

Client Advisory | March 2014

Final Regulations on ACA Employer Mandate Eases Compliance for Employers in 2015

On February 10, 2014, the Department of the Treasury and the Internal Revenue Service issued final regulations on the employer shared responsibility provisions under the Patient Protection and Affordable Care Act (ACA). Although these final regulations do not differ significantly from the proposed regulations, they provide some important clarifications and offer helpful transition relief to employers for 2015. Our client advisory on the proposed regulations is available [here](#).

What Are the Employer Shared Responsibility Provisions?

Employers with 50 or more full-time employees, including full-time equivalents (FTEs), during the preceding calendar year ("applicable large employers") may be subject to an excise tax under the employer shared responsibility provisions if they either (i) fail to offer group health plan coverage to at least 95% of their full-time employees or (ii) offer group health plan coverage that fails to provide minimum value or is unaffordable by the employee, and at least one full-time employee receives a premium tax credit or cost sharing subsidiary for health coverage purchased through a health insurance exchange.

The penalty for failing to offer coverage to full-time employees (and their dependents) is \$2,000 for each full-time employee (excluding up to 30 full-time employees). The penalty for offering coverage to full-time employees (and their dependents) that is unaffordable or fails to provide minimum value is the lesser of \$3,000 for each full-time receiving a credit or subsidy or \$2,000 for each full-time employee (excluding up to 30 full-time employees).

Highlights of Key Changes Made By the Final Regulations

- ♦ **Determining Full-Time Employee Status.** The ACA defines a "full-

time employee" as an employee who is employed on average at least 30 hours per week or 130 hours per month. As under the proposed regulations, an employee's hours of service include the following: (i) each hour for which the employee is paid, or entitled to payment, for the performance of duties; and (2) each hour for which the employee is paid, or is entitled to payment, on account of time during which no duties are performed due to vacation, holiday, illness, incapacity, layoff, jury duty, military duty or leave of absence.

The final regulations exclude the following hours of service for purposes of determining an employee's full-time status:

- ♦ **Volunteer Hours.** Hours worked by a "bona fide volunteer" of a governmental entity or 501(c) tax-exempt entity whose only compensation is reimbursement of reasonable expenses and certain reasonable benefits and nominal fees.
- ♦ **Student Employees.** Hours of service performed by students in positions subsidized through federal, state or local work study programs. However, this is not a general exception for all student employees. Hours of service for which a student employee is paid or entitled to payment in a capacity other than through a federal, state or local work study

program or through an internship or externship program for an outside employer would be counted for determining full-time employee status.

- ♦ **Adjunct Faculty.** The final regulations provide that, until further guidance is issued, employers of adjunct faculty may use any reasonable method for crediting hours of service. A reasonable method set forth in the final regulations is to credit adjunct faculty with 2-¼ hours of service per week for each hour of teaching or classroom time (including class preparation and grading) and an hour of service per week for each additional hour outside of the classroom (such as required office hours or required attendance at faculty meetings).
- ♦ **Measurement Periods.** The final regulations retain the look-back measurement period described in the proposed regulations and provide guidance for employers electing to use a current monthly measurement period. Under the monthly measurement period, an employer determines an employee's full-time status by counting the employee's hours of service for each calendar month. An employer using the monthly measurement period will not be subject to the "offer of coverage" penalty as long as the employee is offered afford-

able, minimum value health coverage no later than the first day of the 4th full calendar month after the employee meets the plan's eligibility requirements.

- ♦ **New Employees "Reasonably Expected" to be Full-Time.** Under both the proposed and final regulations, determining whether a new employee is a full-time employee or variable hour employee depends on whether the new employee is reasonably expected to work on average at least 30 hours per week at his or her start date. The final regulations state that an employer's determination of whether a new hire is or is not a full-time employee is based on the facts and circumstances. Factors to consider include (1) whether the employee is replacing an employee who was or was not a full-time employee; (2) the extent to which employees in the same or comparable positions are or are not full-time employees and (3) whether the job was advertised or otherwise communicated to the new hire as requiring 30 (or more) hours of service or less than 30 hours.
- ♦ **Seasonal Employees.** Similar to variable hour employees, employers may use the look-back measurement period rules to determine the full-time status of seasonal employees. The final regulations define a "seasonal employee" to mean those employees who are hired into a position for which the customary annual employment is six months or less.
- ♦ **Break in Service/Rehired Employee.** The final regulations modify the rules regarding when a rehired employee is treated as a new employee or as a continuing employee. Under the final regulations, if an employee's period of absence for which no hours of service are credited is at least 13 consecutive weeks (reduced from 26 weeks under the proposed regulations), the employee will be treated as a

new employee upon return to employment. The final regulations allow employers to use the "rule of parity" for periods of absence at least four consecutive weeks but less than 13 weeks in length. The 26-week threshold continues to apply to employees of educational institutions.

- ♦ **Dependents.** The final regulations exclude foster children and stepchildren from the definition of dependent and clarify that a child is a dependent for the entire calendar month during which the child attains age 26. Spouses continue to be excluded.
- ♦ **Offers of Coverage.** The final regulations provide that an effective opportunity to decline coverage is not required for an offer of coverage that provides minimum value and is offered either at no cost to the employee or at a cost of no more than 9.5% of the monthly federal poverty line amount for a single individual. This rule may impact employers who require mandatory coverage.
- ♦ **Rates of Pay Safe Harbor.** As mentioned above, an employer may be subject to an excise tax if the health coverage offered to employees is not affordable. The proposed regulations provided three separate safe harbors under which an employer could determine affordability: (1) Form W-2 safe harbor, (2) rate of pay safe harbor and (3) federal poverty line safe harbor.

Under the rate of pay safe harbor, an offer of coverage is treated as affordable if the employee's required contribution for the calendar month for

the lowest cost self-only coverage does not exceed 9.5% of an amount equal to 130 hours multiplied by the lower of the employee's hourly rate of pay as of the first day of the plan year or the employee's lowest hourly rate of pay during the calendar month.

Unlike the proposed regulations, the final regulations allow an employer to use the rate of pay safe harbor for determining affordability even if an hourly employee's rate of pay is reduced during the year. In this situation, the rate of pay is applied separately to each calendar month, rather than to the entire year. In contrast, the rate of pay safe harbor is not available for a non-hourly employee whose base salary is reduced during the plan year.

Transitional Relief

The final regulations extend most of the transition relief provided in the proposed regulations and also provide new transitional rules for 2015.

New transitional relief for 2015 includes:

- ♦ **Applicable Large Employers with Fewer than 100 Full-Time Employees.** Applicable large employers with at least 50 but fewer than 100 full-time employees (including full-time equivalents) during 2014 are not subject to the employer shared responsibility penalties for 2015 (and, for fiscal year plans, that portion of the plan year that carries into 2016). To qualify for this relief, during the period beginning on February 9, 2014 and ending on December 31, 2014, the employer must not reduce its workforce or the overall hours of service for its employees in order to satisfy the workforce size condition. The employer cannot eliminate or materially reduce any health coverage offered to employees as of February 9, 2014, and the

employer must certify, as part of the informational reporting requirements under Section 6056 of the Code, that it meets the eligibility requirements for this transitional relief.

- ♦ **“Offer of Coverage” Threshold Lowered to 70%.** Generally, the proposed and final regulations provide that an employer is not subject to the \$2,000 “offer of coverage” penalty if it offers coverage to at least 95% of its full-time employees (and their dependents). For 2015 (and, for fiscal year plans, that portion of the plan year that carries into 2016), the 95% threshold is lowered to 70% so that employers that offer coverage to at least 70% (or that fails to offer coverage to no more than 30%) of its full-time employees (and their dependents) will not be subject “offer of coverage” penalty. Even if the employer offers coverage to at least 70% of its full-time employees, it may still be subject to the \$3,000 “affordability” penalty for every full-time employee who is not provided affordable coverage and receives a credit/subsidy for health coverage purchased through a health insurance exchange.
- ♦ **Calculation of “Offer of Coverage” Penalty for 2015.** For 2015 (and, for fiscal year plans, that portion of the plan year that carries into 2016),

the \$2,000 “offer of coverage” penalty will be calculated by reducing the employer’s number of full-time employees by 80 rather than 30.

The extended transitional relief includes:

- ♦ **Non-Calendar Year Plans.** Employers with fiscal year plans (those that do not start on January 1) will not be subject to the employer shared responsibility penalties prior to the first day of the plan year that begins in 2015 as long as the employer maintained a fiscal year plan as of December 27, 2012 and offers affordable, minimum value health coverage to full-time employees no later than the first day of the 2015 plan year.
- ♦ **Shorter Measurement Periods for Stability Periods Starting in 2015.** For purposes of stability periods beginning in 2015, employers may use a measurement period of at least 6 consecutive months that begins no later than July 1, 2014 and ends no earlier than 90 days before the first day of the plan year beginning on or after January 1, 2015.
- ♦ **Shorter Period for Determining Applicable Large Employer Status in 2015.** For 2015, an employer may determine its status as an applicable large employer by determining whether it employed on average at least 50 full-time employees (includ-

ing FTEs) during any consecutive 6-month period, as selected by the employer, during the 2014 calendar year (rather than the entire year).

- ♦ **Coverage for Dependents.** An employer will not be subject to a penalty for failing to provide coverage for dependents in 2015 if the employer is taking steps in its 2014 plan year to add dependent coverage.

Next Steps for Employers

Now that the IRS has finalized the employer shared responsibility regulations, employers should evaluate their practices to ensure compliance with the ACA’s employer mandate. Employers should identify full-time and variable hour employees, decide whether to adopt a look-back measurement period for identifying full-time employees, specify its stability and administrative periods and determine whether they will be able to take advantage of the one-year delay for employees with between 50 and 99 employees. The rules are complex, and many issues are still not finalized; however, employers should continue developing their strategy for compliance with the employer mandate provisions.

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