ACA Compliance: Getting Ahead of the Curve

A LexisNexis® White Paper with Cynthia Stamer
The looming implementation of another round of employer mandates under the Affordable Care Act (ACA) has business leaders scrambling for help from legal counsel and other advisors. This flurry of activity is prudent; compliance with ACA is a matter of federal law and many penalties for failure to comply are severe. Employers who do not meet their implementation responsibilities face potential company fines of up to $3,000 per employee, per year, and employers who fail to offer adequate health plans under the ACA could be hit with excise taxes of as much as $36,000 per employee, per year.

Meanwhile, the timetable for ACA implementation has been a moving target. Although most of the ACA milestones have already passed and gone into effect, the compliance deadline for perhaps the most-discussed new rule—the Internal Revenue Code (“Code”) Section 4980H “shared responsibility” or “pay or play” facing “large” employers has moved around since passage of the law in 2010. As of this writing, the current magic deadlines are January 1, 2015, for businesses with more than 100 full-time employees, and January 1, 2016 for businesses with between 50 to 99 full-time employees.

Moreover, earlier this year the U.S. Department of the Treasury also created a “safe harbor” rule under Code Section 4980H. This rule says that employers can avoid the annual penalty provided for in Code Section 4980H(a) of $2,000 per full-time employee if the company can show it offered the opportunity to enroll in employee and dependent coverage under a health plan offering minimum essential coverage to at least 70 percent of their employees by 2015, and to 95 percent of employees by 2016. The rule also clarifies that volunteers will not be considered employees.

Labor and Employment attorneys—and their corporate clients—need to be aware of the rules related to ACA implementation and the various statutory deadlines in order to prepare for compliance with these crucial new rules and to anticipate potential issues impacting other employment concerns that may arise from attempts by employers to reclassify workers or restructure their workforce to minimize health benefit costs and liabilities. The purpose of this white paper is to offer practical information that will help clarify ways in which employers can go about counting and defining their employee universe for ACA compliance purposes.

**ACA Framework**

While the pay-or-play rules of Code Section 4980H have attracted significant attention, it’s important to keep in mind that the ACA added a host of other new mandates and rules to the already complicated federal rules governing employment-based health plans. While Section 4980H is expected to impact only the estimated five percent of health plans maintained by large employers, these other rules apply more broadly. Consequently, it’s important that employers, regardless of size, don’t allow concern over the pay-or-play penalty to distract them from meeting these other requirements, many of which may have significantly greater financial or other implications than the Code Section 4980H penalty.

It’s also important to be clear on the regulatory framework in order to understand the ACA’s various requirements and implementation deadlines. Employer size and whether an arrangement is considered insured or self-insured tend to be the two most common criteria governing the applicability of these federal rules. For purposes of Code Section 4980H and certain other Code rules, there are four “categories” of employer size relevant under the ACA:

- Small Employers (fewer than 25 FTEs)
- Medium Employers (25 – 49 FTEs)
- Large Employers with 50 – 99 FTEs
- Large Employers with 100+ FTEs
The Code’s tax treatment of employers under the ACA generally turns on where a business fits within one of those four size categories. For example, the ACA’s pay-or-play employer mandate only applies to “large employers” and the specific implementation date depends on whether there are more or fewer than 100 “full-time equivalent” or “FTE” employees in the company. Likewise, the small business health-care tax credit only applies to the businesses in the “small employers” category and other ACA rules vary based on the size of the employer.

The chart below illustrates just a few of the different tax rules added by the ACA that apply to employers based on their size.

Unfortunately, that’s not even the end of the complexity with respect to the ACA tax compliance framework. In addition to these multiple categories with different rules and deadlines, different rules even count “employees” slightly differently. And as if that weren’t enough, special rules apply to alternative workforce, leased employees and other contingent workers.

**Defining Your Employee Universe**

Faced with these moving deadlines and confusing guidelines for Code Section 4980H, it’s important for employers to take a deep breath and solve one thing at a time. Without question, the number-one thing that every corporate executive team needs to do right now—if it has not already—is to accurately identify who your common-law employees are under the ACA.

### What Health Insurance Coverage Must an Employer Offer?

<table>
<thead>
<tr>
<th>Rule</th>
<th>Small Employer ≤25 FTEs</th>
<th>Medium Employer 26 – 49 FTEs</th>
<th>Large Employer 50 – 99 FTEs</th>
<th>Large Employer ≥ 100 FTEs</th>
</tr>
</thead>
<tbody>
<tr>
<td>IRC § 162 Employer Premium Deduction</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>IRC § 46R Tax Credit</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>IRC § 4980H Pay or Play (Transition Relief Delays Enforcement to 2015 for Employer of ≥100 FTEs and 2016 if 50 – 99 FTEs)</td>
<td>No</td>
<td>No</td>
<td>Yes beginning 1/1/2016</td>
<td>Yes beginning 1/1/2016</td>
</tr>
<tr>
<td>IRC § 105(h) Self-Insured Health Plan HCE Nondiscrimination</td>
<td>Yes if self-insured</td>
<td>Yes if self-insured</td>
<td>Yes if self-insured</td>
<td>Yes if self-insured</td>
</tr>
<tr>
<td>PHS § 2716 Insured Non-Grandfathered HCE Nondiscrimination</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>$100 per day per non-highly compensation individual discriminated against (delayed by Notice 2011-1 until further notice, plus a possible civil action to enjoin the discriminatory practice)</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Code § 125 Taxability of Contributions Discriminating In Favor of HCE or Key Employees</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Contractual Obligations: Union, Government Contractor, M&amp;A or other obligation</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>

As the previous chart illustrates, the ACA generally sets out responsibilities in the Code based on the number of employees in an organization (in addition to new reporting requirements under changes to the corporate tax code). This definition of a company’s employee universe includes two components that are determined based on the common-law employees employed by the company:

1. Head count of common-law employees
2. Number of hours worked by those employees

This calculation yields the number of FTEs the company has under law.

Under the ACA rules, it’s critical to accurately identify the common-law employees based on a factual analysis, as well as correctly count their hours worked. The ACA determines employee status using the common-law test without application of the “Section 530” relief that may sometimes apply for income and payroll tax purposes. This means employee status depends upon the true factual control that the employer has over the details of work performed, regardless of how the employer labels the worker.

Likewise, the ACA treats an employee as full time if he or she is reasonably expected to work on average at least 30 hours per week, or 130 hours per month for purposes of the Fair Labor Standards Act (FLSA). Variable hour and seasonal employees also may be considered full time under the new ACA rules under many circumstances.

Before embarking on an effort to define the employee universe, however, it’s advisable that employers not get overly aggressive about trying to game this calculation. For example, attempts to reduce employee counts by broad-based characterization of categories of workers as “contract labor” or “contingent workforce” do not reduce the number of FTEs if the worker under the business holds sufficient control over the work performed. Furthermore, misclassification of workers that are common-law employees under the facts and circumstances as contract or leased employees also can create significant other liability if the misclassification results in the employer disregarding lower-paid workers when doing employee benefit plan discrimination testing, fails to properly withhold taxes, or fails to meet wage and hour, immigration or other requirements for employed workers.

Also, even if they accurately know which workers are common-law employees, most employers have some additional up-front work to begin tracking actual employee hours. For instance, assuming a business accurately counts hours worked for hourly employees under the FLSA, most businesses don’t track actual hours worked for salaried, outside commissioned sales and other common-law employees exempt from the FLSA minimum wage and overtime rules. While the existing Code Section 4980H regulations allow employers to use various safe harbors to calculate hours for exempt employees, these deemed rules are designed to overestimate hours worked. Finally, the ACA regulations have specific rules about when an employee qualifies as seasonal or variable hours. Businesses need to know the specific rules and be prepared to defend their treatment of those workers as excludable.

Once you’re ready to define the employee universe, here are a few tips for getting it right:

• Create and fill up the bucket—If an employee is expected to work 30 or more hours per week, he/she is classified as a full-time employee. That’s your starting point.
• Filter out the variable or seasonal employees—An employee is a variable-hour employee if his/her weekly schedule fluctuates above and below 30 hours, and it cannot be immediately determined whether the employee works an average of 30 hours per week. An employee is considered a seasonal employee, and is allowed to be excluded from the full-time employee calculation, if employed on a seasonal basis within the meaning of the FLSA (e.g., during the
holidays) or works no more than 120 days. Generally, the rules that apply to variable-hour employees also apply to seasonal employees.

- Align your health plan “eligibility” definition—The ACA full-time employee definition differs from the “full-time eligibility” requirement that many employers use. It’s important to compare those definitions and, if necessary, create a plan amendment and summary plan description update to comply with ACA and other employee benefit plan laws.
- Evaluate implications of other ACA and other federal and state mandates on your plans and adjust documents, practices, summary plan descriptions, notices and budgets as necessary.

**Meeting Your ACA Responsibilities**

Once the business understands the ACA and other legal framework and knows its workforce, making the tough decisions about how to deal with their ACA compliance obligations becomes pretty straightforward.

For starters, business leaders can make a calculated guess concerning how much it would cost per employee to either pay the penalty or provide coverage. An employer also can predict if their business can qualify for a tax credit, will face a penalty under Code Section 4980H, the nondiscrimination rules or otherwise, and other costs and liabilities. Here are some factors for employers to consider when deciding whether or not to provide coverage:

- For a large employer, the cost of employer coverage vs. cost of the penalty
- Availability and cost of obtaining coverage through a health exchange (with credits and subsidies) for employees
- Competition for finding new employees in the labor market due to turnover if the employer chooses not to make employees fully or partially whole (and they move to an organization that does)
- Size and composition of the workforce—including part-time employees—which might influence the insurance coverage available at a reasonable cost and therefore its value in attracting new workers
- The likelihood that the plan or a cafeteria plan used in connection with its funding will be considered discriminatory under the discrimination rules of the Code
- Legal and other operational costs of maintaining a plan in an evolving legal environment
- The likelihood that the workforce will continue to value the coverage offered in light of the availability of the exchange option.

For those employers that decide not to offer the required health insurance coverage to employees under the ACA, consider fully your range of options.

First, if your company employs less than 100 FTEs in 2015 or 50 FTEs in 2016, Code Section 4980H doesn’t apply. If Code Section 4980H applies, first consider whether it makes more financial sense for your company simply to pay the $2,000 annual penalty per full-time employee enrolling in health coverage through an exchange rather than to incur the cost and other liabilities of offering and providing company-sponsored coverage.

Second, if maintaining a health plan continues to make sense, monitor the employees treated for purposes of the pay-or-play rules as “part-time,” “seasonal” or “variable hours” to make sure they do indeed meet (and continue to meet) the applicable tests so you don’t make an expensive mistake. Then, if an otherwise justifiable business reason exists and it works for your business, consider restructuring your practices for scheduling workers to minimize the number of full-time employees.
Third, your company may want to consider offering a health plan that offers minimum essential coverage but doesn’t meet the minimum value or affordability tests of Code Section 4980H—and then just pay the $3,000 annual penalty per full-time employee who actually enrolls in and obtains subsidized coverage from a health insurance exchange. Employers considering this approach also will need to consider whether the enrollment patterns resulting from this plan design are likely to cause the health plan, the cafeteria plan used to allow employees to pay contributions pre-tax, or both, to be discriminatory under the Code’s rules as the Code applies adverse consequences when health plans discriminate in favor of highly compensated employees.

Fourth, many employers that previously offered insured group health-plan coverage now are electing to self-insure. While most requirements of the ACA and other federal health-plan rules also apply to self-insured plans, the consequences of a discriminatory self-insured health plan are less draconian for the employer. Also, the ACA and the state law preemption rules of the Employee Retirement Income Security Act allow self-insured plans more flexibility in the benefits offered. In addition, depending on how the plan is designed and administered, the PCORI fee assessment or a self-insured plan may be less than for an insured plan.

Finally, regardless of whether an employer chooses to offer coverage going forward and the plan design adopted, all employers regardless of size need to be prepared to meet new requirements to track and report data about their employees and health coverage to the IRS and other agencies, to inform workers about health coverage practices, and other related responsibilities. So whatever decision your business makes about health insurance coverage for employees, ensure that your company takes appropriate steps to amend or terminate its plan and completes these actions with sufficient lead time to provide the 60 days prior notice of material change and meet other notice requirements of the ACA and otherwise applicable law.

**Conclusion**

The key for employers who want to get ahead of the curve on ACA compliance is to study the ACA framework in conjunction with all other applicable compliance requirements, define the employee universe now and assess their “pay or play” exposure and options with the best information in front of them.

No one can predict how the ACA and its implementation regulations may change in the future, depending on how national political trends develop and actual health-care costs evolve. Regardless of those unknowns, however, information and insights gathered now will help employers prepare for whatever lies ahead.
About the Featured Contributor

Cynthia Stamer is a Board-certified, AV®-rated labor and employment attorney, management consultant, policy advocate, author and public speaker. Ms. Stamer helps businesses and government leaders manage legal and other risks using in-depth human resources, insurance, employee benefits, health care, corporate compliance and other legal knowledge. She is a Fellow in the American College of Employee Benefit Council, American Bar Association (ABA) Joint Committee on Employee Benefits Council representative, Past Chair of the ABA RPTE Employee Benefits & Compensation Group and Vice Chair of the ABA TIPS Employee Benefit Committee, Past Chair of the ABA Health Law Managed Care & Insurance Group, and serves in numerous professional and civil leadership roles. Ms. Stamer is a popular speaker and is the author of hundreds of publications. For more information, see www.cynthiastamer.com or email Ms. Stamer at cstamer@solutionslawyer.net.

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