Health Care Reform's
Employer Shared Responsibility Penalties: A Checklist for Employers

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Historically, employers have had complete discretion in deciding whether to offer group health plan coverage to their employees. If they offered coverage, they had to comply with the requirements of the Employee Retirement Income Security Act ("ERISA"), the Internal Revenue Code (the "Code"), and other applicable laws. However, if they did not offer coverage, they were not subject to penalties. It was simply a business decision whether to offer coverage. Starting in 2015, this will change-- employers employing at least a certain number of employees (generally 50 full-time employees or a combination of full-time and part-time employees that is equivalent to 50 full-time employees) will be subject to the employer shared responsibility provisions under Section 4980H of the Code, sometimes referred to as the "large employer play or pay penalties."

In July 2013, IRS announced that the penalties would not take effect until 2015. The one-year delay was welcome news, but it unfortunately resulted in many employers pushing this issue to the back burner. With the IRS just having published final regulations on February 12, 2014, now is a great time to refocus on this issue.

Under these new rules, "large" employers will be subject to a penalty if they either: (1) fail to offer minimum essential coverage to substantially all full-time employees (and their dependents); or (2) offer employer-sponsored coverage to substantially all full-time employees (and their dependents), but the coverage is either not "affordable" or does not provide "minimum value." The penalties are due only if at least one of a large employer's full-time employees receives a premium tax credit for purchasing individual coverage on a Health Insurance Marketplace (hereinafter a "Marketplace").

Although the rules take effect for most employers on January 1, 2015, what an employer's workforce looks like in 2014 is determinative of whether the employer may be subject to the penalties in 2015. Also, many employers may need to start counting hours in 2014 in order to take advantage of the look-back measurement safe harbor that permits full-time or part-time status to be locked in for some period rather than having to track full-time status each month. Time is of the essence in understanding these new rules.

This checklist is intended to help employers:

- Determine whether an employer is a "large" employer (Worksheet #1);
- Calculate the potential penalties (Worksheet #2);
- Identify "full-time employees" for purposes of calculating the penalties (Worksheet #3); and
- Design group health plans to avoid/minimize the penalties (Worksheet #4).

*Important Note: This checklist was originally published on March 20, 2013. It has been updated to reflect the final regulations published on February 12, 2014. The purpose of this checklist is to provide general information about the large employer shared responsibility penalties under the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act (the "Affordable Care Act" or "ACA") that apply to employer-sponsored group health plans. The Affordable Care Act and related guidance go into much more detail and should always be consulted when considering its application to any particular plan. More detailed information about these rules may be found in the **final regulations** and the IRS series of **questions and answers** on the employer shared responsibility provisions. This summary should not be relied on as legal advice or as a legal opinion on any specific facts or circumstances. You are urged to consult legal counsel concerning your situation and any specific legal questions you may have.*

WORKSHEET #1
IS THE EMPLOYER A "LARGE" EMPLOYER?

Basic rule – To be subject to the large employer penalties for a calendar year, an employer must generally employ at least 50 full-time employees or a combination of full-time and part-time employees that equals at least 50 during the preceding calendar year. For example, if an employer has at least 50 full-time employees (including full-time equivalents) for 2014, it will be considered a large employer for 2015. Employers will need to repeat this analysis each year. *Important Note: See pages 3 to 4 below for a special transition rule that gives employers with 50 to 99 employees in 2014 an additional year, until 2016, to comply if they meet certain requirements*.

- Example: An employer that employs 40 full-time employees (that is, employees employed 30 or more hours per week on average) and 20 employees employed 15 hours per week on average has the equivalent of 50 full-time employees.

Some important rules to keep in mind when determining whether an employer is a large employer:

- The rules apply to all types of employers: All employers are potentially subject to the employer shared responsibility provisions, including for-profit, non-profit, and government entities, including federal, state, local, and Indian tribal government employers.

- *Related companies are combined*: In determining whether an employer is "large", the employer includes all related businesses (each referred to as a "company") under Code Sections 414(b), (c), (m), and (o). This means employers have to count all full-time and full-time equivalent employees in the group. Employers who file as qualified separate lines of business ("QSLOBs") for other employee benefit purposes cannot rely on the QSLOB rules for this purpose. If the combined total meets the threshold then each separate company is subject to the employer shared responsibility provisions, even those companies that individually do not employ enough employees to meet the threshold.

- *Common law employees are counted*: The employer must count each of its common law employees. As a result, careful consideration should be given to independent contractors and temporary employees[1] because such individuals are often misclassified. Failing to count all common law employees could cause an employer to conclude it is not "large" when, in fact, it is.

    - ☐ *Employers should assess the true relationship of all individuals who perform services for them*.

- *Some individuals are not counted*: Sole proprietors, partners in a partnership, 2% S Corp shareholders, "leased employees" (as defined in Code Section 414(n)(2)), and workers described in Code Section 3508[2] are not employees for this purpose, so they are not counted. Most employees who work outside the United States are also excluded.[3]

- *Number of full-time employees*: A full-time employee for any month is an employee (including seasonal workers) who is employed for an average of at least 30 hours of service per week, or 120 hours of service in a calendar month. Each such employee counts as one employee for the calendar month.

- *Seasonal workers:* A "seasonal worker," for purposes of determining whether an employer is large, is a worker who performs services on a seasonal basis where, ordinarily, the employment pertains to or is of the kind exclusively performed at certain seasons or periods of the year and which, from its nature, may not be continuous or carried on throughout the year (e.g., agricultural and retail workers employed exclusively during holiday seasons). For this purpose, employers may apply a reasonable, good faith interpretation of the term "seasonal worker."

- *Number of full-time equivalents*: Employers must also include full-time equivalents for each calendar month. All employees (including seasonal workers) who are not employed on a full-time basis for a calendar month are included in calculating the number of full-time equivalents for that month. Converting such employees to a full-time equivalent involves two steps.

    - Step 1 – calculate the aggregate hours of service in a month for the employees who are not full-time employees for the month. Do not include more than 120 hours of service for any employee.

    - Step 2 - divide the total aggregate hours from Step 1 by 120. The result is the number of full-time equivalents for the month.

- *Hours of service*: Hours of service are used in determining whether an employee is a full-time employee and in calculating full-time equivalents. The hour of service rules are described in the final regulations.

- *New employers must use current year*: An employer that was not in existence on any business day in the prior calendar year is considered a large employer in the current year if the employer is reasonably expected to employ an average of at least 50 full-time employees (including full-time equivalents) on business days during the current calendar year and it actually employs an average of at least 50 full-time employees (including full-time equivalents) on business days during the calendar year. In contrast, for the next year (the year after the first year the employer was in existence), the employer will determine its status as a large employer using the rules that generally apply (that is, based on the number of full-time employees and full-time equivalents that the employer employed in the preceding calendar year).

- *Transition relief for employers with 50 to 99 full-time employees in 2014:* For employers with 50 to 99 full-time employees (including full-time equivalents) in 2014, that meet the three conditions described below, no employer shared responsibility payment will apply for any calendar month during 2015.[4] For employers with non-calendar-year health plans, this applies to any calendar month during the 2015 plan year, including months during the 2015 plan year that fall in 2016. In order to be eligible for the relief, an employer must certify that it meets the following conditions:

    - Limited workforce size. The employer must employ on average at least 50 full-time employees (including full-time equivalents), but fewer than 100 full-time employees (including full-time equivalents) on business days during 2014.

    - Maintenance of workforce and aggregate hours of service. During the period beginning on February 9, 2014 and ending on December 31, 2014, the employer may not reduce the size of its workforce, or the overall hours of service of its employees, in order to qualify for the transition relief. However, an employer that reduces workforce size or overall hours of service for bona fide business reasons is still eligible for the relief.

    - Maintenance of previously offered health coverage. During the period beginning on February 9, 2014 and ending on December 31, 2015 (or, for employers with non-calendar-year plans, ending on the last day of the 2015 plan year) the employer does not eliminate or materially reduce the health coverage, if any, it offered as of February 9, 2014. An employer will not be treated as eliminating or materially reducing health coverage if (i) it continues to offer each employee who is eligible for coverage an employer contribution toward the cost of self-only coverage that either (A) is at least 95% of the dollar amount of the contribution toward such coverage that the employer was offering on February 9, 2014 or (B) is at least the same percentage of the cost of coverage that the employer was offering to contribute toward coverage on February 9, 2014; (ii) in the event of a change in benefits under the self-only coverage offered, that coverage provides minimum value after the change; and (iii) it does not alter the terms of its group health plans to narrow or reduce the class or classes of employees (or the employees' dependents) to whom coverage under those plans was offered on February 9, 2014.

☐Check here if employer qualifies for transition relief. If it does, complete the remainder of this checklist, only for 2014, by substituting "100" for "50" below.

☐***The calculation*** *– Average the employer's number of employees across the months in the calendar year to see whether they will be a large employer for the next year. To do so, add full-time employees and full-time equivalent employees (including seasonal workers) for each calendar month. This will give a full-time employee total for January, February, March, etc. Add the 12 monthly totals and divide the sum by 12. Then round down to the next lowest whole number. The result for calendar year 20___ is (enter result here): _________.*

- ***Special rule if the result is 50 or greater****:* There are two potential rules that may reduce the total below 50*. Consider whether to use either rule and check if using (both cannot be used):*

☐***Special rule for seasonal workers***. If the total number of full-time employees and full-time equivalents is 50 or greater for 120 or fewer days, or four or fewer calendar months, in a calendar year, and the employees in excess of 50 employed in that period were seasonal workers, the employer is not a large employer. The 120 days and the four calendar months are not required to be consecutive.

☐***Shorter period for determining large employer status for 2014.*** Rather than being required to use the full 12 months of 2014 to measure whether it has 50 full-time employees (or equivalents), an employer may determine its status as a large employer by using a period of at least six consecutive calendar months (as chosen by the employer) during 2014. For example, an employer could use a period of at least six months through August 2014 to determine its large employer status, leaving it time to analyze the results, to determine whether it needs to offer a plan, and, if so, to choose and establish a plan. *If using this rule, note the short period being used here*: ___________________________.

The result for calendar year 20___ is *(check one box)*:

☐**Less than 50 -** The employer is not a large employer for 20___ and should not be subject to the penalties in 20___. *Stop here, but monitor in future years.*

☐**50 or greater -** *Proceed to Worksheet #2.*

Endnotes

[1] The agencies have indicated that they intend to issue anti-abuse rules to prevent employers from using temporary staffing agencies (or other staffing agencies) purporting to be the common law employer to evade the large employer penalties.

[2] The exclusion of workers described in Code Section 3805 was added by the final regulations. A worker described in Code Section 3805 includes real estate agents and direct sellers.

[3]Generally, an employer will take into account only work performed in the United States. For example, if a foreign employer has a large workforce worldwide, but less than 50 full-time (or full-time equivalent) employees in the United States, the foreign employer generally would not be subject to the penalties. Thus, employees working only abroad, whether or not U.S. citizens, generally will not be taken into account for purposes of determining whether an employer is large.

[4]The relief is also available to new employers (i.e., employers that are not in existence on any business day in 2014). For new employers that would be large employers under the general rules in the final regulations, the transition relief applies if the employer certifies that it: (i) reasonably expects to employ and actually employs fewer than 100 full-time employees (including full-time equivalents) on business days during 2015; and (ii) reasonably expects to meet and actually meets the standards relating to maintenance of workforce and aggregate hours of service and of previously offered health coverage, as measured from the date the employer is first in existence.

WORKSHEET #2
CALCULATING THE PENALTIES

Basic rule -- Large employers (determined in accordance with Worksheet #1) are potentially subject to two penalties, the Section 4980H(a) penalty, which is potentially the larger of the two, and the Section 4980H(b) penalty. The penalties are assessed with respect to full-time employees (determined in accordance with Worksheet #3) on a monthly basis.

Potential subsection (a) penalty: The employer will have to pay a subsection (a) penalty for any month if it does not offer "minimum essential coverage"[5] to substantially all (i.e., 70% for 2015 and 95% for future years) of its full-time employees and their dependents if one or more full-time employees receive a premium tax credit to help pay for coverage on a Marketplace.[6] Important note: If the subsection (a) penalty is triggered, it applies to <u>all</u> full-time employees, not just those who receive premium tax credits or those who were not offered coverage.

- *Subsection (a) calculation*: Generally, for any calendar month, the penalty is equal to the number of full-time employees the employer employed for the month (minus 30) multiplied by 1/12 of $2,000. Important note: For 2015 and any calendar months of 2016 that fall within the employer's 2015 plan year, if a large employer has 100 or more full-time employees (including full-time equivalents) on business days during 2014, the calculation is performed by substituting 80 for 30.

  - $166.67 x ____(# full-time employees – 30) = $_______________

Potential subsection (b) penalty: The employer will have to pay a subsection (b) penalty for any month if it offers minimum essential coverage to substantially all (i.e., 70% for 2015 and 95% for future years) of its full-time employees and their dependents if one or more full-time employees receive a premium tax credit to help pay for coverage on a Marketplace.[6] The penalty could be triggered because the employer did not offer coverage to some full-time employees or because the coverage the employer offered did not provide "minimum value" or was not "affordable."

- *Subsection (b) calculation*: Generally, for any calendar month, the penalty is equal to the number of full-time employees who receive a premium tax credit for that month multiplied by 1/12 of $3,000, not to exceed the subsection (a) penalty.

  - $250 x _____ (# full-time employees who receive a premium tax credit) = $__________ (not to exceed the subsection (a) penalty).

Some important rules to keep in mind when calculating the penalties:

- *Penalties are adjusted for inflation*: Both penalties are adjusted for inflation. The $2,000 and $3,000 penalties shown above are the penalties that would have applied for 2014 had the employer shared responsibility provisions not been delayed to 2015. These amounts will be adjusted for inflation for 2015 and later years.

- *Delayed effective date for some non-calendar year plans:* The preamble to the final regulations provides three pieces of transition relief addressing non-calendar year plans: (1) pre-2015 eligibility transition relief; (2) significant percentage transition relief (all employees); and (3) significant percentage transition relief (full-time employees). The first piece of relief generally addresses employees who are already eligible to participate in the non-calendar year plan. Specifically the pre-2015 eligibility transition relief provides that for any employees (whenever hired) who are eligible for coverage on the first day of the 2015 plan year under the eligibility terms of the plan as of February 9, 2014, (whether or not they take the coverage) and who are offered affordable coverage that provides minimum value effective no later than the first day of the 2015 plan year, the employer will not be subject to a potential employer shared responsibility penalty until the first day of the 2015 plan year. The remaining two pieces of relief generally address employees who have not been eligible to participate in the non-calendar year plan. They provide that if the employer meets certain requirements generally related to the percentage of the employer's employees already eligible for, or participating in, the non-calendar year plan, the relief may be extended to those employees that have not been eligible to participate. Section XV.D.1 of the preamble to the final regulations provides detailed information on the rules for determining whether an employer is eligible for this non-calendar year relief. All of this transition relief applies for the period before the first day of the first non-calendar year plan year beginning in 2015 (the 2015 plan year), but only for employers that maintained non-calendar year plans as of December 27, 2012, and only if the plan year was not modified after December 27, 2012, to begin at a later calendar date.

- ☐ *Non-calendar year plans relying on this delayed effective date must offer full-time employees affordable coverage that provides minimum value no later than the first day of the 2015 plan year. Otherwise, penalties may apply January 1, 2015.*

- *Related companies are <u>not</u> combined for this purpose*: Although the related business rules apply for determining whether an employer is "large," the determination of whether a penalty applies is determined on a company-by-company basis, based on that company's offer of coverage (or lack thereof) and that company's number of full-time employees. *Each company within the group should complete its own Worksheet #2.*

  - ☐ *The 30 (or 80 for 2015) employee reduction is allocated among related companies:* If the employer has related companies, the 30 (or 80) employee reduction (which is part of the subsection (a) calculation) must be allocated ratably among related companies based on each company's number of full-time employees. If a company's allocation is a fractional number that is less than one, it is rounded up to one. This rounding rule may result in the aggregate reduction for the entire group of related companies exceeding 30 (or 80). The companies cannot agree to allocate the 30 (or 80) employee reduction in any other way. *If a related company, note ratable allocation of 30 (or 80) employee reduction here: _____.*

- *Dependent*: Means a natural child or an adopted child until the end of the month in which the child attains age 26. Spouses, stepchildren, and foster children are not dependents and do not have to be offered coverage.

  - ☐ *Transition relief for dependents*: Under transitional relief, there is no penalty for failure to cover dependents during the 2015 plan year if the employer takes steps during 2015 toward satisfying the requirement in the subsequent plan year. This transition relief applies to employers for the 2015 plan year for plans under which: (1) dependent coverage is not offered; (2) dependent coverage that does not constitute minimum essential coverage is offered; or (3) dependent coverage is offered for some, but not all, dependents. The transition relief is not available to the extent the employer had offered dependent coverage during either the plan year that begins in 2013 (the 2013 plan year), or the 2014 plan year and subsequently dropped that offer of coverage. The transition relief applies only for dependents who were without an offer of coverage from the employer in both the 2013 and 2014 plan years and if the employer takes steps during the 2014 or 2015 plan year (or both) to extend coverage under the plan to dependents not offered coverage during the 2013 or 2014 plan year (or both).

- ***Substantially all normally means 95%, but means 70% for 2015:*** The final regulations provide that a large employer will be treated as offering coverage to substantially all of its full-time employees and their dependents for each calendar month in 2015 (and any calendar months during the 2015 plan year that fall in 2016) if, for that month, it offers coverage to 70% or more of its full-time employees. For later years, the final regulations provide that a large employer will be treated as offering coverage to substantially all of its full-time employees and their dependents for a calendar month if, for that month, it offers coverage to all but 5%, or if greater, five of its full-time employees. For this purpose, an employee is treated as having been offered coverage only if the employer has also offered coverage to the employee's dependents. The purpose of the substantially all rule is to provide employers with a margin of error in the event they fail to provide coverage to a small group of full-time employees. However, the rule applies regardless of whether the failure was inadvertent. For related companies, the substantially all rule is applied on a company-by-company basis.

  - ☐ *Employers should consider how to use the rule. Some might save it for inadvertent failures, while others use it to exclude a small group of full-time employees. It is important to note that full-time employees excluded under the rule may trigger a subsection (b) penalty.*

- *Minimum value*: A plan provides minimum value if it covers at least 60% of the total allowed cost of benefits that are expected to be incurred under the plan. The Department of Health and Human Services ("HHS") and the IRS have produced a minimum value calculator. By entering certain information about the plan, such as deductibles and co-pays, into the calculator, employers can get a determination as to whether the plan provides minimum value. Additionally, on May 3, 2013, Treasury and the IRS issued proposed regulations regarding the other methods available to determine minimum value.

- *Affordable coverage*: If an employee's share of the premium for employer-provided coverage costs the employee more than 9.5% of that employee's annual household income, the coverage is not considered affordable for that employee. Because household income is nearly impossible for an employer to determine, the final regulations include three safe harbors that will make it easier for an employer to determine whether coverage is affordable. Use of the safe harbors is optional and an employer may choose to apply the safe harbors for any reasonable category of employees, provided it does so on a uniform and consistent basis for all employees in the category.[7] Generally, health coverage is affordable if the employee's required contribution for the employer's lowest cost self-only coverage that provides minimum value meets one of the following affordability safe harbors:

  - *W-2 safe harbor*: The annual cost of health coverage does not exceed 9.5% of the employee's W-2 wages (shown in Box 1) from the employer (including related companies). This rule does not allow Section 401(k), 403(b), or 125 deferrals to be added back into the Box 1 amount for safe harbor purposes. Additionally, the employee's contribution must remain a consistent amount or percentage during the plan year so that an employer is not permitted to make discretionary adjustments to the required employee contribution for a pay period. Note that this method may result in fluctuations in employee contributions due to changes in Section 401(k) deferrals, unpaid leaves of absence, etc.

  - *Rate of pay safe harbor*: For hourly employees, the monthly cost of health 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 coverage period (generally, the first day of the plan year) or the employee's lowest hourly rate of pay during the calendar month (i.e., mid-year adjustments are permitted for an hourly employee if the rate of pay is decreased, but not if the rate of pay is increased.) For salaried employees, the monthly cost of health coverage does not exceed 9.5% of that employee's monthly salary as of the first day of the coverage period, provided that if the monthly salary is reduced, including due to a reduction in work hours, this safe harbor is not available. Note that Section 401(k), 403(b), and 125 deferrals do not reduce the employee's rate of pay. This may be a more stable method of calculating affordable coverage than the W-2 safe harbor.

- *Federal poverty line (FPL) safe harbor*: The monthly cost of health coverage does not exceed 9.5% of a monthly amount determined as the FPL for a single individual for the state in which the employee is employed, divided by 12.[8] Generally, employers will use the most recently published FPL as of the first day of the plan year, but the final regulations also allow employers to use the FPL in effect six months prior to the beginning of the plan year. The FPL is regularly published in late January, so for 2015, calendar year plans would use the FPL published in January 2014, which is $11,670 for the 48 contiguous states. This would result in an allowable premium of $92.38 for the 48 contiguous states. This may be the easiest method for calculating affordable coverage.

- *Offer of coverage*: Employees must be provided an effective opportunity to accept or decline coverage in order to be treated as having been offered coverage. An offer of coverage must be made at least once each plan year. Employees do not have to be allowed to decline coverage that provides minimum value and is offered either at no cost to the employee or at a cost, for any calendar month, of no more than 9.5% of a monthly amount determined as the FPL for a single individual for the applicable calendar year, divided by 12. The regulations do not provide any specific rules for demonstrating that an offer of coverage was made. Offers of coverage may be made electronically.

    - *Offer of coverage by one company on behalf of a related company:* An offer of coverage by one company to an employee for a calendar month is treated as an offer of coverage by all related companies for that calendar month.

    - *Offer of coverage by staffing firm on behalf of client employer:* For an offer of coverage to an employee performing services for an employer that is a client of a staffing firm, in cases in which the staffing firm is not the common law employer of the individual and the staffing firm makes an offer of coverage to the employee on behalf of the client employer under a plan established or maintained by the staffing firm, the offer is treated as made by the client employer, but only if the fee the client employer pays to the staffing firm for an employee enrolled in health coverage under the plan is higher than the fee the client employer would pay the staffing firm for the same employee if that employee did not enroll in health coverage under the plan.

    - *Offer of coverage by multiemployer or single employer Taft Hartley plan or MEWA:* In addition, an offer of coverage made to an employee on behalf of a contributing employer under a multiemployer or single employer Taft Hartley plan or multiple employer welfare arrangement ("MEWA") is treated as made by the employer. See Section XV.E of the preamble to the final regulations for interim guidance on the application of Section 4980H to multiemployer plans.

Proceed to Worksheet #3

Endnotes

[5] "Minimum essential coverage" is broadly defined to include any group health plan or group health insurance that is not a HIPAA excepted benefit (i.e., stand-alone dental or vision plans).

[6] The IRS will adopt procedures that ensure employers receive certification that one or more employees have received a premium tax credit. The IRS will contact employers to inform them of their potential liability and provide them an opportunity to respond before any liability is assessed or notice and demand for payment is made. The contact for a given calendar year will not occur until after the due date for employees to file individual tax returns for that year claiming premium tax credits and after the due date for large employers to file the information returns identifying their full-time employees and describing the coverage that was offered (if any). If it is determined that an employer is liable for an employer shared responsibility payment after the employer has responded to the initial IRS contact, the IRS will send a notice and demand for payment. That notice will instruct the employer on how to make the payment.

[7] The final regulations clarify that that reasonable categories generally include specified job categories, nature of compensation (for example salaried or hourly), geographic location, and similar bona fide business criteria. However, an enumeration of employees by name, or other specific criteria having a similar effect, is not considered a reasonable category.

[8] The FPL for the 48 contiguous states and the District of Columbia is the same. Hawaii and Alaska have higher FPLs.

WORKSHEET #3
IDENTIFYING FULL-TIME EMPLOYEES IN 2014

Basic rule – Both penalties hinge on whether the employer offers coverage to "full-time employees," so being able to identify full-time employees is of critical importance.

Some important rules to keep in mind when determining whether a company has any full-time employees who might trigger a penalty tax:

- *Related companies are* ***not*** *combined for this purpose*: Although the related business rules apply for determining whether an employer is "large," the determination of whether a penalty applies is determined on a company-by-company basis, based on that company's offer of coverage (or lack thereof) and that company's number of full-time employees. *Each company within the group should complete its own Worksheet #3.*

- *Common law employees are counted*: The rules for determining who is an "employee" are generally the same as described in Worksheet #1 (i.e., common law employees, excluding partners, sole proprietors, partners in a partnership, 2% S Corp shareholders, "leased employees" (as defined in Code Section 414(n)(2)), most employees who work outside the United States, and workers described in Code Section 3805). Again, careful consideration should be given to independent contractors, temporary employees, and other individuals who perform services for the employer but are not treated as common law employees by the employer.

- *Full-time employee:* The statute defines a full-time employee, with respect to any month, as "an employee who is employed on average at least 30 hours of service per week." The final regulations permit employers to treat 130 hours of service in a calendar month as the monthly equivalent of 30 hours of service per week, provided the employer applies this rule on a reasonable and consistent basis.

- *Hours of service*: Hours of service are used in determining whether an employee is a full-time employee. The hour of service rules are explained in the final regulations.

- *Part-time employees*: Penalties do not apply to part-time employees, and there is no need to determine a full-time equivalent (like there is under Worksheet #1).

  - ☐ *Because penalties do not apply to part-time employees, some employers might consider whether reducing employees below the 30-hour threshold could minimize potential penalties.*[9]

- *Two methods for determining full-time status*: The final regulations provide two methods for determining whether an employee has sufficient hours of service to be a full-time employee.

  - *The monthly measurement method:* One method is the monthly measurement method under which a company determines each employee's status as a full-time employee by counting the employee's hours of service for each month. This method can be difficult to administer, especially for variable hour employees because a company will not typically be able to determine until the end of a month, after it is too late to avoid penalties, whether such employees were full-time for the month.

  - *The look-back measurement method:*[10] The other method is the look-back measurement method under which a company may determine the status of an employee as a full-time employee during a future period (called a "stability period"), based upon the hours of service of the employee in a prior period (called a "measurement period"). Under this method, a company will know the employee's status as a full-time employee at the time the company offers coverage. The final regulations describe approaches that can be used for various circumstances, such as for employees who work variable hour schedules, seasonal employees[11], and employees of educational organizations.

Important note: The final regulations clarify that related companies may use different measurement methods. The final regulations do not permit a company to adopt the look-back measurement method for variable hour and seasonal employees while using the monthly measurement method for employees with more predictable hours of service. The final regulations also clarify that a company may apply measurement periods and stability periods that differ in length, or in their starting and ending dates, with respect to: (1) collectively bargained employees and non-collectively bargained employees; (2) each group of collectively bargained employees covered by a separate collective bargaining agreement; (3) salaried employees and hourly employees; and (4) employees whose primary places of employment are in different states. The specifics of the two measurement methods are explained in the final regulations.

The company will use *(check one box): If using different periods and dates for different permitted categories of employees, complete the information below for each category of employees.*

☐ The monthly measurement method.

☐ The look-back measurement method*. Complete the information for ongoing and new employees below.*

- *For ongoing employees note the standard measurement period, the standard stability period, and the standard administrative period being used below:*
  - *Standard measurement period: ________ to ________ (3 to 12 months).*
  - *Standard stability period (typically the plan year): ________ to ________ (3 to 12 months).*[12]
  - *Standard administrative period: ________ to _________ (no longer than 90 days beginning immediately after the standard measurement period and ending immediately before the standard stability period).*

    - Short measurement period for stability period starting in 2015. For stability periods beginning in 2015, the final regulations provide a transition rule that allows a company to use a measurement period of less than 12 months (even if a 12-month measurement period would otherwise be required). The shorter measurement period must be at least six consecutive months, must begin no later than July 1, 2014, and must end no earlier than 90 days before the first day of the plan year beginning on or after January 1, 2015. (*Consider whether to use the special rule, check if using, and note short measurement period*):

      ☐ Short measurement period for 2015 standard stability period: ________ *to* ________.

- *For new employees note the initial measurement period, the initial stability period, and the initial administrative period being used below:*
  - *Initial measurement period: will begin on ________________ and will last for _____ months (3 to 12 months).*[13]

- *Initial stability period will last for _________ months (must generally be the same length as the standard stability period).*[14]
- *Initial administrative period: ________ days (not to exceed 90 days).*[15]

Will the company have any full-time employees (*check one box*)?

☐Yes. The company is potentially subject to a penalty. *Proceed to Worksheet #4.*

☐No. The company will not be subject to the penalties. *Stop here but continue to monitor each year.*

Endnotes

[9] Employers that lower hours to prevent employees from being considered full-time should consult with legal counsel to ascertain whether such individuals could bring viable claims under Section 510 of ERISA or any other nondiscrimination rules such as the Americans with Disabilities Act, the Age Discrimination in Employee Act, or Title VII.

[10] The look-back measurement method for identifying full-time employees is available only for purposes of determining and computing liability for an employer shared responsibility penalty, and not for purposes of determining whether an employer is a large employer.

[11] The final regulations provide that a seasonal employee means an employee in a position for which the customary annual employment is six months or less. The preamble to the final regulations indicates that the reference to customary means that by the nature of the position an employee in the position typically works for a period of six months or less, and that period should begin each calendar year in approximately the same part of the year, such as summer or winter. In certain unusual instances, the employee can still be considered a seasonal employee even if the seasonal employment is extended in a particular year beyond its customary duration (regardless of whether the customary duration is six months or is less than six months). For example, if ski instructors at a resort have a customary period of annual employment of six months, but are asked in a particular year to work an additional month because of an unusually long or heavy snow season, they would still be considered seasonal employees.

[12] For employees determined to be employed on average at least 30 hours per week during the standard measurement period, the standard stability period must be at least 6 consecutive calendar months, but no shorter in duration than the standard measurement period. For employees determined not to be employed on average at least 30 hours per week during the standard measurement period, the standard stability period cannot be longer than the standard measurement period

[13] The initial measurement period may begin on any date between the employee's start date or any date up to and including the first day of the first calendar month following the employee's start date (or on the first day of the first payroll period starting on or after the employee's start date, if later, as set forth in Section 54.4980H-3(d)(3)(ii) of the final regulations).

[14] See Section 54.4980H-3(d)(3) of the final regulations for rules impacting the length of the initial stability period.

[15] The initial administrative period includes all periods between the start date and the date the employee is first offered coverage, other than the initial measurement period. In addition, the initial measurement period and the initial administrative period together cannot extend beyond the last day of the first calendar month beginning on or after the first anniversary of the employee's start date.

WORKSHEET #4
PLAN DESIGNS TO AVOID/MINIMIZE THE PENALTIES

Basic rule – The penalties only apply if one or more full-time employees receive a premium tax credit to help pay for coverage on a Marketplace. Premium tax credits generally are available to help pay for coverage for employees who: (1) have a household income between 100% and 400% of the federal poverty level and enroll in coverage through a Marketplace; (2) are not eligible for coverage through a government-sponsored program like Medicare, Medicaid, or CHIP; and (3) are not eligible for coverage offered by an employer or are eligible only for employer coverage that is unaffordable or that does not provide minimum value. These factors are largely beyond the employer's control, so the employer may be taking a significant risk if it does not offer minimum essential coverage. Rather than hoping that no full-time employee receives a premium tax credit or cost-sharing reduction for coverage through a Marketplace, employers can design their plans to avoid/minimize the penalties.

How to design around the subsection (a) penalty:

- ☐ *Offer minimum essential coverage to substantially all full-time common law employees and their dependents under an employer sponsored plan. Make sure to properly classify all common law employees. Give careful consideration to proper treatment of independent contractors, temporary employees, and leased employees.*

    - An employer may avoid the subsection (a) penalty even if employees are required to pay 100% of the cost of coverage, although doing so could subject the employer to the subsection (b) penalty.

    - A large employer will be treated as offering coverage to substantially all full-time employees and their dependents for a calendar month if it offers coverage to at least 70% of such individuals in 2015 and 95% of such individuals in later years. Remember, any full-time employees who are not offered coverage may still trigger a subsection (b) penalty.

- ☐ *Amend group health plans to reflect a 30 hour of service requirement. Some employers might decide to use a lower hour of service requirement to provide a margin of error.*

- ☐ *Amend plans to provide coverage for all full-time employees and their children (i.e., natural born and adopted children) until the end of the month the child attains age 26.*

- ☐ *Reconsider current plan exclusions because they may not work if the employees being excluded are "full-time employees" under the new rules. Amend plan as needed.*

- ☐ *If using the look-back method to determine full-time employees, consider whether plan amendments may be necessary to document the measurement periods, the stability periods, and the administrative periods.*

How to design around the subsection (b) penalty:

- ☐ *Offer at least one minimum value option (determined using one of the three permissible methods).*

- ☐ *Set the premium so the employee's contribution toward the employer's lowest cost self-only coverage that provides minimum value is "affordable" to all full-time employees. The safest way to do this is to set the premium so it satisfies the W-2, rate of pay, or federal poverty level safe harbor.*

    - If self-only coverage is affordable for some, but not all employees, only those employees for whom it is unaffordable, who receive a premium tax credit to help pay for coverage on a Marketplace, will trigger a penalty.

- Employers might consider requiring highly compensated individuals to pay a higher percentage of compensation to make a plan more affordable for lower-income employees.

- Family coverage does not have to be affordable.

☐ *Plan documents and/or enrollment materials may need to be amended to reflect the affordable premium structure.*

Important rules to keep in mind when designing plans to avoid the penalties:

- *Nondiscrimination rules*: Plans remain subject to other applicable rules. For example, self-funded group health plans are currently subject to the nondiscrimination requirements of Code Section 105(h), and it is only a matter of time until non-grandfathered insured group health plans are subject to similar nondiscrimination rules. Furthermore, any group health plans that allow premiums to be paid on a pre-tax basis through a Section 125 plan must also satisfy the nondiscrimination requirements of Code Section 125. These nondiscrimination rules generally prohibit employers from designing their group health plans to discriminate in favor of highly compensated individuals. When designing plans to avoid the penalties, employers must be careful not to run afoul of nondiscrimination or other applicable rules.

- *Tax deductions*: Employers may not take a tax deduction for any penalties they pay. Employers may deduct the cost of employer-sponsored health coverage for income tax purposes. In addition, the value of employer-provided coverage is generally tax free to employees and is not subject to FICA taxes.

- *Collective bargaining may be required*: Employers with collective bargaining agreements might have to modify those agreements to make health plan changes needed to avoid the penalties.

APPENDIX A

Large Employer Play or Pay Penalties
Flow Chart