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Employer Shared Responsibility – Final Rule

The Patient Protection and Affordable Care Act added section 4980H, the employer shared responsibility requirement (commonly referred to as the "employer pay or play" rule), to the Internal Revenue Code (Code). On February 12, 2014, the Internal Revenue Service issued final regulations implementing the shared responsibility rule. The final regulations retain many aspects of the proposed regulations, with clarifications and additions, and extend many of the transitional rules provided in the proposed regulations. Additionally, the final regulations provide new transition relief for employers with 50 to 99 employees. This e-alert provides a high level overview of the final regulations and does not, therefore, discuss many of the nuances included in the final regulations.

The Basic Shared Responsibility Rule Has Not Changed: Applicable large employers must offer full-time employees and their dependent children affordable and adequate coverage or pay a penalty for every month in which such coverage is not offered.

Who Is an Applicable Large Employer?

An applicable large employer is an employer that employed 50 or more full-time employees (FTE), including full-time employee equivalents, on business days for the preceding calendar year. The determination of whether an employer is an applicable large employer is made on a controlled group basis. Thus, all FTEs and full-time employee equivalents employed by all members of a controlled group will be counted. If the controlled group is then considered to be an applicable large employer, all members of the controlled group are subject to the shared responsibility rules.

New Transition Rule: For the 2015 plan year only, an applicable large employer is an employer with 100 or more FTEs and full-time employee equivalents. Thus, employers that employ between 50 and 99 FTEs and full-time employee equivalents on business days during 2014 will not need to comply with the shared responsibility rules in 2015, subject to the following conditions. The employer must:

- Not reduce the size of its workforce to fall below the 100-employee threshold (though, reductions for bona fide business reasons are permitted);
- Not eliminate or significantly reduce the coverage in effect as of February 9,

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2014; and
- File with the IRS to certify that the employer meets these requirements.

Extended Transition Rule: To determine "applicable large employer" status for 2015, employers may use a shortened time period of any six consecutive calendar months in 2014 rather than the entire year.

Who Is a Full-Time Employee?

Applicable large employers will be required to offer affordable and adequate coverage to their FTEs and their dependent children. An FTE is an employee who averages 30 hours of service per week. "Hours of service" counted in the FTE calculation generally include all hours for which an employee is paid or entitled to payment.

Reinhart Comment: The final regulations did not provide further clarification with respect to "paid" hours. Consequently, open questions remain on exactly which "paid" hours must be counted and how to count them. For example, the regulations do not address how an employer should credit hours when an employee receives disability pay.

How Is Service Measured?

The final regulations provide two methods for determining whether an employee is an FTE: (1) the monthly measurement period and (2) the look-back measurement period. Under either method, the employer must determine the number of hours of service performed by each employee.

For hourly employees, an employer will use the employee's actual hours of service from records of hours worked and hours for which payment is made or due. For non-hourly employees, an employer will use the employee's actual hours of service or may use a days or weeks worked equivalency, whereby the employer will credit the employee with eight hours per day or forty hours per week. All hours of service performed for any member of the controlled group must be taken into account.

Recognizing that certain types of employees, such as commissioned salespeople, adjunct faculty, airline crew and on-call employees, provide unique hours of services issues, the final regulations permit employers to use a reasonable method for crediting hours of service for such employees that is consistent with the shared responsibility rules until further guidance is issued. The final

regulations offer some limited suggestions of reasonable hours crediting methods for some employment classifications.

Reinhart Comment: The final regulations make it clear that employers are not permitted to adopt the look-back measurement method for variable hour and seasonal employees while using the monthly measurement period for employees with more predictable hours of service. Whichever measurement period is selected will likely require changes to the plan eligibility provisions, especially if the look-back method is selected.

Note: The rules governing the measurement methods are extremely complex. Whichever method the employer adopts, it will have to be able to calculate hours of service for each employee for government reporting. If it has not already done so, an employer should determine whether its payroll/Human Resources Information System (HRIS) has the capability to properly capture this information. If the employer adopts the look-back measurement method, it will add more layers of complexity to eligibility determinations and government reporting. Reinhart can provide more in-depth information on the measurement methods upon request.

Monthly Measurement Method

For employers that do not elect to use the look-back measurement period rules described below, the final regulations add a "monthly measurement method" as what appears to be a default option. Under the monthly measurement method, an employer determines each employee's status as an FTE or non-FTE by counting the employee's hours of service for each calendar month.

Reinhart Comment: The monthly measurement method essentially implements the statutory method of determining FTE status in "real-time" (i.e., by reviewing hours of service for a month at the end of the month). Consequently, its use as a prospective method of determining FTE status is limited. Rather, the monthly measurement period may be more beneficial as a "check" or "proof" to ensure coverage was properly offered or not offered. This method may be a viable option for a workforce with very stable hours.

Look-Back Measurement Period

The other option for determining which employees are FTEs is the look-back measurement period. Pursuant to this method, employers will use a

measurement period, an administrative period and a stability period to determine which employees must be offered coverage. The final regulations provide guidance for four categories of employees: ongoing employees; new employees expected to be FTEs; new employees who are variable hour; part-time, or seasonal employees; and rehired employees. The rules for this method have not substantially changed from the proposed regulations.

Extended Transition Rule: For measurement periods beginning in 2014 that affect stability periods beginning in 2015, the final regulations extend the transition rule that allows an employer to adopt a transition measurement period of between six and twelve months that begins no later than July 1, 2014 and ends no earlier than ninety days before the first day of the plan year beginning on or after January 1, 2015.

Reinhart Comment: Employers subject to the shared responsibility rule in 2015 must determine as soon as possible whether they will rely on the look-back measurement period to determine FTE status so that they can establish a transition measurement period. For example, a six-month transition measurement period for an employer who will offer an open enrollment period in November for coverage effective in January must begin no later than May.

Penalties

Under the shared responsibility rules, an employer may be subject to one of two nondeductible penalties: a penalty for failure to offer coverage ((a) penalties) or a penalty for failing to offer affordable and adequate coverage ((b) penalties). An employer can be subject to only one of the penalties per calendar month, not both. Payments are assessed separately for each member of the controlled group, taking into account that member's offer of coverage, or lack thereof, and based only on that member's number of FTEs.

Offer of Coverage

An employer is considered to have "offered coverage" only if the employer offers coverage to both FTEs and their dependent children and if the FTEs have an effective opportunity to enroll or disenroll at least once per year. A dependent child for this purpose is a child as defined under Code section 152(f), which includes a son, daughter, stepson, stepdaughter, foster child and adopted child who has not attained age 26. However, the final regulations clarify that employers are not required to offer coverage to stepchildren or foster children and reiterate

that employers are not required to offer coverage to an employee's spouse.

Extended Transition Rule: The final regulations extend the transition rule for plans that did not offer dependent coverage, offered dependent coverage that was not minimum essential coverage (e.g., a dental or vision only plan), or offered coverage to some but not all dependents. Any employer that "takes steps" during the plan year that begins in 2015 towards covering dependents will not be liable for any penalty payment solely on account of failure to offer coverage to dependents for that year. For a plan that offered coverage to some but not all dependents in 2013 or 2014, the transition rule applies only to those dependents that were not offered coverage at any time in 2013 or 2014.

An offer of coverage by one member of a controlled group is considered an offer of coverage to that employee by all controlled group members. Similarly, an offer of coverage made by a multiemployer plan on behalf of a contributing employer is considered as an offer made by the employer. An offer of coverage to an employee of the staffing company performing services for a client of the staffing company (the client employer) where the staffing company is not the common law employer of the employee may be considered made by the client employer. To do so, the fee the client employer would pay the staffing firm for an employee enrolled in health coverage must be higher than the fee the client employer would pay the staffing firm for the same employee if the employee was not enrolled in the health coverage.

Reinhart Comment: The regulations do not answer all the questions regarding the comparative obligations of a staffing company versus the client employer with respect to the shared responsibility rules. Employers will need to review whether their temporary staff should be counted towards "applicable large employer" status and whether temporary staff qualify as FTEs for purposes of the penalties.

(a) Penalties: Failure to Offer Coverage

Payment of the "(a) penalty" is due if an applicable large employer fails to offer minimum essential coverage to FTEs and their dependents and an FTE enrolls in a qualified health plan (i.e., a plan offered through a state or federally run exchange) and receives a premium tax credit. The monthly payment will equal the total number of FTEs minus 30 multiplied by 1/12 of $2,000 (indexed for 2015).

New Transition Rule: For the 2015 plan year only, the final regulations provide a transition rule under which the 30-employee reduction is increased to 80

employees. Thus, for the 2015 plan year, the monthly payment will equal the total number of FTEs minus 80 multiplied by 1/12 of $2,000.

An employer is considered to have offered coverage to FTEs and their dependents if the employer offers coverage to all but 5% (or, if greater, five) of the employer's FTEs. This safe harbor applies regardless of whether the failure to offer coverage was inadvertent.

New Transition Rule: For the 2015 plan year only, the final regulations provide a transition rule under which the 5% safe harbor is increased to 30%. Thus, for the 2015 plan year, an employer is considered to have offered coverage to FTEs and their dependents if the employer offers coverage to all but 30% of the employer's FTEs.

(b) Penalties: Failure to Offer Affordable and Adequate Coverage

Payment of the "(b) penalty" is due if an applicable large employer fails to offer affordable and/or adequate coverage, and an FTE enrolls in a qualified health plan and receives a premium tax credit. Payment will also be due if an applicable large employer offers coverage to at least 95% but less than 100% of its FTEs and one of the FTEs not offered coverage receives a premium tax credit. The monthly penalty is 1/12 of $3,000 (indexed for 2015).

As noted above, under the transition rule, the 5% safe harbor is increased to 30% for the 2015 plan year. Thus, for the 2015 plan year, payment of the (b) penalty will also be due if an applicable large employer offers coverage to at least 70% but less than 100% of its FTEs and one of the FTEs not offered coverage receives a premium tax credit.

Coverage is considered "adequate" if the coverage pays for 60% of the costs. Coverage is considered "affordable" if the employee's premium for self-only coverage does not exceed 9.5% of the employee's household income. However, recognizing that employers will likely not know an employee's household income, the final regulations provide three safe harbors, based on W-2 wages, monthly rate of pay or the federal poverty line, for an employer to use to determine whether its coverage is affordable.

Additional Transitional Relief

Fiscal Year Plans. An employer that, as of December 27, 2012, offers coverage through a plan that operates on a fiscal year will not be subject to any potential payment under the shared responsibility rule until the first day of the fiscal year that begins in 2015. To be eligible for this transitional relief, generally the employer must have covered or offered coverage under the fiscal year plan to a certain portion of its employees.

Multiemployer Plans. For employers contributing to a multiemployer plan pursuant to a collective bargaining agreement or participation agreement, no penalty will be imposed on the employer for those employees for whom the employer is obligated by the collective bargaining agreement or participation agreement to contribute the multiemployer plan. The multiemployer plan, however, must offer affordable and adequate coverage to FTEs and their dependents.

The final regulations also retain an additional affordability safe harbor for multiemployer plans: coverage will be affordable if the employee's contribution (if any) does not exceed 9.5% of the wages reported to the multiemployer plan, which may be determined based on actual wages or an hourly wage rate under the collective bargaining agreement.