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2015 Health Care Reform Compliance Checklist for Employers

BY PATRICIA A. MORAN

The United States has entered a new era of health care reform. Until now, United States employers were generally not required to provide health care coverage to employees (although many did so for employee relations and competitive reasons). But as of Jan. 1, 2015, under the Affordable Care Act's "employer shared responsibility" mandate, employers of a certain size must either offer coverage to full-time employees, or risk paying a penalty. Employers and their advisers must also wade through a murky swamp of analytical, record-keeping, reporting and disclosure requirements in order to secure compliance and either avoid or minimize penalties.

The basics of the employer shared responsibility rule are generally familiar at this point. Employers who averaged 50 or more full-time (FT) and full-time equivalent (FTE) employees on business days during a preceding calendar year are called "applicable large employers" (ALEs) and are subject to the ACA for a calendar year. "Full time" employees are those who work at least 30 hours of service per week.[1] Monthly FTE employees are determined by adding up all hours of service for employees who are not "full time" (capped at 120 per employee) and dividing by 120.[2]

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Although the rule took effect on January 1, 2015, under a transition rule, certain employers with 50-99 FT and FTE employees can delay compliance until 2016.[3] ALE's are determined on a controlled group basis[4]; each component controlled group member is called an "ALE Member."[5] Additional transition rules apply to certain employers who have non-calendar year plans.[6]

Each ALE Member has three basic compliance options:

- Offer "minimum essential coverage" (MEC) that is "affordable" and provides "minimum value" to at least 95 percent of FT employees and dependents. Under a transition rule, employers who have not offered dependent coverage in the past, but are taking steps to do so, are relieved from the requirement to offer dependent coverage for plan years beginning in 2015. [7] In this case, no penalty is incurred.

- Offer MEC to at least 70 percent[8] (95 percent starting in 2016) of FT employees and dependants that either is not "affordable" or does not provide "minimum value." In this case, the ALE member incurs a monthly

[1] Treas. Reg. § 54.4980H-1(a)(21).
[2] Treas. Reg. § 54.4980H-1(a)(22).
[3] 79 FR 8574 (February 12, 2014).
[4] Treas. Reg. § 54.4980H-1(a)(16).
[5] Treas. Reg. § 54.4980H-1(a)(5).
[6] 79 FR 8570-8572 (February 12, 2014).
[7] 79 FR 8573 (February 12, 2014).
[8] 79 FR 8575 (February 12, 2014).

penalty of $250 per month ($3000 per year) for each of its full-time employees receiving a premium subsidy on an exchange.[9]

■ Do not offer MEC at all, or offer MEC to fewer than 70 percent (95 percent starting in 2016) of FT employees and dependents. In this case, if any FT employee receives a premium subsidy on an exchange, the ALE member incurs a monthly penalty of $167 per month ($2000 per year) for each of its full time employees, excluding the first 30[10] (for 2015, larger employers can exclude 80).[11]

A plan is ''affordable'' if the employee's required contribution to the plan does not exceed 9.5 percent of the applicable taxpayer's household income.[12] A plan provides ''minimum value'' if the plan's share of the total allowed costs of benefits provided under the plan is less than 60 percent of such costs.[13] MEC is a very low bar; most employer-provided plans, other than excepted benefits,[14] will qualify as MEC.[15]

What Employers Need To Do Now

While the basics of the employer shared responsibility rule may seem simple, the particulars are not. The following is a list of the compliance issues my colleagues and I have been seeing frequently in our practices this fall, presented as a checklist for 2015.

1. Identify Controlled Group Members (AKA ALE Members)

Let's say your client's company has only 35 total employees. Since the threshold is 50, it would seem (at first glance) that the client is in the clear. But remember that ALE status is determined by counting up all FT and FTE employees in the ''controlled group.'' A controlled group consists of all persons treated as a single employer under Internal Revenue Code Section 414 (b), (c), (m) or (o). If the client's company is part of a larger controlled group, the company could very well be subject to the ACA.

In ACA parlance, each controlled group member is called an ''Applicable Large Employer Member'' or ''ALE Member.'' The three most common types of controlled groups are:

■ 80 percent or more parent/subsidiary relationship;[16]

■ Two or more corporations, if five or fewer individuals own 80 percent or more of each with 50 percent or more ownership in common (the ''brother-sister'' group);[17] and

■ ''Affiliated service groups'': groups of companies related by ownership, shared services, and/or governance and either engaged in certain specified fields[18] and/or for whom capital is not a material income-producing factor.[19]

The controlled group rules are laden with detail and the ''affiliated service group'' rules are especially murky. For example, constructive ownership rules may apply and some classes of stock may excluded from the ownership calculation.

Note that, while ALE status is determined on a controlled-group basis, each individual ALE member must separately and independently comply with the mandate.

2. Identify ''Employees'' of each ALE Member; Review Independent Contractors

These employer shared responsibility rules direct us to identify ''employees'' using a common law standard.[20] The Internal Revenue Service offers the following explanation of this standard:

> Under the common law standard, an employment relationship exists when the person for whom the services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. Under the common law standard, an employment relationship exists if an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if the employer has the right to do so.[21]

Now more than ever, employers are advised to review their various service providers and make sure that any individuals classified as ''independent contractors'' have been properly classified. Misclassification of an employee as an independent contractor could cause an employer to underestimate its number of employees for ALE status, and may also cause the employer to withhold offers of coverage from eligible full-time employees.

3. Identify and Track ''Hours of Service'' of all Employees

An accurate count of ''hours of service'' is necessary to identify each ALE Member's FT and FTE employees. For purposes of the ACA, ''hours of service'' include:

■ 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 on account of a period of time during which no duties are performed due to vacation, holiday, illness, incapacity (including disability), layoff, jury duty, military duty or a leave of absence.[22]

In general, hours of service are determined by reviewing records of hours worked and hours for which

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[9] Internal Revenue Code § 4980H(b) and Treas. Reg. § 54.4980H-5.
[10] Internal Revenue Code § 4980H(a) and Treas. Reg. § 54.4980H-4.
[11] 79 FR 8575 (February 12, 2014).
[12] Internal Revenue Code § 36B(c)(2)(C)(i).
[13] Internal Revenue Code § 36B(c)(2)(C)(ii).
[14] Excepted benefits include most health care flexible spending accounts, most dental and most vision plans, among others. See Internal Revenue Code § 9832(c).
[15] Treas. Reg. § 1.5000A–2(c).
[16] Internal Revenue Code § 414(b).
[17] *Id.*
[18] Health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting and insurance.
[19] Internal Revenue Code § 414(m).
[20] Treas. Reg. § 54.4980H-1(a)(15).
[21] 78 F.R. 221 (January 2, 2013).
[22] Treas. Reg. § 54.4980H-1(a)(24).

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payment is made. For non-hourly employees, employers may use a ''days-worked equivalency'' (i.e., count eight hours of service for each day for which the employee would be required to be credited with at least one hour of service) or a ''weeks-worked equivalency'' (i.e., count 40 hours of service per week for each week for which the employee would be required to be credited with at least one hour of service).[23]

There are a few limited cases where hours worked by an employee need not be counted towards ''hours of service.'' Hours of service do not include:

■ Hours for which compensation constitutes income from sources outside of the United States;[24]

■ Hours of bona fide volunteers (generally, volunteers for a non-profit entity whose compensation is limited to reasonable expenses, benefits and fees);[25]

■ Hours of students on a Federal work study program (or a similar state or local program);[26] and

■ Members of religious orders who have taken a vow of poverty.[27]

Otherwise, all hours must be counted; an employer cannot exclude hours based on an employee's class or position (e.g. hours must be counted for temps, co-ops, casual and similar employees). All common law employees are potentially ''full-time'' if they meet or surpass the 30 hour/week threshold. The IRS is currently considering cases where hours are difficult to capture, such as adjunct professors and airline employees.[28]

4. Determine ALE Status

Having identified all hours of service of all employees of all ALE Members, the employer then:

■ Counts the number of ''full-time'' employees (30 or more hours per week) in the entire ALE group (using the ''monthly measurement'' method, described below); and

■ Determines the number of FTE employees in the ALE group by adding up all hours of service for employees who are not ''full time'' (capped at 120 per employee) and dividing by 120.

If the employer has on average 50 or more total FT and FTE on business days during the preceding calendar year, the employer is an ALE.[29] Note that for 2015 only, an employer may use any consecutive six-month period in 2014 (rather than the entire 2014 calendar year) to determine ALE status.[30]

5. ALE's with 50-99 FT and FTE: Consider Transition Relief

An ALE with 50 to 99 FT and FTE employees can delay compliance until January 1, 2016, but only if certain requirements are met. First, the ALE must not have reduced its workforce in order to qualify for the transition relief (reductions for bona fide business reasons are excepted). Second, the ALE cannot have eliminated nor materially reduced any health coverage it offered as of February 9, 2014. Finally, the ALE must certify its eligibility for transition relief on Form 1094-C (described below).[31]

6. ALE Members with Non-Calendar Year Plans: Consider Transition Relief

An ALE member that maintained non-calendar year plans as of December 27, 2012, may be able to delay compliance until the first day of the plan year beginning in 2015 (and perhaps later, if the ALE is also eligible for the 50-99 transition relief described above) under transition relief set forth in the preamble to the final employer shared responsibility regulations. However, it is important to note that merely having a non-calendar year plan is not enough; ALE members should carefully review the requirements of the transition relief. Among other requirements, the plan year cannot have changed since December 27, 2012, and, for certain relief, the ALE member must have either offered plan coverage to, or enrolled, certain percentages of its employees during the year ending February 9, 2014. Additionally, transition relief generally only applies if 95 percent of the ALE Member's full-time employees are offered affordable, minimum value coverage as of the first day of the 2015 plan year.[32]

7. Decide on a Compliance Strategy

As noted above, an ALE member has three basic compliance options. It may offer affordable, minimum value coverage to at least 95 percent of its full-time employees and dependents, and avoid all penalties. It may offer MEC coverage to at least 95 percent of full-time employees and dependents (70 percent for 2015, under a transition rule) that is either unaffordable or does not provide minimum value, and risk paying a penalty of $3,000 per subsidized employee. Or, it may offer no coverage, or offer MEC to fewer than 95 percent (70 percent for 2015) of its full-time employees and dependents, and risk a penalty of $2,000 times each full-time employee, if any full-time employee obtains an exchange subsidy.

Each ALE Member may choose a different strategy. For some ALE members, it will make economic sense to risk the penalties. Other ALE members may decide to offer affordable, minimum value coverage and pay no penalty. Each ALE member will need to consider a number of factors: the composition of its workforce, benefit packages offered by its competitors, as well as what it can reasonably afford to provide to its full-time employees.

8. Determine Whether Coverage is ''Affordable''

Employers who wish to avoid penalties altogether will need to offer affordable coverage. A plan is ''affordable'' if the required contribution to the plan does not exceed 9.5 percent of the applicable taxpayer's household income.[33] Since an employer does not know its employees' household income with certainty, the IRS

[23] Treas. Reg. § 54.4980H-3(b).
[24] Treas. Reg. § 54.4980H-1(a)(24)(ii)(C).
[25] Treas. Reg. § 54.4980H-1(a)(24)(ii)(A).
[26] Treas. Reg. § 54.4980H-1(a)(24)(ii)(B).
[27] 79 FR 8551 (February 12, 2014).
[28] 79 FR 8551-8552 (February 12, 2014).
[29] Treas. Reg. § 54.4980H-2. Note that an exception may apply for certain employers with large cohorts of seasonal workers. See Treas. Reg. § 54.4980H-2(b)(2).
[30] 79 FR 8573 (February 12, 2014).
[31] 79 FR 8574 (February 12, 2014).
[32] 79 FR 8570-8572 (February 12, 2014).
[33] Internal Revenue Code § 36B(c)(2)(C)(i).

allows the employer to use one of three ''safe harbors'' in order to determine affordability:

- The W-2 Safe Harbor: coverage is affordable if the employee's annual contribution towards the lowest cost single premium does not exceed 9.5 percent of his or her W-2 wages from the employer. Since W-2 wages are generally not known until the end of the year, this safeharbor is not especially useful for advance planning purposes.[34]

- The ''Rate of Pay'' safe harbor: coverage is affordable if the employee's monthly contribution towards the lowest cost single premium does not exceed 9.5 percent of the following: 130 hours times the lower of (1) the employee's hourly rate of pay as of the first day of the coverage period (usually, the first day of the plan year) or (2) the employee's lowest hourly rate of pay during the calendar month. For salaried employees, employers can generally use the monthly salary for this calculation.[35]

- The ''Federal Poverty Line'' safe harbor: coverage is affordable if the employee's monthly contribution towards the lowest cost single premium does not exceed 9.5 percent of the single federal poverty line for the applicable calendar year, divided by 12.[36]

8. Determine Whether Coverage Provides "Minimum Value"

A plan provides ''minimum value'' if the plan's share of the total allowed costs of benefits provided under the plan is less than 60 percent of such costs. Minimum value is determined using an IRS calculator or an actuarial valuation.[37] Most major medical plans (PPO, HMO, POS) will provide minimum value.

9. Identify and Track "Full-Time Employees"

Proper identification of ''full-time'' employees is necessary both for determining ALE status and for identifying who may be entitled to an offer of coverage. In addition, employers will be required to report ''full-time'' employee data to the IRS. A ''full-time'' employee is a common law employee that averages at least 30 hours of service per week[38] . For ALE status, employers must use a monthly measurement method: under this method, generally, an employee is ''full-time'' if he or she works at least 130 hours of service in a month.[39]

For purposes of identifying new ''full-time'' employees for an offer of coverage, employers generally must use a monthly measurement method. However an employer may use a ''look-back measurement'' method for new hourly, new seasonal and new ''variable hour'' employees.[40] An employee is a variable hour employee if, based on the facts and circumstances at the employee's start date, it cannot be determined whether the employee is reasonably expected to be employed on average at least 30 hours per week during his or her initial measurement period because that employee's hours are variable or otherwise.[41] An employee is a seasonal employee if he or she is hired into a position for which the customary annual employment is six months or less.[42] An employee is a part-time employee if, based on the facts and circumstances at the employee's start date, the employer reasonably expects the employee to average less than 30 hours of service per week during the initial measurement period.[43]

An employer who uses a look-back measurement method tracks an employee's hours during a ''measurement period'' of three to 12 months. If the employee averages at least 30 hours per week during the measurement period, the employee must be considered to be a ''full-time'' employee for a subsequent stability period, which is generally the same length as the measurement period.[44] Unpaid FMLA, jury duty and USERRA leave are generally considered to be hours worked for purposes of the calculation of average hours under the look-back measurement method.[45]

After a new employee has worked for one full ''standard measurement period'' of three to 12 months, he or she is considered to be an ongoing employee (rather than a new employee) and is tested for full-time status using a look-back measurement method.[46]

Under either method, if an employee terminates employment and is rehired, the employee may be treated as a new hire only if the period between the termination and rehire exceeds the lesser of 13 consecutive weeks (26 weeks for educational organizations), or a period of no less than four weeks and at least as long as the employee's period of employment prior to termination.[47]

10. Document any Offers of Coverage

Employers should carefully document and record any offers made to full-time employees. Although the IRS has not provided clear guidance as to the form of the ''offer,'' while not required, employers are advised to obtain a signed, dated document from each full-time employee who receives an offer of coverage, in which the employee attests that he or she has received an offer of coverage and understands the terms (such as costs and benefits). In some industries[48], employers cannot easily collect these offer forms in spite of diligent efforts. In these cases, employers should develop and document a process for distributing and collecting forms, and make extra efforts to communicate the offer (e.g., office posters, language in employee handbooks, postcards, etc.). Offers of coverage may be made electronically, although employees who do not have access to an employer's computers and email system will generally need to consent to the electronic distribution.[49]

11. Start Planning for Reporting Now

Beginning in early 2016, all ALE Members will be required to provide disclosures to full-time employees about their health coverage on new Form 1095-C. In ad-

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[34] Treas. Reg. § 54.4980H—5(e)(2)(ii).
[35] Treas. Reg. § 54.4980H—5(e)(2)(iii).
[36] Treas. Reg. § 54.4980H—5(e)(2)(iv).
[37] 78 FR 25909 (Friday, May 3, 2013).
[38] Treas. Reg. § 54.4980H—1(a)(21).
[39] Treas. Reg. § 54.4980H—3(c).
[40] Treas. Reg. § 54.4980H—3(d).
[41] Treas. Reg. § 54.4980H—1(a)(49).
[42] Treas. Reg. § 54.4980H—1(a)(38).
[43] Treas. Reg. § 54.4980H—1(a)(32).
[44] Treas. Reg. § 54.4980H—3.
[45] Treas. Reg. § 54.4980H—3(d)(6).
[46] Treas. Reg. § 54.4980H—3(d)(1).
[47] Treas. Reg. § 54.4980H—3(c)(4) and (d)(6).
[48] Including staffing, restaurant, home health and hospitality.
[49] See Treas. Reg. § 1.401(a)-12.

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dition, ALE Members will be required to provide the 1095-C Forms and a summary transmittal (new Form 1094-C) to the IRS. 2015 information must be disclosed on Forms 1095-C no later than January 31, 2016,[50] and the Form 1094-C must be transmitted to the IRS no later than February 29, 2016 (March 31, 2016 for electronic filers).[51] The Forms 1094-C and 1095-C, as well as the instructions thereto, are currently in proposed format.[52]

These forms are complicated and detailed, and the proposed forms and instructions are confusing at best. The many data points required to be included on the Form 1095-C include: the name of each covered individual (employee, spouse, dependents), the social security number or date of birth of each covered individual, the months of coverage and various information about the offer of coverage (e.g., type of coverage offered, costs, any safe harbors used to determine affordability, any reasons for non-assessment during one or more months). On the Form 1094-C, ALE members are required to disclose aggregated information from the Forms 1095-C as well as identify any transition relief sought.[53]

Preparation of these forms promises to be time-consuming and complicated. ALE members are urged to familiarize themselves with the forms now, keep watch for any changes or updates to the forms and instructions, and find ways to track and organize the requested information for disclosure. If an ALE member intends to enlist a third party to assist with the forms, the ALE member should be interviewing candidates and entering service agreements (with sound clauses protecting the ALE if the service provider does not deliver as promised).

Once the ALE members submit these reports and the ALE member's employees file their 1040 forms, the IRS will then review the data and, where the data does not line up, take enforcement action. For example, if an ALE Member discloses that an affordable, minimum value offer was made to a full-time employee, but the employee has claimed an exchange subsidy, the IRS may audit the employer and ask for evidence of the offer. ALE members who claim relief under a transition rule may also be subject to further scrutiny.

12. Update Plan Documents

Last but not least, employers who are making changes to their plans should take a careful look at their plan documents, summary plan descriptions, summaries of benefits and coverage, wrap documents, employee handbooks and other materials and make sure that all changes are properly documented and communicated. In particular, employers who are changing their plan eligibility requirements (including rules for identifying ''full -time'' employees) should make sure their employees are aware of the new standards.

In addition, employers who do not have documents such as summary plan descriptions and wrap documents in place for their health and welfare plans are advised to prepare and adopt such documents immediately. The ACA brings a host of new substantive requirements (such as the employer shared responsibility mandate discussed in this article, in addition to new insurance mandates) as well as disclosure obligations (such as notices to participants about certain plan features and the summary of benefits and coverage). With these new requirements comes a likelihood of increased audit activity by the IRS, HHS and the DOL, and the possibility of enforcement action or penalties for companies lacking legally compliant, up-to-date and accurate. In short: the stakes have never been higher.

[50] Treas. Reg. § 301.6056-1(e).

[51] Treas. Reg. § 301.6056-1(g).

[52] Proposed forms and instructions are available at www.irs.gov.

[53] In addition, any entity providing MEC will be required to report certain particulars of the MEC to the IRS and disclose these particulars participants. ALE Members with self-insured plans will report and disclose the MEC as part of Forms 1094-C and 1095-C. Insurers and employers who provide self-funded medical coverage (but who are not ALE Members) will report and disclose the MEC on new Forms 1094-B and 1095-C.