unclear whether employer payments/reimbursements for employees' participation in health care sharing ministries are subject to the ACA market reform excise taxes.

*Example:* A church with more than one employee does not offer group health insurance coverage to its employees. Instead, the church reimburses the costs incurred by its pastors and other staff members to participate in a health care sharing ministry. It is unclear whether these payments represent taxable income to employees. The payments may also subject the church to excise tax penalties under the ACA market reforms. There is also no published guidance concerning whether the church may offer an HRA or FSA in conjunction with the health care sharing ministry.

Organizations considering the option of health care sharing ministries should review the tax implications with the health care sharing organization and their professional advisors.

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## CONCLUSION

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We hope this resource has brought greater clarity to the maze of issues and alternatives surrounding healthcare reimbursements under the ACA. There are a number of important factors to consider when evaluating which option may be best suited for your church or ministry. We highly recommend seeking the advice of professional counsel to assist in your decision-making and to help guard against possible liability exposure for noncompliance.

**Return of Certain Excise Taxes Under Chapter 43 of the Internal Revenue Code**  
(Under sections 4980B, 4980D, 4980E, and 4980G)  
Information about Form 8928 and its separate instructions is at [www.irs.gov/form8928](http://www.irs.gov/form8928).

OMB No. 1545-2148

**Filer's tax year beginning** \_\_\_\_\_ and ending \_\_\_\_\_

**A** Name of filer (see instructions) \_\_\_\_\_

**B** Filer's employer identification number (EIN) \_\_\_\_\_

Number, street, and room or suite no. (if a P.O. box, see instructions) \_\_\_\_\_

City or town, state or province, country, and ZIP or foreign postal code \_\_\_\_\_

**C** Name of plan \_\_\_\_\_

**D** Name and address of plan sponsor \_\_\_\_\_

**E** Plan sponsor's EIN \_\_\_\_\_

**F** Plan year ending (MM/DD/YYYY) \_\_\_\_\_

**G** Plan number \_\_\_\_\_

**Part I Tax on Failure To Satisfy Continuation Coverage Requirements Under Section 4980B**  
Complete a separate Part I, lines 1 through 6, for failures due to reasonable cause and not to willful neglect, and a separate Part I, lines 12 through 14, for other failures, for each qualifying event for which one or more failures to satisfy continuation coverage requirements that occurred during the reporting period (see instructions).

**Section A - Failures Due to Reasonable Cause and Not to Willful Neglect**

	For IRS Use Only	
<b>1</b> Enter the total number of days of noncompliance in the reporting period . . . . .	1	
<b>2</b> Enter the number of qualified beneficiaries for which a failure occurred as a result of this qualifying event . . . . .	2	3
<b>3</b> If you entered 2 or more on line 2, multiply line 1 by \$100 . . . . .		4
<b>4</b> If the failure was not discovered despite exercising reasonable diligence or was corrected within the correction period and was due to reasonable cause, enter -0- here, and go to line 5. Otherwise, enter the amount from line 3 on line 6 and go to line 7 . . . . .		5
<b>5</b> If the failure was not corrected before the date a notice of examination of income tax liability was sent to the employer and the failure continued during the examination period, multiply \$2,500 by the number of qualified beneficiaries for whom one or more failures occurred (multiply by \$15,000 to the extent the violations were more than <i>de minimis</i> for a qualified beneficiary). If the failures were corrected before the date a notice of examination was sent, enter -0- . . . . .		6
<b>6</b> Enter the smaller of line 3 or line 5 . . . . .		7
<b>7</b> If there was more than one qualifying event, add the amounts shown on line 6 of all forms, and enter the total on a single "summary" form. Otherwise, enter the amount from line 6 above . . . . .		8
<b>8</b> Enter the aggregate amount paid or incurred during the preceding tax year for a single employer group health plan or the amount paid or incurred during the current tax year for a multiemployer health plan to provide medical care . . . . .		9
<b>9</b> Multiply line 8 by 10% (.10) . . . . .		10
<b>10</b> Amount from section 4980B(c)(4) . . . . .		11
<b>11</b> Enter the smallest of lines 7, 9, or 10. For a third-party administrator, HMO, or insurance company, the amount you enter on this line filed for all plans you administer during the same tax year cannot exceed \$2 million; reduce the amount you would otherwise enter on this line to the extent the amount for all plans would exceed this limit . . . . .		12

**Section B - Failures Due to Willful Neglect or Otherwise Not Due to Reasonable Cause**

<b>12</b> Enter the total number of days of noncompliance in the reporting period . . . . .		13
<b>13</b> Enter the number of qualified beneficiaries for which a failure occurred as a result of this qualifying event . . . . .		14
<b>14</b> If you entered 2 or more on line 13, multiply line 12 by \$200. Otherwise, multiply line 12 by \$100. . . . .		15
<b>15</b> If there was more than one qualifying event, add the amounts shown on line 14 of all forms, and enter the total on a single "summary" form. Otherwise, enter the amount from line 14 above . . . . .		16

**Section C - Total Tax Due Under Section 4980B**

**16** Add lines 11 and 15 . . . . . **126** **16**

Cat. No. 37742T Form 8928 (Rev. 12-2013)

For Paperwork Reduction Act Notice, see instructions.

Filer's EIN: \_\_\_\_\_ Page 2

**Requirements Under Section 4980D**  
Cause and not to willful neglect, and a separate Part II, for each qualifying event for which one or more failures to satisfy continuation coverage requirements that occurred during the reporting period (see instructions).

	For IRS Use Only	
<b>17</b> Enter the total number of days of noncompliance in the reporting period . . . . .	17	
<b>18</b> Enter the number of qualified beneficiaries for which a failure occurred as a result of this qualifying event . . . . .		19
<b>19</b> If you entered 2 or more on line 18, multiply line 17 by \$100 . . . . .		20
<b>20</b> If the failure was not discovered despite exercising reasonable diligence or was corrected within the correction period and was due to reasonable cause, enter -0- here, and go to line 21. Otherwise, enter the amount from line 19 on line 22 and go to line 23 . . . . .		21
<b>21</b> If the failure was not corrected before the date a notice of examination of income tax liability was sent to the employer and the failure continued during the examination period, multiply \$2,500 by the number of qualified beneficiaries for whom one or more failures occurred (multiply by \$15,000 to the extent the violations were more than <i>de minimis</i> for a qualified beneficiary). If the failures were corrected before the date a notice of examination was sent, enter -0- . . . . .		22
<b>22</b> Enter the smaller of line 20 or line 21 . . . . .		23
<b>23</b> If there was more than one qualifying event, add the amounts shown on line 22 of all forms, and enter the total on a single "summary" form. Otherwise, enter the amount from line 22 above . . . . .		24
<b>24</b> Enter the aggregate amount paid or incurred during the preceding tax year for a single employer group health plan or the amount paid or incurred during the current tax year for a multiemployer health plan to provide medical care . . . . .		25
<b>25</b> Multiply line 24 by 10% (.10) . . . . .		26
<b>26</b> Amount from section 4980D(c)(4) . . . . .		27
<b>27</b> Enter the smallest of lines 23, 25, or 26. For a third-party administrator, HMO, or insurance company, the amount you enter on this line filed for all plans you administer during the same tax year cannot exceed \$2 million; reduce the amount you would otherwise enter on this line to the extent the amount for all plans would exceed this limit . . . . .		28

**Section C - Total Tax Due Under Section 4980D**

**34** Add lines 28 and 33 . . . . . **127** **34**

**Part III Tax on Failure To Make Comparable Archer MSA Contributions Under Section 4980E**

**35** Aggregate amount contributed to Archer MSAs of employees within calendar year . . . . . **35**

**36** Total tax due under section 4980E. Multiply line 35 by 35% (.35) . . . . . **128** **36**

**Part IV Tax on Failure To Make Comparable HSA Contributions Under Section 4980G**

**37** Aggregate amount contributed to HSAs of employees within calendar year . . . . . **37**

**38** Total tax due under section 4980G. Multiply line 37 by 35% (.35) . . . . . **137** **38**

**Part V Tax Due or Overpayment**

**39** Add lines 16, 34, 36, and 38 . . . . . **39**

**40** Enter amount of tax paid with Form 7004 . . . . . **40**

**41** Tax due. Subtract line 40 from line 39. If less than zero, enter -0-, and go to line 42. If the result is greater than zero, enter here and attach a check or money order payable to "United States Treasury." Write your name, identifying number, plan number, and "Form 8928" on your payment . . . . . **41**

**42** Overpayment. Subtract line 39 from line 40 . . . . . **42**

**Sign Here**

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Your signature \_\_\_\_\_

Print/Type preparer's name \_\_\_\_\_ Preparer's signature \_\_\_\_\_ Telephone number \_\_\_\_\_ Date \_\_\_\_\_

Firm's name \_\_\_\_\_ Date \_\_\_\_\_ Check  if self-employed PTIN \_\_\_\_\_

Firm's address \_\_\_\_\_ Firm's EIN \_\_\_\_\_ Phone no. \_\_\_\_\_