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LEGAL ALERT

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Rules on 90-Day Waiting Period Limit and Identifying Full-Time Employees Released

On August 31, the Internal Revenue Service released two notices relating to key provisions for employers under the Patient Protection and Affordable Care Act (PPACA). The first, IRS Notice 2012-58, confirms and broadens the safe-harbor rules proposed in prior guidance for determining who are full-time employees (FT employees) under the large-employer shared responsibility provisions of Internal Revenue Code (Code) section 4980H, under which employers may become subject to penalties for failure to provide health plan coverage. Notice 2012-58 also provides for an administrative "protection" period that allows employers time to enroll newly-eligible FT employees without becoming subject to a penalty under Code section 4980H, as well as a process for transitioning between the methods for determining full-time status for new employees and ongoing employees.

The safe-harbor rules under Notice 2012-58 are coordinated with the rules in the second IRS notice, Notice 2012-59, relating to the 90-day waiting period limit for group health plan participation under Public Health Service Act (PHSA) section 2708. Notice 2012-59 is part of a joint effort by the tri-agency task force[1] to issue guidance, and it was issued in substantially similar form by the Department of Labor (as Technical Release No. 2012-02), and the Department of Health and Human Services on the same date.

This Legal Alert describes key aspects of IRS Notices 2012-58 and 2012-59, first addressing the 90-day waiting period limit. It also provides background on previously-issued guidance under Code section 4980H and PHSA section 2708 and how that guidance coordinates with the new rules. Employers can rely on the guidance in the two new IRS notices, as well as the guidance previously issued in IRS Notices 2011-36, 2011-73 and 2012-17 to the extent it has not been superseded by the latest notices, through the end of 2014.

90-Day Waiting Period Limit – PHSA Section 2708

Previous Guidance. PHSA Section 2708 provides that a group health plan cannot impose a waiting period of more than 90 days in plan years beginning on or after January 1, 2014. In IRS Notice 2011-36, the IRS requested comments on both the 90-day waiting period limit and the employer shared responsibility rules of Code section 4980H. Notice 2011-36 also solicited comments on the application of the waiting period limitation in situations in which a plan provides that employees (or certain classes of employees) are eligible for coverage once they complete a specified cumulative number of hours of service within a specified period (such as 12 months) and coordination of the 90-day limit with the look-back/stability period safe harbor for determining FT employees under Code Section 4980H, which was also proposed in Notice 2011-36 (and which is discussed below). Notice 2012-17 and guidance contemporaneously issued by DOL and HHS outlined various approaches to these issues then under consideration by the task force. That guidance contemplated that, for purposes of counting the 90 days, the waiting period would begin on the date that an employee would otherwise be eligible for coverage

[1] The tri-agency task force consists of the Internal Revenue Service (IRS), the Department of the Treasury, the Employee Benefits Security Administration of the Department of Labor (DOL), and the Department of Health and Human Services (HHS), which are also referred to above as the agencies.

under the plan, i.e., when he or she is in an eligible category, as the category or categories may be defined by the plan or the employer. However, any coverage waiting period based solely on the lapse of time could not be longer than 90 days, and waiting periods could not be designed to avoid compliance with the 90-day limit.

Notice 2012-59. The new guidance adopts the rules proposed in Notice 2012-17 and expands upon those rules in several respects. The rules are described as temporary guidance that will remain effective at least until December 31, 2014, with regulations or other future guidance becoming effective after adequate time for employers to comply with any new requirements. Comments on these rules are being accepted through September 30, 2012.

Notice 2012-59 defines the "waiting period" as a period of time that must pass before coverage for an employee or dependent, who has otherwise met the plan's substantive eligibility conditions, can become effective. Consistent with the proposed guidance, Notice 2012-59 provides that other conditions for eligibility under the terms of the plan are generally permissible under PHSA section 2708, such as limiting coverage to FT employees or employees who work at a certain location, unless the conditions are designed to avoid the 90-day waiting period limitation. Furthermore, Notice 2012-59 clarifies that a plan meets its obligation under PHSA section 2708 if the employee is permitted to elect coverage that would begin within the 90-day limitation period, even if the employee does not actually make an election until after the end of the 90-day period.

If a health plan conditions eligibility on an employee being full-time or completing a specified number of hours of service in a given period, Notice 2012-59 provides that the plan may take a reasonable period of time to determine whether a new employee with a variable work schedule is reasonably expected to work full-time or the number of hours required to become eligible under the plan. The period may include a measurement period that is consistent with the initial measurement period permitted for determining FT employees under Code section 4980H, discussed further below, and this rule applies even if the employer is not a large employer subject to Code section 4980H. The use of an initial measurement period will not be considered an attempt to avoid compliance with the 90-day waiting period limit of PHSA section 2708 if a waiting period of up to 90 days is imposed after the initial measurement period, as long as the employee has an opportunity for coverage to become effective within 13 months after his or her start date. If the employee's start date is a date other than the first day of a calendar month, the time remaining between the start date and the first day of the next calendar month may be added to this 13-month period.

A series of examples in the Notice emphasize several points regarding the application of these rules, including the following: (1) coverage may become effective after the 13-month period ends (or 13 months plus the time remaining until the next calendar month) if the delay results solely from the length of time taken by the employee to complete the enrollment materials; (2) a plan that has a cumulative hours of service eligibility requirement must make coverage available to an employee no later than the 91st day after the date that the employee first meets the hours requirement; and (3) a cumulative hours of service requirement of more than 1,200 hours will be considered designed to avoid compliance with PHSA section 2708.

Shared Responsibility – Code Section 4980H

Background. The shared responsibility provision of Code section 4980H requires an employer with 50 or more FT employees to make an "assessable payment" if it does not provide health plan coverage or the health plan coverage it provides is not affordable, and, as a result, any of its FT employees are certified to receive either a premium tax credit to purchase health coverage through an exchange under Code

section 36B or a cost-sharing reduction payment (i.e., a subsidy) for that coverage under section 1402 of PPACA. More specifically, a FT employee could qualify for the tax credit or subsidy because the employer does not provide the employee with minimum essential coverage, the coverage offered by the employer is unaffordable based on the employee's household income or the employer's coverage does not provide minimum value (i.e., does not cover at least 60% of the cost of benefits). An employer's failure to provide a FT employee with applicable coverage could trigger a payment under Code section 4980H of up to $2,000 per FT employee per year for employers that offer no coverage or up to $3,000 per FT employee per year for whom coverage is unaffordable or does not meet the minimum value rule.

Thus, the definition of FT employee is key in determining whether and, if so, to what extent, an employer may incur tax under Code section 4980H. Under the Code, an employee is considered full-time to the extent that he or she works 30 or more hours per week. The Code also provides that coverage under an employer-sponsored health plan is affordable to an employee if the employee's required contribution does not exceed 9.5% of the employee's household income for the taxable year. In addition, seasonal employees are excluded from the employer's workforce for purposes of determining whether the employer is a large employer subject to the employer shared responsibility provisions.

Previous Guidance. In Notice 2011-36, the IRS requested comments on the application of Code section 4980H and proposed several definitions and related rules for identifying the employers subject to section 4980H and the determination of FT employees, including rules for counting hours of service for hourly paid and other employees, identifying employees who are full-time equivalents or seasonal employees and the steps for calculating the number of FT employees of an employer. Notice 2011-36 also included a proposed look-back/stability period safe harbor for determining whether ongoing employees are FT employees for purposes of Code section 4980H. Under the safe-harbor method, an employer would determine each employee's full-time status by looking back at a defined period of three to 12 consecutive months (the measurement period), to determine whether the employee averaged at least 30 hours of service per week or at least 130 hours of service per calendar month. If so, the employee would be treated as a FT employee during a subsequent "stability period" of up to 12 months (regardless of his or her actual hours worked during that period), with the length of the stability period based on the length of the initial measurement period. In Notice 2011-73, the IRS proposed that employers would be able to use an employee's W-2 wages as a safe harbor to determine whether employer-provided coverage is affordable under Code section 4980H and asked for comments on this approach.

Notice 2012-17, issued in February 2012, confirmed that proposed regulations will provide that employers may rely on employees' W-2 wages for determining whether coverage is affordable under Code section 4980H. In addition, Notice 2012-17 signaled that proposed regulations will coordinate the rules under PHSA section 2708 and Code section 4980H and will provide that an employer will not be subject to the shared responsibility payment under Code section 4980H for a new hire for at least the first three months following the employee's date of hire. However, it indicated the regulations will say new hires who are expected to work full-time on an annual basis and who work full-time for the first three months of employment must be offered health coverage no later than the end of that three-month period in order for the employer to avoid an assessable payment under Code section 4980H with respect to those employees.

Notice 2012-17 also described the expected approach for determining whether a new hire is a FT employee, noting that:

- To the extent that an employer cannot determine whether a new hire will work full-time on an annual basis, the employee must be offered coverage under the plan:

- After the first three months of employment, if the employee works full-time during those first three months and his or her hours reasonably represent his or her future work schedule; or
- If the employee does not work full-time during the first three months, or the employee works full-time during this period but his or her hours are not reasonably representative of his or her future work schedule, the employer may evaluate the employee's hours over a second three month period (and future three-month "stability periods") to determine whether the employee should be considered full time. Under these circumstances, the employer will not owe an assessable payment during the first or second three months of employment, and the employer will not owe an assessable payment for any additional three-month stability period during which the employee does not work an average of 30 hours per week, provided the employee is offered coverage after the end of the first three-month stability period during which the employee reaches an average of 30 hours per week.

The IRS requested comments on the proposals outlined in Notice 2012-17. Finally, Notice 2012-17 noted that the IRS intended to issue future guidance coordinating the rules for new hires with additional rules for ongoing employees and rules regarding the treatment of employees who change status.

IRS Notice 2012-58. Notice 2012-58 adopts several of the rules proposed in the prior guidance, modifying and expanding the safe-harbor rules for determining full-time status under Code section 4980H for ongoing employees and new employees (including employees who have variable or otherwise uncertain hours and seasonal employees) and providing additional rules regarding transitioning employees from the methods for identifying new FT employees to the method for identifying ongoing FT employees. Notice 2012-58 also provides for optional administrative periods that the employer may use to determine which employees are full-time, notify employees of their coverage options, collect employee elections and other data, and enroll them in coverage. If an employer elects to use an administrative period, during that period the employer will not be subject to an assessable payment under Code section 4980H for failing to provide coverage to either new hires or ongoing employees who have met the standards to be considered full-time during a recently completed measurement period.

Safe Harbor for Ongoing Employees. The Notice provides that employers will be permitted to use the three-month to 12-month look back and stability periods for determining whether ongoing employees are full-time as proposed in Notices 2011-36 and 2012-17 and expands on that guidance as follows:

- The look-back measurement period for ongoing employees is referred to as the "standard measurement period."
- An ongoing employee is defined as an employee who has worked for the employer for at least one complete standard measurement period.
- The employer may determine the length of the standard measurement period (from three to 12 months), as well as the start and end dates for the period. Different periods may be used for different categories of employees, but the determination must be made on a uniform and consistent basis for all employees in the same category, with the following permissible categories:

  - Collectively bargained and non-collectively bargained employees;
  - Salaried and hourly employees;
  - Employees of different entities; and
  - Employees in different states.

- Once an employer determines that an employee is a FT employee during a standard measurement period, the subsequent stability period must be at least six months or the duration of the standard measurement period, if longer. In contrast, if an employer determines that an employee is not a FT employee during a standard measurement period, the employer may treat the employee as part-time during the subsequent stability period if that period is equal to or shorter than the standard measurement period.
- Finally, the Notice provides employers with the option to implement a 90-day administrative "protection" period following the standard measurement period, but before the beginning of the subsequent stability period during which coverage will be provided to FT employees. If an ongoing employee who was part-time becomes full-time and, thus, is newly eligible for coverage, the employer will not be subject to an assessable payment for failure to provide coverage to the newly eligible FT employee during this optional administrative period. However, ongoing employees who are covered as FT employees under the plan based on their average hours worked during a previous measurement period cannot be removed from the plan during the administrative period (for instance, if the employer has determined that the employee was not a FT employee based on average hours worked during the immediately preceding standard measurement period). Therefore, if an administrative period is used, it must overlap the end of the stability period for the prior standard measurement period. The guidance does not indicate whether an employer that chooses to use an administrative period must do so for all employees or may elect to use this option only for certain categories of employees.

The Notice specifically confirms that an employer may choose a 12-month standard measurement period that ends just before the start of the plan's annual open enrollment season in an effort to align the eligibility determination process with the plan's current enrollment process. Employers subject to the shared responsibility provisions of Code section 4980H will need to carefully analyze this guidance if their plan(s) exclude any employees who are not full-time (i.e., employees who work less than 30 hours per week). Employers will need to determine the practicality of using the safe harbor, the best approach for selecting the duration and start/end dates of the standard measurement period and the stability period for each plan and each category of ongoing employees, as well as whether the 90-day administrative period may ease implementation of the new rules.

Safe Harbor for New Employees. As proposed in Notice 2012-17, an employee who is reasonably expected to work full-time as of his or her start date must be offered coverage no later than the 91st day after his or her start date. Notice 2012-58, however, revises the Notice 2012-17 proposed safe harbor for determining which new hires are not reasonably expected to work full-time because of their status as variable-hour or seasonal employees and when those employees should be considered FT employees for purposes of Code section 4980H:

- The look-back measurement period for new variable-hour or seasonal employees (i.e., employees other than "ongoing employees") is referred to as the "initial measurement period" under the Notice. Examples indicate that the employer may begin an employee's initial measurement period on his or her start date or the first day of the next month.
- A new employee is a "variable-hour" employee if (a) based on the facts and circumstances on his or her start date, the employer cannot determine that the employee is reasonably expected to work, on average, at least 30 hours per week, or (b) the employee is expected to work at least 30 hours per week initially, but the period of employment at more than 30 hours per week is reasonably expected to be limited, and the employer cannot determine that the employee will work on average at least 30 hours per week over the initial measurement period. Employers may define certain of these limited-duration employees as "seasonal" employees using a reasonable good faith interpretation of that term through 2014.

- The three-month incremental measurement periods contemplated under Notice 2012-17 have been extended, allowing an employer to use from three-month to 12-month periods, consistent with the standard measurement period for ongoing employees, and the subsequent stability period for new variable-hour employees must be the same duration as the stability period for ongoing employees.
- As with ongoing employees, once an employer determines that a variable-hour or seasonal employee was a FT employee during the initial measurement period, the subsequent stability period must be at least six months or the duration of the initial measurement period, if longer. However, if the employer determines that the employee was not a FT employee during the initial measurement period, the subsequent stability period must not be longer than the shorter of (a) the initial measurement period plus one month, or (b) the remaining standard measurement period for ongoing employees (plus any optional administrative period) in which the initial measurement period ends.
- As noted above, Notice 2012-58 also provides safe-harbor transition rules to transition employees from the safe harbor for new employees to the safe harbor for ongoing employees. These rules apply once an employee has completed one standard measurement period. Under the transition rule, and employer using 12-month measurement periods will need to test new variable-hour employees for FT employee status at least twice during a single 12-month period: at the end of the initial measurement period and again based on the standard measurement period used for ongoing employees that begins during or at the end of the initial measurement period. Since these periods will often overlap, an employee may be determined to be a FT employee based on one measurement period, but not an FT employee based on a second, overlapping measurement period, due to changes in his or her work schedule. In such circumstances:

    - If the new employee is determined to be a FT employee during the initial measurement period, that employee must be treated as a FT employee for the duration of the associated stability period, even if the stability period includes months during an overlapping standard measurement period in which the employee has been re-tested and was determined to no longer be a FT employee.
    - If the new employee is determined not to be a FT employee during the initial measurement period, but is determined to be a FT employee under an overlapping or immediately following standard measurement period, that employee must be treated as a FT employee for the duration of the stability period associated with the standard measurement period, even if that stability period begins before the end of the stability period associated with the initial measurement period.

- Similar to the safe-harbor for ongoing employees, following the initial measurement period, the employer has the option to apply a 90-day administrative period to perform the necessary analysis of whether the variable-hour and seasonal employees are full-time. However, the 90-day period must include any days after the employee's start date (excluding the initial measurement period) during which the employee is not offered coverage, even if those days occur prior to beginning of the initial measurement period. This would occur in cases in which the employer opts to begin the initial measurement period on a date after the employee's start date, such as the first day of the calendar month following the start date.
- In addition, the Notice provides that the combined length of the initial measurement period and the optional administrative period cannot extend beyond the last day of the calendar month beginning on or after the first anniversary of the employee's start date. This means that the optional administrative period and the safe-harbor initial measurement period, combined, cannot exceed 13 months for variable-hour and seasonal employees.

Finally, the Notice also confirms that an employee is not considered eligible for minimum essential coverage under a health plan during any safe-harbor measurement or administrative period before coverage takes effect. Accordingly, during these periods an employee may be eligible for a premium tax credit under Code section 36B or a cost-sharing reduction under PPACA section 1402, even though the employer may not be subject to an assessable payment for failure to provide coverage during the period because the employer has complied with the safe-harbor rules.

Notice 2012-58 provides that employers may rely upon the guidance at least through the end of 2014, including covering any measurement period beginning in 2013 or 2014 and any associated stability period(s). It further says that future regulations or other guidance will not be effective before January 1, 2015 to the extent those rules are more restrictive. In addition, the Notice requests comments on four issues, including whether safe-harbor rules are needed for temporary or other short-term employees, whether special rules are needed for mergers and acquisitions and how seasonal workers should be defined. Comments on Notice 2012-58 and these additional questions are due by September 30, 2012.

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If you have any questions about this Legal Alert, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

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