Health Care Reform

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Employer Shared Responsibility Final Regulations- Transitions Rules and Other Important New Guidance

The recently released IRS final regulations on the Affordable Care Act (ACA) 4980H employer shared responsibility rules (often called the pay or play rules) largely formalized the rules previously described in proposed regulations originally released in January 2013.

However, the new rules contain some clarification and significant new guidance in two principal areas: transition rules including a delay in enforcement for smaller employers, and details related to defining full-time employees.

This issue brief will focus on the transition rules and other new information contained in the final regulations. New guidance specifically addressing hours of service and measurement periods will be described in detail in a separate issue brief.

Background

The ACA employer shared responsibility rules apply only to applicable large employers. An applicable large employer is defined as an employer with at least 50 full-time equivalents during the preceding calendar year. For purposes of determining whether an employer is an applicable large employer, full-time employees and hours of service for other non-full time employees are taken into account.

4980H generally provides that an applicable large employer is subject to an assessable payment (usually referred to by employers as a penalty) if either (1) the employer fails to offer the opportunity to enroll in minimum essential coverage (MEC) to its full-time employees (and their dependents) under an eligible employer-sponsored plan [4989H(a)], or (2) the employer offers the opportunity to enroll in MEC under an eligible employer-sponsored plan and one or more full-time employees is certified as having received a subsidy when purchasing individual health insurance through a public exchange [4980H(b)].

A full-time employee can qualify for ACA subsidies only if (1) they are not eligible for the employer plan, (2) the employer's plan is unaffordable (as defined by the ACA) for employee-only coverage, or (3) the plan is not a minimum value plan (generally a plan with at least a 60% actuarial value).

Transition Rules

The regulations contain a number of important transition rules, some of which delay when the rules will impact

certain employers, and others that change how certain measurements and calculations are treated.

Delay in Enforcement for Employers with Fewer than 100 FTE

Enforcement of the shared responsibility rules is delayed until 2016 for employers with fewer than 100 full-time equivalents (FTEs). To determine the number of full-time equivalents (FTEs), the employer must use the existing 4980(H) counting methodology, taking into account both full-time employees and the number of FTEs represented by the other (non-full-time) employees.

- To determine employer size for purposes of this delay, an employer is allowed to use any 6 consecutive months of employment data in 2014 (see more below).
- To take advantage of this delay, an employer will need to certify in writing to the IRS that they have met certain conditions. The administrative process and the required form for providing this certification to the IRS have yet be determined. The employer must certify that:
- The employer did not reduce its workforce or reduce employees' hours or service between February 9, 2014 and December 31, 2014 in order to qualify for the one-year transition delay.
- The employer did not materially reduce the health coverage it offered on February 9, 2014.
- Generally, an employer with 50-99 FTE and a non-calendar year plan will be subject to the rules on its first plan year in 2016.

2015 Transition Rules

The final regulations also contain a number of important transition rules that will affect possible 4980H liability for employers with 100 or more FTE.

Determining Applicable Large Employer status – Under 4980H, the determination of applicable large employer status is based on the average employment over the 12 months of the prior calendar year. For one year only, employers are allowed to use the average over 6 consecutive months during 2014 to determine their status for 2015.

To determine "applicable large employer" status in 2015 (or total FTEs):

1. Choose 6 consecutive months during 2014 and add:
2. Total full-time employees (30 hours of service or more per week); and
3. Total hours of service for all other employees ÷ 120
4. Then average the monthly totals for the 6 consecutive months chosen to determine total FTEs.
5.

***Keep in mind that for 2016 and beyond, employers will need to perform this same calculation, but use all 12 months of the previous calendar year. Employers are only allowed to use a 6-month period as transition relief going into 2015.

95% margin of error rule will be 70% for 2015 only – The proposed regulations contain a rule that relieves employers of any liability under 4980H(a) as long as the employer offers MEC to at least 95% of all full-time employees. For 2015 only, employer will not face any 4980H(a) liability as long as MEC is offered to at least 70%

of all full-time employees. Full-time employees not offered coverage could still qualify for subsidized individual health insurance through a public exchange, which would expose an employer to the 4980H(b) assessable payment of $250/month for each employee receiving a subsidy.

Example: Assume 200 FTEs (subject to the rules in 2015) and 150 full-time employees. Employer offers MEC to 115 of the full-time employees (approx. 75%). There is no assessable payment under 4980H(a), but if any of the 35 full-time employees not offered coverage qualify for subsidized coverage through a public exchange, the employer may owe an assessable payment for each such employee under 4980H(b).

4980H(a) assessable payment not applied to first 80 full-time employees for 2015 – When calculating assessable payments under 4980H(a) for an employer who fails to offer MEC to at least 70% of all full-time employees, the first 80 full-time employees are ignored. This waiver of 80 employees rule applies only to 2015. Beginning in 2016, the 4980H(a) assessable payment will be based on the number of full-time employees, not counting the first 30. Note that when calculating assessable payments under 4980H(b), employer liability cannot exceed the total assessable payment under 4980H(a), including the waiver of the first 80 full-time employees. Consequently, an employer with 80 or fewer full-time employees (as defined by the ACA) will not be liable for any ACA assessable payments in 2015, even if some employees purchase subsidized individual health insurance.

Example 1: Assume 200 FTEs (subject to the rules in 2015) and 150 full-time employees. Employer chooses not to offer MEC to any of the full-time employees.

- 4980H(a) assessable payment = 150 – 80 waiver X $2000 = $140,000

Example 2: Assume 200 FTEs (subject to the rules in 2015) and 150 full-time employees. Employer offers MEC to 115 of the full-time employees (approx. 75%).

- 4980H(a) assessable payment = $0 because employer offered MEC to at least 70%
- 4980H(b) assessable payment = $3000/yr. for any full-time employee that qualifies for, and purchases, subsidized coverage through a public exchange, but in no case can the (b) penalty exceed the maximum liability under (a) ($140,000 in this example) regardless of how many employees choose to purchase subsidized individual coverage.

Note – it is unlikely that all full-time employees not offered the required coverage will choose coverage through a public exchange (versus through a spouse or other family member), and even if they do choose coverage through a public exchange, only those with household income under 400% of FPL will qualify for subsidized coverage.

Example 3: Assume 105 FTEs (subject to the rules in 2015) and 80 full-time employees. Employer chooses not to offer MEC to any of the full-time employees.

- 4980H(a) assessable payment = 80 – 80 waiver X $2000 = $0
- 4980H(b) assessable payment = $0 because it cannot exceed total potential assessable payment under 4980H (a)

Offering dependent coverage – To avoid 4980H assessable payments, an employer must make an offer of coverage to full-time employees and their dependents (offering coverage to the employee spouse is not required). In 2015, no assessable payment will be due for plans that do not currently offer coverage to dependents, if the plan

is taking steps during 2015 to do so in 2016.

Non-Calendar Year Plans

Employers with 100 or more FTEs and a non-calendar plan year, who are subject to the shared responsibility rules in 2015, do not have to comply until the plan's 2015 plan year, so long as certain criteria are met. Employers unable to meet the following criteria will be subject to the shared responsibility rules effective January 1, 2015, regardless of their plan year.

No change in plan year – To qualify for this transition relief, the employer must not have modified the plan year since December 27, 2012. This rule applies only if the employer modified the plan year to a later month in the year. If the employer made a change to an earlier month, they would still qualify for the transition relief, assuming other conditions are met. Plan year changes made for other bona fide business reasons may also be permitted.

Significant percentage tests – An employer with a non-calendar year plan must also meet one of two different "significant percentage tests." The all employee test is similar to the rules contained in prior guidance. The full-time percentage test is a new option that may allow some additional employers to take advantage of the non-calendar year transition rule:

- Significant percentage test based on all employees
- The employer either (1) covered at least one-quarter (25%) of all employees (including part-time) as of any date in the 12 months ending on February 9, 2014, or (2) offered coverage to one-third (33.33%) or more of all employees (including part-time) during the open enrollment period that ended most recently before February 9, 2014.
- Significant percentage test based on full-time employees
- The employer either (1) covered at least one-third (33.33%) of all full-time employees as of any date in the 12 months ending on February 9, 2014, or (2) offered coverage to one-half (50%) or more of all full-time employees during the open enrollment period that ended most recently before February 9, 2014.

In either case, to avoid 4980H assessable payments, an employer is required to offer coverage to the required percentage of full-time employees as of the first plan year in 2015.

Employer Reporting

The IRS has released proposed rules related to Affordable Care Act (ACA) employer and insurance carrier reporting requirements. The ACA created two new sections in the Tax Code: sections 6055 and 6056. These sections require employers to report certain information designed to provide the IRS with the information necessary to administer the individual mandate "tax" and employer penalties under the employer shared responsibility rules.

Originally, the employer reporting rules were to go into effect in 2015 for coverage provided during 2014. However, in July 2013, the IRS announced a delay in the reporting requirements. Due to this enforcement delay, employers will not be required to comply with these reporting requirements, which will include information related to coverage provided during 2015, until early in 2016. Reporting will be on a calendar year basis regardless of the employer's

plan year.

The final regulation makes it clear that even employers with fewer than 100 FTEs, who are not subject to the shared responsibility rules until 2016, will still be required to fulfill 6055 and 6056 reporting requirements beginning in 2016 (for 2015 data).

Employer Affordability Safe Harbors

An employee's ability to qualify for subsidies when purchasing individual health insurance through a public exchange is based, in part, on their household income. The IRS had previously released proposed employer affordability safe harbors to address the fact that the employer will not know an employee's household income, making it difficult to determine how to set contribution to offer affordable coverage. Employer are allowed to use one of three safe harbor methods that have been finalized in these rules.

- W-2 wage safe harbor
- Rate of Pay safe harbor
- Federal poverty level safe harbor

Employee Classifications, Hours of Service, and Defining Full-Time Employees

In addition to the various rules described above, the final regulations provided clarification and amendments on several other issues related to which employees must be treated as full-time employees. Included below is a brief summary of areas addressed. A more comprehensive analysis of these rules is contained in a separate issue brief.

- Hours of service
- Clarification on use of the equivalency methods for non-hourly employees
- Examples illustrating the reasonableness of various methods for determining full-time status of adjunct faculty, layover hours, and on-call hours
  - Exclusion for hours of service provided by bona fide volunteers, work study students, and members of a religious order
- Short-term employees – in general, no special exceptions for short-term or temporary employees are allowed when determining full-time status.
- Break in Service Rules
- Break in service rules apply whether the employer uses a month-to-month determination or the optional look-back measurement method to determine full-time status; and
- Employers must treat employees as continuing employees rather than new hires if an employee resumes employment within 13 weeks (rather than 26 weeks as previously required), except for educational organizations, which must continue to use 26 weeks.
- Look-Back Measurement Method
- Factors are provided to consider when determining an employee's status as a full-time versus variable hour employee;
  - Seasonal employee is defined as an employee in a position for which the customary annual employment is 6 months or less;
- Further guidance is provided for temporary staffing firms; and
- Clarification is provided on the treatment of changes in employment status.

Summary

Now that final regulations have been issued, employers are expected to move forward to implement any necessary plan changes to address the 4980H requirements. Smaller employers (those with fewer than 100 FTE) will welcome the additional year to prepare. The final rules also help by answering some of the outstanding questions related to defining full-time employees. As has been the case since the proposed rules were released over a year ago, employers who have not previously offered health coverage to most employees working at least 30 hours per week face a much more challenging transition.