

February 12, 2014

QUICK START OVERVIEW

FINAL Employer Shared Responsibility Provisions under the ACA

Treasury and the IRS released final regulations on the Employer Shared Responsibility provisions (a/k/a Employer Mandate, Play or Pay, or IRC Section 4980H) under the ACA on February 10, 2014. This Quick Start Overview is intended to provide a high level summary of the final guidance to help you hit the ground running in 2014 to determine when and how to prepare for ESR compliance during the next few months. The final rule contains new transition rules and interim guidance discussed below.

BACKGROUND ON EMPLOYER SHARED RESPONSIBILITY (ESR) / CODE SECTION 4980H

Employers meeting certain full-time employee thresholds will be subject to the Employer Shared Responsibility (ESR) provisions under section 4980H of the Internal Revenue Code (added by the Affordable Care Act, or ACA). Under these provisions, employers that do not offer affordable health coverage that provides a minimum level of coverage to their full-time employees may be subject to an ESR penalty/assessment if at least one of their full-time employees receives a premium tax credit for purchasing individual coverage in a public insurance Exchange/Marketplace.

ESR penalty/assessments were originally scheduled to take effect for applicable large employers in 2014, but were delayed until 2015 by guidance issued in July 2013. ESR provisions do not apply to employers (or a controlled group of employers) with less than 50 full-time employees (including equivalents).

TRANSITION RULE DELAYS ESR PENALTIES UNTIL 2016 FOR MID-SIZED FIRMS UNDER 100 FULL-TIME EMPLOYEES (INCLUDING EQUIVALENTS)

- Calendar Year plans: ESR penalties are delayed for all calendar months of 2015 for employers employing on average from 50 to 99 full-time employees (including equivalents) on business days in 2014.
- Non-Calendar Year Plans: ESR penalties are delayed for all calendar months of 2015 PLUS any calendar months in 2016 that fall within the 2015 plan year for employers employing on average from 50 to 99 full-time employees (including equivalents) on business days in 2014.

While this transition rule is welcome relief for mid-size employers, it is not automatic. There are four conditions of eligibility for this mid-size employer transition rule:

- Limited Workforce Size – As described above, employers must employ on average from 50 to 99 full-time employees (including equivalents) on business days in 2014. Size is determined in accordance with the otherwise applicable rules for determining status as an applicable large employer (ALE).
- Maintenance of Workforce and Aggregate Hours of Service – During the period between February 9, 2014, and December 31, 2014, the employer cannot reduce the size of its workforce or the overall hours of service of its employees in order to decrease its workforce below 100 full-time employees (including equivalents), other than for bona fide business reasons.
- Maintenance of Previously Offered Health Coverage – During the coverage maintenance period the employer must not eliminate or materially reduce the health coverage, if any, it offered as of February 9, 2014.
 - Must offer either (1) at least 95% of the dollar amount of the employer contribution in effect on 2/9/14 for employee only coverage, or (2) the same or higher percentage contribution toward cost of coverage in effect on 2/9/14;
 - Any change in benefit design for employee only coverage must meet minimum value;
 - Employer cannot alter the plan to narrow or reduce the class or classes of employees (or the employees' dependents) eligible for coverage on 2/9/14.

The “coverage maintenance period” means (1) for an employer with a calendar year plan, the period between February 9, 2014, and December 31, 2015, and (2) for an employer with a non-calendar year plan, the period beginning on February 9, 2014, and ending on the last day of the plan year that begins in 2015.

- Certification of Eligibility for Transition Relief -- The employer must certify on a prescribed form that it meets the eligibility conditions above.

TRANSITION RULE PERMITTING SHORTER PERIOD TO DETERMINE APPLICABLE LARGE EMPLOYER STATUS FOR 2015 -- APPLICABLE TO THE 50/100 FULL TIME EMPLOYEE THRESHOLD (INCLUDING EQUIVALENTS)

Under the ESR provisions, employers will determine each year, based on their current number of FTE employees, whether they will be considered an applicable large employer for the next year. The FTE calculation is used solely to determine the employer's size for purposes of the 50 or 100 full-time employee threshold and is not used to calculate any ESR penalty/assessment amounts.

- Employers will use information about the employees they employ during 2014 to determine whether they employ enough employees to be subject to the ESR provisions in 2015.
- Rather than being required to use the full twelve months of 2014 to measure whether it has 50+ or 100+ FTE employees, an employer may measure FTEs using any six-consecutive-month period in 2014.

2015 TRANSITION RULES FOR FIRMS NOT DELAYED TO 2016 – GENERALLY FIRMS OF 100 OR MORE FULL-TIME EMPLOYEES (INCLUDING EQUIVALENTS)

The ESR penalties/assessments will generally apply in 2015 to applicable large employers with 100 or more full-time employees (including equivalents) without any additional delay. (Such penalty/assessments could potentially also apply to a mid-sized firm that could not meet the four eligibility conditions for the delay to 2016. For purposes of this section, I will refer to all firms subject to ESR penalty/assessments in 2015 as large size firms).

The final ESR rules include transitional provisions that assist implementation of the ESR provisions in 2015 only. The preamble to the final rule clearly states that this transitional relief is NOT available for periods on or after January 1, 2016 (or, if applicable, for any period after the last day of the 2015 plan year).

These 2015 only transitional relief rules are:

- Relief for non-calendar year plans
- Shorter measurement periods for stability period starting during 2015
- Offer of coverage for January 2015
- Coverage for dependents
- Limited 70% substantial offer rule for 2015

Transition Relief (Until the 2015 Plan Year) for Employers Maintaining a Non-Calendar Year Plan as of December 27, 2012:

For employers that maintained non-calendar year plans as of December 27, 2012, the following transition guidance applies for the period prior to the first day of the non-calendar 2015 plan year; provided the plan year was not modified after December 27, 2012, to begin later in the calendar year.

Under the transition guidance below, no assessable ESR payment will be due for any month prior to the first day of the 2015 plan year for any full-time employees who (1) are offered affordable coverage that provides MV no later than the first day of the 2015 plan year, and (2) were not eligible for coverage under any group health plan maintained by the applicable large employer member as of February 9, 2014 that has a calendar year plan year. Note that this transition relief is not automatic – the employer must meet one of the two prongs below.

- Significant Percentage Transition Guidance (All Employees). -- The employer meets this prong if it (1) had, as of any date in the 12 months ending on February 9, 2014, at least one quarter of all of its employees covered under the non-calendar year plan, or (2) offered coverage under the plan to one third or more of all of its employees during the open enrollment period that ended most recently before February 9, 2014.

-- OR --

- Significant Percentage Transition Guidance (Full-Time Employees). -- The employer meets this prong if it (1) had, as of any date in the 12 months ending on February 9, 2014, at least one third of its full-time employees covered under the non-calendar year plan, or (2) offered coverage under the plan to one half or more of its full-time employees during the open enrollment period that ended most recently before February 9, 2014.

Shorter Measurement Periods For Stability Period Starting During 2015

Like the proposed regulations, the final regulations include an optional alternative method to determine full-time employee status referred to as the look-back measurement method.

For purposes of stability periods beginning in 2015, employers may adopt a transition measurement period that is shorter than 12 consecutive months but that is:

- no less than 6 consecutive months, and
- begins no later than July 1, 2014, and
- ends no earlier than 90 days before the first day of the plan year beginning on or after January 1, 2015 (90 days being the maximum permissible administrative period).

For example, an employer with a calendar year plan that must comply with the ESR provisions as of January 1, 2015 may use a transition measurement period from March 15, 2014, through October 14, 2014 (seven months), followed by an administrative period ending on December 31, 2014 for coverage to be effective January 1, 2015.

This transition guidance applies to a stability period beginning in 2015 through the end of that stability period (including any portion of the stability period falling in 2016), and applies to individuals who are employees as of the first day of the transition measurement period. For employees hired during or after the transition measurement period the general rules for new employees under the look-back measurement method apply.

Offer Of Coverage For January 2015

The final regulations provide, in general, that if an applicable large employer member fails to offer coverage to a full-time employee for any day of a calendar month, that employee is treated as having not been offered coverage during that entire month.

Since many employers offer coverage for a new year effective as of the first pay period beginning on or after the first day of the year, the final regulations provide the following transition rule solely for purposes of January 2015: if an applicable large employer member offers coverage to a full-time employee no later than the first day of the first payroll period that begins in January 2015, the employee will be treated as having been offered coverage for January 2015.

Coverage For Dependents

Under the final rule, the ESR provision that employers offer coverage to dependents of their full-time employees will not apply in 2015 to employers that are taking steps to arrange for such coverage to begin in 2016. The earlier proposed version of the ESR regulation had provided that the dependent coverage requirement would not apply in 2014 to employers that were taking steps to arrange for such

coverage to begin in 2015. This is essentially a one year extension of the dependent coverage requirement.

Dependents do not include spouses by ACA definition. In addition, the final rule excludes foster children and stepchildren from the dependent coverage requirement for ESR purposes.

Limited 70% Substantial Offer Rule For 2015 (Reverting Back to 95% for 2016)

For purposes of section 4980H(a) penalty assessment (a/k/a the \$2,000 or must offer penalty) under the ESR provisions, an applicable large employer member is treated as offering coverage to its full-time employees (and, to the extent required, their dependents) for a month if, for that month, it offers coverage to at least 95% (or that fails to offer to no more than 5%) of its full-time employees (and, to the extent required, their dependents).

The final ESR regulation provides transition relief for each calendar month during 2015, and any calendar months during a 2015 plan year that fall in 2016, that an applicable large employer member offers coverage to at least 70 percent (or that fails to offer to no more than 30 percent) of its full-time employees (and, to the extent required, their dependents). Such employers will not be subject to an assessable payment under section 4980H(a) during those months.

However, applicable large employer members qualifying for this transition relief continue to be subject to a potential assessable payment under section 4980H(b) (a/k/a the \$3,000 or unaffordability penalty) for full-time employees among the 30% not offered coverage who purchase individual market coverage in a public Exchange/Marketplace and receive a premium tax credit.

REMAINING TRANSITION GUIDANCE FROM 2014 STILL IN EFFECT

The preamble to the proposed ESR regulations provided transition relief that allowed flexibility for individuals to make changes in salary reduction elections for group health plans provided through section 125 cafeteria plans for non-calendar cafeteria plan years beginning in 2013.

This transition relief is still available to the extent there are non-calendar cafeteria plan years that began in 2013 still in effect. See the transition rule summary below.

However, the initial availability of qualified health plans on an Exchange/Marketplace was a one-time event at the beginning of 2014 only affecting

employee decisions during 2013 non-calendar plan years. Consequently, the final ESR rules do not extend this relief to non-calendar cafeteria plan years beginning in 2014.

Transition Relief for Salary Reduction Elections for Health Coverage under Cafeteria Plans with Fiscal Cafeteria Plan Years Beginning in 2013:

The availability of health plan coverage through an Exchange/Marketplace beginning in 2014 does not constitute a change in status under current cafeteria plan rules. Therefore, under the proposed regulation, employers are permitted to amend their written cafeteria plans to permit one or both of the following changes to salary reduction elections:

- An employee who elected to salary reduce through the cafeteria plan for health plan coverage with a non-calendar plan year beginning in 2013 may prospectively revoke or change his or her health plan election once, during that plan year, without regard to whether the employee experienced a change in status event.
- An employee who failed to make a salary reduction election through his or her employer's cafeteria plan for health plan coverage with a non-calendar plan year beginning in 2013 before the deadline for making elections for the cafeteria plan year beginning in 2013 is allowed to make a prospective salary reduction election for health plan coverage on or after the first day of the 2013 plan year of the cafeteria plan, without regard to whether the employee experienced a change in status event.

Note that employers are "permitted" to amend their non-calendar plan year 125 plans under the transitional rule but they are not required to amend them. The written section 125 plan document must be amended by 12/31/14 to reflect this transition relief and be effective retroactively to the first day of the 2013 plan year.

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This overview is not intended to be a comprehensive summary of the final regulation. Rather, it is intended to provide a high level summary of portions of the regulation that describe special transition rules for 2015 that affect employer implementation of the Employer Shared Responsibility requirement. The final regulation addresses other issues not summarized in this overview, which will be addressed in detail at a later date.

Please contact me if you have any questions.

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