Planning for the 2014 Employer Health Insurance Mandate

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Key Dates

- March 23, 2010- PPACA
- June 28, 2012- Supreme Court decision
- November 6, 2012- election
- December 28, 2012- employer mandate regulations
- January 1, 2013- .9% & 3.8% "pay for" taxes began
- May 8, 2013- DOL guidance on Marketplace notice
- **July 1, 2013-** minimization steps must begin
- **October 1, 2013-** distribution of Marketplace notice to all employees
- **January 1, 2014-** health insurance Marketplace opens
- First day of 2014 fiscal plan year- employer mandate & penalties take effect

The Employer Mandate

- Beginning in 2014 ***large employers*** will become subject to nondeductible ***penalty taxes*** unless they ***offer*** adequate and affordable group health insurance to their ***full-time*** employees (and dependents in 2015)

- ***Small*** employers exempt from this mandate/penalty but not other ACA provisions

- No mandate to cover ***part-time*** employees

- ***Large*** employer and ***full-time*** employee determinations for 2014 based on 2013 demographics

Employer, Employee, Hours

- "Employer"- include related entities in "large" test
  - Apply controlled group and affiliated service group rules of IRC section 414(b), (c), (m) and (o)
- "Employee"- apply common law test
  - Exclude self-employed owners and >2% S corp shareholders
  - Include workers not on payroll but subject to employer direction and control (independent contractors, staffing company/PEO?)
- "Hours"- include hours worked and hours paid while not working (paid holiday, vacation, jury duty, etc.)
  - Optional 8 hours/day, 40/hours week equivalencies

Determine "Small" Exemption

- **50 or more** full-time employees + "full time equivalents" in prior calendar year = ***large*** employer for next calendar year
- Full-time employee = **30 or more** hours per week or 130 or more hours per month
  - IRS math 52 weeks x 30 hours divided by 12 = 130 hours/month
- Only for small employer determination part-time employee hours are converted to "full-time equivalents" (FTEs)
- Calculation made for each ***month*** in prior year then averaged to determine status for the following year

Small Employer Calculation

Template for determining full-time employees and FTEs for a ***month***:

1. List all employees for the month and their hours
2. Sort by hours (high to low)
3. Number of employees at 130 or more hours = "actual" full-time employees
4. Total the hours for all other employees (but don't count more than 120 hours for any one employee) = total "part-time" hours
5. Divide total part-time hours by 120 = number of "full-time equivalents" (FTEs) (carry to first decimal point)
6. Number of "actual" full-time employees + number of FTEs = testing "number" for that month

Small Employer Exemption

Determine the ***average number for the prior calendar year***:

1. Add the calendar year monthly totals, divide by 12 and round down to the next lowest whole number

2. If the resulting number is ***49 or less*** the employer is "small" and exempt from the mandate for the following calendar year

3. If the resulting number is ***50 or higher*** the employer is "large" and subject to the mandate for the following year (unless the seasonal employer exception applies)

Monthly Calculation Example

For the month of January 2013 employer had 72 employees:

12 salaried and hourly employees who worked 130 or more hours ("actual" full time employees)

10 hourly employees who worked between 121 and 129 hours (limit to 120 hours each = 1,200 total part-time hours for these 10)

50 hourly employees who each worked <121 hours and collectively worked 4,000 hours

Total "part-time" hours = 1,200 + 4,000 = 5,200
Divide 5,200 hours by 120 = 43.3 FTEs
12 "actual" full time + 43.3 FTEs = ***55.3 "number" for January 2013***

Special 2013 Transition Rule

- Special transition rule for 2013:
  - Don't have to test all 12 months of 2013
  - Can use ***any 6 or more consecutive month period***
  - 28 possible testing periods (6 or more consecutive months)
  - Recommendation: test all 28 iterations until you find one <50
  - Make permanent record of test results and underlying data to support 2014 exemption when IRS proposes a penalty

- Any employment practice changes need to be in place by 7/1/13 to capture the requisite 6 month minimum period

- Note: future years will test using all 12 months
  - Will need interim/estimated testing to prepare for adverse consequences when or if 50 threshold exceeded

Seasonal Worker Exception

- If employer fails the <50 general test may still be exempt if:
  - Workforce exceeded 50 for no more than 120 days or 4 months
  - 100% of the employees in excess of 50 for those 120 days or 4 months were seasonal workers
- Employer can chose any 120 days or 4 months, not required to be consecutive
  - Suggestion: test as many combinations as needed to demonstrate exemption
- "Seasonal" workers include those in agriculture, retail during holidays and "other" reasonably determined seasonal businesses (summer help in resort areas)

Exempt Small Employer- Stop Here

- 49 or less in 2013 = exempt small employer in 2014: stop here
- Determine whether to offer health insurance, to whom and at what cost without regard to the employer mandate/penalty
- But other "patient protection" reforms will apply to coverage offered
- Be mindful that offering affordable coverage to lower income employees will make them ineligible for Marketplace subsidies
- Be mindful that in 2015 new non-discrimination requirements will apply after IRS issues regulations

Large Employer- Identify 2014 Full-Time Employees

- Large employer allowed to categorize 2014 ongoing employees based on look-back to 2013 hours
- Full-time employee = 30 or more hours per week (130 hours per month)
- Threshold strategy: determine whether it makes business sense to impose a cap on the number of hours certain employees will be permitted to work in 2013 in order to make them all part-time employees in 2014
  - Virginia example- 37,000 hourly employees limited to 29 hours/week in 2013

"Look Back" Full-Time Determination

- IRS optional "look back" methodology to determine every ongoing employee's future status
  - Test the employee's hours during a prior **measurement period**
  - Analyze the data, make the status determination and notify and enroll "full-time" employees during an optional **administrative period**
  - Based on hours of employment during the measurement period treat employees as full-time or part-time during a future **stability period**

Sample "Look Back" Methodology

- 12 month measurement and stability periods for a calendar year health plan:
  - Measurement period 11/1/0001 to 10/31/0002 (12 months)
  - Administrative period 11/1/0002 to 12/31/0002 (2 months)
  - Stability period calendar year 0003 (12 months)
- Example:
  - During the "measurement period" employee F works an average of 32 hours/week and employee P works an average of 28 hours/week
  - Final calculations of average hours of F and P are made during the "administrative period"
  - During the following "stability period" employee F "deemed" to be a full-time employee and P "deemed" to be a part-time employee irrespective of the actual number of hours worked

Special Transition Rule for 2013

- Measurement and stability periods must generally be the same length (ideally 12 months each)
- Transition rule: employers may use a "short" 2013 measurement period and still get a 12 month 2014 stability period if the measurement period:
  - Is at least 6 consecutive months long
  - Ends <90 days before 1/1/2014
  - Begins no later than July 1, 2013
- 13 possible full month measurement periods in 2013

Prepare Final "Full-Time" Report

- After running the 13 iterations prepare a final analysis and report (with supporting payroll data)
- Keep report as proof of which 2013 employees are "deemed" to be full-time (and can subject the employer to penalties) in 2014
- Use report to rebut any IRS assertion of penalties

What About New Employees?

- If "reasonably expect" employee to work 30 or more hours/week treat as full-time and offer coverage within 90 days of hire
- If unable to determine whether employee will average 30 or more hours/week ("variable hour" employee) measure actual employment over a maximum 12 month period and if full-time offer coverage within one month (13 month rule)

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Will You “Pay” or “Play”?

- Identify cost of minimum qualifying coverage that needs to be offered to full-time employees to avoid penalties
  - Many employers may offer both minimum qualifying coverage (to meet the mandate) and traditional more comprehensive coverage
- 4 requirements to avoid all penalties
  - **offer** coverage to **all full-time** employees that
    - provides ***minimum essential coverage***
    - provides ***minimum value***
    - is ***affordable***

Who Must Be Offered Coverage?

- Full-time employees and their dependent children until age 26
- Transition relief for dependent coverage - no 2014 penalties for failure to offer dependent coverage
- No requirement to ever offer spouse coverage
- Offering must be communicated to full-time employees so they have an effective opportunity to participate
  - Recommendation: keep signed election forms or other acknowledgement from all full-time employees

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OOPS- 5% Margin of Error

- Statute requires offering coverage to ALL full- time employees
  - Missing 1 of 10,000 could = $20M penalty
- 5% margin of error allowed by IRS regulations
- Employer not subject to penalty for a particular month if less than 5% of full-time employees are not offered coverage (or 5 employees if > 5%)
  - Could miss 500 of 10,000 but not 501
- Coverage failure does not have to be inadvertent
  - But probably best to not purposely exclude 5%
  - Save 5% in case of actual administrative error

Minimum Essential Coverage

- In the large group market the ***minimum essential coverage (***MEC***)*** requirement means simply offering a group health plan that provides medical care
  - Relatively easy to qualify

- In the fully insured individual and small group market the policy must cover ***Essential Health Benefits (EHB),*** a much broader term encompassing 10 specific benefits

Minimum Actuarial Value

- Employer's offering must provide at least a ***60% minimum actuarial value***
- Actuarial value (AV) is a relative measure of a plan's "generosity"
  - A plan providing 60% AV would be expected to cover 60% of the cost of medical/health needs of a standard population
  - Employee would cover cost of remaining 40% through co-pays and deductibles
  - HHS and IRS provide AV calculators and safe harbors
- For comparison shopping 4 levels of AV:
  - Bronze 60% (the base level for employer mandate)
  - Silver 70% (the base level for Marketplace subsidies)
  - Gold 80%
  - Platinum 90%

Affordability

- Statute: coverage is affordable if the employee's premium for self-only coverage is no more than 9.5% of the employee's ***household*** income
- IRS temporarily allowing use of employee's W-2 Box 1 (gross wages subject to income tax) as = household income
- Box 1 is AFTER pre-tax 401(k) and cafeteria plan deductions
- Affordability is measured on cost of ***employee-only*** coverage under the lowest cost 60% minimum value (Bronze) plan offered by the employer
  - Premium can't reflect wellness incentives except tobacco cessation

Affordability Safe Harbors

- 3 IRS safe harbors on affordability of employee premium for employee-only coverage:
  - 9.5% of Box 1 wages
  - 9.5% of lowest hourly wage x 130 hours per month
  - 9.5% of Federal Poverty Level (FPL)
- Examples
  - Employee earns \$5,000/month (Box 1), employee-only coverage affordable at \$475/month
  - Employee paid \$9.00 per hour, coverage affordable at \$111.15/month (\$9.00 x 130 x 9.5%)
  - Under current FPL of \$11,490 coverage affordable at \$90.96/month (probably about \$92/month by 2014)
    - Use this option as a design based safe harbor?

Marketplace Subsidies

- Intent of ACA:
  - Individuals and households under 100% FPL covered by Medicaid (Supreme Court overturned Federal coercion)
  - Individuals and households 100% to 400% FPL receive government subsidized coverage from the Marketplace if employer doesn't offer adequate and affordable coverage
  - Employer penalties would pay for some of the subsidies
- Marketplace subsidy sets employee's premium for 2nd lowest cost Silver plan at 2% - 9.5% of household income on inverse sliding scale
  - 100%-133% FPL pay 2% of household income for a Silver plan, government pays the balance
  - 300%-400% FPL pay 9.5% of household income for a Silver plan, government pays the balance

Premium Tax Credit Table

- Percentage of household income contribution towards 2nd lowest cost Silver (70%) coverage in Marketplace:
  - 100% to 133% FPL	2%
  - From 133% to 150%	3% to 4%
  - From 150% to 200%	4% to 6.3%
  - From 200% to 250%	6.3 % to 8.05%
  - From 250% to 300%	8.05% to 9.5%
  - From 300% to 400%	9.5%
- Example of inverse linear sliding scale
  - 225% FPL is half way between 200%-250% band
  - Household income contribution half way between 6.3% and 8.05% = 7.04%
- Online calculator: search “Kaiser Subsidy-Calculator”

Advance Premium Tax Credit

- Marketplace pays subsidy directly to insurer
- No subsidy available if affordable employer coverage
- Above 400% FPL = no government subsidy
  - 70% of US households under 400% FPL
- Employers only penalized with respect to employees receiving Marketplace subsidies
- Employer penalty exposure = full-time employees with household income between 100% and 400% FPL

2013 Federal Poverty Levels (FPL)

- One person household
  - FPL $11,490
  - 133% FPL $15,282
  - 400% FPL $45,960
- Two person household
  - FPL $15,510
  - 133% FPL $20,628
  - 400% FPL $62,040
- Four person household
  - FPL $23.550
  - 133% FPL $31,321
  - 400% FPL $94,200

Potential Employer Penalties

- "Large" employer penalty exposure:
  - ***Inadequate/Unaffordable $3,000 annual penalty***: offer minimum essential coverage but less than 60% AV or unaffordable = $250 monthly penalty for each full-time employee receiving subsidized coverage from the Marketplace (the "tack-hammer penalty")
  - ***No coverage $2,000 annual penalty***: offer no minimum essential coverage and one or more employees receive subsidy = $167 monthly penalty X number of full-time employees in excess of 30 (employer penalized on employees with coverage from employer, Medicare, Medicaid, Tricare or going without coverage, the "sledgehammer penalty")

Employer Penalties

- Both penalties require at least one full-time employee receive subsidized coverage from the Marketplace
  - Subsidized coverage available between 100% and 400% of FPL
  - Under 100% FPL supposedly covered by Medicaid?
- Penalties only apply with respect to full-time employees (part-time employees ***cannot*** generate employer penalties)
- The **Inadequate/Unaffordable** penalty cannot exceed the **No Coverage** penalty
- Penalties calculated monthly, paid annually in arrears
- Penalties are non-deductible (as opposed to employer provided health insurance)

"No Penalty" Examples

- Large employer complies with intent of statute
  - Offers "adequate" and "affordable" coverage to all full-time employees in 2014
  - Also offers coverage to dependent children in 2015
- Employer has <30 full-time employees but is "large" due to large part time workforce
  - No penalty since the "no coverage penalty" only applies to full-time employees in excess of 30

“No Penalty” Examples

- Employer limits all hourly paid employees to <30 hours/week in 2013 but offers adequate and affordable coverage to full-time employees in 2014 (Commonwealth of Virginia example)
- Employer offers no coverage but limits all employees < 400% FPL to <30 hours/week in 2013 (no full-time employee can qualify for subsidized coverage in 2014)
- Employer’s offers no coverage but only employs folks >400% FPL or if <400% FPL are covered by spouse, Tricare, Medicare or Medicaid or choose to remain uninsured (risky strategy)

Inadequate/Unaffordable Penalty Example

- 100 full-time employees, employer offers adequate but **unaffordable** coverage
- 30 employees obtain coverage from spouse, Tricare, Medicare or Medicaid
- 30 employees >400 FPL buy coverage from employer
- 30 employees refuse to purchase any coverage (potentially subject to the individual mandate penalty)
- 10 employees under 400% FPL purchase subsidized coverage in the Marketplace
- ***Inadequate/Unaffordable Penalty***:
  - $3,000 x 10 employees receiving subsidies = **$30,000**

No Coverage Penalty Example

- Same facts as above except employer does not offer any coverage
- Since at least 1 employee received a subsidy penalty = \$2,000 x (100 full-time employees-30) = **\$140,000**
- Recommendation: large employers will generally want to offer minimum essential coverage that is unaffordable or fails minimum value rather than offering nothing

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Penalty Limitation Example

- The Inadequate/Unaffordable penalty cannot be more than the No Coverage Penalty
- Employer has 80 half-time and 40 full-time employees
- Covered by mandate (40 full-time + 40 FTEs exceeds 50)
- Employer offers no coverage
- All 40 full-time employees are under 400% FPL and purchase subsidized coverage in the Marketplace
- Penalty lesser of :
  \$3,000 x 40 full-time employees receiving subsidies = \$120,000
  \$2,000 x (40 total full-time employees-30) = **\$20,000**
- Recommendation: if not offering coverage limit number of full-time employees to 30 or less (make all other employees part-time?)

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Tension between Employer Penalty and Marketplace Subsidies

- Best interest of employer (penalty avoidance) can be in direct conflict with best interest of employee (obtaining health insurance subsidy from the Marketplace)
- Value of coverage employer has to offer to avoid a penalty can be far less than the value of the subsidy the employee can obtain from the Marketplace
- Marketplace subsidies unavailable if employee offered "affordable" self-only coverage through employer
  - Spouse and dependents also ineligible for subsidies if employer offers family coverage

Tension between Employer Penalty and Marketplace Subsidies

- Example where employer best interest trumps:
  - Employee earns $30,000 as breadwinner for a family of 4 (under 133% FPL)
  - Employer offers Bronze level (60%) employee-only coverage at $200/month and offers family coverage for an additional $800/month
  - Coverage is adequate and affordable ($200/month is lees than 9.5% of income), employer avoids penalty
  - Employee, spouse and dependents are all ineligible for a Marketplace subsidy

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Tension between Employer Penalty and Marketplace Subsidies

- Example where employee best interest trumps:
  - Employee earns $30,000 as breadwinner for a family of 4 (under 133% FPL)
  - No affordable employer coverage offered
  - Employee qualifies for subsidized Silver coverage (70%) for entire family for $50/month (2% of household income)
  - Actual premium for family coverage probably >$11,000
  - Government subsidy probably >$11,000

Tension between Employer Penalty and Marketplace Subsidies

- Tension severe at lower income levels:
  - Employer avoids $3,000 penalty by offering Bronze level self-only coverage for $200/month
  - Family could purchase Silver level coverage on the Marketplace for $50/month if no affordable employer coverage available
  - Employee $11,000+ economic benefit conflicts with employer $3,000 economic loss
  - When employees realize this tension what reaction?

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Tension between Employer Penalty and Marketplace Subsidies

- Extreme Tension:
  - Employer renews coverage 7/1/2013 without concern for minimum value or affordability
  - 10/1/2013 employer distributes required notice of new Marketplace and potential subsidies
  - 1/1/2014 family purchases subsidized Silver level coverage for $50/month (or Bronze for $-0-)
  - At 7/1/2014 renewal employer offers affordable self-only coverage at $200/month to avoid penalty
  - Family losses subsidized coverage after 6 months
  - Result?

Tension between Employer Penalty and Marketplace Subsidies

- Tension even exists at higher income levels:
  - Employee earns $90,000 as breadwinner for a family of 4 (almost 400% of FPL)
  - Employer avoids $3,000 penalty by offering Bronze level self-only coverage for $700/month (9.3%)
  - Family could purchase Silver level coverage on the Marketplace for same $700/month if no affordable employer coverage available
  - Employee $7,000+ economic benefit conflicts with employer $3,000 economic loss

Tension between Employer Penalty and Marketplace Subsidies

- Partial compromise for 2014?
  - Employer offers affordable Bronze level self-only coverage but doesn't offer spouse/dependent coverage
  - Employer avoids $3,000 penalty
  - Employee pays $200/month for self coverage from employer and $50/month for subsidized spouse/dependent coverage from the Marketplace
  - But in 2015 employer will have to offer dependent coverage to avoid penalty
  - Long term strategy don't offer spouse coverage?

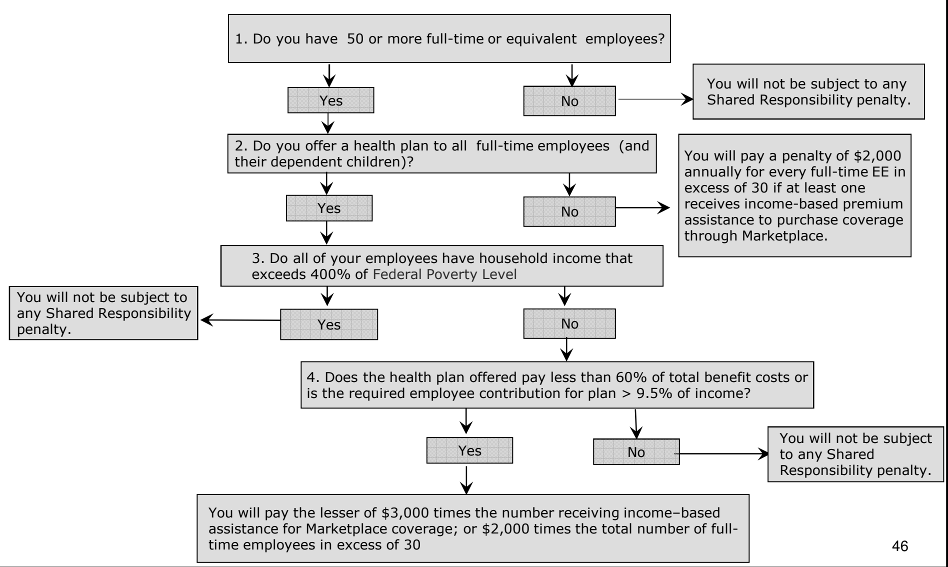
What happens above 400% FPL?

- Employee age 57 earns $95,000 as breadwinner for a family of 4 (406% FPL)
- Unsubsidized premium probably > $25,000
- Government subsidy = $-0- (earnings >400% FPL)
- Likely result: family will remain uninsured unless employer offers heavily subsidized coverage

Caution in Strategizing for Penalty Mitigation

- ERISA Section 510- employers may not …”discharge, fine, suspend, expel or discriminate against a participant or beneficiary…for the purpose of interfering with the attainment of any right to which such participant may become entitled under the plan…”
- ACA Section 1558- “No employer shall discharge or in any manner discriminate against any employee with respect to…compensation, terms, conditions or other privileges of employment because the employee…” has received a premium tax credit (subsidy) or is a whistleblower

Flowchart on Employer Mandate



Assessment and Collection Procedures

- **HHS** will notify employer when employee applies for subsidized marketplace coverage
  - employer will have opportunity to "contest" subsidy
- In January each year **employers** will file new reports with IRS that report (on monthly basis) employee full or part time status, whether offered adequate and affordable coverage, cost of coverage, etc.
- **Employees** report premium subsidies on their individual tax returns (beginning with 2014 returns due by 10/15/2015)

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Assessment and Collection Procedures

- IRS will match data from HHS, employer and employees (probably late 2015) and send a proposed penalty assessment for 2014 to employer
- Employer will have an opportunity to dispute/clarify the facts that led to the proposed assessment
- Ultimately IRS will bill the employer for the penalties (separate from other tax returns)
- Query: will GAAP require calculation/accrual of estimated penalties long before IRS assessment?

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Parallel Individual Mandate

- Separate from employer mandate to ***offer*** coverage, individuals will be penalized for not ***purchasing*** coverage
- Individual mandate penalty greater of flat dollar amount or specified percentage of income in excess of income tax filing threshold:
  - 2014 $95 or 1% of excess
  - 2015 $325 or 2% of excess
  - 2016 $695 or 2.5% of excess
- Exceptions/exemptions from individual penalty:
  - lowest cost plan exceeds 8% of household adjusted gross income
  - gap in coverage for 3 months or less
- IRS prevented by statute from collecting individual penalty via tax liens and levies (only from refunds)

Legal Issues & Planning

- Determination of related employers, common law employees and hours of service
- Exploration of opportunities to “break” a single employer or related entities apart to qualify for the small employer exemption (no later than July 1, 2013)
- Exploration of changes in employment practices (limit certain employees to <30 hours/week) to minimize “full-time” population in 2014 (start no later than July 1, 2013)
- Consideration of employment law concerns over any strategies under consideration

Appendix- Employer Mandate "Numbers"

- 5%- margin of error permitted in offering coverage to all full-time employees
- 6- minimum number of months to test under 2013 transition rules for small employer and full-time employee determinations for 2014
- 9.5%- maximum % of income self-only premium for coverage to be "affordable"
- 30- threshold hours per week to be full-time employee
- 30- threshold number of full-time employees before any penalty tax applies
- 50- threshold average number of full-time employees and "full-time equivalents" in prior calendar year to be treated as large employer subject to mandate in following year

Appendix- Employer Mandate Numbers

- 60%- Bronze level of coverage (employer mandate)
- 70%- Silver level of coverage (Marketplace subsidy)
- 80%- Gold level of coverage
- 90%- Platinum level of coverage
- 90- maximum days in waiting period before new employee must be offered coverage
- 120- divisor into total part-time hours in a month to determine "full-time equivalents"
- 130- threshold hours per month to be treated as full-time employee (functional counterpart to 30 hours/week)
- $166.67- monthly "no coverage" penalty
- $250- monthly "unaffordable coverage" penalty

Questions?

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