Holland & Hart

**Beth Nedrow**

Partner
406.896.4635
Billings
enedrow@hollandhart.com

# Time to Pay the PPACA Piper! Proposed Regulations Provide Detail on 'Pay or Play' Feature of Health Care Reform

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A key feature of the federal health care reform statute known as PPACA (the Patient Protection and Affordable Care Act) is the requirement that some employers may have to pay a penalty if they don't offer health coverage to their employees. This has often been referred to as the "pay or play" penalty, but the IRS refers to it as the "employer shared responsibility" provision. Penalties will be assessed beginning in 2014 and are based on employee hours tracked for 2013, so planning in 2013 is crucial.

Just which employers are subject to the penalty and how it will be calculated are now a little clearer, following the IRS's publication of proposed regulations and other guidance in late December 2012. Employers can rely on the proposed regulations at least until final regulations are issued.

The employer shared responsibility provision is a non-deductible excise tax that the IRS has authority to collect from an "applicable large employer" if a series of events and conditions occur. The excise tax is generally $2,000 per each full-time employee (above 30) for failure to offer the required coverage, or if coverage is offered but doesn't meet the affordability or value requirements, then $3,000 per full-time employee who receives a premium tax credit and elects coverage through the federal or one of the state health care exchanges.

The excise tax will apply only if *all* three of the following occur:

1. The employer is an "applicable large employer." An applicable large employer is one who employed 50 full-time employees (or full-time employee equivalents) during the preceding calendar year, calculated by averaging its employees across the months in the year. In making this determination here are a few key principles:
    - The "employer" for this purpose includes all entities in the same controlled group.
    - Employees are generally considered full-time if they work, on average, at least 30 hours of service per week (or 130

hours per month).

- Part-time employees are counted using mathematical rules that convert them to full-time equivalents. For any month, the total hours worked by part-time employees (up to 120 per employee) are added and then divided by 120.
- There is an exception that can apply to employers with seasonal employees. An employer won't be considered an applicable large employer if the employer's workforce only goes over 50 employees for 120 or fewer days and it's due to seasonal employees.
- If an employer has a fluctuating workforce that goes above and below 50, a transition rule allows the employer to use any period of 6 consecutive months rather than the full 12 months of 2013. This is an important planning feature for smaller employers.

2. At least one full-time employee is certified to receive a premium tax credit or cost-sharing reduction and enrolls in coverage on a health care exchange. Premium tax credits are available to help pay for coverage for employees who are between 100-400% of the federal poverty level and enroll in coverage through a health care exchange. However, premium tax credits are not available to individuals who are eligible for coverage through a government-sponsored program like Medicaid or CHIP (a fact that is especially interesting given PPACA's Medicaid expansion).
3. The employer either:
    a. fails to offer substantially all (at least 95%) of its full-time employees (and their dependents) the opportunity to enroll in "minimum essential coverage" (this is sometimes referred to as the 4980H(a) scenario for the Internal Revenue Code Section where it is described); or
    b. does offer the coverage described in (a), but the coverage is "unaffordable" or does not provide "minimum value" (this is sometimes referred to as the 4980H(b) scenario).

These elements are too complex to summarize in this brief article. Instead, each employer should work with its attorneys, consultants, insurers and other advisors to study how the requirements apply to the employer's particular circumstances. A few of the notable high-level issues, however, are:

- Although the previous requirement under PPACA to offer coverage to dependents up to age 26 could be avoided if the employer did not offer any dependent coverage, the pay or play penalty effectively requires employers to offer coverage to dependents or risk paying the penalty. Significantly, the regulations clarify that spousal coverage is **not** required, and failure to offer spousal coverage will not trigger any pay or play penalties.
- Coverage will be "unaffordable" if the employee's premium share for self-only coverage exceeds 9.5% of the employee's modified adjusted gross household income (or 9.5% of one of three alternate

safe harbors: W-2 wages, rate of pay, or federal poverty line). This means that premiums for family or dependent coverage will not be relevant for this purpose.

If all of the above three requirements are met, then the penalty may apply to the employer. The amount of the penalty is based on the number of full-time employees of the employer (which for this purpose is the individual entity, and not the controlled group of related companies). There is another set of detailed rules for determining who is considered a full-time employee for this purpose. In general, an employee is considered full-time for this purpose if the employee was employed on average at least 30 hours of service per week. For employees paid on an hourly basis, actual hours are used. For other employees, either actual hours or certain equivalency methods can be used. There are also numerous other special rules for new employees, variable hours employees, seasonal employees, changes in employment status, breaks in service, and other situations.

The proposed regulations include a transitional rule for fiscal year plans. If certain coverage requirements are met, a fiscal year plan may be able to avoid pay or play penalties until as late as the plan year beginning in 2014.

Employers may wonder how the IRS intends to enforce the pay or play penalty. Significantly, the proposed regulations would not require employers to self-report or otherwise demonstrate compliance on a regular basis. Instead, the proposed regulations provide that the penalty will be triggered by the IRS sending the employer a notice of potential liability and the opportunity to respond. Future guidance is expected on how this process will work. Practically, employers would not receive any notification for 2014 penalties until well into 2015 - after the employees' individual tax returns are filed where the premium tax credits will be claimed, and after the due date for applicable large employers to file the information return describing their coverage offerings (another feature of PPACA not detailed here, first due in 2015).

For questions on the pay or play feature of health care reform, or any other aspect of PPACA or benefits law, contact a member of the Benefits Law Group.

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