Potential Employer Penalties Under the Patient Protection and Affordable Care Act (ACA)

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Summary

On Tuesday July 2, 2013, the Obama Administration posted a blog on employer requirements and the ACA. Based on the White House blog, the administration (1) plans to revamp employer reporting requirements, and therefore suspend employer reporting requirements for 2014, and (2) because employer payments are dependent on the reporting requirements, no payments will be collected in 2014. The Administration noted that these changes were in response to employers' concerns about the reporting requirement.

This report provides information on the statutory requirements and the proposed regulations issued to implement these statutory requirements in December 2012. This report does not yet reflect the proposed Administration changes. The report will be fully updated once additional information becomes available.

The White House blog posting is available at http://www.whitehouse.gov/blog/2013/07/02/we-re-listening-businesses-about-health-care-law.

The Patient Protection and Affordable Care Act (ACA, P.L. 111-148), as amended, increases access to health insurance coverage, expands federal private health insurance market requirements, and requires the creation of health insurance exchanges to provide individuals and small employers with access to insurance. To ensure that employers continue to provide some degree of coverage, the ACA includes a "shared responsibility" provision. This provision does not explicitly mandate that an employer offer employees health insurance; however, the ACA imposes penalties on "large" employers if at least one of their full-time employees obtains a premium credit through the newly established exchange. According to the Congressional Budget Office (CBO), employers are projected to pay $130 billion in penalty payments over a 10-year period.

The ACA sets out a two-part calculation for determining, first, which firms are subject to the penalty (e.g., definition of large), and, second, to which workers within a firm the penalty is applied. Because the treatment of part-time and seasonal workers differs across these two parts of the calculation, this has led to some confusion among policymakers and employers. For example, part-time employees are included in what is termed a full-time equivalent calculation to determine if an employer has at least 50 full-time equivalent employees (FTEs) and is thus considered large for purposes of applying the penalty. However, the actual penalty, if applicable, is levied only on full-time workers (those working at least 30 hours a week on average). This report discusses these definitions and the application to the employer penalty in greater detail.

The potential employer penalty applies to all common law employers, including an employer that is a government entity (such as federal, state, local, or Indian Tribal government entities) and an employer that is a nonprofit organization that is exempt from federal income taxes. If a franchise is owned by one individual or entity, employees in each of the franchises must be aggregated to determine the number of both full-time equivalent and full-time employees.

The actual amount of the penalty varies depending on whether an employer currently offers insurance coverage or not. In order for employers who do provide health insurance coverage to avoid paying a penalty, health insurance coverage that is both *affordable* and *adequate* must be offered to the employee. Coverage is considered affordable if the employee's required contribution to the plan does not exceed 9.5% of the employee's household income for the taxable

year. However, IRS has provided a safe harbor for employers to use the employee's W-2 income for this calculation (since most employers do not readily have information on an employee's household income). A health plan is considered to provide adequate coverage if the plan's actuarial value (i.e., the share of the total allowed costs that the plan is expected to cover) is at least 60%. This report provides greater detail on these requirements.

The total penalty for any applicable large employer is based on its number of full-time employees. The ACA specified that working 30 hours or more a week is considered full-time. However, the statute did not specify what time period (i.e., monthly or annually) employers would use to determine if a worker is full-time. To address this issue, the Secretary of Health and Human Services (HHS) and the Secretary of Labor have published proposed regulations to provide guidance for employers to use to determine which employees are considered full-time employees for purposes of administering the ACA employer penalty provision. The proposed regulations provide employers some flexibility to designate certain *measurement* or look-back periods (up to 12 months) during which they will calculate whether a worker is full-time or not. Once an employee is determined to be full-time, there will then be an *administrative* period to enroll employees in a health plan, if necessary. If an employer penalty is levied under the ACA requirements, it applies only for the time period following the administrative period, which is called the *stability* period. Employers are *not* penalized if an employee enters the exchange and receives a premium credit during the measurement period. In addition, because of this latest guidance, it is unlikely that employers will pay a penalty for seasonal workers who do not work at least 30 hours, on average over a pre-specified time period (up to 12-months). This report describes these proposed regulations in greater detail and provides examples of potential dates when employers will need to begin measuring full-time status for their on-going employees.

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Employer-sponsored health insurance is an important source of coverage for the nonelderly, covering about 58% of workers in 2011. Large firms were more likely to provide health insurance to their employees as compared to small firms. According to Kaiser Family Foundation, 99% of firms with 200 or more employees offered health insurance coverage to their workers, while 59% of firms with 3 to 199 employees offered health insurance coverage in 2011. Among very small firms (with 3 to 9 employees), 48% offered health insurance coverage.

The Patient Protection and Affordable Care Act (ACA, P.L. 111-148, as amended) was intended to expand insurance coverage in the U.S. To ensure that employers continue to provide some degree of coverage the ACA includes a "shared responsibility" provision.[1] The provision does not explicitly mandate that employers offer their employees acceptable health insurance. However, it does impose penalties on certain firms with at least 50 full-time *equivalent* employees, if one or more of their full-time employees obtain a premium tax credit through the newly established health insurance exchanges.[2] An individual may be eligible for a premium tax credit if his or her income is below certain thresholds and the individual's employer does not offer health coverage, or offers insurance that is "not affordable" or does not provide "minimum value," as defined by the ACA. The employer penalties are effective beginning in 2014.

This report describes the potential employer penalties, as well as proposed regulations to implement the ACA employer provisions. The regulations address insurance coverage requirements; methodologies for determining whether a worker is considered full time; provisions relating to seasonal workers and corporate franchises; and other reporting requirements.

Employer Penalty Calculation

The ACA sets out a two-part calculation for determining, first, which firms are subject to the penalty, and, second, to which workers within a firm the penalty is applied. Specifically, the ACA establishes a rule for determining whether an employer is considered "large" under the ACA definition and, therefore, potentially subject to a penalty. The actual amount of the penalty, if applicable, will depend on whether the employer currently provides health insurance coverage or not and if the coverage meets certain criteria with respect to adequacy and affordability. The penalty is only applicable to full-time workers. The following discusses this calculation in greater detail.

Employers Subject to the Potential Penalty

According to the ACA, only a large employer is subject to penalties regarding employer-sponsored health insurance. A "large employer" is defined in the ACA (as related to the employer penalty) as an employer who employed an average of at least 50 full-time *equivalent* employees (FTEs) on business days during the preceding calendar year.[3] As shown in **Table 1**, in order to

[1] Section 1513 of ACA enacted IRC Section 4980(H).

[2] For more information about exchanges under the ACA, see CRS Report R42663, *Health Insurance Exchanges Under the Patient Protection and Affordable Care Act (ACA)*, by Bernadette Fernandez and Annie L. Mach. For more information on premium credits in particular, see CRS Report R41137, *Health Insurance Premium Credits in the Patient Protection and Affordable Care Act (ACA)*, by Bernadette Fernandez and Thomas Gabe.

[3] Internal Revenue Code (IRC) §4980H(c)(2), as amended by §1513 and §10106 of the ACA, and as amended and renumbered by §1003 of P.L. 111-152. The statute uses the term *full-time employee* in the definition of large employer, (continued...)

determine whether an employer is a "large employer," both full-time and part-time employees are included in the calculation. "Full-time" is defined as having worked on average at least 30 hours per week.[4] However, full-time seasonal employees who work under 120 days during the year are excluded from this calculation.[5] Hours worked by part-time employees (i.e., those working less than 30 hours per week) are converted into FTEs and are included in the calculation used to determine whether a firm is a large employer. To do this, overall hours worked by part-time employees during a month are added up, and the total is divided by 120 and added to the number of full-time employees to get the number of FTE workers.[6]

For example, consider a firm with 35 full-time employees (30 or more hours). Assume the firm also has 20 part-time employees who all work 24 hours per week (96 hours per month). These part-time employees' hours would be treated as equivalent to 16 full-time employees for the month, based on the following calculation:

20 employees x 96 hours / 120 = 1920 / 120 = 16

Thus, in this example, the firm would be considered a "large employer," based on a total FTE count of 51—that is, 35 full-time employees plus 16 FTEs based on the number of part-time hours worked.

The ACA also specifies how an employer of multiple entities (such as a franchise owner with several restaurants) is treated with respect to the 50-FTE requirements. The ACA follows the Internal Revenue Service (IRS) aggregation rules governing *controlled groups*.[7] Specifically, if one individual or entity owns (or has a substantial ownership interest in) several franchises, all those franchises are essentially considered one entity. In this case, for purposes of the 50-FTE rule, the employees in each of the franchises must be aggregated to determine the number of FTEs.

This calculation only determines if an employer is considered "large" for purposes of potentially being subject to a penalty. The actual penalty is only applicable to full-time workers and is discussed in the next section.

(...continued)

but then expands on the definition of large employer to include both full- and part-time workers. For employers not in existence throughout the preceding calendar year, the determination of large employer is based on the average number of employees a firm reasonably expected to be employed on business days in the current calendar year. Any reference to an employer includes a reference to any predecessor of that employer.

[4] IRC §4980H(c)(4).

[5] IRC §4980H(c)(2)(B). In addition, an employer will not be considered a large employer if its number of full-time employees exceeded 50 for 120 days or less.

[6] Section 4980H(c)(2)(E) specifies that for purposes of determining FTEs, the aggregate number of hours of service of employees who are not full-time employees for the month is divided by 120 to get an FTE. However, for purposess of determining who is a full-time worker for the assessment of the actual penalty, proposed regulations released on December 28, 2012, would treat 130 hours of service in a calendar month as the monthly equivalent of 30 hours of service per week (52 x 30). Thus, a worker who worked 130 hours a month would be considered full-time for purposes of the penalty payment.

[7] The controlled group rule applies under §414 (b), (c), (m), or (o) of the IRC and includes employees of partnerships, proprietorships, etc., which are under common control by one owner or group of owners.

Table 1. Determination and Potential Application of Employer Penalty for Categories of Employees

Employee category	How is this category of employee used to determine "large employer"?	Once an employer is determined to be a "large employer," could the employer be subject to a penalty if this type of employee received a premium credit?
Full-time	Counted as one employee, based on a 30-hour or more work week	Yes
Part-time	Prorated (calculated by taking the hours worked by part-time employees in a month divided by 120)	No
Seasonal	Not counted, for those working up to 120 days in a year	Not likely under current "safe-harbor" options
Temporary Agency Employees	Generally counted as an employee of the temporary agency (except for those workers who are independent contractors)[a]	Yes, for those employed by the temporary agency and who are determined to be full-time, on average, for up to 12 months
Franchise Employees	For franchise owners, if they own more than one entity, all employees across the entities must be counted	Yes, for those counted as working for the franchise and who are full-time, on average, for up to 12 months

Source: CRS analysis of P.L. 111-148 and P.L. 111-152.

a. The controlled group rule applies under §414 (b), (c), (m), or (o) of the IRC and includes employees of partnerships, proprietorships, etc., which are under common control by one owner or group of owners.

Potential Tax Penalties on Large Employers

Regardless of whether or not a large employer offers coverage, it will be potentially liable for a penalty *only if* at least one of its full-time employees obtains coverage through an exchange and receives a premium tax credit. For purposes of determining the penalty, a "full-time employee" includes only those individuals working on average 30 hours or more per week. As shown in **Table 1**, part-time workers are *not* included in the penalty calculations (even though they are included in the determination of a "large employer"). An employer will *not* pay a penalty for any part-time worker, even if that part-time employee receives a premium credit. As discussed under implementation issues below, employers are not likely to pay a penalty for seasonal workers if they work less than 30 hours on average over a pre-specified time period (up to 12 months).

Penalty for Large Employers Not Offering Coverage

Individuals who are not offered employer-sponsored coverage and who are not eligible for Medicaid or other programs may be eligible for premium tax credits for coverage through an exchange. Eligible individuals will generally have income of at least 100% and up to 400% of the federal poverty level (FPL).[8]

[8] CRS Report R41137, *Health Insurance Premium Credits in the Patient Protection and Affordable Care Act (ACA)*, by Bernadette Fernandez and Thomas Gabe.

A large employer who does not offer coverage will be subject to a penalty if any of its full-time employees obtain coverage through an exchange and receive a premium tax credit. For 2014, the *monthly* penalty assessed to an employer who does not offer coverage will be equal to the number of its full-time employees minus 30 (the penalty waives the first 30 full-time employees) multiplied by one-twelfth of $2,000 for any applicable month (see **Figure 1**). After 2014, the penalty payment amount will be indexed by a premium adjustment percentage for each subsequent calendar year.[9]

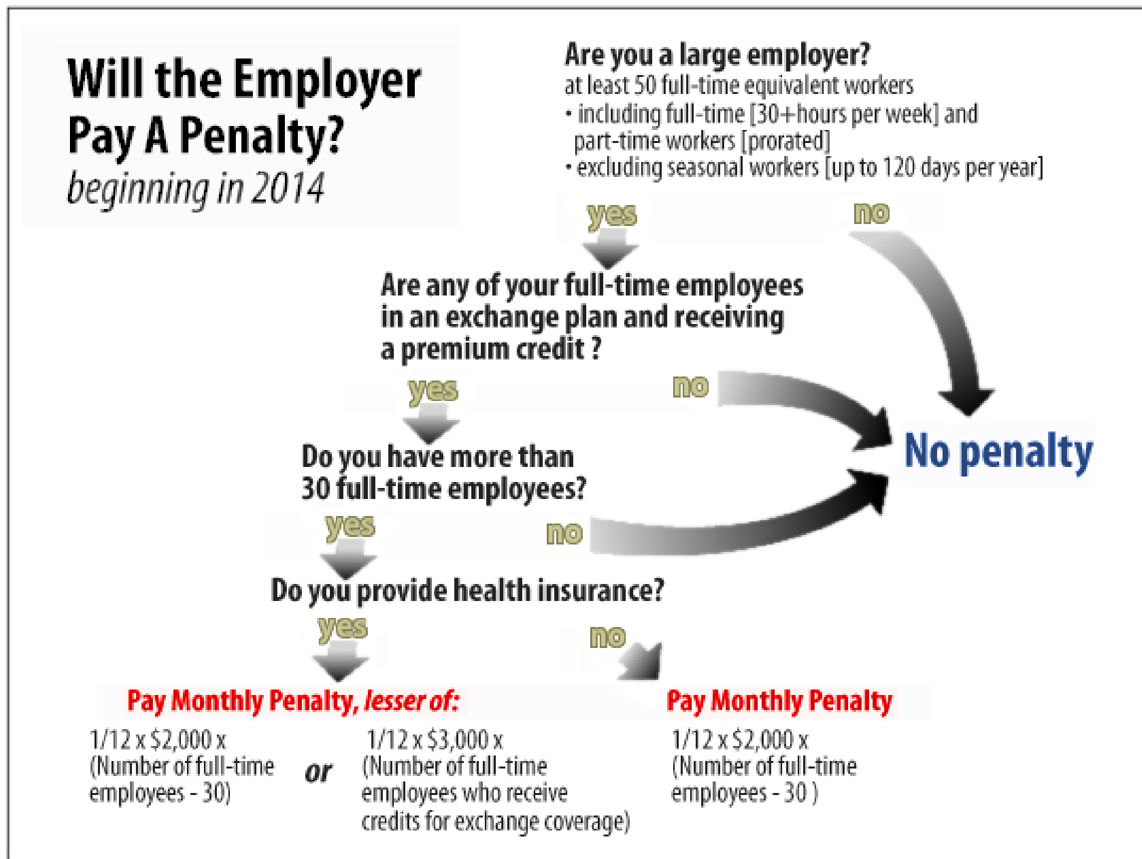
Penalty for Large Employers Offering Coverage

Individuals who are offered employer-sponsored coverage can only obtain premium credits for exchange coverage if, in addition to the criteria above, their employer's coverage fails to meet one of two criteria. The first criterion relates to affordability. The individual's required contribution toward the plan premium for self-only coverage cannot exceed 9.5% of his/her household income. The second criterion has to do with adequacy. The health plan must pay for at least 60%, on average, of covered health care expenses to be considered adequate. Employers who offer health insurance coverage that is inadequate or unaffordable will *not* be treated as meeting the employer requirements if at least one full-time employee declines their coverage and obtains a premium credit in an exchange plan.

If a penalty is assessed in 2014, the *monthly* penalty assessed to an employer for each full-time employee who receives a premium credit will be one-twelfth of $3,000 for any applicable month. However, the total penalty for an employer is limited to the *total* number of the firm's full-time employees minus 30, multiplied by one-twelfth of $2,000 for any applicable month. After 2014, the penalty amounts are indexed by a premium adjustment percentage for each subsequent calendar year (see **Figure 1**).

[9] Per IRC §4980H(c)(5) and ACA §1302(c)(4), the premium adjustment percentage is the national average premium growth rate.

Figure 1. Determining If an Employer Will Pay a Penalty



Source: CRS analysis of P.L. 111-148 and P.L. 111-152.

Note: These penalties are for 2014; penalties in future years will be adjusted.

Implementation Issues

While the ACA specifies certain rules about how the employer penalty is calculated and the amount of the penalty, the law directed the Secretary of Health and Human Services (HHS) and the Secretary of Labor to provide more detailed guidance to distinguish between an employer and an independent contractor, develop methodologies to determine which employees are considered full-time, and address other implementation issues. The discussion below is based on proposed regulations issued on December 28, 2012.[10]

Definition of Employer

The ACA definition of an employer is based on the common law standard which states that an employment relationship exists if an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In contrast, an independent contractor

[10] The proposed regulation can be found at http://www.irs.gov/pub/newsroom/reg-138006-12.pdf.

is an individual who controls what will be done and how it will be done and the contract dictates the desired result of the work. The IRS provides further guidance on the distinction between an employee versus independent contractor.[11] In this context, a temporary worker is not an employee of the firm he or she is "leased" to but rather an employee of the temporary agency.

The potential employer penalty applies to all common law employers, including an employer that is a government entity (such as federal, state, local or Indian Tribal government entities) and an employer that is a nonprofit organization that is exempt from federal income taxes.

As noted earlier, the ACA follows the controlled group IRS rule, in that an employer of multiple entities must aggregate employees across all entities to determine if the employer met the 50-FTE requirement. However, recent guidance from the IRS does not make a determination about whether the controlled group rule applies to government entities or churches, or a convention or association of churches. In the December 28, 2012 proposed regulation, IRS has said that until further guidance is issued, government entities, churches, and a convention or association of churches may rely on a reasonable good faith interpretation of the IRC controlled group rule.

Definition of Seasonal Workers

The definition of seasonal worker differs across the two-part calculation used to determine the ACA employer penalty. Specifically, the seasonal worker definition varies depending on whether it is used in the first part of the calculation, which determines whether an employer is considered large (i.e., the 50-FTE calculation), or the second part of the calculation, which determines how many employees are considered full-time for purposes of setting the dollar amount of the penalty.

For the first part of the calculation—determining whether a firm meets the ACA definition of an applicable large employer—if a seasonal employee works less than 120 days during a year, he or she is not included in the FTE calculation. In this instance, the definition of a seasonal worker is not limited to agricultural or retail workers.

For the second part of the calculation—determining how many employees are considered full-time for purposes of applying the penalty—the 120-day period is not used to determine whether someone is a seasonal worker. Instead, IRS Notice 2012-58 *Determining Full-time Employees for Purposes of Shared Responsibility for Employers Regarding Health Coverage*[12] provides that, at least in 2014, employers are permitted to use instead a reasonable, good faith interpretation of the term "seasonal employee." However, the notice further states that it is not a reasonable, good faith interpretation of the term "seasonal employee" to treat an employee of an educational organization, who works during the active portions of the academic year, as a seasonal employee. The Treasury and the IRS have indicated that final ACA regulations may tighten the definition of seasonal employee to include a specific time limit in the form of a defined period.

[11] See http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Independent-Contractor-(Self-Employed)-or-Employee%3F.

[12] See Internal Revenue Service Notice 2012-58, http://www.irs.gov/irb/2012-41_IRB/ar07.html.

Definition of Variable Hour Employees

The proposed regulations provide that a new employee is a variable hour employee if, based on the facts and circumstances at the start date, it cannot be determined that the employee is reasonably expected to be employed on average at least 30 hours per week. In some cases, variable hour employees may not work the necessary 30 hours on average over a specified time period (up to 12 months) to be considered full-time. However, a new employee who is expected to be employed initially at least 30 hours per week may be a variable hour employee, if, based on the facts and circumstances at the start date, the period of employment at more than 30 hours per week is reasonably expected to be of limited duration.

Methodology to Determine Full-Time Status

The total penalty for any applicable large employer is based on its number of full-time employees. The ACA specified that working 30 hours or more a week is considered full-time. However, the statute did not specify what time period (i.e., monthly or annually) employers would use to determine if a worker is full-time. The ACA directed the Secretary of HHS and the Secretary of Labor to provide regulatory guidance to employers to determine full-time status of their employees.[13]

IRS Notice 2012-58 describes safe harbor methods that an employer may use to determine which employees are considered full-time employees for purposes of administering the ACA employer penalty provision.[14] The safe harbor methods include a *measurement,* or *look-back,* period that allows an employer to measure how many hours an employee averaged per week during a defined period of not less than three and not more than 12 consecutive months. If an employee is determined to have worked full-time during the measurement period, an employer will then have the option of entering an *administrative period* during which the employee may be enrolled in a health plan. Following the administrative period, the employee would be treated as a full-time employee during a *stability period.* (The full-time classification would remain in place during the stability period so long as the worker remained an employee, regardless of how many hours he or she worked.) The IRS notice defines how the measurement, administrative, and stability periods are determined for three groups of workers (see **Table 2** and **Figure 2**):

- on-going employees;
- new employees: reasonably expected to work full-time;
- new employees: safe-harbor for variable hour and seasonal employees.

On-Going Employees

An on-going employee is generally an employee who has been employed for at least one complete standard measurement period. This is a defined period of not less three, but not more than 12 consecutive months. Under the safe-harbor method for on-going employees, an employer determines each on-going employee's status by looking back at the standard measurement period. According to the IRS, an employer has the flexibility to determine the months when the standard

[13] IRC Code Section 4980H(c)(4)(B).

[14] See Internal Revenue Service Notice 2012-58, http://www.irs.gov/irb/2012-41_IRB/ar07.html.

measurement period starts and ends, provided that the determination is made on a uniform and consistent basis for all employees in the same category. During this measurement period, the employer must first determine if the employee worked on average at least 30 hours per week per month.

If the employer determines that an employee averaged at least 30 hours per week, then the employer treats the employee as a full-time employee during a subsequent "stability period," regardless of the number of hours the employee works during the stability period, so long as he or she remains an employee.

Table 2. Time Frame for Determining Full-Time Status

	Measurement Period	Administrative Period	Stability Period
Definition	Measure (on average) whether employees are full time or not	Identify and enroll full-time employees	Period in which penalty may be due relative to employees found to be full-time during measurement period
On-going Employees	3 to 12 months[a]	Up to 90 days (may neither reduce nor lengthen the measurement or stability period - can overlap prior stability period)	At least 6 months but cannot be shorter in duration than measurement period
New employees hired as full-time	Not applicable	Up to 90 days to enroll	Not applicable
New variable hour and seasonal employees	3 to 12 months[b]	Up to 90 days (measurement period and administrative period cannot exceed 13 months)[c]	3 to 12 months but cannot be longer than measurement period

Source: CRS interpretation of IRS Notice 2012-58: Determining Full-time Employees for Purposes of Shared Responsibility for Employers Regarding Health Coverage.

a. For ongoing employees, this is referred to as the "standard" measurement period.

b. For new employees, this is referred to as the "initial" measurement period.

c. Technically, the initial measurement and administrative period cannot last beyond the final day of the first calendar month beginning on or after the one year anniversary of the employee (about 13 months).

A penalty, if applicable, is incurred only during the *stability period* which lasts at least six consecutive calendar months and is no shorter in duration than the standard measurement period designated by the employer. If an employer determines that an employee did not work full-time during the standard measurement period, the employer would not be required to treat the workers as full-time during the subsequent stability period. However, if an employee was full-time during the measurement period, then the employer could potentially pay a penalty during the stability period if all other criteria were met (e.g. full-time employees entered the exchange and received a premium tax credit, and any health insurance coverage offered was not adequate or affordable).

Employers may create different measurement and stability periods for different categories of employees. These periods can differ either in length or in their starting and ending dates for the following categories of on-going employees:

- collectively bargained and non-collectively bargained employees;
- salaried and hourly employees;
- employees of different entities (i.e., controlled groups); and
- employees located in different states.

The rules also provide an option to use an administrative period (between the measurement and stability periods) to determine which ongoing employees are eligible for coverage and to notify and enroll employees in health care plans. However, any administrative period between the standard measurement period and stability period may neither reduce nor lengthen the measurement period or stability period. The administrative period following the standard measurement period may last up to 90 days, and overlaps with the prior stability period to prevent any gaps in coverage.

New Employees Reasonably Expected to Work Full-Time

If an employee is reasonably expected at his or her start date to work full-time, an employer that offers group health plan will not face an ACA penalty if it covers new workers within three calendar months of their start date. This provision applies to new workers who are expected to work full-time.

Variable Hour and Seasonal Employees

The IRS guidance allows employers to use an initial measurement period of three to 12 consecutive months (as selected by the employer) to determine whether new variable hour employees or seasonal employees are full-time. The employer measures the hours of service completed by the new employee during the initial measurement period, and determines whether the employee completed an *average of 30 hours of service per week or more during this period*. If an employee is determined to be full-time during the initial measurement period, the employer would have up to three months to enroll him or her in a health insurance plan. However, the initial measurement period and administrative period cannot last beyond the final day of the first calendar month beginning on or after the worker's one year anniversary (about 13 months). For example, an employer takes 12 months to measure whether workers are full-time, the employer then has up to one month to enroll them in a plan. Similarly, if employers choose 10 months as the initial measurement period, they have three months to enroll them.

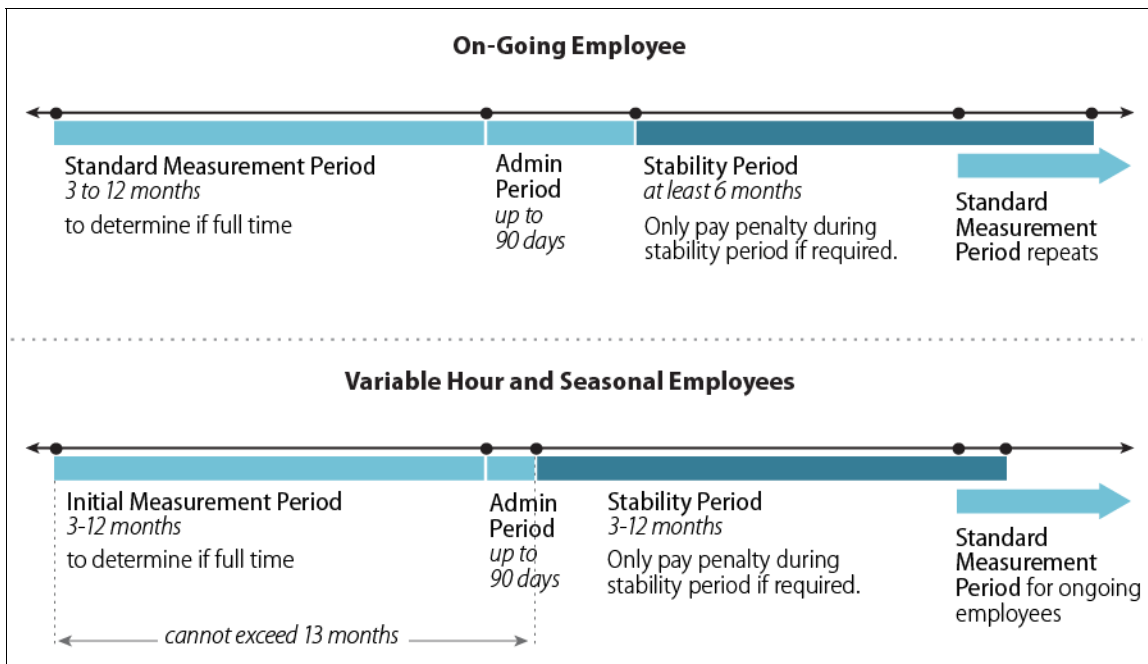
During this 13-month period, workers without coverage can enroll in the newly created health insurance exchanges and receive premium tax credits. Employers are not required to pay a penalty for this 13-month period. As noted above, the penalty period begins only after the administrative period if the employer does not provide adequate and affordable coverage and at least one of its employees enters an exchange and receives a premium credit.

The definition of full-time is based on the entire 12-month measurement period. So, if a variable-hour employee works full-time some weeks and part-time others, the total hours worked in the 12-month period, divided by the number of weeks as an employee works, would result in the average number of hours worked per week.

The following is an example from the December 28, 2012, proposed regulation[15] regarding how to account for the hours of seasonal employees. Employer D offers health plan coverage only to full-time employees (and their dependents). Employer D uses a 12-month initial measurement period for new variable hour employees and seasonal employees that begins on the start date and applies an administrative period from the end of the initial measurement period through the end of the first calendar month beginning after the end of the initial measurement period. Employer D hires Employee S, a ski instructor, on November 15, 2015, for an anticipated season during which Employee S will work through March 15, 2016. Employer D determines that Employee S is a seasonal employee based upon a reasonable good faith interpretation of that term. Employee S's initial measurement period runs from November 15, 2015, through November 14, 2016. Employee S is expected to have 50 hours of service per week from November 15, 2015, through March 15, 2016, but is not reasonably expected to average 30 hours of service per week for the 12-month initial measurement period.

Figure 2. Determining Full-Time Employees

Time periods under Proposed IRS Guidelines



Source: CRS based on IRS Notice 2012-58 Determining Full-time Employees for Purposes of Shared Responsibility for Employers Regarding Health Coverage.

Effective Dates for Employer Penalty

Under the ACA, the employer penalty is effective for months beginning after December 31, 2013. Thus, employers that intend to utilize the look-back measurement period for determining full-time status for ongoing employees for 2014 will need to begin their measurement period in 2013 to have a corresponding stability period for 2014. IRS and the Treasury recognize that employers who want to have a 12-month measurement period and a 12-month stability period may face

[15] The proposed regulation can be found at http://www.irs.gov/pub/newsroom/reg-138006-12.pdf.

constraints the first year, given that the regulation has not yet been finalized. Thus, IRS is offering a transitional measurement period that can be (for first year of implementation only) shorter than the stability period. IRS recognizes that these periods may differ depending on whether the employer's health plan or the firm's financial operations are based on a calendar or a fiscal year. Also, the guidance states that employers who use a full 12-month measurement period are not required to begin the measurement period before July 1, 2013 (see example in **Table 3** for employer with fiscal year starting on November 1, 2014). **Table 3** shows some examples IRS provides in its guidance of start and end dates for the measurement, administrative, and stability periods which meet requirements outlined in the proposed rule (dated December 28, 2012).

Table 3. Examples of Start and End Dates During Transition Period

To Determine Full-Time Status of On-Going Employees

Plan Year	Transitional Measurement Period	Administrative Period	Stability Period
Calendar Year	April 15, 2013 – Oct. 14, 2013[a]	Oct. 15, 2013 – Dec. 31, 2013	Jan. 1, 2014 – Dec. 31, 2014
Fiscal Year Starting On:			
April 1, 2014	July 1, 2013 – Dec. 31, 2013	Jan. 1, 2013 – March 31, 2014	April 1, 2014 – March 31, 2015
July 1, 2014[b]	June 15, 2013 – April 14, 2014	April 15, 2014 – June 30, 2014	July 1, 2014 – July 1, 2015
Nov. 1, 2014	September 1, 2013 – August 31, 2014	September 1, 2014 – Oct. 31, 2014	November 1, 2014 – November 1, 2015

Source: CRS analysis based on IRS Proposed Regulation posted on December 28, 2012.

a. During the transition period, an employer with a calendar year could have a later start date if they shorten the administrative period.

b. An employer with a fiscal year beginning on July 1, 2014 must use a measurement period that is longer than 6 months to comply with the required measurement period beginning by no later than July 1, 2013 and ending no earlier than 90 days before the stability period.

Coverage Requirements for Employers

To avoid a potential penalty, employers who do provide health insurance coverage must provide affordable and adequate coverage to employees and their dependents. The following defines affordable and adequate in greater detail.

Definition of Dependent Coverage

According to the proposed regulation, the term dependent means a child of an employee who has not attained age 26.[16] Absent knowledge to the contrary, applicable large employers may rely on an employee's representation about that employee's children and the ages of those children. Dependent does not include the spouse of an employee.

[16] For more information about dependent coverage under ACA, see CRS Report R41220, *Preexisting Condition Exclusion Provisions for Children and Dependent Coverage under the Patient Protection and Affordable Care Act (ACA)*, by Bernadette Fernandez.

Definition of "Affordable" Coverage

Under the ACA, coverage under an employer-sponsored plan is affordable to a particular employee if the employee's required contribution to the plan does not exceed 9.5% of the employee's household income for the taxable year.[17] Household income is defined as the modified adjusted gross income of the employee and any members of the employee's family (which would include any spouse and dependents) who are required to file an income tax return. Modified adjusted gross income is adjusted gross income plus certain foreign income and tax-exempt interest. A concern was raised that employers may not be able to determine household income of a worker in a cost-effective manner. To address this concern and provide employers a more workable option for determining the affordability of their health insurance coverage, Treasury and the IRS have proposed a safe harbor provision, whereby affordability of an employer's coverage would be measured by reference to an employee's wages from that employer. Wages for this purpose would be the total amount of wages as defined on a worker's W-2 Tax and Wage Statement.[18] According to the IRS, by allowing employers to base their affordability calculations on each employee's W-2 wages (which employers know) instead of each employee's household income (which employers generally do not know), the safe harbor could provide a more "workable and practical method" for measuring the affordability of an employer's coverage. In most instances, if employer-sponsored coverage were affordable based on the employee's W-2 wages, it would also be affordable based on the employee's household income because household income is equal to or greater than the employee's W-2 wages.

Under this safe harbor, employer coverage would be deemed affordable if the employee's portion of the self-only premium for the employer's lowest cost coverage that provides minimum value (see below for definition of minimum value) must not exceed 9.5% of the employee's W-2 wages. Although the determination of whether an employer met the safe-harbor provision would be made after the end of the calendar year, an employer could also use the safe harbor prospectively, at the beginning of the year, by structuring its plan and operations to set the employee contribution at a level so that the employee contribution for each employee would not exceed 9.5% of the employee's W-2 wages for that year. If an employee's contribution is more than 9.5% of his W-2 wage income, and he wanted to enter the exchange and receive a premium credit, the exchange would have to validate that his premium contribution also would have exceeded 9.5% of his household income.

In the rare case that an employee's household income is less than the employee's W-2 wages (e.g., because of adjustments to gross income for alimony paid or losses due to self-employment), the proposed safe harbor would address those situations by allowing the employer to rely on an employee's W-2 wages for analyzing the affordability of the employer's health coverage with respect to that employee. The safe harbor, however, would not affect an employee's eligibility for a premium credit which would continue to be based on the affordability of employer-sponsored coverage relative to an employee's household income.

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[17] See IRC Section 5000A(e)(1)(B) and Section 36B(c)(2)(C)(i).

[18] In either case the calculator would permit an employer-sponsored plan to enter information about the plan's benefits, coverage of services, and cost-sharing terms to determine whether the plan provides minimum value. See IRS Notice 2011-73, http://www.irs.gov/pub/irs-drop/n-11-73.pdf.

Definition of Adequate Coverage

Under the ACA, a plan is considered to provide adequate coverage (also called minimum value) if the plan's actuarial value (i.e., share of the total allowed costs that the plan is expected to cover) is at least 60%.[19] According to a preliminary analysis done by the Actuarial Research Corporation for CRS, the majority of employer-sponsored plans would meet the actuarial value requirements in the ACA.

On November 26, 2012, HHS issued final regulations on how to calculate actuarial value when determining the minimum value of a plan that allows employers to use one of three potential approaches for determining whether an employer plan provides minimum value.

- An actuarial value calculator (AV calculator) is available to employers from the Department of Health and Human Services (HHS).[20]
- An array of design-based safe harbors in the form of checklists that would provide a simple, straightforward way to ascertain that employer-sponsored plans provide minimum value (MV) without the need to perform any calculations or obtain the assistance of an actuary.
- For plans with nonstandard features that preclude the use of the AV calculator or the MV calculator without adjustments, an appropriate certification by a certified actuary.

The actuarial value calculation for determining minimum value includes the *employer* contributions to health savings accounts (HSAs) and health reimbursement accounts (HRAs) that are part of a high deductible health plan (HDHP).

Reporting and Other Requirements

The Department of Labor has delayed release of regulations requiring employers to provide employees written notice concerning (1) the existence of an exchange, including services and contact information; (2) the employee's potential eligibility for premium credits and cost-sharing subsidies if the employer plan's share of covered health care expenses is less than 60%; and (3) the employee's potential loss of any employer contribution if the employee purchases a plan through an exchange. According to a recent Frequently Asked Questions (FAQs), the Department of Labor expects the timing for distribution of notices will be the late summer or fall of 2013 which will be coordinated with the open enrollment period for Exchanges.[21]

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[19] Actuarial value is a summary measure of a plan's generosity, expressed as a percentage of medical expense estimated to be paid by the issuer for a standard population and set of allowed charges. In other words, actuarial value reflects the relative share of cost-sharing that may be imposed. On average, the higher the actuarial value of a plan, the lower the cost-sharing for the enrollee. Actuarial value does not consider the cost of premiums and the adequacy of provider networks, and plans with the same actuarial value do not necessarily include the same set of covered benefits.

[20] The data underlying the MV calculator are expected to be claims data reflecting typical self-insured employer plans. Further information on the AV methodology can be found at http://ccio.cms.gov//resources/files/Files2/0242012//Av-csr-bulletin.pdf. The AV calculator is available at http://cciio.cms.gov/resources/regulations/index.htm/#pm.

[21] See Frequently Asked Questions at http://www.dol.gov/ebsa/faqs/faq-aca11.html.

Beginning in 2014, large employers will have certain reporting requirements with respect to their full-time employees.[22] As prescribed by the Secretary of Labor, they will have to provide a return including the name, address, and employer identification number; a certification as to whether the employer offers its full-time employees (and dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan; the length of any waiting period; months coverage was available; monthly premiums for the lowest-cost option; the employer plan's share of covered health care expenses; the number of full-time employees; and the name, address, and tax identification number of each full-time employee. Additionally, an offering employer will have to provide information about the plan for which the employer pays the largest portion of the costs (and the amount for each enrollment category). The employer must also provide each full-time employee with a written statement showing contact information for the person required to make the above return, and the specific information included in the return for that individual. The Secretary is to work to provide coordination with other requirements, and an employer may enter into an agreement with a health insurance issuer to provide necessary returns and statements. IRS Notice 2012-33 invited comments on issues arising from these requirements, including on possible approaches for coordinating and minimizing duplication.[23]

Finally, those firms with more than 200 full-time employees that offer coverage must automatically enroll new full-time employees in a plan (and continue enrollment of current employees). Automatic enrollment programs will be required to include adequate notice and the opportunity for an employee to opt out.[24] According to Notice IRS 2012-17, in view of the need for coordinated guidance between the Department of Labor (DOL) and other agencies to implement the ACA, and the goal to provide employers sufficient time to comply, DOL has concluded that its automatic enrollment guidance will not be ready to take effect until 2014.[25]

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[22] ACA Section 1502.

[23] IRS Notice 2012-33 can be found at http://www.irs.gov/pub/irs-drop/n-12-33.pdf.

[24] ACA Section 1511.

[25] IRS Notice 2012-17 can be found at http://www.irs.gov/irb/2012-09_IRB/ar10.html.