

Employee Benefits and Executive Compensation Alert

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Don't Play and Also Pay: Navigating the Employer-Sponsored Health Coverage Mandate

On Friday, August 31, the Internal Revenue Service (IRS) issued much anticipated guidance regarding the application of the employer-sponsored health coverage mandate (often called the “play or pay rules” under health care reform). Employers need to begin planning for these rules as soon as possible. While the employer coverage mandate itself does not apply until 2014, it may be necessary to begin tracking the hours of employees as soon as this October in order to facilitate compliance.

The Play or Pay Rules Generally

The employer-sponsored health coverage mandate is designed to require “applicable large employers”¹ either to provide employees with adequate and affordable health coverage or to require those employers to pay certain penalties for their failure to do so. Specifically, penalties are triggered if:

- (1) An employer fails to offer all of its “full time employees” the opportunity to enroll in an employer-sponsored health plan; or (2) the employer-sponsored health plan offered to “full time employees” is “unaffordable” or fails to provide “minimum value”; AND
- Any employee impacted by such a failure purchases individual health insurance coverage through a State-based or Federally-facilitated Exchange and qualifies for a subsidy.²

Failure to Provide Coverage

Employers who fail to provide coverage to all of their “full time employees” are subject to a penalty of \$2,000 per year (assessed on a monthly basis) multiplied by their total “full time employee” count.³ For employers that provide health coverage, the challenge with respect to this rule is identifying all of their “full time employees”—and making sure all such employees are offered coverage. In the event that even one “full time employee” is not offered coverage and subsequently attains subsidized coverage through an exchange, the penalty is applied to all “full time employees.” Thus, with respect to any employees who do receive employer-sponsored coverage, the employer could end up “playing” and “paying.”

Generally, health care reform defines a “full time employee” as any employee working on average at least 30 hours a week. The new IRS guidance clarifies that this definition not only includes those individuals who can be reasonably expected to work on average at least 30 hours a week, but may also encompass certain “variable-hour employees.”

The guidance provides a safe harbor for determining if an employee is full time that allows employers some relief from the need to monitor employee status on a monthly basis. This is especially useful for those employers with high turnover and a significant number of variable-hour employees. Specifically, the guidance allows an employer to monitor the hours of a variable-hour employee over a three to twelve month “measurement” or “look-back” period to determine if the employee averaged 30 or more hours per week during that period. The employer can then rely on those results for purposes of determining whether coverage should be offered to that employee during a subsequent six-to twelve- month “stability period” to avoid the no coverage penalty.

The new guidance also introduces the concept of an administrative period between a measurement period and its corresponding stability period to allow employers to enroll employees determined to be full time based on the prior measurement period. Depending upon the length of the measurement, stability, and administrative periods elected, the first measurement period for some employers may begin as early as October 1, 2012.

Failure to Provide Affordable/Adequate Coverage

The second penalty under the play or pay rules applies to employers who offer all of their full time employees coverage, but such coverage is too expensive or deemed inadequate. The penalty, \$3,000 per year (assessed on a monthly basis), applies only with respect to those full time employees who

actually receive subsidized health coverage through an exchange.

For purposes of this rule, coverage is deemed to be “unaffordable” if the employee premium for the lowest-priced “employee only” plan option available through an employer exceeds 9.5% of that employee’s household income. The new guidance issued last week confirms that employers do not have to actually determine an employee’s household income for purposes of administering this rule. Instead, an employer can assume that an employee’s household income is equal to the W-2 income provided to that employee by the employer for purposes of determining if the coverage it offers is affordable.

This penalty is also triggered if the coverage provided through an employer-sponsored plan does not provide “minimum value.” A plan fails to provide minimum value if the plan’s share of the total allowed costs of benefits provided under the plan is less than 60% of such costs. Definitive guidance on how to make this determination has not yet been issued; however, preliminary indications from the government suggest that a calculator will be made available for purposes of making these determinations.⁴ In addition, the government has suggested that certain safe-harbor checklists will be issued to allow employer-sponsored plans to confirm they offer minimum value without performing any calculations.

Additional Guidance Regarding the Limitation of Waiting Periods

Health care reform prohibits employer-sponsored health plans from imposing waiting periods of greater than 90 days. The Departments of the Treasury, Labor, and Health and Human Services issued joint guidance last Friday on the prohibition of extended waiting periods for participation in employer-sponsored plans. Among other things, the new guidance describes the interaction of this rule with the no-coverage penalty discussed above. It clarifies that the use of properly designed measurement periods will not be deemed to be a violation of the 90-day waiting period limitation. It also provides additional information about how this rule should be applied in practice, including with respect to part-time employees.

Preparing for 2014—Avoiding Penalties Is Not as Simple as Merely Providing Coverage

To avoid this result, it is necessary for employers to evaluate which employees are eligible for coverage under existing plans, track the hours of any excluded employees, monitor the income of low-paid full time employees in relationship to plan premiums, and, once further guidance is issued, confirm their plan offers adequate coverage. This is no small task, but with thorough planning, employers can implement the required plan changes and tracking systems necessary to avoid penalties.

Venable’s **Employee Benefits and Executive Compensation Group** looks forward to helping employer-clients continue to navigate health care reform as they prepare for 2014.

¹ The term “applicable large employer” means any employer with fifty (50) or more full time equivalent employees during the preceding calendar year. For this purpose, the hours of part-time employees are aggregated.

² Individuals/families with income of up to 400% of the federal poverty level may qualify for a subsidy. For 2012, this amount is \$44,680 for an individual and \$92,200 for a family of four. Exchanges are the new marketplaces that will offer individual health coverage in 2014.

³ This penalty applies on a controlled group basis, meaning that all full time employees within a group of closely related companies may need to be counted for purposes of calculating the penalty. For purposes of calculating this penalty, the first 30 full time employees can be disregarded.

⁴ Plans with nonstandard features will be able to rely on actuarial certifications in lieu of relying on the calculator.