

Planning for the 2014 Employer Health Insurance Mandate

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Timeline

- March 23, 2010- PPACA
- June 28, 2012- Supreme Court: individual mandate a legal tax, Medicaid expansion can't be forced
- November 6, 2012- election
- December 28, 2012- IRS proposed regulations
- January 1, 2013- .9% & 3.8% "pay for" taxes start
- No later than July 1, 2013- take steps to minimize impact of mandate
- January 1, 2014 (or possibly first day of 2014 fiscal plan year) - employer mandate takes effect

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The Employer Mandate

- Beginning in 2014 **large employers** will become subject to nondeductible **penalty taxes** unless they **offer** adequate and affordable group health insurance to their **full-time** employees (and dependents in 2015)
- **Small** employers exempt from mandate (but not other ACA provisions)
- Coverage of **part-time** employees never required
- **Large** employer and **full-time** employee determinations for 2014 based on 2013 demographics

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Step 1: Testing Universe

- “Employer”- include related entities
 - Apply controlled group and affiliated service group rules of IRC section 414
- “Employees”- apply common law test
 - Include everyone on payroll except self-employed owners or >2% S corp shareholders
 - Include workers not on payroll but subject to employer direction and control (1099 independent contractors, staffing company workers?)
- “Hours”- include hours worked and hours paid while not working (paid holiday, vacation, jury duty, etc.)
 - 8 hours/day, 40/hours week equivalencies

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Step 2: “Small” Exemption

- **50 or more** full-time employees + “full time equivalents” in prior calendar year = large employer for next calendar year
- Full-time employee = **30 or more** hours per week or 130 or more hours per month
 - 52 weeks x 30 hours divided by 12 = 130 hours/month
- Solely for purposes of the small employer determination part-time employee hours are converted into “full-time equivalents” (FTEs)
- Calculation made for each **month** in prior year then averaged to determine status for the following year

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Small Employer Exemption

Determining full-time employees and FTEs for a *month*:

1. List all employees for the month (include “related” companies)
2. List each employee’s hours
3. Number of employees with 130 or more hours = “actual” full-time employees
4. Total the hours for all other employees (but don’t count more than 120 hours for any one employee) = total “part-time” hours
5. Divide total part-time hours by 120 = number of “full-time equivalents” (FTEs) (carry to first decimal point)
6. Add number of “actual” full-time employees to the number of FTEs = testing “number” for that month

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Small Employer Exemption

Determine the *average number for the prior calendar year*:

1. Add the monthly totals, divide by 12 and round down to the next lowest whole number
2. If the resulting number is **49 or less** the employer is “small” and exempt from the mandate for the following calendar year
3. If the resulting number is **50 or higher** the employer is “large” and subject to the mandate for the following year (unless the seasonal employer exception applies)

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Monthly Calculation Example

For the month of January 2013 employer had 72 employees:

12 salaried and hourly employees who worked 130 or more hours (“actual” full time employees)

10 hourly employees who worked between 121 and 129 hours (limit to 120 hours each = 1,200 total part-time hours for these 10)

50 hourly employees who each worked <121 hours and collectively worked 4,000 hours

Total FTE hours = 1,200 + 4,000 = 5,200

Divide 5,200 hours by 120 = 43.3 FTEs

Add 12 “actual” full time = **55.3 full-time and FTEs for January 2013**

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Special 2013 Transition Rule

- Special transition rule for 2013:
 - Instead of all 12 months use **any 6 or more consecutive month period** in 2013
 - 28 possible testing periods (6 or more consecutive months)
 - Recommendation: test all 28 iterations until you find one <50
 - Make permanent record of test results and underlying data to support exemption when IRS proposes a penalty
- Any employment practice changes need to be in place by 7/1/13 to capture the requisite 6 month minimum period
- Note: future years will test using all 12 months
 - Will need interim/estimated testing to prepare for adverse consequences when or if 50 threshold exceeded

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Seasonal Worker Exception

- If employer fails the <50 test may still be exempt if:
 - Workforce exceeded 50 for no more than 120 days or 4 months
 - 100% of the employees in excess of 50 for those 120 days or 4 months were seasonal workers
- Employer can chose any 120 days or 4 months, not required to be consecutive
 - Suggestion: test as many combinations as needed to demonstrate exemption
- “Seasonal” workers include those in agriculture, retail during holidays and “other” reasonably determined seasonal businesses (summer help in resort areas)

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Exempt Small Employer- Stop Here

- If exempt small employer for 2014 stop here
- Determine whether to offer health insurance, to whom and at what cost without regard to the employer mandate
- Other “patient protection” reforms will apply to coverage offered
- Be mindful that offering affordable coverage to lower income employees will make them ineligible for Marketplace subsidies
- Be mindful that in 2015 new non-discrimination requirements will apply after IRS issues regulations

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Step 3: Large Employer- Determine 2014 Full-Time Employees

- Large employer identifies 2014 full-time employees based on look-back to 2013 hours
- Full-time employees = employees who work 30 or more hours per week (130 hours per month)
- Threshold strategy: determine whether it makes business sense to impose a cap on the number of hours employees (or categories of employees) will be permitted to work in 2013 in order to control/minimize the number of “deemed” full-time employees in 2014
 - Virginia example- all hourly limited to 29 hours/week

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Step 4: Making the Full-Time Employee Determination

- Use IRS optional “look back” methodology to determine every ongoing employee’s future status
 - Test the employee’s hours during a “measurement period”
 - Analyze the data, make the status determination and notify and enroll full-time employees during an optional “administrative period”
 - Based on hours of employment during the measurement period treat employees as full-time or part-time during a future “stability period”

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Sample Methodology

- For full 12 month measurement and stability periods for a calendar year health plan could use:
 - Measurement period 11/1/0001 to 10/31/0002 (12 months)
 - Administrative period 11/1/0002 to 12/31/0002 (2 months)
 - Stability period calendar year 0003 (12 months)
- Example:
 - During the measurement period employee F works an average of 32 hours/week and employee P works an average of 28 hours/week
 - Final calculations of average hours of F and P are made during the administrative period
 - During the following stability period employee F “deemed” to be a full-time employee and P “deemed” to be a part-time employee irrespective of the actual number of hours worked

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Special Transition Rule for 2013

- Measurement and stability periods must generally be the same length (ideally 12 months each)
- Transition rule: employers may use a “short” 2013 measurement period and still get a 12 month 2014 stability period if the measurement period:
 - Is at least 6 consecutive months long
 - Ends <90 days before 1/1/2014
 - Begins no later than July 1, 2013
- 13 possible full month measurement periods in 2013

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Prepare Final Full-Time Analysis

- After running the 13 iterations prepare a final analysis and report (with supporting payroll data)
- Keep report as proof of which 2014 employees are “deemed” to be full-time (and can subject the employer to penalties)
- Use report to rebut any IRS assertion of penalties with respect to any employees “deemed” to be part-time for 2014

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Step 5: Work With Benefits Advisor

- Identify cost of minimum qualifying coverage that needs to be offered to “deemed” full-time employees to avoid penalties
 - Many employers may offer both bare bones minimum qualifying coverage and traditional more comprehensive coverage
- To qualify for penalty avoidance offering must
 - provide **minimum essential coverage**
 - provide **minimum value**
 - be **affordable**

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Minimum Essential Coverage

- In the large group market the **minimum essential coverage (MEC)** requirement means simply offering a group health plan that provides medical care
- In the individual and small group market the products must cover **Essential Health Benefits (EHB)**, a much broader term encompassing 10 specific benefits

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Actuarial Value (Metal Levels)

- Employer's offering must provide at least a **60% minimum actuarial value**
- Actuarial value (AV) is a relative measure of a plan's "generosity"
 - A plan providing 60% AV would be expected to cover 60% of the cost of covered services of a standard population
 - Employee would cover cost of remaining 40% through co-pays and deductibles,
 - HHS and IRS provide AV calculators and safe harbors
- For comparison shopping 4 levels of AV:
 - Bronze 60% (the base level for employer mandate)
 - Silver 70% (the base level for Marketplace subsidies)
 - Gold 80%
 - Platinum 90%

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Who Must Be Offered Coverage?

- Full-time employees and their dependent children until age 26
- Transition relief for dependent coverage- no 2014 penalties for failure to offer dependent coverage
- No requirement to offer spouse coverage
- Offering must be communicated to full-time employees so they have an effective opportunity to participate
 - Recommendation: keep signed election forms or other acknowledgement from all full-time employees

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OOPS- 5% Margin of Error

- Statute requires offering coverage to ALL full-time employees
 - Missing 1 of 10,000 could = \$20M penalty
- 5% margin of error allowed by IRS regulations
- Employer not subject to penalty for a particular month if less than 5% of full-time employees are not offered coverage (or 5 employees if greater than 5%)
 - Could miss 500 of 10,000 but not 501
- Coverage failure does not have to be inadvertent
 - But probably best to not purposely exclude 5%
 - Save 5% in case of actual administrative error

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Affordability

- Statute: coverage is affordable if the employee's premium for self-only coverage is no more than 9.5% of the employee's **household** income
 - No practical way for an employer to know household income
- IRS temporarily allowing use of employee's W-2 Box 1 (gross wages subject to income tax) as = household income
- Box 1 is AFTER pre-tax 401(k) and cafeteria plan deductions
- Affordability is measured on **employee-only** coverage under the lowest cost 60% minimum value (Bronze) plan offered by the employer

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Affordability Safe Harbors

- 3 IRS safe harbors on affordability of the employees share of premium for employee-only coverage:
 - 9.5% of Box 1 wages
 - 9.5% of lowest hourly wage x 130 hours per month
 - 9.5% of Federal Poverty Level (FPL)
- Examples
 - Employee earns \$5,000/month (Box 1), employee-only coverage affordable at \$475/month employee share of premium
 - Employee paid \$9.00 per hour, coverage affordable at \$111.15/month ($\$9.00 \times 130 \times 9.5\%$)
 - Under current FPL of \$11,490 coverage affordable at \$90.96/month (probably about \$94/month by 2014)
 - Use as a design based safe harbor?

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Marketplace Subsidies

- Intent of health care reform:
 - Individuals and households under 133% FPL covered by Medicaid (Supreme Court overturned Federal coercion)
 - Individuals and households between 133% and 400% FPL receive government subsidized coverage from the Marketplace
 - Employer penalties would pay for the subsidies
- Marketplace subsidy sets employee's premium for Silver coverage at 2%- 9.5% of household income on inverse sliding scale
 - 100%-133% FPL household pays 2% of its income for a Silver plan, government pays the balance
 - 300%-400% FPL household pays 9.5% of its income for a Silver plan, government pays the balance

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Premium Tax Credit Table

- Percentage of household income contribution towards Silver (70%) coverage in health care Marketplace:

– Less than 133% FPL	2%
– From 133% to 150%	3% to 4%
– From 150% to 200%	4% to 6.3%
– From 200% to 250%	6.3 % to 8.05%
– From 250% to 300%	8.05% to 9.5%
– From 300% to 400%	9.5%
- Example of inverse linear sliding scale
 - 225% FPL is half way between 200%-250%
 - Household income contribution half way between 6.3% and 8.05% = 7.04%

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Premium Tax Credit

- Subsidy only available if no affordable employer coverage
- Above 400% FPL = no government subsidy
 - 70% of US households under 400% FPL
- Employers only penalized with respect to employees receiving Marketplace subsidies
- Employer penalty exposure = full-time employees with household income between 100% and 400% FPL

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2013 Federal Poverty Levels (FPL)

- One person household
 - FPL \$11,490
 - 133% FPL \$15,282
 - 400% FPL \$45,960
- Two person household
 - FPL \$15,510
 - 133% FPL \$20,628
 - 400% FPL \$62,040
- Four person household
 - FPL \$23,550
 - 133% FPL \$31,321
 - 400% FPL \$94,200

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Employer Penalties

- “Large” employer penalty exposure:
 - **Inadequate/Unaffordable \$3,000 annual penalty:** offer minimum essential coverage but less than 60% AV or unaffordable = \$250 monthly penalty for each full-time employee receiving subsidized coverage from the marketplace (the “tack-hammer penalty”)
 - **No coverage \$2,000 annual penalty:** offer no minimum essential coverage and one or more employees receive subsidy = \$166.67 monthly penalty X number of full-time employees in excess of 30 (penalized on employees with coverage from employer, Medicare, Medicaid, Tricare or going without coverage, the “sledgehammer penalty”)

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Employer Penalties

- Both penalties require at least one full-time employee receive subsidized coverage from the Marketplace
 - Subsidized coverage available between 100% and 400% of FPL
 - Under 100% FPL supposedly covered by Medicaid?
- Penalties only apply with respect to full-time employees (part-time employees **cannot** generate employer penalties)
- The Inadequate/Unaffordable penalty cannot exceed the No Coverage penalty
- Penalties calculated monthly, paid annually in arrears
- Penalties are non-deductible (as opposed to employer provided health insurance)

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“No Penalty” Examples

- Large employer complies with intent of statute
 - Offers “adequate” and “affordable” coverage to all full-time employees in 2014
 - Also offers coverage to dependent children in 2015
- Employer has <30 full-time employees but is “large” due to large part time workforce
 - No penalty since the “no coverage penalty” only applies to number of full-time employees in excess of 30

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“No Penalty” Examples

- Employer limits all hourly paid employees to <30 hours/week in 2013 but offers adequate and affordable coverage to full-time employees in 2014 (Commonwealth of Virginia example)
- Employer offers no coverage but limits all lower income employees (less than 400% FPL) to <30 hours/week in 2013 (no full-time employee can qualify for subsidized coverage in 2014)
- Employer’s offers no coverage but all full-time employees <400% FPL are covered by spouse, Tricare, Medicare or Medicaid or choose to remain uninsured (risky strategy)

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Inadequate/Unaffordable Penalty Example

- 100 full-time employees, employer offers adequate but unaffordable coverage
- 30 employees obtain coverage from spouse, Tricare, Medicare or Medicaid
- 30 employees >400 FPL buy coverage from employer
- 30 employees refuse to purchase any coverage (potentially subject to the individual mandate penalty)
- 10 employees under 400% FPL purchase subsidized coverage in the Marketplace
- **Inadequate/Unaffordable Penalty:**
 - \$3,000 x 10 employees receiving subsidies = **\$30,000**

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No Coverage Penalty Example

- Same facts as above except employer does not offer any coverage
- Since at least one employee received a subsidy penalty = $\$2,000 \times (100 \text{ full-time employees} - 30) = \mathbf{\$140,000}$
- Recommendation: large employers will generally be better off offering minimum essential coverage that is unaffordable or fails minimum value than dropping coverage altogether

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Penalty Limitation Example

- The Inadequate/Unaffordable penalty cannot be more than the No Coverage Penalty
- Employer has 80 half-time and 40 full-time employees
- Covered by mandate (40 full-time + 40 FTEs exceeds 50)
- Employer offers no coverage
- All 40 full-time employees are under 400% FPL and purchase subsidized coverage in the Marketplace
- Penalty lesser of :
 - $\$3,000 \times 40$ full-time employees receiving subsidies = \$120,000
 - $\$2,000 \times (40 \text{ total full-time employees} - 30) = \mathbf{\$20,000}$
- Recommendation: if not offering coverage limit number of full-time employees to 30 or less (make all other employees part-time)

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Tension between Employer Penalty and Marketplace Subsidies

- Marketplace subsidies unavailable if employee offered “affordable” self-only coverage through employer
 - Spouse and dependents also ineligible for subsidies if employer offers them coverage even with no employer contribution
- Offering spouse and dependent coverage in 2014 can be damaging to low income employees
 - If employee offered affordable employee-only coverage no employer penalty
 - But offering spouse and dependent coverage prevents the spouse and dependents from receiving subsidized marketplace coverage

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Tension between Employer Penalty and Marketplace Subsidies

- Example:
 - Employee age 33 earns \$34,575 as breadwinner for a family of 4 (150% FPL)
 - Silver family plan premium from Marketplace \$13,000
 - If employer doesn't offer affordable coverage
Marketplace premium = 4% of income = \$1,383 and subsidy = \$11,617
 - "Affordable" self-only employer coverage @ 9.5% = \$3,284, if employer also offers spouse/dependent coverage no Marketplace subsidies for any family members

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What happens above 400% FPL?

- Employee age 57 earns \$95,000 as breadwinner for a family of 4 (406% FPL)
- Unsubsidized premium \$25,000
- Government subsidy = \$-0- (earnings >400% FPL)
- Likely result: family will remain uninsured unless employer offers heavily subsidized coverage

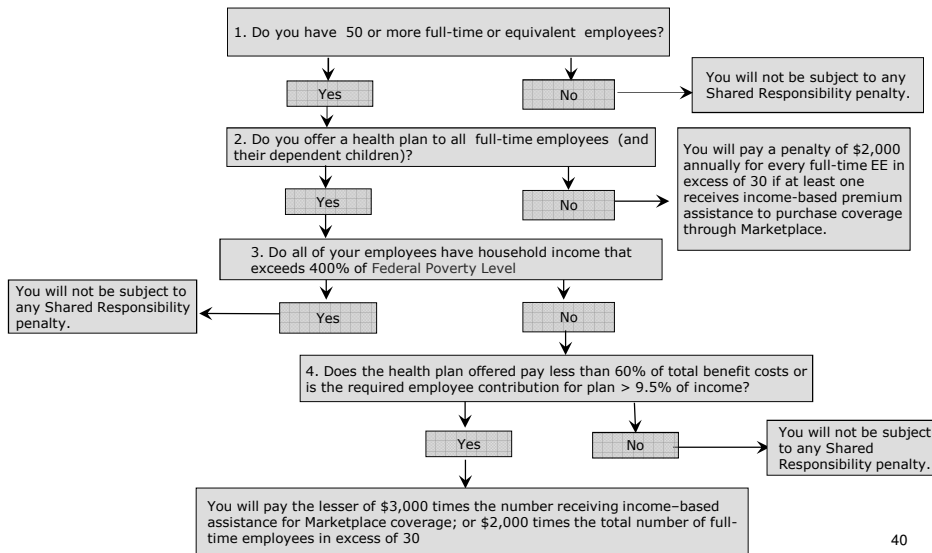
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Word of Caution in Strategizing for Penalty Mitigation

- ERISA Section 510- employers may not ...”discharge, fine, suspend, expel or discriminate against a participant or beneficiary...for the purpose of interfering with the attainment of any right to which such participant may become entitled under the plan...”
- ACA Section 1558- “No employer shall discharge or in any manner discriminate against any employee with respect to...compensation, terms, conditions or other privileges of employment because the employee...” has received a premium tax credit (subsidy) or is a whistleblower

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Flowchart on Employer Mandate



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Assessment and Collection Procedures

- **HHS** will notify employer when employee applies for subsidized marketplace coverage
 - employer will have opportunity to “contest” subsidy
- In January each year **employers** will file new reports with IRS that report (on monthly basis) employee full or part time status, whether offered adequate and affordable coverage, cost of coverage, etc.
- **Employees** report premium subsidies on their individual tax returns (beginning with 2014 returns due by 10/15/2015)

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Assessment and Collection Procedures

- IRS will match data from HHS, employer and employees (probably by November of following year) and send a proposed penalty assessment to employer
- Employer will have an opportunity to dispute/clarify the facts that led to the proposed assessment
- Ultimately IRS will bill the employer for the penalties (separate from other tax returns)
- Query: will GAAP require calculation/accrual of estimated penalties long before IRS assessment?

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Parallel Individual Mandate

- Separate from employer mandate to **offer** coverage, individuals will be penalized for not **purchasing** coverage
- Individual mandate penalty greater of flat dollar amount or specified percentage of income in excess of income tax filing threshold:
 - 2014 \$95 or 1% of excess
 - 2015 \$325 or 2% of excess
 - 2016 \$695 or 2.5% of excess
- Exceptions/exemptions from individual penalty:
 - lowest cost plan exceeds 8% of household adjusted gross income
 - gap in coverage for 3 months or less
- IRS prevented by statute from collecting individual penalty via tax liens and levies (only from refunds)

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Legal Issues & Planning

- Determination of related employers, common law employees and hours of service
- Exploration of opportunities to “break” a single employer or related entities apart to qualify for the small employer exemption (no later than July 1, 2013)
- Exploration of changes in employment practices (limit groups of employees to <30 hours/week) to minimize full-time population in 2014 (start no later than July 1, 2013)
- Consideration of employment law concerns over any strategies under consideration

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Questions?

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