The Employer Shared Responsibility Under the Affordable Care Act

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A key component of the Patient Protection and Affordable Care Act ("ACA"), the federal health care reform law, is the "employer shared responsibility." Essentially, it is a "pay or play" program applicable to "large" employers. A large employer must offer group health insurance that is affordable and provides minimum value to all full-time employees or risk having to pay certain assessments. On February 10, 2014, the Internal Revenue Service issued final regulations regarding the employer shared responsibility. The following is a general summary of the more than 225 pages of regulations and explanatory materials regarding the employer shared responsibility. Although the assessments will not become effective until 2015[1], employers will need to engage in a significant amount of planning between now and then to ensure that they are compliant with these regulations. Note that employers should consult their attorneys regarding the application of the rules to their particular circumstances or industry.

What are the assessable payments under the employer shared responsibility?

The ACA's employer shared responsibility consists of two different assessments: 4980H(a) liability and 4980H(b) liability (named in reference to the two particular statutory provisions). 4980H(a) applies when (1) the employer fails to offer full-time employees and their dependents the opportunity to enroll in minimum essential coverage (MEC) under an employer sponsored health plan; and (2) at least one full-time employee is certified as having received a tax credit for the purchase of health insurance through a health care exchange. 4980H(b) liability applies when the employer offers a health plan to its full-time employees and their dependents, but (1) one or more full-time employees is certified as receiving the premium tax credit to purchase health insurance; and (2) the employer's coverage is unaffordable or does not provide minimum value (MV).

How much are the assessments?

The assessment under 4980H(a) is $166.67 per month ($2000 per year) for each full-time employee, with the first 30 employees excluded. For example, if an employer with 100 full-time employees fails to offer group health insurance to all of them, it will pay the fee for 70 employees for each month it does not provide insurance. Employers do not get partial credit for offering health insurance to some of its full-time employees.

Under 4980H(b), the assessment is $250 per month ($3,000 per year) for each full-time employee who is certified as receiving the premium tax credit.

Which employers are subject to the employer shared responsibility?

Only a "large" employer is subject to the fees. The ACA defines a large employer as having on average at least 50

[1] The ACA provided that the employer shared responsibility would take effect on January 1, 2014, but the Obama administration postponed this until 2015.

full-time employees during the preceding calendar year. This is calculated by averaging the number of full-time equivalents (FTEs) including seasonal employees, per month. For purposes of determining FTEs, full-time is 120 hours per month. If an employer was not in existence during the prior calendar year, an employer is a large employer for the current calendar year if it is reasonably expected to employ at least 50 FTEs.

Are there any exceptions to who is a large employer?

There is an exception relating to seasonal workers. If an employer's FTEs exceed 50 for 120 days or fewer and the excess employees are seasonal workers, then the employer is not a large employer. Seasonal workers are those employees who perform services on a seasonal basis, such as retail workers employed solely during the holiday season. The IRS instructs that employers may apply a reasonable, good faith interpretation of who is a seasonal worker.

Can a company divide up its employees among several subsidiaries to avoid being a large employer?

No. The ACA provides that related corporate entities are aggregated and treated as a single employer for determining coverage as a large employer.

If an employer is unsure whether it will meet the 50 FTE threshold until the year is over, how will it know whether it has to expand coverage to all full-time employees by the beginning of the next calendar year?

The IRS recognizes that employers that are close to the 50 FTE threshold may need time to consider year-end data in determining whether they are large employers. The regulations provide that with respect to an employee who was not offered coverage in the prior calendar year, the employer will not be subject to an assessable payment if it offers coverage to that employee on or before April 1 of the first year in which the employer is an applicable large employer.

Who is a full-time employee for purposes of the assessments?

For purposes of the assessments (as opposed to determining whether the employer is an applicable large employer), the ACA defines full-time as 30 hours of service per week, and the regulations explain that 130 hours per month is the monthly equivalent. "Hours of service" is broader than hours worked. It includes each hour for which an employee is paid, including vacation and sick time, holidays, and other paid leaves of absence.

How should an employer calculate whether an employee is full-time or not?

The statute contemplates that liability will be assessed on a monthly basis, and thus the regulations require employers to determine on a monthly basis whether an employee is full-time or not. An employer must use actual hours to determine hours of service for hourly employees. For non-hourly employees, employers may use actual hours or use an equivalency of 8 hours per day or 40 hours per week, provided that the equivalency does not substantially understate an employee's hours of service or understate hours of service for a substantial number of employees.

The IRS recognizes that determining whether an employee is full-time every month (and thus entitled to benefits) may be difficult or burdensome, particularly if an employee has varying hours of work or a fluctuating schedule. To address this concern and to give employers flexibility, the regulations provide alternatives to a month-by-month determination. In the case of on-going employees, an employer has the option of using a "look-back measurement" method for determining full-time status. Essentially, the employer selects a measurement period of three to twelve months and calculates whether the employee on average had 30 hours of service per week during that period. If so, the employer must treat the employee as full-time during a subsequent "stability period," which must be at least six months but no shorter than the length of the measurement period. Thus, for example, if the employer used a twelve-month look-back measurement period beginning on January 1, 2014, employees who are determined to be full-time

must be treated as full-time for all of 2015.

An employer may also utilize an optional administrative period of up to 90 days between the measurement period and the stability period in order to determine which on-going employees are eligible for health insurance coverage during the subsequent stability period. However, the administrative period cannot create a gap in coverage. An employee who was enrolled in coverage must remain enrolled during the administrative period.

The regulations also address new employees. If a new employee is "reasonably expected" to be a full-time employee at his or her start date, an employer will be liable for the assessment if it fails to offer health insurance by the end of the employee's initial three full calendar months of employment and any subsequent months for which coverage was not offered. Factors for determining whether a new employee can reasonably be expected to work full time include: (1) whether the individual is replacing a full-time employee; (2) whether employees in comparable or same positions are full-time; or (3) whether the job was advertised or communicated to the individual as full-time. Thus, if an employer expects based on these factors that an employee will be full-time, it can only impose a three-month waiting period for health insurance coverage; it cannot wait to the conclusion of some measurement period.

For new employees who are expected to work a variable schedule, an employer may use an initial measurement period of between three and twelve months to determine whether the employee was employed on average 30 hours of service per week. If so, the employee must be treated as full-time during a stability period, which must be the same length as the one used for on-going employees. As in the case of on-going employees, employers may use an optional administrative period of up to 90 days. However, the initial measurement period and the administrative period cannot extend beyond the last day of the full calendar month after the first anniversary of the employee's start date.

Can an employer use a temporary staffing company or some other structure to avoid having an individual work "full-time?"

No. An employment arrangement designed to evade the application of the 4980H fees is not permitted. For example, if an employer employed an individual for 20 hours and a staffing company supplied the same individual to the employer for another 20 hours, the IRS would treat that individual as working full-time.

If an employee works part-time for two related companies, how should that individual be treated?

If the employee works for two entities that constitute a single employer, then the individual is full-time if the total hours of service for both entities exceed 30 hours.

Can an employer reduce employees' hours to below 30 hours to avoid triggering full-time benefits?

There is nothing in the ACA that specifically prohibits employers from reducing an employee's hours to below the 30-hour threshold. However, some employee groups have taken the position that doing so would violate ERISA, the federal employee benefits law, which prohibits employers from taking an adverse action against employees to prevent them from obtaining a benefit under a plan. This is an issue that is likely to be the subject of litigation.

Can an employer exclude students from a determination of who is full-time?

For purposes of the assessments, hours of service do not include time spent by students in positions subsidized through federal work study programs or similar state programs. All other hours of service by student employees must be counted.

Do on-call hours count as hours of service for purposes of determining whether an employee is full-time?

An employer must count on-calls hours for which payment is made by the employer, for which the employee is required to remain on the employer's premises, or for which the employee's activities are substantially restricted,

preventing the employee from using the time for his or her own purposes.

Does the ACA prevent an employer from offering group health insurance to employees who are not full-time?

No. Employers may always offer coverage more expansively, subject to compliance with any nondiscrimination or other applicable requirements.

How should employers treat employees who are rehired after termination?

In general, if an employee provides no hours of service for 13 weeks and then begins to have hours of service, the employer may treat the employee as having terminated employment and then having been rehired as a new employee. In that instance, the employer may use the rules for new employees to determine full-time status.

Alternatively, an employer may use a "rule of parity" for employees with breaks in service. An employer may treat the employee as having been terminated if the break in service is more than 4 weeks (and less than 13 weeks) and longer than the employee's employment before the break. For example, if an employee works for 3 weeks, quits, and then is rehired 6 weeks later, the employee can be treated as a new employee.

For purposes of 4980H(a) liability, what constitutes an offer of coverage to a full-time employee?

As mentioned above, an employer may be liable for the 4980H(a) assessment for each month it fails to offer health insurance to full-time employees and their dependents. To constitute an offer of coverage, the employee must have an effective opportunity to enroll in coverage or decline to do so at least once per year. The regulations state that whether an employee had an effective opportunity depends on all of the facts and circumstances, including the adequacy of the employer's notice about open enrollment and the period of time for enrollment.

To whom must the employer offer coverage?

In addition to the employee, offers of coverage must be given to the employee's dependents. Dependents under the ACA include the employee's children who are under the age of 26 years of age. It does not include the employee's spouse.

If the plan allows for an employee's election of coverage from a prior year to continue for every successive plan year unless the employee opts out, will that constitute an offer of coverage?

Yes.

If an employer contributes to a multiemployer health plan, is that an offer of coverage?

Yes. An offer of coverage by a multiemployer plan to which the employer contributes constitutes an offer of coverage made by or on behalf of the employer.

To avoid the assessment under 4980H(a), the employer must offer "minimum essential coverage" or MEC. What coverage will count as MEC?

Generally, coverage under an eligible employer sponsored plan will constitute minimum essential coverage. Note that there is no requirement under the ACA that employers offer "essential health benefits" or a "qualified health plan." These terms, under the law, apply to plans that are offered on the state exchanges for which the tax credit subsidy is available. Employer-sponsored plans are not required to meet these terms.

Does an employer have an obligation under the ACA to automatically enroll employees in its health plan?

Employers with more than 200 full-time employees will be required to automatically enroll employees into their

health plans, subject to any legal waiting period. This rule is not yet in effect.

What if an employer fails to offer coverage to a small number of full-time employees?

The ACA provides that an employer will owe the 4980H(a) assessment if it fails to offer coverage to all full-time employees and at least one full-time employee is certified as receiving the premium tax credit or cost-sharing reduction. However, the Treasury Department and the IRS have decided to exercise their administrative authority to allow for a margin of error — that an employer need only offer coverage to 95% of its full-time employee. Thus, an employer will not be assessed the fee if it offers coverage to all but 5% of its full-time employees (or, if greater, five employees). This relief is available regardless of whether the failure to offer coverage was inadvertent or not.

What happens if a full-time employee fails to pay his or her portion of the premium?

If an employee enrolls in coverage but fails to pay his or her portion of the premium, the employer is treated as having offered coverage to that employee for the remainder of the coverage period.

For purposes of 4980H(b) liability, when is an employer's coverage unaffordable?

Coverage is unaffordable if the employee's cost for individual coverage exceeds 9.5% of his or her household income for the taxable year.

How is an employer to know what an employee's household income is?

The Treasury Department and the IRS acknowledge that employers might not know employees' household income for purposes of determining 4980H(b) liability. Therefore, they have created three safe harbors that employers may use to determine whether coverage is unaffordable:

- **Form W-2**: An employer can determine affordability for purposes of 4980H(b) liability by reference to the amounts reported in Box 1 of Form W-2. Coverage will be affordable if the employee's cost of coverage does not exceed 9.5% of the Form W-2 wages.

- **Rate of pay**: An employer may determine affordability by multiplying the hourly rate of hourly employees by 130 hours to determine a monthly wage amount, and then determine whether the employee's cost of coverage exceeds 9.5% of this monthly wage amount. This is a design-based safe harbor, meaning that employers can assess affordability prospectively.

- **Federal poverty line**: Employers may also rely on a design-based safe harbor using the Federal poverty line for a single individual. Coverage is affordable if the employee's cost for individual coverage does not exceed 9.5% of the poverty line for a single individual.

For purposes of 4980H(b) liability, when does an employer's coverage fail to provide "minimum value" or MV?

A plan provides minimum value if the percentage of allowed costs paid by the plan (as opposed to the employee) are in the aggregate at least 60% of the total costs. The Department of Health and Human Services has issued proposed regulations relating to this and has created a calculator to help employers assess whether their plans provide minimum value or not.

Both 4980H(a) and 4980H(b) liability are triggered only if an employee has received a premium tax credit. How will an employer know if this has occurred?

To be determined. Guidance will be issued explaining how an employer will be given notice and how employers can respond to any such notice. Guidance will also be issued as to how and when the IRS will notify employers of potential liability.

Are there any reporting requirements relating to the employer shared responsibility?

Yes. An applicable large employer will need to report to the IRS certain information regarding the health care coverage offered to employees. It will also have to furnish a statement to each full-time employee by January 31 regarding health insurance coverage during the preceding calendar year.

When do the regulations take effect?

The regulations are effective on January 1, 2015. However, employers may not be subject to assessments as of that date under transition relief rules. Employers who offer plans that are not on a calendar year may not be subject to assessments until the first month of the plan year beginning sometime after January 1, 2015. Transition relief may also be available for employers who provide health insurance to a significant percentage of its employees, although not 95% of its full-time employees. Further, employers may also be eligible for transition relief relating to dependent coverage. In general, employers may not be subject to an assessment for plan year 2015 solely on account of a failure to offer coverage to dependents. Finally, an applicable large employer with at least 50 FTEs but fewer than 100 FTEs may be eligible for special transition relief for all 2015 and for any month of the 2015 plan year that falls within calendar year 2016. These transition relief rules have specific eligibility requirements which must be satisfied in order to delay the imposition of the assessments.