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HEALTH CARE

You've determined you're a large employer covered by the ACA, but that's just the beginning, attorneys Wendy K. Voss and Jesse L. Noa of Potter Anderson & Corroon LLP say in this BNA Insights article, Part II of a three-part series.

The next step is understanding the large employer's obligation to provide ''minimum essential coverage'' that is ''affordable'' and provides ''minimum value'' to eligible employees, as well as the potential penalties and available safe harbors, the authors write. Now is the time to create a healthy compliance strategy for 2015 and 2016, they advise.

Your Company Is a 'Large Employer' Under the Affordable Care Act—Now What? Requirements for Coverage and Potential Penalties

BY WENDY K. VOSS AND JESSE L. NOA

The Affordable Care Act (the ACA or the Act) requires ''large employers'' (90 DLR I-1, 5/9/14) with 50 or more full-time employees to offer health insurance coverage to their eligible employees and their dependents or face the possibility of significant penalties.[1] For many employers, determining whether they are large employers will be a complicated endeavor; for others, it will be a straightforward one. Regardless, determining whether an employer is covered under the ACA is just the beginning of the inquiry for large employers. These employers must understand their obligation to provide ''minimum essential coverage'' that is ''affordable'' and provides ''minimum value'' to eligible employees. They also should be aware of the potential penalties for failing to fulfill those obligations, and the safe harbors that exist within the proposed regulatory framework.

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I. Required Coverage

As an initial matter, it is important to note that application of the ACA's large employer requirements has been delayed until Jan. 1, 2016, for those with 50-99 full-time employees.[2] All other large employers will need to comply (or face penalties) beginning Jan. 1, 2015.

a. Dependent Coverage. If an employer is a covered large employer and wishes to avoid possible penalties, then it must offer ''minimum essential coverage'' to its

[1] *See* Shared Responsibility For Employers Regarding Health Coverage, 79 Fed. Reg. 8,544 (Feb. 12, 2014) (to be codified at pts. 1, 54 & 301) (hereafter Shared Responsibility), *available at* http://www.gpo.gov/fdsys/pkg/FR-2014-02-12/pdf/2014-03082.pdf.

[2] *See* Treasury and IRS Issue Final Regulations Implementing Employer Shared Responsibility Under the Affordable Care Act for 2015, U.S. Dep't of the Treasury (Feb. 10, 2014), *available at* http://www.treasury.gov/press-center/press-releases/Pages/jl2290.aspx (28 DLR A-10, 2/11/14).

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full-time, otherwise eligible, employees and their dependents. The required coverage must be available to eligible employees and dependents no later than 90 days after the date the employees establish such eligibility. Although an employer has no financial obligation in regard to its employees' dependents, the failure to provide a plan that includes the option of dependent coverage will cause the employer to be treated as though it had made no offer of coverage.

However, so long as employers are taking steps during the 2015 plan year (including any portion of a noncalendar plan year that falls in 2016), they may not be liable for penalties for not offering dependent coverage.

This relief is available for plans that have never offered dependent coverage, have offered dependent coverage that does not fulfill the minimum essential coverage requirements of the ACA, or that have offered coverage for some, but not all, dependents. Employers that offered qualifying dependent coverage in 2013 or 2014 plan years but then dropped that coverage still would be liable for a penalty for failure to provide qualifying coverage.

b. Minimum Essential Coverage. Minimum essential coverage (MEC) is the coverage an individual must have to comply with the ACA's individual mandate and avoid the individual mandate penalty tax. MEC also describes certain types of coverage that large employers may be required to offer to avoid a penalty, which are designated as ''eligible employer-sponsored plans'' in the regulations.[3] The ACA itself defines an eligible employer-sponsored plan as a group health plan that is (a) a governmental plan, (b) any other plan or coverage offered in the small or large group market within a State, or (c) a grandfathered health plan that is offered within a group market. The final regulations clarify that the term also includes a ''self-insured group health plan offered by . . . an employer to the employee.'' (26 C.F.R. § 5000A(f)(1)(B)). Essentially, any health plan offered by a large employer will qualify as providing minimum essential coverage.

c. Minimum Value. The employer's plan also must meet the ''minimum value'' requirement to avoid triggering penalties. A plan will fail to provide the minimum value if the plan's share of the total allowed costs of benefits provided under the plan is less than 60 percent. The final regulations governing minimum value provide that employers may use one of several methods in determining whether the plan provides minimum value. For example, employers can use the minimum value calculator[4] provided by the Centers for Medicare & Medicaid Services; or, pursuant to a proposed rule and additional guidance issued by the Internal Revenue Service (IRS), use a safe harbor checklist that will be finally established by Health and Human Services (HHS) or the IRS; or, for plans with nonstandard features (such as those that would prevent the use of the minimum value calculator), obtain a certification by an actuary who is a member of the American Academy of Actuaries.[5]

The proposed safe harbors are intended to simplify the valuation process for large employers that offer typical group health coverage.[6] For example, the proposed regulations would allow a safe harbor for plans that have a $3,500 integrated medical and drug deductible, 80 percent plan cost-sharing, and a $6,000 maximum out-of-pocket limit for employee cost-sharing, provided that the plan covers all of the benefits included in the minimum value calculator discussed above. Another proposed safe harbor would be offered for plans with a $4,500 integrated medical and drug deductible, 70 percent plan cost-sharing, a $6,400 maximum out-of-pocket limit, and a $500 employer contribution to an HSA.

The proposed regulations suggest a final safe harbor for plans with a $3,500 medical deductible, $0 drug deductible, 60 percent plan medical expense cost-sharing, 75 percent plan drug cost-sharing, a $6,400 maximum out-of-pocket limit, and drug co-pays of $10/$20/$50 for the first, second and third prescription drug tiers, with 75 percent coinsurance for specialty drugs. Final guidance on these safe harbor checklists will be forthcoming.

Employers that offer and contribute to Health Savings Accounts (HSA) or integrated Health Reimbursement Accounts (HRA) that may be used only for cost-sharing must ensure that they account for these benefits when determining minimum value. Briefly stated, an employer's contributions to such plans should be counted toward the total anticipated medical spending of the standard population that will receive benefits under the plan and adjusted to reflect the expected spending for health care costs in a benefit year. The HHS Minimum Value Calculator provides a means to account for such costs.[7] By contrast, with the exception of programs designed to prevent tobacco use, funds spent towards wellness programs would not be used to reduce cost sharing under the proposed regulations.

d. Affordability. Plans that provide minimum essential coverage and minimum value also must be ''affordable'' to comply with the ACA. Plans are defined as being affordable if they require an employee to contribute 9.5 percent or less of his/her household income[8] for the taxable year towards self-only coverage. Employees who

[3] *See* 26 C.F.R. § 5000A(f)(1)(B). *See also* 26 C.F.R. § 1-36B-2(c)(3). Even if the coverage offered by a large employer does not meet the ACA's minimum value and affordability standards, it still is likely to constitute MEC, so that an individual with such coverage will not be subject to a penalty tax.

[4] The minimum value calculator can be found at http://www.cms.gov/cciio/resources/Regulations-and-Guidance/index.html.

[5] *See* Patient Protection and Affordable Care Act; Standards Related to Essential Health Benefits, Actuarial Value, and Accreditation, 78 Fed. Reg. 12,834, 12,868 (Feb. 25, 2013) (to be codified at 45 C.F.R. pts. 147, 155 & 156) (hereafter ''Rule on Establishing Minimum Value''), *available at* http://www.gpo.gov/fdsys/pkg/FR-2013-02-25/pdf/2013-04084.pdf.

[6] *See* Minimum Value of Eligible Employer-Sponsored Plans and Other Rules Regarding the Health Insurance Premium Tax Credit, 78 Fed. Reg. 25,909, 25,912 (proposed May 3, 2013) (hereafter ''Minimum Value Guidance''), *available at* http://www.gpo.gov/fdsys/pkg/FR-2013-05-03/pdf/2013-10463.pdf.

[7] *See* Minimum Value Calculator Methodology, Dep't of Health & Human Servs. (last visited May 7, 2014), *available at* http://www.cms.gov/CCIIO/Resources/Regulations-and-Guidance/Downloads/mv-calculator-methodology.pdf (noting inclusion of HSAs and HRAs in calculating minimum value).

[8] ''Household income'' is defined as the aggregate of the taxpayer's modified adjusted gross income and the modified adjusted gross income of the taxpayer's dependents who also are required to file tax returns. 26 U.S.C. § 5000A(b)(4)(B).

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are required to pay more than this may be eligible for a premium tax credit when purchasing insurance through a state or federal market place. Because penalties will be triggered under the Act only if an eligible employee of a covered employer uses a premium tax credit, those employers that provide affordable plans will be shielded from liability.

By way of example, assume that a certain employee's annual household income is $36,320. The employer's health insurance plan would be affordable if the employee was required to contribute $3,450 per year for self-only coverage. If the plan required a higher contribution, or the employee's household income was lower, then the cost would exceed 9.5 percent of the employee's household income and the insurance would be unaffordable.

II. Affordability Safe Harbors

The final regulations provide three safe harbors that employers may use to determine whether the coverage offered will qualify as affordable. So long as affordable coverage is offered, the employer will not be subject to penalties.

The safe harbor categories are the Form W-2 safe harbor, the rate of pay safe harbor, and the federal poverty line safe harbor—all of which recognize that an employer is unlikely to have information regarding its employees' household (i.e., combined) income.

The use of the safe harbors is optional, and an employer can use one or more of them for all of its employees or for any ''reasonable'' category of employees, provided it does so on a uniform and consistent basis for all employees in a category. Employers may categorize their employees into permissible categories such as those that are covered by a given collective bargaining agreement, salaried employees, hourly employees, and employees located in different states. Even if the coverage offered in fact is not ''affordable'' for a particular employee, or is not ''affordable'' throughout the year, if the employer can satisfy the terms of one of the safe harbors, it will not be subject to a penalty under the Act.

a. Form W-2 Safe Harbor. The Form W-2 safe harbor is based on the wages paid to the employee by that employer as reported in Box 1 of the Form(s) W-2. To use this safe harbor, the employer must make a full-year offer of coverage. In that case, the employer will not face penalties if the employee's required contribution for the calendar year for the employer's lowest cost self-only coverage does not exceed 9.5 percent of that employee's Form W-2 wages for the calendar year.

If the employer is a member of a large employer group and another member also pays wages to the employee, the employee's total wages from the group may be counted while only one of the employers will be responsible for providing affordable coverage to the employee. In all cases, the employee's contribution must remain a consistent amount or percentage of wages during the calendar year, which requirement is intended to prevent large employers from making discretionary adjustments to the employees' required contributions.

Use of this safe harbor might be beneficial to employers because the determination of affordability is made only once, at the end of the calendar year, rather than monthly, and on an employee-by-employee basis. Thus, its use may avoid issues related to monthly fluctuations in pay or serve to reduce administrative burdens.

For example, this safe harbor would be satisfied where an eligible employee's yearly salary was $24,000 and the monthly contribution for self-only coverage was $100, or $1,200 per calendar year. Because $1,200 is less than 9.5 percent of the employee's yearly pay (9.5 percent of $24,000 is $2,280), the safe harbor applies.

b. Rate of Pay Safe Harbor. The rate of pay safe harbor can be satisfied if an hourly employee's monthly contribution for the lowest cost self-only coverage does not exceed 9.5 percent of the employee's assumed monthly income.

To determine an employee's assumed monthly income, the employer must multiply the employee's applicable hourly rate of pay by 130. The applicable hourly rate is the lower of the employee's lowest hourly rate during the calendar month or the rate in effect on the first day of coverage (generally, the first day of the plan year).

For example, an employer that wanted to use the rate of pay safe harbor for an employee making $7.25 per hour at the beginning of the coverage period would multiply that rate by 130, resulting in an assumed monthly income of $942.50. In turn, 9.5 percent of that amount is approximately $89.54. Accordingly, the employer would be able to claim this safe harbor if the employee's monthly contribution was less than $89.54.

An employer can satisfy the rate of pay safe harbor with respect to a non-hourly employee if the employee's required monthly contribution for the lowest cost self-only coverage is no greater than 9.5 percent of the employee's monthly salary. However, if the monthly salary is reduced, whether due to a reduction in work hours or otherwise, the safe harbor is not available.

If it is taking this safe harbor, an employer may use any reasonable means for converting payroll periods to monthly salary. Moreover, if coverage is offered during at least one day during the calendar month, the entire calendar month is counted both for determining the employee's assumed income and for determining the employee's share of the premium for the calendar month.

c. Federal Poverty Line Safe Harbor. The ''federal poverty line'' (FPL) safe harbor applies if, for a calendar month, the employee's contribution for the lowest cost self-only coverage does not exceed 9.5 percent of a monthly amount established as the FPL in that year for a single individual, divided by 12.

For example, if the FPL is $11,670 (the rate established for 2014), the employer can claim the safe harbor if the employee's contribution does not exceed $92.39 for a calendar month (($11,670 x .095) / 12). This safe harbor may protect employers from penalties that otherwise would apply where employees' take home pay fluctuates because their hours fluctuate.

III. Penalties

There are two ways that large employers risk penalties related to employee coverage. The first way is by failing to provide any coverage at all. The second way is by providing coverage that either is not affordable or does not meet the minimum value requirements as discussed above.

a. Penalties for Failing to Provide Coverage. Large employers that fail to offer any coverage to their employees (or fail to offer coverage to dependents) could be liable if even one full-time employee receives a federal premium subsidy for marketplace coverage. Employers that fall into this category will face a monthly penalty equal to 1/12 of $2,000 (approximately $167/month) for each full-time employee after the first 30 full-time employees.

To calculate the potential annual penalty, employers should multiply $2,000 by the number of full-time employees over 30 employees. For example, the monthly penalty for an employer that has 200 full-time employees and fails to provide any coverage to its employees (or dependents) will be approximately $28,333 per month (1/12 x $2,000 x 170), or an annual amount of $340,000 ($2,000 x 170).

For 2015 only, however, the calculation has been modified. Because large employers with 50-99 employees will not be subject to the mandate (or possible penalties) that year, those employers with 100 or more employees may subtract 80 from the number of full-time employees, rather than 30.

b. Penalties for Providing Coverage That Fails to Meet the Minimum Value or Affordability Requirements. If a covered employer offers health insurance to its employees, but that coverage either is not affordable or does not provide minimum value, then the employer will be liable for either 1/12 of $3,000 ($250) times the number of employees receiving a subsidy, or 1/12 of $2,000 times the total number of full-time employees minus 30, whichever is less.

For example, assume that a company with 300 full-time employees offers coverage that is not affordable, and 100 full-time employees receive a subsidy. In that case, the penalty would be $25,000 per month (100 x 1/12 x $3,000 = $25,000) or an annual penalty of $300,000. This is because the alternative formula based on the total number of full-time employees less 30 would result in a higher penalty ((300-30) x 1/12 x $2,000 = $45,000/month, or $540,000/year).

Again, for 2015 only, the calculation has been modified. Because large employers with 50-99 employees will not be subject to the mandate that year, employers with 100 or more employees that are calculating the penalty due based on the number of full-time employees may subtract 80 from the number of such employees, rather than 30.

IV. Reporting Requirements

Under the ACA, large employers must file returns that report information about the coverage the employer made available to full-time employees during one or more months in the calendar year and the identity of the employees to whom the coverage was offered.[9] In turn, the employers also must furnish related statements to employees so that employees may determine whether they may claim a premium tax credit. The final regulations state that these information returns must be filed annually no later than Feb. 28, or March 31 if filed electronically. Penalties for failure to report will apply for tax years after 2015.[10]

V. Conclusion

Large employers should take steps now to finalize their compliance strategy for 2015 and 2016. First and foremost, they should make an informed decision whether to offer qualifying coverage to their employees or to be subject to possible penalties.

If large employers elect to offer coverage, they should review the benefits under their plans, eligibility requirements, cost-sharing provisions, and required employee contributions to ensure that the offered plans are both affordable and meet the minimum value requirement. They also should review the transition rules to determine which, if any, apply to them. Employers that fail to act prudently and with sufficient planning may face substantial tax penalties.

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[9] *See* 26 U.S.C. § 6056. The information required to be reported includes (a) a certification as to whether the employer offered to its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage, (b) the length of any waiting period with respect to such coverage, (c) the months during the calendar year for which coverage under the plan was available, (d) the monthly premium for the lowest cost option in each of the enrollment categories under the plan, (e) the employer share of the total allowed costs of benefits provided under the plan, (f) the number of full-time employees for each month during the calendar year, and (g) the name, address, and tax identification number of each full-time employee during the calendar year and the months (if any) during which such employee (and any dependents) were covered under any such health benefits plans.

[10] *See* Information Reporting by Applicable Large Employers on Health Insurance Coverage Offered Under Employer-Sponsored Plans, 79 Fed. Reg. 13,231, 13,245, 13,248 (Mar. 10, 2014) (to be codified at 26 C.F.R. pts. 301 & 602), *available at* http://www.gpo.gov/fdsys/pkg/FR-2014-03-10/pdf/2014-05050.pdf.

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