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Employment Law Update

The Affordable Care Act:

Issues Concerning Employers

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(Replaces outdated Employment Law Update from January 2013)

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The "Employer Mandate"

Perhaps the most significant provision is what is commonly called the "employer mandate." It is also referred to as "pay or play," "employer-shared responsibility," or "Section 4980H," the latter of which is a reference to the Internal Revenue Code section. Technically, the ACA does not require employers to provide health insurance to their employees, but it does impose new taxes or penalties on some employers that don't provide both adequate and affordable health insurance to employees.

Which employers are covered?

Employers that have 50 or more full-time employees (or full-time-equivalent employees) during the preceding calendar year are covered, while employers with fewer than 50 full-time employees (or full-time-equivalent employees) are not covered. Employers that are not covered will not suffer any tax or penalty for not providing health insurance to employees. There is also an exception to the 50-employee threshold where (1) the employer's workforce exceeds 50 full-time employees for 120 days or fewer during the calendar year *and* (2) the employees in excess of 50 employed during the 120 day period were "seasonal" workers.

A full-time employee is one who works 30 or more hours per week on average. Part-time employees are counted as partial full-time employees. The precise formula for counting part-time employees as full-time-equivalent employees is to take the total number of hours worked in a month by the part-time employees and divide by 120 to get the number of full-time-equivalent employees for the month. For example, an employer with 20 part-time employees each working 96 hours per month would have 1,920 total hours (i.e., 20 x 96), which divided by 120 would be counted as 16 full-time-equivalent employees (1,920 ÷ 120 = 16).

More detailed information and more examples can be found in IRS Notice 2012-58, which can be found at www.irs.gov/pub/irs-drop/n-12-58.pdf.

What does the employer mandate require?

A covered employer must either provide to its full-time employees health coverage that is both adequate and affordable or pay a tax penalty. Coverage is not required to be offered to part-time employees, who are those working on average less than 30 hours per week.

Adequate coverage must provide "minimum essential coverage." The details of what constitutes adequate coverage are beyond the scope of this article, but it basically requires a plan structured so that participants do not pay more than 40% of the cost of covered

claims. Most health insurers are familiar with the requirements of what minimum coverage must be provided, and a December 2011 HHS study found that virtually all current employer-sponsored health plans satisfy this minimum value requirement.

Most employers are more concerned with the "affordable" requirement. To be considered "affordable," the cost to the employee of individual coverage (not family coverage) offered by the employer may not exceed 9.5% of the employee's "household income." The 9.5% is for 2014 and may change in later years depending on the growth in premiums for the health insurance market. What constitutes "household income" is not necessarily what the employer pays the employee, and the employer will not necessarily know what the employee's "household income" is. Household income is defined as the modified gross income of the taxpayer, plus the aggregate modified gross income of all other individuals for whom the taxpayer is allowed a deduction for personal exemptions for the taxable year. This makes offering "affordable" coverage somewhat of a guessing game for an employer. However, there is a "safe harbor" if employers meet the 9.5% affordability threshold based on information contained in the employee's W-2 form. Even then, an employee's W-2 wages may depend on how many hours are worked, so it is still somewhat of a variable.

The following is an example of determining whether the coverage is "affordable" under the Act. If the total premium for individual coverage in an employer's plan is $5,500 for the year, and an employee's total household income is $45,000 for the year, 9.5% of $45,000 is $4,275. As long as the employee's share of the single premium is less than $4,275, the coverage will be "affordable" as to that employee. The employer would have to pay at least $1,225 or around 23% of the cost. If you take the same example except that the employee makes $35,000 per year. The coverage would be affordable if the cost to the employee is $3,325. To make it "affordable," the employer would have to pay at least $2,175 or around 40% of the premium.

When does the employer mandate become effective?

The effective date of the employer mandate has been a moving target. The requirement for covered employers to provide adequate and affordable health coverage to full-time employees or pay a penalty was originally scheduled to begin on January 1, 2014, but even though there was no amendment to the law, the Obama administration announced that it was delaying enforcement for a year. So, the new start date for the employer mandate is **January 1, 2015**.

Later, the Obama administration announced that **for employers with between 50 and 99 employees, it would not enforce the employer mandate until January 1, 2016.**

Additionally, the Obama administration also announced that it would allow **employers with 100 or more employees to avoid penalties if they offer coverage to at least 70 percent of the employer's full-time (30 or more hours) employees in 2015**.

Because the determination of the number of employees is based on the *preceding calendar year*, employers who are over or are sufficiently close to the 50-employee threshold need to be aware of that issue the year before the effective date.

If you want to see the actual regulations regarding these delays, you can find them here: http://federalregister.gov/a/2014-03082. If you want to see the Treasury Department's press release announcing them, you can find it here: http://1.usa.gov/1lY0jsz.

What are the consequences if no coverage is provided or the coverage provided is not "affordable"?

Covered employers providing no coverage must pay a tax penalty equal to the number of full-time employees, less 30, times $166.67 per month (or $2,000 per year). Those dollar amounts are for 2014, and they may be increased in later years under an indexing scheme described in the Act. For example, an employer with 50 full-time employees who does not offer coverage will have to pay $3,333.40 per month (i.e., 50 - 30 = 20; 20 x $166.67 = $3,333.40) or $40,000 per year (i.e., 50 - 30 = 20; 20 x $2,000 = $40,000). An employer with 100 full-time employees who does not offer coverage would pay $11,666.90 per month (i.e., 100 - 30 = 70; 70 x $166.67 = $11,666.90) or $140,000 per year (i.e., 100 - 30 = 70; 70 x $2,000 = $140,000).

Covered employers who provide to employees coverage that is not considered "affordable" (that is, it costs the employee more than 9.5% of the employee's household income) may have to pay a penalty of $3,000 for each employee, but only if the employee declines the coverage offered by the employer, purchases coverage through an insurance exchange, and receives a tax credit or subsidy. In other words, there is no penalty to the employer if it offers coverage that is not "affordable" if the employee buys the coverage anyway or if the employee does not buy health insurance at all (though there may be consequences to the employee if he or she does not buy any coverage). The total amount of the penalty for not providing "affordable" coverage is capped at the amount the employer would have paid if no coverage were offered to any employees (that is, the number of employees, less 30, times $2,000 per year). For example, assume that in 2014 an employer with 100 full-time employees offers coverage, but for 20 of those employees the coverage is not "affordable," and all 20 of those purchase coverage through an exchange and receive a tax credit. For each employee receiving a tax credit, the employer would owe $3,000, for a total penalty of $60,000. The employer would also save the

amount that it would have otherwise paid for its portion of the health coverage for those employees.

Grandfathered Plans and Non-Grandfathered Plans

A grandfathered plan is a group health plan or individual insurance policy that was in existence on March 23, 2010, and has not had any significant reduction or elimination in benefits or significant changes in the percentage the employee must pay for coverage or for deductibles/co-pays. Grandfathered plans were also required to notify participants of their grandfathered status. Even grandfathered plans must comply with some requirements of the ACA, such as no lifetime limits on coverage and the extension of parents' coverage to their children up to 26 years old. Unlike non-grandfathered plans, grandfathered plans may, among other things, still require cost-sharing for immunization or preventive care, may have different review or appeal processes, and may discriminate in favor of more highly-compensated employees. The exemption from the requirements of the nondiscrimination provisions of the ACA is one significant reason for some employers to retain grandfathered status, but some health insurers are not even offering plans with grandfathered status, especially for smaller employers. It is unlikely your plan is considered a grandfathered plan.

Nondiscrimination Rules

The ACA includes a nondiscrimination provision that imposes penalties if a non-grandfathered plan is found to be discriminatory in favor of "highly compensated individuals," or "HCI." Regulations implementing the nondiscrimination requirement have not yet been issued, so we do not know exactly what they will provide. However, there are some statutory provisions, and there have been already in place nondiscrimination regulations for employer health plans that are self-insured (as opposed to insured plans where the employer purchases a group health plan from a health insurance company). We can get a general idea of what the nondiscrimination regulations will provide, but not precisely, so the information here about the nondiscrimination rules are not set in stone.

An HCI will likely be defined as (a) one of the five highest-paid officers, (b) a shareholder who owns more than 10% of the employer's stock, or (c) an individual who is among the highest-paid 25% of all employees. Some individuals can be excluded from the group of the highest-paid 25% of employees and disregarded for purposes of discrimination testing if they don't participate in the plan. Those are employees who have not completed three years of service, employees who are under 25 years old, employees who work less than 35 hours per week or are seasonal employees, collectively bargained employees, and non-resident aliens who receive no U.S. source earned income.

Also, employees covered by a collective bargaining agreement and not covered by the plan can be ignored for discrimination testing purposes. Employees governed by a collective bargaining agreement can be offered a separate plan with different benefits and different contribution requirements.

An employer who offers identical health benefits to all full-time employees with the same contribution requirements regardless of age, years of service, or compensation will not be in violation of the nondiscrimination rules.

It is possible for an employer to offer health coverage in a manner that varies in terms of coverage or contribution for different employees, but it must evaluate whether the differences comply with the nondiscrimination rules. For example, an employer could have different contribution requirements for salaried employees than hourly employees, but not for executives and other employees.

We have to wait for the final regulations to come out, but it is anticipated that penalties will be stiff for failing to comply. Some who are following the issue say that the penalties for unintentional violations likely will be $100 per day per person discriminated against up to a maximum of $500,000 or 10% of the employer's previous year's health plan costs. There may be other penalties for intentional violations. It is unclear if smaller employers with under 50 employees will be subject to any penalty.

More guidance is needed before we can say anything definite, but you should be aware if you are an employer that has differences in eligibility, contribution, or benefits, you may need to make changes in the future to comply with the nondiscrimination rules. There may also be civil lawsuits to enforce compliance. Again, these rules apparently will not apply to grandfathered plans, so this is one of the more significant reasons that employers may want to retain grandfathered status if they are one of the few employers that have it.

Limits on Employee Contributions to Health Care Flexible Spending Accounts.

Employee contributions to health care flexible spending accounts will be reduced to $2,500 per year for plan years beginning in 2013.

Health Insurer Rebates

If an employer provides health coverage to its employees, it may receive a rebate from the health insurer because the ACA has provisions that govern how much a health insurer can spend on administrative costs. An employer can use the rebate to pay future premium costs, allocating it proportionately according to the proportion paid by the employees and

the employer. An employer who pays 100% of premiums can use it all itself, but if employees pay a portion, some of the rebate must be allocated to the employees to reduce their premiums. The employer can also just distribute the rebate as a payment to employees in accordance with the proportion paid by the employee. How those payments are treated for taxes depends on how the contribution was treated, i.e., pre-tax contributions or after-tax contributions. Small rebates may be used to indirectly benefit employees, such as enhancements to a wellness program.

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