I. Background
   A. The Patient Protection and Affordable Care Act (P.L. 111-148) (ACA)
      i. Enacted March 23, 2010
      ii. Includes Sec. 9010 (Imposition of Annual Fee on Health Insurance Providers)
      iii. Effective January 1, 2014
   B. Amended by the Health Care and Education Reconciliation Act of 2010 (P.L. 111-150) (HCERA)
      i. Enacted March 30, 2010
   C. ACA Sec. 9010 is not part of the Internal Revenue Code

II. Proposed Regulations
   B. Public comments due: June 3, 2013
      i. 89 comments received
   C. Public hearing: June 21, 2013

III. Department of the Treasury and Internal Revenue Service (IRS)
   B. Plan is to issue final regulations

IV. Sec. 9010 imposes an annual fee (Annual Fee) on all insurance companies in the business of providing Health Insurance for U.S. health risks.
   A. An insurance company that is subject to the Annual Fee is referred to as a Covered Entity.
   B. The IRS is responsible for administering and enforcing Sec. 9010 and collecting the Annual Fee.

V. Sec. 9010 specifies the total Annual Fee revenue to be collected from all Covered Entities for each calendar year.
   A. 2014 $ 8.0 billion
   B. 2015 11.3 billion
   C. 2016 11.3 billion
   D. 2017 13.9 billion
   E. 2018 14.3 billion
F. After 2018, the total Annual Fee revenue to be collected will be the amount of the prior year’s Annual Fee increased by the rate of premium growth as defined in Internal Revenue Code (IRC) § 36B(b)(3)(A)(ii) (relating to indexing of the premium assistance credit).
   i. Each Covered Entity must determine the Annual Fee on a calendar year basis, even if it has adopted a different fiscal year.

VI. The amount of Annual Fee each Covered Entity owes is its proportionate share of the total U.S. health insurance market for the preceding calendar year.
   A. Several exceptions and exclusions apply.

VII. Compliance
   A. By May 1st of each year, each Covered Entity must file Form 8963 (Report of Health Insurance Provider Information) reporting the amount of Net Premiums Written in the immediately preceding calendar year.1
   B. Although a Covered Entity is not liable for the Annual Fee unless its Net Premiums Written in a preceding calendar year are more than $25 million, a Covered Entity must file Form 8963 each year, even if the Net Premiums Written in the preceding calendar year are less than $25 million.
      i. A Covered Entity that fails to file Form 8963 may be subject to penalties.
   C. IRS will calculate the Annual Fee each Covered Entity owes.
   D. Preliminary Fee Calculation
      i. IRS will send each Covered Entity a Preliminary Fee Calculation that includes the following information:
         (a) The Covered Entity’s apportioned Annual Fee
         (b) The Covered Entity’s Net Premiums Written for Health Insurance of U.S. health risks
         (c) The Covered Entity’s Net Premiums Written for Health Insurance of U.S. health risks taken into account after the application of the Statutory Exclusion
         (d) The aggregate Net Premiums Written for Health Insurance of U.S. health risks taken into account for all Covered Entities
         (e) A reference to the error correction procedures published by the IRS in the Internal Revenue Bulletin (IRB)²
      ii. The IRS intends to publish guidance as to the date by which it will send each Covered Entity a Preliminary Fee Calculation³
   E. Error Correction Report

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1 As of the date of this outline, the IRS had not yet released Form 8963 either in draft or final form.
2 As of the date of this outline, the IRS had not yet published these procedures.
3 As of the date of this outline, the IRS had not yet published this information.
i. After reviewing this information, each Covered Entity can submit an Error Correction Report to IRS identifying any errors.

ii. The IRS will be publishing guidance addressing:
   (a) The format for the submission of Error Correction Reports, and
   (b) The date by which a Covered Entity must submit an Error Correction Report.

F. Final Fee Calculation

i. By August 31st of each year, the IRS will send each Covered Entity a Final Fee Calculation of the Annual Fee the Covered Entity owes for the preceding calendar year.

ii. The IRS will base its final calculation on:
   (a) The Forms 8963 submitted by each Covered Entity
   (b) Any other information available to the IRS, including:
       1. The Supplemental Health Care Exhibit (SHCE) filed with the National Association of Insurance Commissioners (NAIC)
       2. The NAIC Annual Statement
       3. The Accident and Health Policy Experience Exhibit filed with the NAIC
       4. Medical Loss Ratio (MLR) Annual Reporting Form filed with the Center for Medicare & Medicaid Services' (CMS') Center for Consumer Information and Oversight of the U.S. Department of Health and Human Services (HHS)
       5. Any similar statements filed with NAIC, with any state government or with the federal government pursuant to applicable state or federal requirements

iii. The Final Fee Calculation will include the following information:
   (a) The Covered Entity’s apportioned Annual Fee
   (b) The Covered Entity’s Net Premiums Written for Health Insurance of U.S. health risks
   (c) The Covered Entity’s Net Premiums Written for Health Insurance of U.S. health risks taken into account after the application of the Statutory Exclusion
   (d) The aggregate Net Premiums Written for Health Insurance of U.S. health risks taken into account for all Covered Entities

G. Each Covered Entity must pay the Annual Fee stated in the Final Fee Calculation by September 30th of each year for the preceding calendar year.

i. Covered Entities must make payments electronically.

ii. No tax return is required to be filed with the payment.

H. The IRS Proposed Regulations point out:

i. A Covered Entity’s Final Fee Calculation may differ from its Preliminary Fee Calculation because:

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4 As of the date of this outline, the IRS had not yet published this guidance.
(a) Of changes made under the error correction process, or
(b) The IRS discovered additional information relevant to the fee calculation through
other information sources.

ii. Even if a Covered Entity did not submit an Error Correction Report, its Final Fee
Calculation may differ from its Preliminary Fee Calculation because of information the
IRS discovered about that Covered Entity through other information sources.

iii. A change in the aggregate net premiums written for Health Insurance of U.S. health risks
(the denominator of the apportionment fraction) can affect each Covered Entity’s Annual
Fee because each Covered Entity’s Annual Fee is a fraction of the aggregate Annual Fee
collected from all Covered Entities.

I. Refunds

i. Because the Annual Fee is treated as an excise tax:
   (a) After the Error Correction Report, no IRS administrative appeal procedure is
   available.
   (b) A Covered Entity may request a refund of an excess or erroneous Annual Fee by
   filing a refund claim with IRS.
   (c) If the IRS denies the refund claim, the Covered Entity may file a refund action in
   federal court.

ii. The proposed regulations do not address how a Covered Entity’s liability for the Annual
Fee for a calendar year could be affected as a result of:
   (a) Other Covered Entities’ successful refund claims, or
   (b) Litigation favorable to other Covered Entities

VIII. Covered Entity

A. Definition: Any entity with net premiums written for Health Insurance for U.S. health risks
during a calendar year that is:
   i. A health insurance issuer, including an insurance company, an insurance service
   organization, or an insurance organization that is required to be licensed to engage in the
   business of insurance in a state and that is subject to the laws of the state that regulate
   insurance.
   ii. A health maintenance organization (HMO) that includes:
      (a) A federally qualified HMO
      (b) An organization recognized under state law as an HMO, or
      (c) A similar organization regulated under state law for solvency the same as an HMO
   iii. A tax-exempt organization that would be subject to taxation under subchapter L (as an
   insurance company) if it were not tax-exempt
      (a) Therefore, an HMO that is tax-exempt under IRC Sec. 501(c)(3) or IRC Sec.
      501(c)(4) is treated as a Covered Entity, unless it qualifies for an exception.
   iv. An entity that provides health insurance under:
      (a) Medicare Advantage
IX. Covered Entity Exceptions

A. Self-Insured Employer
   i. An entity that self-insures the health risks of its current and/or former employees, whether or not through a third-party administrator or a voluntary employees’ beneficiary association (VEBA)
   ii. A health insurance company, which otherwise qualifies as a Covered Entity, to the extent it self-insures the health risks of its current and/or former employees

B. Governmental Entity
   i. The U.S.
   ii. Any state, Washington, D.C., or political subdivision thereof
   iii. Any Indian tribal government
   iv. Any public agency created by a state or political subdivision, organized as a nonprofit under state law, and which contracts with the state to administer state Medicaid benefits through local providers or HMOs

C. Certain Nonprofit Corporations
   i. If it meets all of the following requirements:
      (a) Incorporated as a nonprofit corporation under state law
      (b) Prohibits the inurement of net earnings to any insider under IRC Sec. 501(c)(3) standards
      (c) Prohibits a substantial part of its activities from consisting of lobbying activities under IRC Sec. 501(c)(3) standards
      (d) Prohibits carrying on any political activities under IRC Sec. 501(c)(3) standards
      (e) Receives more than 80% of its revenues from government programs that target low-income, elderly, or disabled populations under the Social Security Act
         1. For example: Medicare, Medicaid or Children’s Health Insurance Program (CHIP)
   ii. Preamble: “An entity is not required to be exempt from tax under section 501(a) to qualify for this exception.”

D. Certain VEBAs
   i. A VEBA described in IRC Sec. 501(c)(9) that is established by an entity to provide health care benefits

X. Controlled Groups

A. Definition: A group of two or more entities, where at least one is a Covered Entity, that are treated as a single employer under the rules for work opportunity credits or qualified deferred compensation plans.
i. Membership in a Controlled Group is determined on December 31 of each calendar year.

ii. A Controlled Group is treated as a single Covered Entity.

(a) In determining the premiums written for Health Insurance for all U.S. health risks, all the premiums written by all members of a Controlled Group are combined.

iii. The Preamble states that a Controlled Group must take into account the Net Premiums Written for all members of the Controlled Group for the entire calendar year.

(a) Thus, the Net Premiums Written by a new member of a Controlled Group, for the period before it joined the Controlled Group, must be reported by the Controlled Group.

(b) Conversely, the Net Premium Written by a Covered Entity that left a Controlled Group, for the period before it left the Controlled Group, is not reportable by the Covered Entity's former Controlled Group.

B. Designated Entity

i. The Controlled Group must select one entity as the Designated Entity to act on behalf of the Controlled Group. The Designated Entity:

(a) Files Form 8963 for the Controlled Group

(b) Receives IRS communications for the Controlled Group

(c) Files the Error Correction Report for the Controlled Group

(d) Pays the Annual Fee for the Controlled Group

ii. The Designated Entity is identified on Form 8963.

iii. If a Controlled Group is also an affiliated group that files a consolidated return, the common parent is automatically the Designated Entity.

C. All members of a Controlled Group are jointly and severally liable for the total Annual Fee for which the Controlled Group is liable.

D. Foreign Entity

i. A foreign entity that is taxable under IRC Sec. 881 on U.S. source income from premiums written for Health Insurance of U.S. health risks is included in a Controlled Group.

XI. Net Premiums Written

A. Definition: Premiums written, including reinsurance premiums written, reduced by reinsurance ceded, and reduced by ceding commissions and MLR rebates with respect to the particular tax year

XII. Health Insurance

A. Definition: Benefits consisting of medical care (provided directly, through insurance or reimbursement, or otherwise) under any hospital or medical service policy or certificate, hospital or medical service plan contract, or HMO contract offered by a health insurance issuer.

i. Includes limited scope dental and vision benefits and retiree-only health insurance

B. Exclusions
i. Coverage only for accident, disability income or any combination thereof

ii. Coverage issues as a supplement to liability insurance

iii. Liability insurance, including general liability insurance and automobile liability insurance

iv. Workers’ compensation or similar insurance

v. Automobile medical payment insurance

vi. Credit-only insurance

vii. Coverage for on-site medical clinics

viii. Other insurance coverage that is similar to the insurance coverage above under which benefits for medical care are secondary or incidental to other insurance benefits

ix. Long-term care, nursing home care, home health care, or community-based care, or any combination thereof

x. Coverage only for a specified disease or illness

xi. Hospital indemnity or other fixed indemnity insurance

xii. Medicare supplemental health insurance

xiii. Student administrative health fee arrangements

xiv. Travel insurance

xv. Indemnity reinsurance

XIII. U.S. Health Risk

A. Definition: The health risk of any individual who is:

i. A U.S. citizen

ii. A resident of the U.S., or

iii. Located in the U.S.

XIV. Computation of Annual Fee

A. The portion of the aggregate statutory Annual Fee that a Covered Entity owes is apportioned to each Covered Entity based on a fraction that represents the Covered Entity’s share of the health insurance market during the prior calendar year.

i. Numerator – The Covered Entity’s Net Premiums Written by the Covered Entity in the preceding calendar year for Health Insurance for all U.S. health risks

ii. Denominator – The aggregate of all the Net Premiums Written by all Covered Entities in the preceding calendar year for Health Insurance for all U.S. health risks

(a) The IRS will determine the amount that is included in the denominator.

XV. Statutory Exclusion

A. In determining the amount of Net Premiums Written by a Covered Entity in a calendar year for Health Insurance of U.S. health risks that is included in the numerator of the apportionment fraction, the following amount of Net Premiums Written are taken into account:

i. First $25 million Disregarded
ii. Next $25 million 50% included
iii. More than $50 million 100% included

(a) Thus, the first $37.5 million of Net Premiums Written by a Covered Entity in a calendar year are not included in the numerator of the apportionment fraction.

B. The amount of Net Premiums Written by a Covered Entity includes the aggregate Net Premiums Written by a Controlled Group that is treated as a single Covered Entity.

C. Thus, a Covered Entity (including a Controlled Group) having less than $25 million of Net Premiums Written in a calendar year is not liable for the Annual Fee.

i. Nevertheless, the Covered Entity is required to File Form 8963 to report its Net Premiums Written.

XVI. 50% Exclusion

A. A Covered Entity that is tax-exempt under one of the following provisions can exclude 50% of the Net Premiums Written that relate to the entity’s exempt activities:

i. IRC Sec. 501(c)(3) – Charitable, etc.
ii. IRC Sec. 501(c)(4) – Social welfare
iii. IRC Sec. 501(c)(26) – High risk health insurance pool
iv. IRC Sec. 501(c)(29) – Consumer Operated and Oriented Plan (CO-OP)

B. But the Net Premiums Written by a Covered Entity that are derived from an “unrelated trade or business” are not subject to the 50% Exclusion.

C. The eligibility for the 50% Exclusion for Covered Entities in a Controlled Group is determined separately for each Covered Entity.

XVII. Controlled Group – Exclusions and Exception

A. The Statutory Exclusion is applied to the Controlled Group’s combined premiums.

B. The 50% Exclusion is applied to each entity separately.

C. The Covered Entity exceptions are applied to each entity separately.

D. Ordering – Based on the Preamble, the ordering of the exclusions and exception appears to be:

i. Determine which entities in the Controlled Group qualify for a Covered Entity Exception (e.g., certain nonprofit entities).

(a) These entities are not Covered Entities.

(b) The Net Premiums Written by these entities are not included in the numerator of the apportionment fraction.

ii. The Statutory Exclusion is applied to the remaining aggregate Net Premiums Written by all the Covered Entities in the Controlled Group.

iii. For each Covered Entity included in the Controlled Group that qualifies for the 50% Exclusion, 50% of its Net Premiums Written are excluded from the numerator of the apportionment fraction.
iv. But the Preamble does not address how the Statutory Exclusion is allocated to Covered Entities that qualify for the 50% Exclusion and to Covered Entities that do not.

XVIII. Deduction of Annual Fee
A. The Annual Fee is not tax deductible by a taxable entity.
B. The Annual Fee is not deductible by a tax-exempt entity in determining its unrelated business taxable income.

XIX. Penalties
A. For failing to file Form 8963:
   i. $10,000 plus lesser of:
      (a) $1,000 per day while the failure continues, or
      (b) The Annual Fee that is due for the required Form 8963
   ii. A "reasonable cause" exception applies.
B. For underreporting the amount of Net Premiums Written:
   i. The excess of:
      (a) The Annual Fee that is due based on the correct amount of Net Premiums Written,
      over - -
      (b) The Annual Fee that is determined based on the amount of Net Premiums actually reported
   ii. This penalty is in addition to the Annual Fee for which the Covered Entity is liable.

XX. Disclosure
A. Forms 8963 are not subject to the restrictions on public disclosure.
B. IRS and Treasury are considering making available to the public the information reported on Form 8963, including:
   i. The identity of the Covered Entity, and
   ii. The amount of its Net Premiums Written
C. The IRS and Treasury have requested comments on which reported information the IRS should make publicly available.

NOTE: The views expressed herein are those of the author and do not necessarily reflect the views of Ernst & Young LLP.