CLIENT NEWS BRIEF

Digging Deeper Into Recent Affordable Care Act Topics: Guidance Employers Need To Know

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If you thought you were finally getting a handle on the Affordable Care Act (ACA), the influx of IRS guidance that came at the end of the 2015 calendar year probably reopened some old wounds. On December 29, 2015, we alerted you to IRS Notice 2015-87 (Notice), a compilation of Questions and Answers intended to provide guidance on a number of complex and highly technical topics related to group health plan market reform and employer shared responsibility requirements. The purpose of this Client News Brief is to dig a little deeper into the topics addressed by the IRS Notice that may be of particular interest to state, school, and other local public agency employers. In addition, we encourage you to watch our video on some common questions and issues that arise from the implementation of the Affordable Care Act.

1. Affordability Calculations – Inflation Adjustments

Under the ACA, coverage offered by applicable large employers to their full-time employees must be affordable in order for the employer to avoid liability. Coverage is affordable if the employee's required contribution for self-only coverage does not exceed 9.5% percent of the taxpayer's household income. Since employers are unlikely to know their employees' household incomes, the ACA provides various safe harbors to assist employers in determining whether their offers of coverage are under the affordability threshold of 9.5%. The Notice states that the IRS intends to amend the regulations to clarify that this 9.5% threshold in the affordability safe harbors is subject to the same annual adjustments for inflation as contained elsewhere in the ACA. Specifically, this amount will be adjusted as follows: 9.56% for plan years beginning in 2015; and 9.66% for plan years beginning in 2016. The same adjustments apply to the 9.5% referenced in the ACA with respect to the Multiemployer Plans, as well as to the reporting of "Qualifying Offers."

2. Penalty Increases – Inflation Adjustments

The Notice also clarifies the adjusted amounts relative to the $2,000 and $3,000 penalty amounts, or "assessable payments," applicable to employers under the employer shared responsibility provisions of the ACA. Generally, section 4980H of the Internal Revenue Code provides that an applicable large employer may be subject to an assessable payment if certain conditions are met related to the failure to offer appropriate coverage to full-time employees. For 2015, the adjusted $2,000 assessable payment amount is $2,080, and the adjusted $3,000 assessable payment amount is $3,120. In 2016, these assessable payment amounts will go up to $2,160, and $3,240, respectively. The Treasury and IRS anticipate that they will post future adjustments on the IRS.gov website.

3. Affordability & Transition Relief

The Notice addresses how various types of common arrangements are treated, or will likely be treated, for purposes of determining an employee's required contribution towards the cost of self-only employer-sponsored coverage. This category of guidance is particularly significant to employers because much of

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the IRS treatment described in the Notice will likely change how employers currently view employee and employer contributions to health care and impact whether coverage is affordable for purposes of the ACA. However, there is some transition relief for employers – described below in the relevant sections – if an arrangement was in place prior to or on December 16, 2015. For an arrangement to be in place prior to or on December 16, 2015, it must meet one the following conditions:

1) The employer offered the arrangement (or a substantially similar arrangement) for a plan year including December 16, 2015; or
2) A board, committee, or similar body or an authorized officer of the employer specifically adopted the arrangement before December 16, 2015; or
3) The employer had provided written communications to employees on or before December 16, 2015 indicating that the opt-out arrangement would be offered to employees at some time in the future.

Contributions to HRA

Employer contributions to a plan-integrated health reimbursement arrangement (HRA) are counted toward the employee's required contribution (meaning they reduce the dollar amount of that required contribution) only if: (1) an employee may use the contribution to pay premiums; and (2) the amount of the employer's annual contribution is required under the terms of the arrangement or otherwise determinable within a reasonable time before the employee must decide whether to enroll in the eligible employer-sponsored plan. This is true even if the amount may be used for cost-sharing and/or for other health benefits not covered by that plan in addition to premiums.

Flex Contributions

Under a § 125 cafeteria plan, the employee's enrollment in a group health plan generally is funded by salary reduction but may also be funded by employer flex contributions. If the employer flex contribution qualifies as a "health flex contribution," it will count towards the employee required contribution, reducing the amount of the required contribution. To qualify as a health flex contribution, all of the following conditions must be met: (1) the employee may not opt to receive the amount as a taxable benefit (i.e., cash); (2) the employee may use the amount for minimum essential coverage; and (3) the employee may use the amount exclusively to pay for medical care. For instance, if an employee may use the flex contribution towards life insurance or dependent care through the cafeteria plan, the contribution is not a health flex contribution. Similarly, if the employee may opt to receive the contribution as cash instead of putting it towards health care, the contribution is not a health flex contribution. If the employer flex contribution is not a health flex contribution, it does not reduce an employee's required contribution, which may negatively impact the affordability of coverage.

As a form of transition relief, all employer flex contributions that are available to pay for health coverage, regardless of whether they qualify as health flex contributions, will count toward reducing the employee's required contribution for plan years beginning before January 1, 2017 unless the flex contribution arrangement was adopted after December 16, 2015, or substantially increases the amount of the flex contribution after December 16, 2015.

Employers that wish to offset the cost of the employee's required contribution should review their plan structure to ensure that the flex contribution is only available for medical-related expenses.

Opt-out Payments

The Notice focuses on the IRS position regarding the treatment of unconditional opt-out arrangements. An unconditional opt-out arrangement is an arrangement that provides for a payment to an employee that is conditioned solely on an employee declining coverage and not on an employee satisfying any other meaningful requirement, such as proof of coverage elsewhere. For instance, consider an employer that offers employees group health coverage through a § 125 cafeteria plan, requiring employees who elect self-only coverage to contribute $200

per month toward the cost of that coverage but offering employees an additional $100 per month in taxable wages if they decline coverage, no questions asked. This is an unconditional opt-out arrangement.

The IRS considers such an arrangement to be analogous to a "cash or coverage" arrangement – the employee must choose between receiving the $100 payment and enrolling in health care coverage. The IRS intends to issue proposed regulations that require employers to include the amount of the opt-out payment in the employee's required contribution for purposes of the employer shared responsibility provisions. Referring back to our example, under this rule, the employer would report $300 as the monthly required employee contribution towards the cost of coverage, rather than $200 because the employee is foregoing $100 in order to enroll in health care coverage. The likely intent behind this rule is to deter employers from incentivizing employees to decline health care coverage, particularly in instances where coverage is not available to them elsewhere. The proposed regulations will also likely address and request comments on the treatment of opt-out payments that are conditioned on the satisfaction of additional conditions, such as proof of coverage. However, the Notice does not elaborate on what position the IRS is likely to take on these arrangements.

The regulations will apply only for periods after the issuance of final regulations, but the IRS and Treasury anticipate that any unconditional opt-out arrangements adopted after December 16, 2015 will be subject to the rule. In other words, employers that are subject to the ACA should consider these anticipated regulations prior to approving a new opt-out or cash-in-lieu arrangement after December 16, 2015, because these opt-out payments may increase the employee required contribution to the cost of health care coverage.

4. "Hour of Service"

For purposes of determining full-time status of employees, the ACA defines the term "hour of service" as each hour for which an employee is paid, or entitled to payment, for the performance of duties for the employer; and each hour for which an employee is paid, or entitled to payment by the employer for a period of time during which no duties are performed due to vacation, holiday, illness, incapacity (including disability), layoff, jury duty, military duty or leave of absence (as defined in 29 CFR 2530.200b-2(a)). The Notice provides clarification on certain limitations to this definition, particularly with regard to its reference to 29 CFR 2530.200b-2(a), which is an existing federal Department of Labor regulation. The Notice clarifies that an "hour of service" for purposes of the ACA does not include any of the following:

1) Hours after the individual terminates employment with the employer.
2) An hour for which an employee is directly or indirectly paid, or entitled to payment, on account of a period during which no duties are performed if such payment is made or due under a plan maintained solely for the purpose of complying with applicable workers' compensation, or unemployment or disability laws.
3) An hour for a payment which solely reimburses an employee for medical or medically related expenses incurred by the employee.
4) Periods during which the employee is not performing services but is receiving payments in the form of workers' compensation wage replacement benefits under a program provided by the state or local government.

The Notice clarifies that the limitation contained in 29 CFR 2530.200b-2(a) regarding the maximum amount of hours that may be credited to an employee for a single continuous period during which the employee performs no duties does not apply in the ACA context (please note that there does exist a 501-hour limit on hours of service required to be credited to an employee of an educational organization during employment break periods, which continues to apply).

The Notice further clarifies that periods during which an individual is not performing services but is receiving payments due to short-term disability or long-term disability do result in hours of service for any part of the period during which the recipient retains status as an employee for the employer, but only if payments are made from an arrangement to which the employer contributed to directly or indirectly. For example, disability payments made by or from a trust fund or insurer to which the employer contributes to or pays premiums for would be deemed to be made by the employer and therefore would count towards the employee's hours of service as long as the employee remains employed. A disability arrangement for which the employee contributed to on an after-tax basis would be treated as an arrangement to which the employer did not contribute, meaning it would not be considered hours of service.

5. Rehire/Break Rules for Staffing Agencies

Under the ACA regulations, specific rules apply to educational organizations regarding the identification of full-time employees, including how to treat breaks in service. The Treasury and IRS anticipate amending these regulations to extend the same rules to employees of third-party staffing agencies or other employers that are not technically "educational organizations," but that employ individuals that provide services for educational organizations. For instance, the rules would apply to an employer with respect to a bus driver who is primarily placed to provide bus driving services for an educational organization, regardless of whether the employer itself is an educational organization.

6. Aggregation Rules (Government Entities)

The ACA regulations include certain aggregation rules for purposes of determining whether an employer has 50 or more full-time and full-time equivalent employees, and therefore is an applicable large employer. Specifically, the following groups may in each case be treated as a single employer: (1) corporations that are part of a controlled group of corporations, (2) groups of other types of entities that are under common control, and (3) members of an affiliated service group. The aggregation rules do not expressly address the application of these standards to government entities, which are defined as the government of the United States, any State or political subdivision thereof, and any Indian tribal governments, and likely include local governmental agencies such as school districts. The Notice clarifies that government entities may apply a reasonable, good faith interpretation of the employer aggregation rules for purposes of determining whether a government entity is an applicable large employer, and therefore subject to the employer shared responsibility provisions and reporting requirements of the ACA.

Please note that this news brief does not detail every element of the topics discussed above. We encourage you to review the Notice for a full review of the topics addressed by the Treasury and IRS.

If you have any specific questions regarding the impact of this Notice on your organization, please contact one of our nine offices located statewide. You can also visit our website, follow us on Facebook or Twitter, or download our Client News Brief App.