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Pay or Play—Employer Shared Responsibility Penalties

The Affordable Care Act (ACA) requires applicable large employers (ALEs) 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 “employer shared responsibility” or “pay or play” rules.

Beginning in 2015, ALEs 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 ALE does not offer coverage, or the ALE offers coverage that is either not “affordable” or does not provide “minimum value.”

These employer penalties were set to take effect on Jan. 1, 2014. However, on July 2, 2013, the Treasury **delayed 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 [final regulations](#) on the ACA’s employer shared responsibility rules. **Under the final regulations, ALEs that have fewer than 100 full-time (and full-time equivalent) employees generally will have an additional year, until 2016, to comply with the pay or play rules.** ALEs with 100 or more full-time (and full-time equivalent) employees must comply with the pay or play rules starting in 2015.

APPLICABLE LARGE EMPLOYERS

Only an ALE may be subject to shared responsibility penalties regarding employer-sponsored health coverage. An ALE is an employer with, on average, **at least 50 full-time employees, including full-time equivalent employees (FTEs)**, 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 ALE calculation on a monthly basis by dividing their total number of monthly hours worked by 120. These are called full-time equivalent employees (FTEs).

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:

$$20 \text{ employees} \times 96 \text{ hours}/120 = 1920/120 = 16$$

This company would be considered an ALE, 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.



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

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

Employee category	How is this category of employee used to determine ALE status?	Once an employer is determined to be an ALE, could the employer be subject to a penalty if this type of employee received a premium tax 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 ALEs

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

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

ALEs that change their plan years after Feb. 9, 2014, to begin on a later calendar date are not eligible for the delay. In addition, to qualify for this delay, an ALE must meet the following three eligibility conditions:

1. The ALE 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 ALE may not reduce the size of its workforce or the overall hours of service of its employees to satisfy the workforce size condition; and
3. During the coverage maintenance period, the ALE may not eliminate or materially reduce the health coverage, if any, it offered as of Feb. 9, 2014.

In addition, the ALE must certify that it meets all of the eligibility requirements, as part of the transmittal form the ALE is required to file with the IRS under the Section 6056 employer reporting requirements.

POTENTIAL PENALTIES

Regardless of whether or not an ALE 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.

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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 an ALE. An ALE 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 plan is not **affordable**, meaning that 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, or 9.66 percent for plan years beginning in 2016); 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 an ALE 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 **transition relief** that will phase in the "substantially all" requirement over two years. Thus, an ALE 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 70 percent**—or fails to offer coverage to no more than 30 percent—of its full-time employees (and dependents) for each calendar month during 2015 (and any calendar months during the 2015 plan year that fall in 2016); and
- **At least 95 percent**—or fails to offer coverage to no more than 5 percent (or, if greater, five)—of its full-time employees (and dependents) in 2016 and beyond. 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, ALEs 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 ALEs Not Offering Coverage—The 4980H(a) Penalty

Under Section 4980H(a), an ALE will be subject to a penalty if it does not offer coverage to "substantially all" full-time employees (and dependents) and any of its full-time employees receives a premium tax credit or cost-sharing

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reduction toward their Exchange plan. Under the ACA, the monthly penalty assessed on ALEs that do not offer coverage to substantially all full-time employees and their dependents will be equal to:

The ALE's number of full-time employees (minus 30) X 1/12 of \$2,000, for any applicable month

The final regulations include **transition relief for 2015** that allows ALEs with 100 or more full-time employees (including FTEs) to reduce their full-time employee count by 80, instead of by 30, when calculating the penalty. This relief applies for 2015 plus any calendar months of 2016 that fall within the ALE's 2015 plan year.

After 2014, the penalty amount will be indexed by the premium adjustment percentage for the calendar year. This adjustment mechanism is not affected by the one year delay for the employer shared responsibility rules.

Penalty for ALEs 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 through an Exchange 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, or 9.66 percent for plan years beginning in 2016) or the employer's plan must pay for less than 60 percent, on average, of covered expenses. Note that ALEs using an affordability safe harbor **may have to continue using a contribution percentage of 9.5 percent** (instead of the adjusted percentage) to measure their plan's affordability.

The monthly penalty assessed on an ALE 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 2014, the penalty amounts will be indexed by the premium adjustment percentage for the calendar year. This adjustment mechanism is not affected by the one year delay.

AFFORDABILITY AND MINIMUM VALUE

The final regulations provide safe harbor approaches for assessing whether an ALE's coverage is affordable. Although the ACA measures affordability based on household income, these safe harbors allow an ALE to measure affordability based on:

- The employee's **W-2 wages**;
- The employee's **rate of pay**; or
- The federal poverty level (FPL) 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. Note that ALEs using an affordability safe harbor **may have to continue using a contribution percentage of 9.5 percent** (instead of the adjusted percentage) to measure their plan's affordability.

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 allows 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.

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- **Approach Two: Checklists**—HHS and the IRS provided 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, 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 FPL safe harbor) or no cost to the employee. Thus, an ALE 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 provide 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 an ALE 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 ALE 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 employer shared responsibility provision.

Examples

Table 2 on the next page shows four types of scenarios reflecting health coverage offerings of four ALEs (columns A through D) and whether any employer penalty applies. In these ALE 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 ALE offers coverage and whether an employee receives a premium tax credit or cost-sharing reduction. The four scenarios are:

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

Scenario B—The ALE does not offer coverage, and one or more full-time employees receive a subsidy 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 ALE’s annual penalty would be $(50-30) \times \$2,000$, or \$40,000.

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

Scenario D—The ALE offers coverage, but one or more full-time employees receive a subsidy for Exchange coverage. The number of full-time employees receiving the subsidy is used in the penalty calculation for an ALE 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 ALE with 50 full-time employees; or
- The number of full-time employees who receive subsidies for Exchange coverage, multiplied by \$3,000.

Note: These examples do not take into account the one-year delay for medium-sized ALEs or the transition relief allowing ALEs with 100 or more full-time employees to reduce their full-time employee count by 80 when calculating the 4980H(a) penalty. They also do not take into account any adjustments that are made to the penalty amounts for years after 2014.

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

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

Table 2. Potential Annual Penalties for ALEs
(Applies to For-Profit and Nonprofit Organizations)

Not an ALE: Less than 50 full-time (and FTE) employees	ALE: 50 or more full-time (and FTE) 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	Scenario B	Scenario C	Scenario D
	No full-time employees receive subsidies for Exchange coverage	One or more full-time employees receive subsidies for Exchange coverage	No full-time employees receive subsidies for Exchange coverage	One or more full-time employees receive subsidies for Exchange coverage

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No penalty	No penalty	Number of full-time employees minus 30, multiplied by \$2,000	No penalty	Lesser of: <ul style="list-style-type: none">• 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 ALE has 30 or fewer full-time employees, because penalty is based on the lesser of the two calculations)
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REPORTING AND OTHER REQUIREMENTS

The 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

All employers must provide all new hires and current employees with a written notice regarding Exchanges. The Department of Labor (DOL) set a compliance deadline for providing the Exchange notices that matched up with the start of the first open enrollment period under the Exchanges, as follows:

- 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**.
- New Hires—Employers must provide the notice to each new employee **at the time of hiring beginning Oct. 1, 2013**.

The notice must contain information regarding:

- The existence 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.

Reporting of Health Coverage

Under Internal Revenue Code (Code) Section 6056, ALEs have certain reporting requirements with respect to their full-time employees. Also, employers that sponsor self-insured plans must comply with similar reporting requirements under Code Section 6055, with respect to individuals covered under the self-insured plan. These reporting requirements were also delayed for one year, until 2015. Thus, the first returns will be due in 2016 for coverage provided in 2015. However, the IRS is encouraging voluntary compliance for 2014.

On March 5, 2014, the IRS released **two final rules** on these reporting requirements, which apply for calendar years beginning after **Dec. 31, 2014**. The IRS also issued [Q&As on Section 6055](#) and [Q&As on Section 6056](#).

- [Final regulations under Section 6056](#) require ALEs subject to the employer shared responsibility rules to report to the IRS and to full-time employees information on the health coverage offered to full-time employees.
- [Final regulations under Section 6055](#) require health insurance issuers, self-insured health plan sponsors, government agencies that administer government-sponsored health insurance programs and other entities that provide minimum essential coverage to report information on that coverage to the IRS and to covered individuals.

Under these rules, forms must be filed with the IRS annually, no later than **Feb. 28 (March 31, if filed electronically)** of the year following the calendar year to which the return relates. Due to the one-year delay, the first returns required to be filed are for the 2015 calendar year, and must be filed no later than **Feb. 29, 2016** (Feb. 28, 2016, being a Sunday), or **March 31, 2016**, if filed electronically.

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Reporting entities will also be required to furnish statements annually to individuals on or before **Jan. 31** of the year immediately following the calendar year to which the statements relate. This means that the first statements (the statements for 2015) must be furnished no later than **Feb. 1, 2016** (Jan. 31, 2016, being a Sunday).

Employers will generally have to provide a return including:

- The employer's name, address and employer identification number (EIN);
- 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;
- Months coverage was available;
- Monthly premiums for the lowest-cost option;
- The number of full-time employees; and
- The name, address and taxpayer identification number (TIN) of each full-time employee.

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. However, these agreements do not transfer the employer's liability under either the employer shared responsibility rules or these reporting requirements.

AUTOMATIC ENROLLMENT REQUIREMENT

The 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.

MORE INFORMATION

Please contact Olson Insurance for more information on the ACA's pay or play rules.

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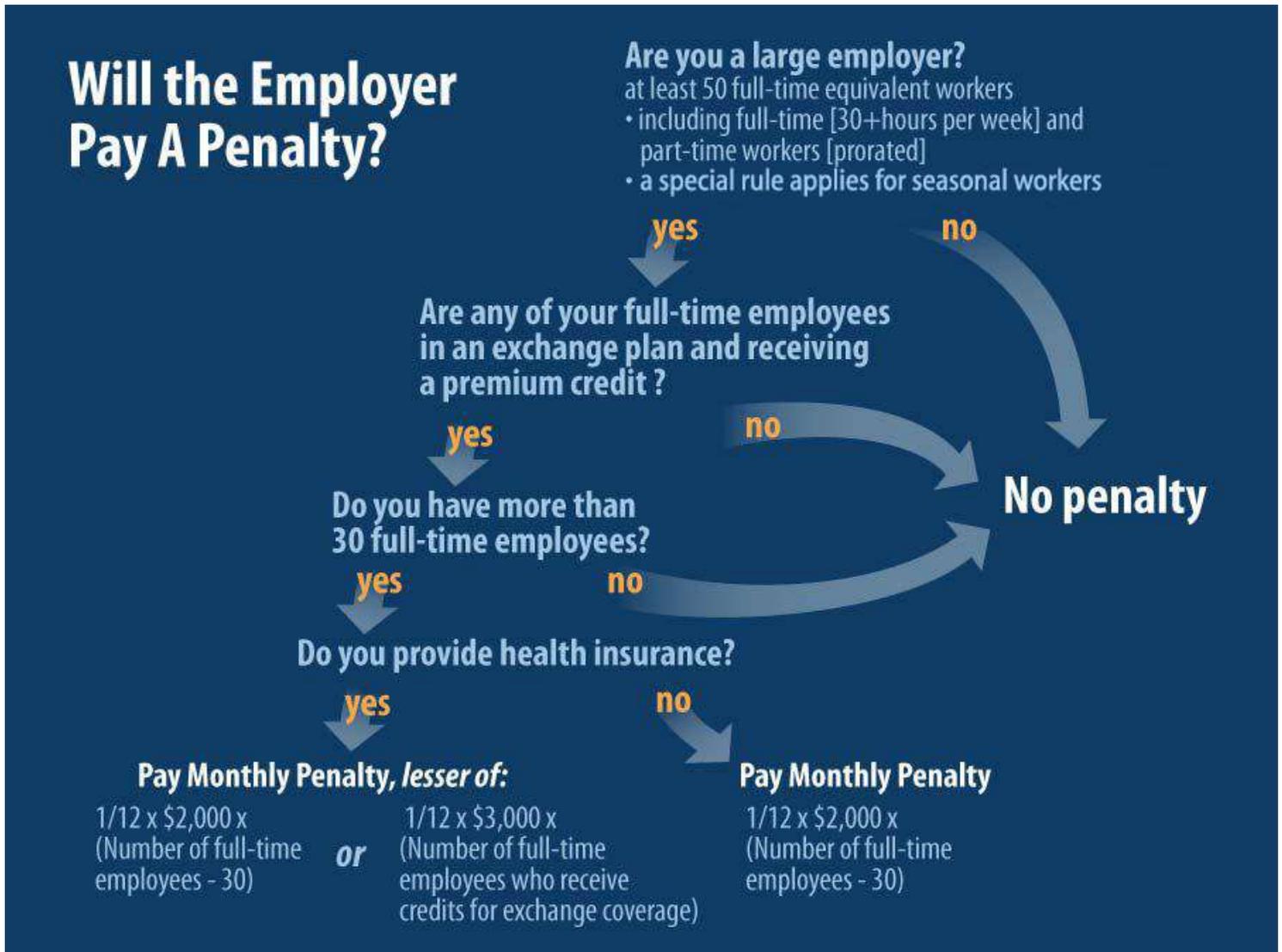
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DETERMINING IF AN EMPLOYER WILL PAY A PENALTY

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 employer 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

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