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Potential Penalties for Employers Under the "Pay or Play" Rules

> Companies with more than 200 full-time employees that offer coverage must automatically enroll new full-time employees in a plan (and continue enrollment of current employees).

The Affordable Care Act 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.

The employer mandate provisions were set to take effect on Jan. 1, 2014. However, on July 2, 2013, the Treasury announced that the employer mandate penalties and related reporting requirements would be delayed until 2015. Therefore, these payments will not apply for 2014. On July 9, 2013, the IRS issued Notice 2013-45 to provide guidance on the delay, releasing subsequent proposed rules on Sept. 5, 2013. Future guidance may also affect the rules outlined in this article.

Once the employer mandate goes into effect, 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 further described in this article, 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."

Determining Large Employer Status

Only a large employer may be subject to penalties regarding employer-sponsored health coverage. A "large employer" is an employer with, on average, at least 50 full-time employees, including full-time equivalents, during the preceding calendar year.

To determine whether an employer is a large employer, 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 taking their total number of monthly hours worked divided by 120.

For example: A company has 35 full-time employees (30-plus 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

The example 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.

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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 employee category 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

Potential Penalties

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

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 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 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 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 his or her household income; or
- The plan pays for less than 60 percent, on average, of covered health care expenses.

Other ACA provisions will also affect whether full-time employees 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) and, if found eligible, are to be enrolled in those programs. Exchange premium tax credits will not be an option. This could affect whether any of an employer's full-time employees obtain premium tax credits in an exchange, and if so, how many.

"Substantially All" Requirement

The proposed 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. Under the regulations, an employer will not be liable for a 4980H(a) penalty for a calendar month if it offers coverage to all but 5 percent (or, if greater, five) of its full-time employees and dependents for that month.

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.

Penalty for Large Employers Not Offering Coverage

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. In 2014, the monthly penalty assessed on employers that do not offer coverage will be equal to the number of full-time employees (minus 30) multiplied by 1/12 of $2,000 for any applicable month. In subsequent years, the penalty amount would be indexed by the premium adjustment percentage for the calendar year.

Penalty for Large Employers Offering Coverage

Employers that do offer coverage 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'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, or the employer's plan must pay for less than 60 percent of covered expenses.

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 total number of the company's full-time employees (minus 30), multiplied by 1/12 of $2,000 for any applicable month. After 2014, the penalty amounts would be indexed by the premium adjustment percentage for the calendar year.

On Jan. 2, 2013, IRS issued proposed regulations that 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 proposed regulations state 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. 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 proposed 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 his or her 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 below 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 credit.

Table 2. Potential Annual Penalties 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		Offers coverage	
	A No full-time employees get credits for exchange coverage	B 1 or more full-time employees get credits for exchange coverage	C No full-time employees get credits for exchange coverage	D 1 or more full-time employees get credits 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 get credits 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)

The four scenarios are:

Scenario A - The large employer does not offer coverage, but no full-time employees receive credits for exchange coverage. No penalty assessed.

Scenario B - The large employer does not offer coverage, and one or more full-time employees receives

credits for exchange coverage. The annual penalty calculation is the number of full-time employees minus 30, times $2,000. In this example (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 credits for exchange coverage. No penalty assessed.

Scenario D - The large employer offers coverage, but one or more full-time employees receives credits for exchange coverage. The number of full-time employees receiving the credit 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 credits 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 premium credits, 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 premium credits, then the potential annual penalty on the employer 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.

Automatic Enrollment Requirement

Companies with more than 200 full-time employees that offer coverage must 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.

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.

They 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
- 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.

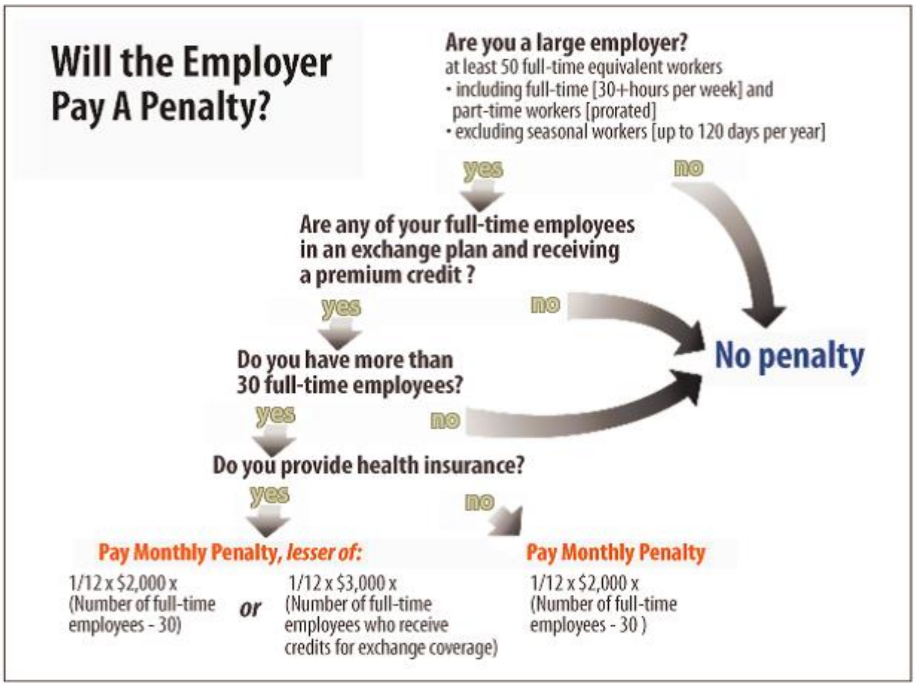

Image source: Congressional Research Service