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Pay or Play—Employer Shared Responsibility Penalties

The Affordable Care Act (ACA) requires certain large employers to offer affordable, minimum value health coverage to their full-time employees (and dependents) or pay a penalty. This employer mandate provision is also known as the "shared responsibility" or "pay or play" rules.

Beginning in 2015, applicable large employers will face penalties if one or more of their full-time employees obtains a premium tax credit or cost-sharing reduction through an Exchange. As described in greater detail below, an individual may be eligible for a premium tax credit or cost-sharing reduction either because the employer does not offer coverage or the employer offers coverage that is either not "affordable" or does not provide "minimum value."

> The employer mandate provisions were set to take effect on Jan. 1, 2014. However, on July 2, 2013, the Treasury announced **the delay of the employer mandate penalties and related reporting requirements for one year, until 2015**. Therefore, these payments will not apply for 2014. On July 9, 2013, the IRS issued Notice 2013-45 to provide more formal guidance on the delay. No other provisions of the ACA are affected by the delay.

On Feb. 12, 2014, the IRS published long-awaited **final regulations** on the ACA's employer shared responsibility rules. **Under the final regulations, applicable large employers that have fewer than 100 full-time employees generally will have an additional year, until 2016, to comply with the pay or play rules.** Large employers with 100 or more full-time employees must comply with the pay or play rules starting in 2015.

APPLICABLE LARGE EMPLOYERS

Only an applicable large employer may be subject to shared responsibility penalties regarding employer-sponsored health coverage. An "applicable large employer" (ALE) is an employer with, on average, **at least 50 full-time employees, including full-time equivalents,** during the preceding calendar year.

In order to determine whether an employer is an ALE, both full-time and part-time employees are included in the calculation. Full-time employees are those working an average of **30 or more hours per week** (or 130 hours in a calendar month). The hours worked by part-time employees (that is, those working less than 30 hours per week) are included in the calculation of a large employer on a monthly basis by dividing their total number of monthly hours worked by 120.

EXAMPLE

A company has 35 full-time employees (30+ hours). In addition, the company has 20 part-time employees who all work 24 hours per week (96 hours per month). These part-time employees' hours would be treated as equivalent to 16 full-time employees, based on the following calculation:

20 employees X 96 hours/120 = 1920/120 = 16

This company would be considered a large employer, based on a total full-time equivalent count of 51. That is, 35 full-time employees plus 16 full-time equivalents based on part-time hours.

Table 1 illustrates whether certain groups of employees are counted in determining whether an employer is a large employer and whether they are included in any penalty calculation.

Table 1. Determination and Potential Application of Employer Penalty for Categories of Employees

Employee category	How is this category of employee used to determine "large employer"?	Once an employer is determined to be a large employer, could the employer be subject to a penalty if this type of employee received a premium credit?
Full-time	Counted as one employee, based on a 30-hour or more work week	Yes
Part-time	Pro-rated (calculated by taking the hours worked by part-time employees in a month divided by 120)	No
Seasonal	Counted in initial calculation, but a special rule may apply	Yes, for the month in which the seasonal worker is full-time
Temporary Agency	Generally, counted as working for the temporary agency (except for those workers who are independent contractors)	Yes, for those counted as working for the temporary agency

Delayed Implementation for Medium-sized Employers

The final rules **delay implementation for medium-sized employers** that are covered by the employer mandate. ALEs that have fewer than 100 full-time employees will have an additional year, until 2016, to comply with the pay or play rules. Thus, the employer shared responsibility provisions will generally apply to:

- Employers with 100 or more full-time employees starting in 2015; and
- Employers with 50-99 full-time employees starting in 2016.

To qualify for this delay, an employer must meet the following three eligibility conditions:

1. The employer must employ a limited workforce of at least 50 full-time employees (including FTEs) but fewer than 100 full-time employees (including FTEs) on business days during 2014;
2. During the period beginning on Feb. 9, 2014, and ending on Dec. 31, 2014, the employer may not reduce the size of its workforce or the overall hours of service of its employees in order to satisfy the workforce size condition; and
3. During the coverage maintenance period, the employer may not eliminate or materially reduce the health coverage, if any, it offered as of Feb. 9, 2014.

In addition, the employer must provide an appropriate certification stating that it meets all of the eligibility requirements. The forthcoming section 6056 employer reporting final regulations are expected to provide that an applicable large employer that otherwise qualifies for this delay will provide this certification as part of the transmittal form it is required to file with the IRS under the section 6056 employer reporting regulations.

However, under the final regulations, **employers that change their plan years after Feb. 9, 2014, to begin on a later calendar date are not eligible for the delay**.

POTENTIAL PENALTIES

Regardless of whether or not a large employer offers coverage, it will be potentially liable for a penalty ***only if*** at least one of its full-time employees receives a premium tax credit or cost-sharing reduction for coverage purchased through an Exchange. A full-time employee includes only those individuals working 30 hours or more per week.

As shown in Table 1, part-time workers are *not* included in penalty calculations, even though they are included in the determination of whether an employer is a large employer. An employer will not pay a penalty for any part-time worker, even if that part-time worker receives a premium tax credit or cost-sharing reduction.

Beginning in 2014, individuals who are not offered employer-sponsored coverage and who are not eligible for Medicaid or other programs may be eligible for premium tax credits for coverage purchased through an Exchange. These individuals will generally have income between 100 percent and 400 percent of the federal poverty level (FPL). Individuals who satisfy the requirements for receiving the premium tax credit may also qualify to receive cost-sharing reductions under Exchange plans.

Individuals who are offered employer-sponsored coverage can only obtain premium tax credits or cost-sharing reductions for Exchange coverage if, in addition to the other criteria above, they also are not enrolled in their employer's coverage and their employer's coverage meets either of the following criteria:

- The individual's required contribution toward the plan premium for self-only coverage exceeds 9.5 percent of their household income (adjusted to **9.56 percent for plan years beginning in 2015** under Rev. Proc. 2014-37); or
- The plan does not provide minimum value, meaning that it pays for less than 60 percent, on average, of covered health care expenses.

Other ACA provisions will also affect whether full-time employees can obtain premium tax credits or cost-sharing reductions for Exchange coverage. For example, Exchanges are required to have "screen and enroll" procedures in place for all individuals who apply for premium tax credits. This means that individuals who apply for premium tax credits must be screened for Medicaid and the State Children's Health Insurance Program (CHIP) eligibility and, if found eligible, are to be enrolled in those programs. Exchange premium tax credits will not be an option for these individuals. This could affect whether any of an employer's full-time employees obtain premium tax credits or cost-sharing reductions in an Exchange and, if so, how many.

"Substantially All" Requirement

The 4980H(a) penalty will not apply to a large employer that intends to offer coverage to all of its full-time employees but fails to offer coverage to a few of these employees, regardless of whether the failure to offer coverage was inadvertent.

The final regulations provide that an employer will satisfy the requirement to offer minimum essential coverage to "substantially all" of its full-time employees and their dependents if it offers coverage to **at least 95 percent** of its full-time employees and dependents. According to the IRS, the alternative margin of five full-time employees is designed to accommodate relatively small employers because a failure to offer coverage to a handful of full-time employees might exceed 5 percent of the employer's full-time employees.

However, the final regulations provide **transition relief** that will phase in this requirement. For each calendar month during 2015 (and any calendar months during the 2015 plan year that fall in 2016), a large employer that offers coverage to **at least 70 percent**—or that fails to offer coverage to no more than 30 percent—of its full-time employees and dependents will not be subject to a 4980H(a) penalty.

Also, large employers that qualify for the transition relief from the 4980H(a) penalty for 2015 plan years are still subject to potential 4980H(b) penalties for that time period (for example, if the health plan coverage is unaffordable or does not provide minimum value).

Penalty for Large Employers Not Offering Coverage—The 4980H(a) Penalty

Once the employer mandate provision becomes effective, a large employer will be subject to a penalty if any of its full-time employees receives a premium tax credit or cost-sharing reduction toward their Exchange plan. Under the ACA, the monthly penalty assessed on employers that do not offer coverage to substantially all full-time employees and their dependents will be equal to the number of full-time employees (minus 30) multiplied by 1/12 of $2,000 for any applicable month.

The final regulations include **transition relief for 2015** that allows employers with 100 or more full-time employees (including FTE employees) to reduce their full-time employee count by 80 when calculating the penalty. This relief applies for 2015 plus any calendar months of 2016 that fall within the employer's 2015 plan year.

In subsequent years, the penalty amount is expected to be indexed by the premium adjustment percentage for the calendar year.

Penalty for Large Employers Offering Coverage—The 4980H(b) Penalty

Employers that do offer coverage to substantially all full-time employees and dependents may still be subject to penalties if at least one full-time employee obtains a premium tax credit or cost-sharing reduction in an Exchange plan because the employer did not offer coverage to all full-time employees, or the employer's coverage is unaffordable or does not provide minimum value. To trigger a penalty, the employee's required contribution for self-only coverage must exceed 9.5 percent his or her household income (adjusted to **9.56 percent for plan years beginning in 2015** under Rev. Proc. 2014-37) or the employer's plan must pay for less than 60 percent of covered expenses. Note that applicable large employers using an affordability safe harbor **may have to continue using a contribution percentage of 9.5 percent** in 2015 (instead of the adjusted 9.56 percent) to measure their plan's affordability.

In the first year that the employer mandate is applicable, the monthly penalty assessed on an employer for each full-time employee who receives a premium credit will be 1/12 of $3,000 for any applicable month. However, the total penalty for an employer would be limited to the 4980(a) penalty amount. After the first year, the penalty amounts are expected to be indexed by the premium adjustment percentage for the calendar year.

AFFORDABILITY AND MINIMUM VALUE

The final regulations provide safe harbor approaches for assessing whether an employer's coverage is affordable. Although the ACA measures affordability based on household income, these safe harbors allow an employer to measure affordability based on the employee's **W-2 wages**, the employee's **rate of pay** or the **federal poverty level for a single individual**. Eligibility for premium tax credits or cost-sharing reductions will still be based on household income, but the employer will not be subject to a penalty for that employee, even if he or she ultimately receives a premium tax credit or cost-sharing reduction.

Also, on Feb. 25, 2013, the Department of Health and Human Services (HHS) issued a final rule that outlines the following approaches for determining whether an employer's health coverage provides minimum value:

- ***Approach One: Calculator—***HHS has released an MV Calculator that permits an employer to enter information about its health plan's benefits, coverage of services and cost-sharing terms to determine whether the plan provides minimum value.
- ***Approach Two: Checklists—***HHS and the IRS will provide an array of design-based safe harbors in the form of checklists that employers can use to compare to their plan's coverage. If a plan's terms are consistent with or more generous than any one of the safe harbor checklists, the plan would be treated as providing minimum value. In May 2013, the IRS specified three safe harbor plan designs that satisfy minimum value and stated that they expect to release more in future guidance.

- ***Approach Three: Actuarial Certification—***An employer-sponsored plan may seek certification by an actuary to determine the plan's minimum value if the plan contains nonstandard features that preclude the use of the MV Calculator and safe harbor checklists.

In addition, a plan in the small group market that meets any of the "metal levels" of coverage (that is, bronze, silver, gold or platinum) provides minimum value.

OFFER OF COVERAGE

The final regulations provide that if an employee has not been offered an effective opportunity to accept coverage (or decline to enroll), the employee will not be treated as having been offered the coverage for purposes of the employer shared responsibility provision. This offer must be made at least **once during the plan year**.

The employee must also have an effective opportunity to decline an offer of coverage that is not minimum value coverage or that is not affordable. However, under the final regulations, an effective opportunity to decline is not required for an offer of coverage that provides minimum value and is either affordable (determined based on the federal poverty level safe harbor) or no cost to the employee. Thus, an employer may not render an employee ineligible for subsidized coverage by providing an employee with mandatory coverage (that is, coverage which the employee is not offered an effective opportunity to decline) that does not meet minimum value.

For an employee to be treated as having been offered coverage for a month (or any day in that month), the coverage offered, if accepted, must be applicable for that month (or that day). The final regulations clarify that if a large employer fails to offer coverage to a full-time employee for any day of a calendar month during which the employee was employed, the employee is treated as not being offered coverage during that entire month. However, a full-time employee who terminates employment in a calendar month will be treated as having been offered coverage during that month as long as the employee would have been offered coverage for the entire month if he or she had been employed for the entire month.

If an employee enrolls in coverage but **fails to pay the employee's share of the premium on a timely basis**, the employer is not required to provide coverage for the period for which the premium is not timely paid, but will still be treated as having offered that employee coverage for the remainder of the coverage period (typically the remainder of the plan year) for purposes of the shared responsibility provision.

Examples

Table 2 on the next page shows four types of scenarios reflecting health coverage offerings of four large employers (columns A through D) and whether any employer penalty applies. In these large-employer scenarios, the employer size is assumed to remain constant, at 50 full-time employees, throughout the year. The table provides examples of the penalty consequences based on whether the employer offers coverage and whether an employee receives a premium tax credit or cost-sharing reduction.

Note: These examples do not take into account the one-year delay for medium-sized employers or the transition relief allowing employers with 100 or more full-time employees to reduce their full-time employee count by 80 when calculating the 4980H(a) penalty.

The four scenarios are:

Scenario A - The large employer does not offer coverage, but no full-time employees receive subsidies for Exchange coverage. No penalty would be assessed.

Scenario B - The large employer does not offer coverage and one or more full-time employees receive subsidies for Exchange coverage. The annual penalty calculation is the number of full-time employees minus 30, multiplied by $2,000. In this example (using 50 full-time employees), the penalty would not vary if only one employee or all 50 employees received the credit. The employer's annual penalty would be (50-30) X $2,000, or $40,000.

Scenario C - The large employer offers coverage and no full-time employees receive subsidies for Exchange coverage. No penalty would be assessed.

Scenario D - The large employer offers coverage, but one or more full-time employees receive subsidies for Exchange coverage. The number of full-time employees receiving the subsidy is used in the penalty calculation for an employer that offers coverage. The annual penalty is the lesser of:

- The number of full-time employees minus 30, multiplied by $2,000 – or $40,000 for the employer with 50 full-time employees; or
- The number of full-time employees who receive subsidies for Exchange coverage, multiplied by $3,000.

Although the penalties are assessed on a monthly basis (with the dollar amounts above divided by 12), this example uses annual amounts, assuming the number of affected employees is the same throughout the year.

If the employer with 50 full-time employees had 10 full-time employees who received subsidies, then the potential annual penalty on the employer for those individuals would be $30,000. Because this is less than the overall limitation for this employer of $40,000, the employer penalty in this example would be $30,000.

However, if the employer with 50 full-time employees had 30 full-time employees who received subsidies, then the employer's potential annual penalty for those individuals would be $90,000. Because $90,000 exceeds this employer's overall limitation of $40,000, the employer penalty in this example would be limited to $40,000.

Table 2. Potential Annual Penalties Beginning in 2014 for Large Employers

Applies to For-Profit and Nonprofit Organizations

Not a Large Employer: Less than 50 full-time equivalent employees	**Large Employer: 50 or more full-time equivalent employees**			
	Does not offer coverage to substantially all full-time employees (and dependents)		Offers coverage to substantially all full-time employees (and dependents	
	Scenario A No full-time employees receive subsidies for Exchange coverage	**Scenario B** One or more full-time employees receive subsidies for Exchange coverage	**Scenario C** No full-time employees receive subsidies for Exchange coverage	**Scenario D** One or more full-time employees receive subsidies for Exchange coverage
No penalty	No penalty	Number of full-time employees minus 30, multiplied by $2,000	No penalty	Lesser of: Number of full-time employees minus 30, multiplied by $2,000 Number of full-time employees who receive subsidies for Exchange coverage multiplied by $3,000 (Penalty is $0 if employer has 30 or fewer full-time employees, because penalty is based on the lesser of the two calculations)

AUTOMATIC ENROLLMENT REQUIREMENT

ACA requires companies with more than 200 full-time employees that offer coverage to automatically enroll new full-time employees in a plan (and continue enrollment of current employees). Automatic enrollment programs will be required to include adequate notice and the opportunity for employees to opt out.

This automatic enrollment provision will not go into effect until regulations are issued. The Department of Labor (DOL) has indicated that this provision will not go into effect before 2014.

REPORTING AND OTHER REQUIREMENTS

ACA also imposes certain reporting requirements on employers, both with respect to the Exchange and the health coverage that they offer to employees.

Exchange Notice Requirement

Employers must provide all new hires and current employees with a written notice regarding Exchanges. ACA required employers to provide the Exchange notice by March 1, 2013, but the DOL delayed this deadline. On May 8, 2013, the DOL set a compliance deadline for providing the Exchange notices that matches up with the start of the first open enrollment period under the Exchanges, as follows:

- New Hires—Employers must provide the notice to each new employee **at the time of hiring beginning Oct. 1, 2013**. For 2014, the DOL will consider a notice to be provided at the time of hiring if the notice is provided within 14 days of an employee's start date.
- Current Employees—With respect to employees who are current employees before Oct. 1, 2013, employers were required to provide the notice **no later than Oct. 1, 2013**.

The notice must contain information regarding:

- The existent of an Exchange, including services and contact information;
- The employee's potential eligibility for premium tax credits and cost-sharing reductions through the Exchange if the employer plan's share of covered health expenses is less than 60 percent; and
- The employee's potential loss of any employer contribution if the employee purchases a plan through the Exchange.

The DOL also provided model Exchange notices for employers to use, which will require some customization. The notice may be provided by first-class mail, or may be provided electronically if the requirements of the DOL's electronic disclosure safe harbor are met. Federal agencies plan to issue more specific guidance on this notice requirement in the future.

Reporting of Health Coverage

Large employers and offering employers (those who offer minimum essential coverage through an employer sponsored plan and pay for a portion of the costs) will have certain reporting requirements with respect to their full-time employees. These reporting requirements were also delayed for one year, until 2015.

On Sept. 5, 2013, the IRS released two proposed rules on the ACA's health coverage reporting requirements. The **first proposed rule** would require large employers subject to the pay or play rules to report to the IRS and covered individuals information on the health care coverage offered to full-time employees. The **second proposed rule** would require health insurance issuers, self-insured health plan sponsors, government agencies that administer government-sponsored health insurance programs and any other entity that provides minimum essential coverage to report information on that coverage to the IRS and covered individuals.

Pay or Play—Employer Shared Responsibility Penalties

Employers will have to provide a return including:

- The employer's name, address and employer identification number;
- A certification as to whether the employer offers its full-time employees (and dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan;
- The length of any waiting period;
- Months coverage was available;
- Monthly premiums for the lowest-cost option;
- The employer plan's share of covered health expenses;
- The number of full-time employees; and
- The name, address and tax identification number of each full-time employee.

Additionally, an offering employer will have to provide information about the plan for which the employer pays the largest portion of the costs (and the amount for each enrollment category).

The employer must also provide each full-time employee with a written statement showing contact information for the person required to make the above return, and the specific information included in the return for that individual. An employer may enter into an agreement with a health insurance issuer to provide necessary returns and statements.

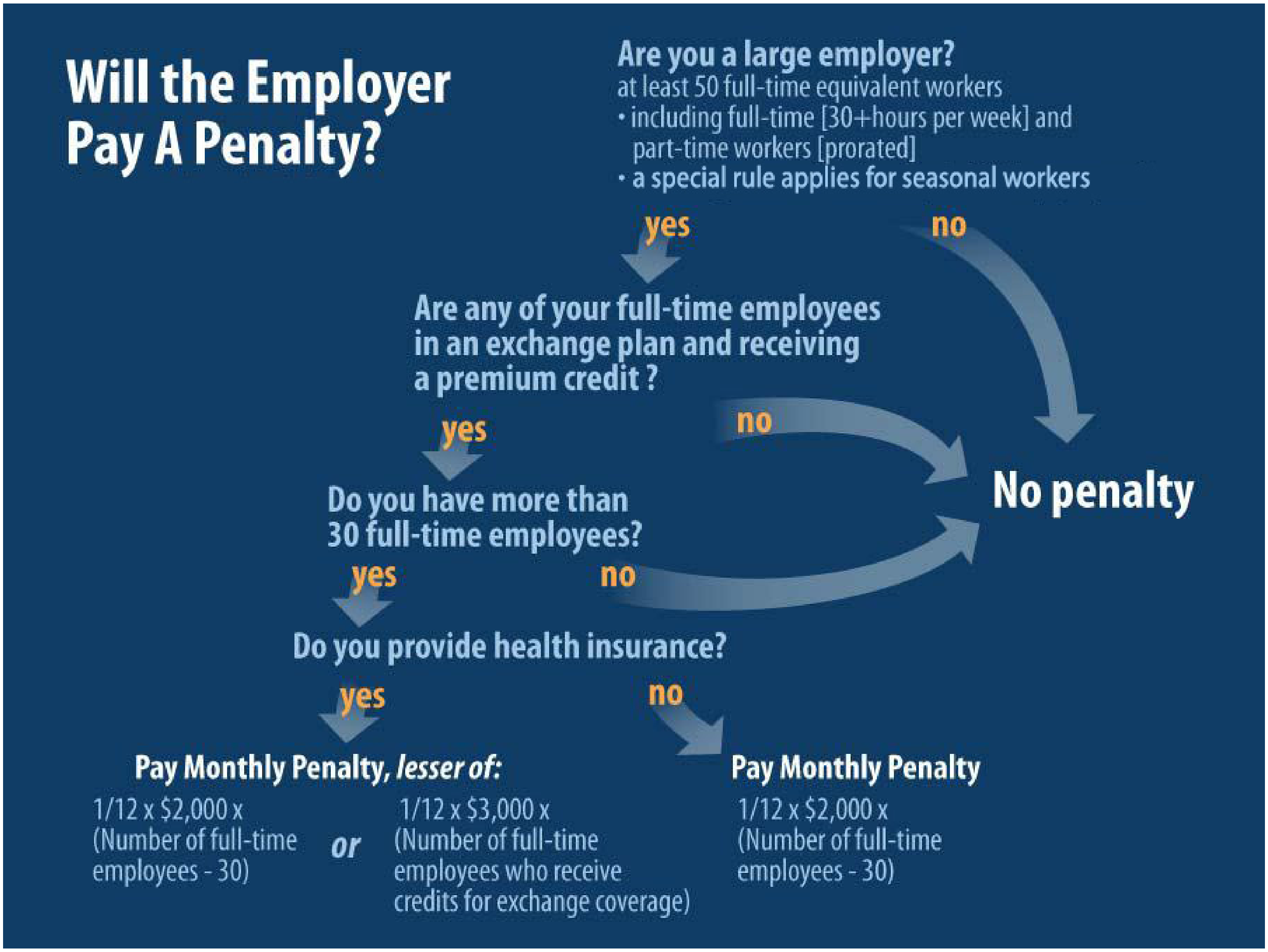
MORE INFORMATION

Please contact SDMI Insurance and Financial Services for more information on the ACA's pay or play rules.

Pay or Play—Employer Shared Responsibility Penalties

DETERMINING IF AN EMPLOYER WILL PAY A PENALTY

The following flow chart summarizes the employer shared responsibility rules in broad terms. It gives a general overview of how the various provisions under the shared responsibility rules fit together to determine possible penalties. **It does not include all the rules that may apply to a specific employer to determine its potential liability for a penalty.**



Source: Congressional Research Service