TriBridgePartners LLC

UBA
Compliance Advisor

What every HR leader should know about compliance

The Play-or-Pay Penalty and Counting Employees under the ACA

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Introduction

Beginning in 2015, to comply with the Patient Protection and Affordable Care Act (ACA) "large" employers must offer their full-time employees health coverage, or pay one of two employer-shared responsibility/ play or pay penalties. An employer is considered "large" for 2015 if it has 100 or more full-time or full-time equivalent employees. Most employers with 50 to 99 full-time or full-time equivalent employees will not be required to offer coverage until 2016, as long as they largely continue their workforce size and the benefits, eligibility, and contribution levels they had in effect in February 2014. On February 12, 2014, the IRS published a final regulation that answers a number of questions about how an employer determines if it has enough employees to be considered large, and if it is large, what it must do to avoid penalties. The regulations also describe the penalty that is due if the employer does not offer coverage that complies with the rules. This Q&A is based on the final regulation. The IRS also has published a helpful Q and A. Although the U.S. Presidential election in 2016 and subsequent political movement has made the fate of the ACA uncertain, it has yet to be repealed and the employer shared responsibility provisions are still in effect.

Because employees work a variety of schedules, the rules are long, and in some situations, they are complicated. In many situations, employers will not need to go through a detailed analysis or adopt the more complex processes to meet their obligation under the ACA.

Section 1 – Which Workers Must Be Counted?

Q1: What types of workers need to be counted?

A1: An individual is counted under the ACA if he or she is a "common-law employee." Individuals who receive medical coverage during any month through the TRICARE program or through a health care program run by the Secretary of Veterans Affairs do not have to be counted during that month (but should still be offered coverage if they are eligible for coverage).

Q2: What is a "common-law employee"?

A2: A "common-law employee" is a person who receives detailed direction about how a task is to be performed from the recipient of his or her services. While it, unfortunately, is not always totally clear whether a worker is a common-law employee, if the company determines the worker's hours, provides the location where the work is done, provides the equipment needed to do the job, dictates how the work is done, expects the worker to work primarily or exclusively for the employer, asks the worker to perform a function that's key to the employer's business, and expects the relationship to continue indefinitely, the worker generally will be a common-law employee who must be counted. See Appendix A for additional information on how to decide if a person is a common-law employee of the employer.

Q3: Who is not a common-law employee?

A3: The regulations specifically say that independent contractors, sole proprietors, 2% subchapter S shareholders, partners in a partnership, some leased employees, most real estate agents, and most people who are "direct sellers" (those who sell consumer goods that will be used or resold in a home, rather than a retail setting, like a newspaper distributor or Pampered Chef distributor) are not common-law employees.

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Note: If, as a practical matter, a person functions as an employee, for purposes of the ACA (and several other laws) the person will be considered an employee by the government even if the parties try to describe the relationship as a non-employment relationship. This means that re-designating long-time employees as 1099 workers is unlikely to be successful, particularly if the workers continue to perform the same functions as they did when they were W-2 employees. The government has been cracking down on entities that misclassify employees as independent contractors. The ACA will provide another area of potential dispute. Employers that choose to consider individuals in unclear situations as non-employees should take care to document their reasoning and should consult with legal counsel since the penalties for misclassifying a worker can be significant.

Q4: Does an employer need to count leased employees?

A4: Leased employees who provide services to the employer under an agreement between the employer and a leasing organization may or may not be considered a common-law employee of the employer that is receiving the worker's services. A worker will not be considered a "common-law employee" simply because he is considered an employee for retirement plan purposes under Section 414(n) of the Internal Revenue Code. (An employee is a 414(n) leased employee if there is an agreement between the entity receiving the worker's services and the leasing organization, the individual performs services under the primary direction and control of the entity receiving the worker's services, and the individual works on a substantially full-time basis for the receiving entity for at least one year.)

Note: Professional employer organization (PEO) arrangements vary; employers who use PEOs or other leasing organizations should consult with experienced legal counsel.

If the employer controls how the worker does the job and spends his day, the employer likely is the common-law employer, even though the PEO hired the worker and issues the W-2.

In situations in which the employer receiving the worker's services is the common-law employer, an offer of coverage made by the PEO "on behalf of" the employer will be considered to be an offer of coverage by the employer. In order for an offer of coverage to be "on behalf of" the employer, the employer must pay a higher fee to the PEO for those employees who enroll in the PEO's plan. In other words, if the contract provides for a flat fee per employee placement regardless of whether the employee enrolls in the PEO's coverage, the employer will not be considered to have made an offer of coverage.

Even if the PEO offers coverage on behalf of the employer, the employer will be responsible for reporting on common-law employees if it is "large."

Employers with PEO arrangements may wish to provide within the PEO contract who is responsible for providing coverage.

Q5: Does an employer need to count temporary agency employees?

A5: An employer will need to count its temporary workers if the employer is their common-law employer. Unfortunately, because temporary employee arrangements vary so widely, there is not a black-and-white answer to this question. Ultimately, the more control the temporary agency keeps and the shorter the placement, the greater the likelihood the temporary agency is the common-law employer. Appendix B includes the factors that are considered when deciding if the agency or employer is the common-law employer; due to the importance of correctly classifying workers, employers with temporary employees may wish to consult with their attorneys.

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Temporary employees employed directly by the employer are common-law employees who will need to be counted.

Temporary workers may be eligible for treatment as variable-hours employees (see Q&A 97) if their hours are expected to fluctuate. Simply being a short-term employee does not make a worker variable hours or seasonal.

In situations in which the employer receiving the worker's services is the common-law employer, an offer of coverage made by the temporary staffing firm "on behalf of" the employer will be considered to be an offer of coverage by the employer. In order for an offer of coverage to be "on behalf of" the employer, the employer must pay a higher fee to the temporary staffing firm for those employees who enroll in the temporary staffing firm's plan. In other words, if the contract provides for a flat fee per employee placement regardless of whether the employee enrolls in the staffing company's coverage, the employer will not be considered to have made an offer of coverage.

Note: The IRS has said that if an employer attempts to avoid penalties by having the same worker work directly for the employer 20 hours per week and as an agency temporary employee for 20 hours a week, the worker will be considered a full-time common-law employee of the employer.

Q6: Does an employer need to count employees who work overseas?

A6: No. Only hours worked in the U.S. that are taxed as U.S. source income are counted, so employees are not counted while they are working overseas. (If an employee works part of the year in the U.S. and part of the year in another country, only hours worked within the U.S. need to be counted.)

Q7: Are foreign workers counted?

A7: Yes. All hours worked in the U.S. that generate U.S. source income for income tax purposes are counted. This means that hours worked in the U.S. by noncitizens (such as those here on most visas or who have a green card) are counted. The IRS has specifically said that workers holding H-2A and H-2B visas must be considered.

Q8. Are there special rules for students?

A8: Work-study hours (paid through a federal or other governmental program) do not need to be considered. All other hours for which the student is paid must be counted.

> ***Example:*** Kathy has a work-study job that requires her to work 10 hours per week. She also works in the cafeteria (in a non-work-study job) 15 hours per week. Only the 15 hours of cafeteria work are counted.

Note: The employer merely has to offer coverage to full-time employees. Because dependents may remain on their parent's plan until age 26, it is likely that many students would decline offered coverage.

Q9: Are there special rules for interns?

A9: There are no exemptions for interns. Hours worked in a paid internship must be considered (although in many cases the employer for which the student is interning, and not the educational institution, will be the "common-law employer" of the intern).

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Note: An employer does not have to offer coverage to individuals who work fewer than 90 days, so although summer interns who stay 90 days or less will need to be counted if the employer is the common-law employee, they will not need to be offered coverage.

Q10: Are union employees counted?

A10: Yes. An employer is responsible for its employees, even if they are covered by a union-sponsored health plan.

Q11: Are seasonal workers counted?

A11: In most cases, seasonal workers must be counted. In certain circumstances, they may be excluded (see Q&A 30).

Q12: Are retirees counted if they are covered by the employer's group health plans?

A12: Retirees are not "common-law employees," so they do not need to be counted.

Section 2 – What Hours Must Be Counted?

Q13: What hours must be counted?

A13: With a few exceptions, any hour for which an employee is paid must be counted. This means that in addition to pay for hours worked, vacation, holiday, sick time, layoff, jury duty, military duty, and any paid leave are counted. The exceptions are for:

- Hours worked by a student as part of a Federal Work-Study Program (or a similar state or local program)
- Hours which are considered income from sources outside the United States
- Hours performed as a "bona fide volunteer"
- An hour for which an employee is paid during which no duties are performed, if the payment is made to comply with workers' compensation, unemployment, or disability insurance laws.
- An hour of service for a payment, which reimburses an employee for medical or medically related expense incurred by the employee.

Q14: Must an employer count hours for which an employee is unpaid but receiving disability or workers' compensation?

A14: Periods during which an individual is not performing services but is receiving payments from short-term disability or long-term disability will result in hours of service, if the individual retains status as an employee, unless the payments are made from an arrangement to which the employer did not contribute directly or indirectly. Disability paid for by the employee with after-tax contributions would be an arrangement to which the employer did not contribute, and would not result in hours of service. Workers' compensation payments under state or local government programs are not hours of service.

Q15: Must an employer count hours of unpaid FMLA, USERRA, or jury duty?

A15: Unpaid FMLA, USERRA, and jury duty are not considered when determining if the employer is large enough for the play or pay requirements to apply. These periods also are not considered if the employer uses the monthly measurement method. These periods do count if the employer uses the look-back measurement method.

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Q16: Who is a "bona fide volunteer"?

A16: A bona fide volunteer is an employee of a governmental entity or an organization that is tax-exempt under Section 501(c) of the Internal Revenue Code if the employee's compensation from that organization is limited to:

- Reimbursement for, or a reasonable allowance for, expenses
- Reasonable benefits, including length of service awards, and nominal fees customarily paid by similar entities to their volunteers

Bona fide volunteers will include many volunteer firefighters and other emergency responders, as well as those who volunteer for non-profits.

Q17: How are the hours of hourly employees counted?

A17: For employees who are paid hourly, actual hours worked or paid must be used.

Q18: How are the hours of non-hourly employees counted?

A18: For employees who are not paid hourly, an employer may use any of these methods:

- Counting actual hours worked or for which vacation, holiday, etc. are paid
- Crediting an employee with eight hours' work for each day for which the person was paid for at least one hour of work, vacation, holiday, etc.
- Crediting an employee with 40 hours' work for each week for which the person was paid for at least one hour of work, vacation, holiday, etc.

Q19: Must an employer use the same method of counting hours for all non-hourly employees?

A19: No. An employer can use different methods for different classes, as long as the classes are reasonable and consistently applied. So, for example, an employer could use the eight hours method with Location A and the 40 hours method with Location B.

Additionally, employers under common control are not required to use the same method with respect to employees in the same classes.

Q20: May an employer change the method for counting hours of service of non-hourly employees?

A20: An employer can change the method every calendar year.

Q21: Are there limits on using these methods?

A21: Yes. An employer cannot use a method that would understate an employee's hours or the total hours worked by its workforce. For example, an employer could not use the eight hours method with an employee who works three 10-hour days per week to reduce him from a full-time/30-hour per week employee to a non-full-time employee.

Q22: Are there special rules for individuals paid commission only, adjunct professors, and pilots?

A22: The IRS is continuing to consider specific rules for employees with schedules that are particularly difficult to count. In the meantime, the employer is expected to use a reasonable method of counting hours that considers all time related to performance of the function.

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The IRS has provided an optional safe harbor for adjunct faculty. Under the safe harbor, the faculty member is credited with 2.25 hours for each hour of classroom time plus one hour for each hour outside the classroom the faculty member is required to spend for non-classroom duties such as office hours or departmental meetings.

There is not a safe harbor for commissioned employees, although the regulations say that to be reasonable, time spent on a salesperson's travel or completing paperwork cannot be ignored. Presumably, use of the eight- or 40-hour method will be simplest with commissioned employees. The regulations include factors to consider when calculating hours for airline personnel.

Q23: Are there special rules for substitute teachers?

A23: There are no special rules for substitute teachers. A short-term substitute may qualify as a temporary employee, depending on how the arrangement is set up. A long-term substitute, for example a sub for a maternity leave, will likely be a common-law employee of the school.

Q24: How is an employee who transfers between employers in a controlled or affiliated service group handled?

A24: If an employee works for multiple employers in a controlled or affiliated services group, all hours of service for any employer in the group are added together. The employer for whom the employee worked the most hours during the month is responsible for the employee for that month.

Q25: How is on-call or waiting pay handled?

A25: The regulations do not provide specific guidance, but they require the employer to take a reasonable approach, which includes crediting an hour of service for any on-call hour for which:

- Payment is made or due (presumably even at a discounted rate),
- The employee must remain on the employer's premises, or
- The employee's activities are substantially restricted so that the employee is effectively unable to use the time for his own purposes.

Section 3 – Determining If the Employer Is Large Enough for Penalties to Be an Issue

The ACA provides that an employer that has a certain number of full-time employees or full-time employee equivalents must provide health coverage or pay one of two penalties. Under the ACA, an employer is a "large employer" for a calendar year if it employed an average of at least 50 full-time or full-time equivalent employees during the prior calendar year. However, for 2015 many employers with between 50 and 99 employees will have a one-year exemption from the requirement – these mid-sized employers will need to offer acceptable coverage in 2016 or pay penalties. See Q&A 116 for the requirements an employer with 50 to 99 employees must meet to be able to wait until 2016.

Important: Employers must count an employee's actual hours each calendar month during a calendar year to determine if the employer is a "large employer" – the look-back measurement and stability periods may not be used when determining if the employer is "large."

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Q26: When determining if an employer is "large," who is a "full-time employee"?

A26: A "full-time" employee is a common-law employee (see Q&A 2) who worked an average of 30 or more hours per week during a calendar month. Any employee who averaged 30 or more hours per week (130 hours in a calendar month) is considered one full-time employee. Actual hours worked are not considered for this calculation.

Q27: Who is a "full-time equivalent" employee?

A27: Part-time employees (those who average less than 30 hours per week) count on a pro-rata basis and their hours are combined to create "full-time employee equivalents." This is done by adding up the hours of all less than full-time (30 hours) employees for a calendar month and dividing the total by 120. All hours worked by the full-time equivalent employee are considered for this calculation, including any overtime.

> ***Example:*** In July, Bill worked 96 hours, Jane worked 82 hours, and Sam worked 103 hours. Their combined hours (281) divided by 120 = 2.34 full-time equivalent employees for July.

Q28: What happens if there are companies that are commonly owned by another company or a group of people (part of a controlled or affiliated service group)?

A28: All employees of the employers in a controlled group or an affiliated service group are combined when deciding if the employer has 50 (or 100 in 2015) or more full-time employees or equivalents. Basically, if an employer is part of a family of companies, all of the companies may need to be added together to see if the employer is a large employer. The controlled group rules apply to private, church, and government plans. Employers can be part of a controlled group even if they have separate federal employer identification numbers. The controlled group rules that are used under the ACA are very similar to the rules that apply to 401(k) plans, so if the employer sponsors a 401(k) plan, any entities in the controlled group have probably been identified.

> ***Example:*** Ann owns the Clean Car Wash, which has 22 full-time employees, and Diaper Day Care, which has 30 full-time employees. Both Clean Car Wash and Diaper Day Care are considered large, because 22 + 30 = 52.

> ***Caution:*** Determining whether an employer is part of a controlled group can be complicated and small details can be very important. It is highly recommended that an attorney or accountant familiar with the entity's entire setup make this determination. If an employer incorrectly determines that it is not "large" because it omitted an entity that should have been included, the employer may have to pay significant penalties.

Q29: If an employer knows it is a large employer, does it need to know exactly how many full-time and full-time equivalent employees it has?

A29: The reporting rules will generally require an employer to report the total number of employees and the number of full-time employees for each month. The first reports will be due in early 2016, based on 2015 data.

Q30: How does an employer determine if it is a large employer?

A30: The basic rule is that an employer's status as "large" (or not) is based on its average number of employees over the prior calendar year (even if the employer has a non-calendar year plan). The employer must add the total number of full-time and full-time equivalent employees for each calendar month, add each month's total together, and divide by 12. If there is a fractional number of full-time equivalent

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employees for a month, the fraction is kept (to the nearest hundredth). If there is a fraction after the total calendar year average is determined, the fraction is dropped (i.e., the employer rounds down).

An employee who averages 30 or more hours per week (130 hours per month) counts as one full-time employee for the month. Employees who average fewer than 30 hours per week for a calendar month have their hours combined to determine the number of full-time equivalent employees. See Appendix C for an example.

If the result is 50 or more (in 2015, due to transition relief, there were some exceptions for employers between 50 and 100 that met transition relief requirements), the employer is a "large employer" and subject to the penalty for the next year, except that if the employer only exceeds the 50 full-time/full-time equivalent threshold for less than four calendar months or 120 days (which do not need to be consecutive) during the year **and** seasonal workers caused it to exceed the 50 (or 100) employee threshold, the seasonal workers can be disregarded when deciding if the employer is large.

Q31: Were there special rules for 2015?

A31: Yes. When deciding if the employer is "large" for 2015 (which involves counting employees during 2014), employers may, but are not required, to use the special rule.

Under this rule, the employer may count full-time and full-time equivalent employees over any six (or more) consecutive months in 2014, instead of counting employees for the entire 2014 calendar year. There is no requirement that the six (or more) month period be representative of the employer's work-force. The six-month rule may not be used if the employer wants to apply the seasonal workers rule.

An employer with 50 to 99 employees that cannot meet the requirements to qualify for the delay (see Q&A 116 for details) will have to pay penalties for 2015 unless it offers affordable, minimum value coverage to the required number of employees.

Q32: Who are seasonal workers?

A32: For purposes of the large-employer test, "seasonal workers" means retail employees who work only during holiday seasons and others who perform work that, by its nature, is only performed at certain times of the year (such as harvesting or tax season). Seasonal workers need to be counted unless the limited exception described in Q&A 30 applies.

Q33: What happens if an employer grows during the year?

A33: Large-employer status is on a calendar-year basis, based on the average number of employees during the prior calendar year. If an existing employer that was below the 50 (or 100) employee threshold grows during a calendar year, it will not have to offer coverage until the next calendar year.

In addition, if an employer first becomes "large," it will have until April 1 following the year in which it becomes large to offer coverage. This special rule is only available once, even if the employer moves back and forth between large and small status.

Q34: What happens if an employer shrinks during the year?

A34: Large-employer status is on a calendar-year basis, based on the average number of employees during the prior calendar year. If an existing employer falls below 50 (or 100) employees during a calendar year, it will have to offer coverage until the next calendar year to avoid penalties (but see Section 4 regarding the "free-employees" rule).

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Q35: What happens if a new company is created?

A35: If an employer is in business for no part of the prior calendar year, the employer will need to determine if it is likely to average enough full-time/full-time equivalent employees during the year to be considered “large.” If the employer expects to average 50 or more employees during the year (100 or more employees in 2016), and reaches that number, the new employer will need to offer coverage during its startup year or penalties will apply.

If the employer exists for any part of the calendar year, employee hours are averaged over the time the employer was in business.

Q36: What if a company is purchased or merged?

A36: The IRS is considering specific rules for this situation, but in the meantime, the successor employer will be responsible for the prior company's obligations. There also are no rules set for a merger late in the year between two entities that are each small. Presumably, until specific rules are issued, the employers should average the combined head count over the calendar year.

Q37: Does this requirement apply to government employers and non-profits?

A37: Yes. This requirement applies to all types of employers – private businesses, governments (including cities, counties, public schools, and Indian tribes), and non-profits.

Q38: How does this calculation work for non-calendar year plans?

A38: Determining whether an employer is “large” is a calendar-year calculation, regardless of the employer’s plan year or renewal date.

Q39: What if the employer determines it averages fewer than 100 employees in 2014 (assuming the employer is eligible for the temporary exemption)?

A39: The employer will not need to be concerned about the employer-shared responsibility penalties for 2015. (It will need to determine employees’ average hours, including any employed by employers in its controlled or affiliated services group, each calendar year going forward.)

Note: If an employer that is not “large” voluntarily offers coverage, the coverage does not have to be affordable or provide minimum value, and the employer can require that employees work more than 30 hours per week to be eligible. However, other ACA requirements will apply to the small group plan, such as the 90-day waiting period and prohibitions on pre-existing condition limitations and dollar limits on essential health benefits.

Q40: Are employees of small employers eligible for the premium tax credit/subsidy?

A40: Employees of small employers are eligible for the premium tax credit/subsidy only if the employer does not offer affordable (self-only), minimum value coverage. They are not eligible for the premium tax credit/subsidy if they are eligible for affordable, minimum value coverage through their employer (even if they do not elect the employer coverage and even though the small employer is not required to offer coverage).

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Section 4 – Applying the Requirement to Offer Coverage ("A" or "No Offer" Penalty)

Under the ACA, a large employer must offer minimum essential coverage to most of its full-time employees (and dependents) or pay a $2,000 per year ($166.67 per month), indexed, penalty on all of its full-time employees, if even one employee receives a premium tax credit (which some people call the premium subsidy). When applying this penalty, some employees may be excluded (the "free-employees" rule). The details of this requirement are being phased in over 2015 and 2016.

In 2015, a large employer (usually, this means the employer averaged 100 or more full-time or full-time equivalent employees during 2014) was required to offer minimum essential coverage to at least 70% of its full-time employees or pay a $2,000 per year ($166.67 per month), indexed, penalty on all of its full-time employees, if even one employee receives a premium tax credit. When applying this penalty, if the employer has 100 or more full-time or full-time equivalent employees 80 employees may be excluded.

Beginning in 2016, four key changes will take effect:

- An employer will be considered "large" if it has **50** or more full-time or full-time equivalent employees during the prior calendar year.
- An employer must offer minimum essential coverage to at least **95%** of its full-time employees to avoid the $2,000 (indexed) penalty.
- An employer must offer minimum essential coverage to the natural and adopted dependent children of those full-time employees to avoid the $2,000 (indexed) penalty.
- When applying the penalty, the number of employees that may be disregarded under the "free-employees rule" will be reduced to **30**.

Q41: What does it mean that the penalty is indexed?

A41: The penalties are "indexed" to reflect changes in the average health insurance premium. However, for purposes of this Q&A, the un-indexed figures are used.

The indexed amounts for the $2,000 penalty, based on calendar years, are:

2015: $2,080
2016: $2,160
2017: $2,260
2018: $2,320
2019: $2,500
2020: $2,570
2021: $2,700

The indexed amounts for the $3,000 penalty, based on calendar years, are:

2015: $3,120
2016: $3,240
2017: $3,390
2018: $3,480
2019: $3,750
2020: $3,860
2021: $4,060

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Q42: Does a large employer need to offer coverage to employees who aren't full-time (30 or more hours per week)?

A42: No. An employer does not have to offer coverage to employees who are not considered full-time. (It must include part-time employees when deciding if the employer is a large employer, but for no other purpose.)

Q43: Which full-time employees must be offered minimum essential coverage to avoid the "A" penalty?

A43: "Most" employees who average 30 or more hours per week during a month must be offered coverage, or a penalty will apply. For 2015, "most" means 70% of the employer's full-time employees. For 2016 and later, "most" means 95% of the employer's full-time employees. When deciding if an employee is full-time (30 or more hours per week) for this requirement, the employee's hours may be counted using the monthly method or the look-back method. These methods are explained in Section 6 and Section 7.

Q44: If an employer is part of a controlled group, is the percentage of full-time employees offered coverage measured on a group or entity basis?

A44: If an employer is part of a controlled group, each separate entity must meet the 70% (95% for 2016 and later) offer threshold.

> ***Example:*** ABC Corp. is part of a controlled group. The total controlled group has 300 full-time employees and 260 are offered minimum essential coverage. ABC Corp. has 50 full-time employees and 20 (40%) are offered coverage in 2015. ABC will owe the $2,000 penalty on each of its 50 full-time employees, less its share of the 80 "free" employees.

Q45: Are there limits on which employees may be excluded?

A45: No. During 2015, a large employer may exclude 30% of its full-time employees. During 2016 and later years, a large employer may exclude 5% of full-time employees. It does not matter whether the exclusion is deliberate or inadvertent.

Note: Because there can be differences of opinion as to whether a particular worker is a common-law employee, and record keeping sometimes is inaccurate, employers may wish to reserve some or all of the excludable percentage as a margin for error.

Q46: If an employer is very small, how is the excludable percentage applied?

A46: There are no clear rules on rounding yet.

Beginning in 2016, when the 5% exclusion applies, an employer may exclude five employees if that is more than 5% of its workforce. There is no similar minimum number for 2015.

Q47: What happens to the excluded employees?

A47: The excluded employees may enroll in the health insurance Marketplace (which is sometimes called the exchange). If they receive a premium tax credit/subsidy, the $3,000 per year ($250 per month) penalty explained in Section 5 will apply to each excluded employee who receives a premium tax credit.

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Q48: What happens if the employer offers coverage to some, but not the required percentage, of its employees (for example, to 60% of them)?

A48: If coverage is offered to fewer than the required percentage of full-time employees (70% in 2015 and 95% in 2016 and later years), the $2,000 per employee per year penalty will apply on all employees (except the "free employees") – including those who are offered coverage.

> ***Example:*** Abacus Company has 350 employees and has a calendar year plan. 300 of the employees are full-time (work 30 or more hours per week). In 2015, Abacus offers coverage to 160 (53%) of the full-time employees. Abacus will owe a penalty of $440,000 [$2,000 x (300 – 80)] because it has offered coverage to less than 70% of its full-time employees. It may exclude 80 of the ineligible employees when calculating the penalty. The penalty is due on all of the full-time employees, even the 160 who are offered coverage. No penalty is due on the 50 part-time employees.
>
> In 2016, Abacus offers coverage to 240 (80%) of its 300 full-time employees. Abacus will owe a penalty of $540,000 [$2,000 x (300 – 30)] because it has offered coverage to less than 95% of its full-time employees. It may exclude 30 of the ineligible employees when calculating the penalty. The penalty is due on all of the full-time employees, even the 240 who are offered coverage. No penalty is due on the 50 part-time employees.

Q49: What if an employer can't satisfy minimum participation requirements?

A49: The IRS says in the final regulations that because the guaranteed issue rules apply in the large group market, minimum participation requirements should not be a problem. In the small group market, minimum participation must be waived during small group open enrollment (from November 15 through December 15 each year).

Note: The regulations issued by the U.S. Department of Health and Human Services (HHS) on guaranteed issue were not entirely clear, and some carriers have been imposing minimum participation requirements. This IRS statement should give employers leverage in the fully insured market. Stop-loss carriers are not covered by the ACA, so self-funded plans may continue to have issues with some reinsurers.

Q50: What dependents must be offered coverage?

A50: Minimum essential coverage must be offered to the full-time employee's dependent children until the end of the month in which they reach age 26. Much of the usual IRS definition of "child" applies, which means that natural and adopted children are included, and employers cannot impose other requirements, such as financial dependence or that the child lives with the employee.

Applicable dependent children includes only the following children meeting the Code Section 152(f)(1) definition:

- Sons and daughters
- Stepchildren
- Adopted children
- Foster children

Financial dependence, living arrangements, and marital status of the child are irrelevant for purposes of determining if a child is a dependent that must be offered coverage. Dependents under age 26 cannot be excluded from coverage even if they have access to their own employer coverage.

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In addition, employers that did not cover some or all dependent children in 2013 and 2014 do not need to cover all dependent children until 2016. Employers are not required to contribute toward dependent child coverage.

Q51: Must coverage be offered to spouses?

A51: No. An employer only needs to offer coverage to dependent children. (It is not unusual for the IRS to define “dependents” to include children, but not spouses – look, for example, at your federal income tax return, which separates spouse from dependents.)

Q52: What is minimum essential coverage?

A52: Minimum essential employer-sponsored coverage includes an insured or self-funded church, governmental, or ERISA welfare benefit plan that provides medical care directly or through insurance or reimbursement. (An HMO is considered an insured plan.)

Generally, any medical policy offered in the small- or large-group market that meets these requirements will be minimum essential coverage. IRS regulations state that these types of limited coverage will ***not*** qualify as minimum essential employer-sponsored coverage:

- Accident only
- Disability income
- Liability, including general, automobile, and supplemental liability
- Workers’ compensation
- Automobile medical payment
- Credit only
- On-site medical clinics
- Limited scope (“standalone”) dental or vision
- Long-term care, nursing home care, home health care, community-based care or any combination of these
- Specified diseases or illnesses
- Hospital indemnity or other fixed indemnity insurance
- Medicare supplement

It appears that a policy that simply covers preventive care will provide enough coverage of medical care to be considered “minimum essential coverage.” A health reimbursement arrangement (HRA) is considered “minimum essential coverage.”

Q53: Are there special rules for multiemployer plans?

A53: The IRS has requested comments on how best to handle multiemployer plans. In the meantime, if the employer is required to make a contribution to a multiemployer plan with respect to some or all of its employees under a collective bargaining agreement or related participation agreement and the multiemployer plan offers affordable, minimum value coverage to eligible employees and dependents, the employer will meet the offer of coverage test. The IRS has said it will give at least six months’ notice of any change.

Q54: When is coverage considered offered?

A54: Coverage is "offered" for a month if it is available for the entire month. (A partial month’s coverage will count if the employee's coverage is terminating or if a new employee’s coverage does not begin until

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the first of the following month.) Coverage will be considered offered if the employee has failed to pay the premium after being provided with a 30-day grace period to make the payment. The employee must have an effective opportunity at least once a year to accept or decline the offered coverage. However, this requirement will automatically be met if coverage is offered that meets minimum value and is either offered at no cost to the employee or at an employee cost for single coverage of no more than 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.78% in 2020, and 9.83% in 2021) of the federal poverty line (FPL) for a single individual, divided by 12. It appears that a simple notice of the right to add or drop coverage will meet this requirement. Elections for coverage that automatically renew unless the employee makes an affirmative change also are considered acceptable annual offers.

Q55: What kind of proof that coverage was offered is needed?

A55: There is no particular method required to provide proof that coverage was offered, but employers will want to implement procedures so that they can demonstrate that coverage was offered to an employee if verification is requested.

Q56: How is the penalty calculated?

A56: The penalty is calculated each month at the rate of $166.67 (indexed) for each full-time employee, less the "free-employees." (Although the penalty is calculated monthly, it will be paid annually. See Section 8 for details.)

> ***Example:*** Dave's Donuts does not offer medical coverage to its employees. Dave has 60 full-time employees and 12 part-time employees. In 2016, two employees purchase coverage through a Marketplace. Dave will owe a penalty of $5,000.10/month [(60 full-time employees minus 30 excludable employees; the part-time employees are not counted for purposes of the penalty) x $166.67].

Q57: What happens if the employer is part of a controlled or affiliated service group?

A57: If some employers in the group offer minimum essential coverage to the required percent of their full-time employees and others do not, only those employers who do not offer coverage must pay the $2,000 penalty **on their own employees**.

Also, the employers that are part of a controlled or affiliated service group share the "free employees" pro rata. If one employer doesn't need the free employees because it offers minimum essential coverage, its share of the "free employees" may **not** be shared. If dividing the free employees creates percentages, each employer may round up to a whole employee, so that the group may actually have more than the stated number of free employees.

> ***Example 1:*** In 2015, Black Co. and Green Bros. are in a controlled group. Black has 70 full-time employees and 12 full-time equivalent employees and offers minimum essential coverage to its full-time employees. Green has 48 full-time employees and no full-time equivalent employees and doesn't offer coverage. The controlled group has a total of 130 full-time/full-time equivalent employees and 118 full-time employees.
>
> In 2015, the law allows Black and Green to subtract as many as 80 full-time employees from the total; however, the 80 is shared pro rata by the controlled group companies. So:

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Black has 59% of the full-time employees in the controlled group (70/118 = 0.59). Black then has 48 “free” employees (80 x 59% = 47.46, rounded up to 48).

Green has 41% of the full-time employees (48/118 = 0.41). Green then has 33 “free” employees (80 x 41% = 32.54, rounded up to 33).

The penalty for Green for 2015 will be $30,000 (48 - 33 = 15 employees x $2,000). Black will not owe a penalty for 2015.

Example 2: In 2016, Newton Co. and Overton, Inc. are in in controlled group. Newton has 22 full-time employees and 12 full-time equivalent employees. Overton has 18 full-time employees. The controlled group has a total of 52 full-time/full-time equivalent employees and 40 full-time employees. Neither Newton nor Overton offers minimum essential coverage.

In 2016, the law allows Newton and Overton to subtract 30 from the total; however, the 30 is shared pro rata by the controlled group companies. So:

Newton has 55% of the group’s full-time employees (22/40 = 0.55). Newton has 17 “free” employees (30 x 55% = 16.5, rounded up to 17).

Overton has 45% of the group’s full-time employees (18/40 = 0.40). Overton has 14 “free” employees (30 x 45% = 13.5, rounded up to 14).

The penalty for Newton will be $10,000 per year (22 - 17 = 5 employees x $2,000) and for Overton it will be $8,000 (18 - 14 = 4 employees x $2,000).

Q58: What happens if an employer doesn’t offer coverage to its full-time employees, but no one gets a subsidy?

A58: If no employee receives a premium tax credit/subsidy, no penalty will apply. As the subsidy is available to employees who earn as much as 400% of the federal poverty line (FPL) (for 2021, 400% of FPL is $51,520 for a single person or $106,000 for a family of four in all states but Alaska and Hawaii), this is unlikely.

Section 5 – Applying the Requirement to Offer Affordable, Minimum Value Coverage (“B” or “Inadequate Coverage” Penalty)

An employer that offers minimum essential coverage to substantially all of its full-time employees may still owe penalties if the coverage it offers is inadequate because it is not “affordable” and/or it does not provide “minimum value.” It also may owe penalties on the employees it does not offer coverage to who receive a premium subsidy.

Q59: What is "affordable" coverage?

A59: Coverage is considered affordable if it costs less than 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) of the employee's household income. Because employers rarely know an employee's household income, employers may meet the affordability requirement through one of three safe harbor options – the W-2 safe harbor, the rate of pay safe harbor, and the federal poverty line safe harbor.

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The IRS has determined that opt-out arrangements increase an employee's contribution for health coverage beyond the amount of the salary reduction.

The IRS announced that it intends to propose regulations that will treat an unconditional opt-out arrangement (an arrangement providing for a payment conditioned solely on an employee declining coverage under an employer's health plan and not on an employee satisfying any other meaningful requirement) in the same manner as a salary reduction for purposes of determining an employee's required contribution relating to affordability.

Federal agencies also anticipate that mandatory inclusion in the employee's required contribution of amounts offered or provided under an unconditional opt-out arrangement that is adopted after December 16, 2015, (a "non-relief-eligible opt-out arrangement") will apply for periods after December 16, 2015. Employers who have had opt-out arrangements in place prior to December 16, 2015, will not be required to increase the amount of an employee's contribution for reporting purposes on the 1095-C but individual taxpayers may rely on opt-out payments as increasing their cost for purposes of tax credit eligibility.

Q60: What is the W-2 safe harbor?

A60: Under the W-2 safe harbor, coverage is affordable if the employee's contribution for self-only coverage is less than 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) of his W-2 (Box 1) income for the current year. That means the determination is made after the calendar year ends (although an employer can test against the prior year's W-2 to get a sense of whether the employee's contribution is acceptable). Employers that choose to use this method may not change the employee's contribution level (dollar amount or percentage) during the calendar year (or during the plan year if the plan operates on a non-calendar year). Employers that use this method may not make discretionary contributions (for example, an employer may not make an extra contribution at year-end to make the employee's share low enough that it becomes affordable).

Note: Box 1 income excludes deferrals to 401(k), 403(b), and Section 125 plans.

> ***Example:*** Matt is employed by Acme from January 1, 2015, through December 31, 2015. Matt's total earnings for 2015 are $26,000 and his Box 1 W-2 earnings are $24,000. Matt's share of his premium cost is $200 per month, or $2,400 per year. Matt's premium is unaffordable since $2,400 is more than 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.78% in 2020, and 9.83% in 2021), of Matt's W-2/Box 1 earnings for the year.

Q61: Does the W-2 safe harbor adjust for partial-year employees?

A61: Yes. If the employee is only offered coverage for part of a year, an adjustment to W-2 income is made by multiplying the IRS Form W-2 wages by a fraction equal to the number of calendar months for which coverage was offered over the number of calendar months in the employee's period of employment during the calendar year. (If coverage is offered for at least one day during the calendar month, or the employee is employed for at least one day during the calendar month, the entire calendar month is counted in determining the applicable fraction.)

> ***Example:*** Carol begins employment with Employer X on May 15, 2015. X offers Carol and her dependents minimum value coverage during the period from August 1, 2015, through December 31, 2015. The employee contribution for self-only coverage is $100 per calendar month, or $500 for Carol's period of coverage. For 2015, Carol's IRS Form W-2 wages are $15,000. Carol's W-2

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wages are multiplied by 5/8 (five calendar months of coverage offered over eight months of employment during the calendar year). Affordability is determined by comparing the adjusted Form W-2 wages ($9,375, or $15,000 x 5/8) to the employee contribution for the period for which coverage was offered ($500). Because $500 is less than 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) of $9,375 (Carol's adjusted Form W-2 wages for 2015), Carol's coverage is affordable ($500 is 5.33% of $9,375).

Q62: Does the W-2 safe harbor adjust for unpaid leaves?

A62: The regulations do not make any adjustment for unpaid leaves (which increases the chance the employee's coverage will be unaffordable).

Q63: What is the rate of pay safe harbor?

A63: Under the rate of pay safe harbor, coverage is affordable for an hourly employee if the hourly employee's contribution for self-only coverage is less than 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) of his rate of pay at the start of the coverage period, or if less, 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) of the employee's lowest rate of pay during the calendar month, times an assumed 130 hours worked during a month (regardless how many hours the employee actually works). For salaried employees, the monthly salary at the beginning of the coverage period is used. If the salaried employee's monthly salary is reduced during the year (even if due to a reduction in hours) the rate of pay method may not be used. If the salaried employee is paid other than monthly, the employer may use any reasonable method to convert a payroll period to monthly salary.

If an employee works one day in a month, he or she is considered to have worked the entire month for purposes of both the employee's share of the premium and assumed income for the calendar month.

Note: This method excludes tips and overtime and disregards any pay increase the employee may receive during the year. It does not require an adjustment if the employee takes unpaid leave.

> ***Example:*** Duluth Corp. uses the rate of pay method. Emily is salaried and earns $60,000 per year ($5,000 per month). The least expensive minimum value plan offered by Duluth costs the employee $115 per month. Coverage is affordable for Emily since $115 is 2.3% of $5,000.
>
> Ed is hourly. He earns $10 per hour from January through June and $11 per hour from July through October and $9 per hour for November and December. Ed's coverage is affordable for January through October [$10 x 130 = $1,300; 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) x 1,300 = $123.50], but not November and December [$9 x 130 = $1,170; 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) x 1,170 = $111.15]. If Ed gets a premium subsidy for November and December, Duluth will owe a penalty of $250 for each of those two months.

Q64: What is the federal poverty line safe harbor?

A64: Under the federal poverty line (FPL) safe harbor, coverage is affordable if the employee's contribution for self-only coverage is less than 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% 2019, 9.78% in 2020, and 9.83% in 2021) of FPL as of the start of the plan year for the state in

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which the employee lives. For 2021, the FPL for a single person in the 48 contiguous states and Washington, D.C., is $12,880, so the maximum employee contribution for self-only coverage would be $105.51 per month. (FPL for a single person in 2021 in Alaska is $16,090, and in Hawaii it is $14,820.)

Because FPL figures are released near the end of January, an employer may, but is not required to, use the FPL in effect within the six months before the start of the plan year.

The FPL method does not look at the employer's actual hours or pay. It does not need to be adjusted for leaves of absence.

> ***Example:*** Frank is employed by Sea County for all of 2021. Sea County uses the FPL method and sets the employee premium for self-only coverage for its least expensive minimum value plan at $90 per month, below 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) of FPL (which is $105.51 for 2021). Frank works full-time from January through December 10, but is laid off from December 11 to 31. Coverage is considered affordable for Frank, even for December, because Frank's actual hours and pay do not matter with this method.

Q65: Which safe harbor method should be used?

A65: Each safe harbor method has pluses and minuses. The W-2 method allows the most flexibility, but is done after the end of the year, which limits the employer's ability to predict and make any needed adjustments. Use of Box 1 income may cause significant understatement of income for employees who make large pre-tax contributions to group or retirement plans. Adjusting is not allowed for unpaid leaves, which may cause coverage to become "unaffordable."

The rate of pay safe harbor understates most hourly employees' income since it only assumes 130 hours per month of work. It also excludes overtime and pay increases. As a practical matter it cannot be used for employees with very low base wages, like some who receive tips or commissions. It cannot be used if a salaried employee's wage drops. However, it is a design-based method, which reduces the need to track employees separately.

The FPL method does not look at employees' pay at all. The amount is low, but it would be simple to apply and may be attractive to employers who have employees with compensation that varies widely from month to month.

Q66: May an employer use different safe harbor methods with different groups of employees?

A66: Yes. The employer may use any reasonable classification method. Reasonable classes include (but are not limited to) hourly or salary, geographic location, and job category.

Q67: May an employer require employee contributions based on a percentage of wages (to a cap)?

A67: The IRS has specifically said in the regulations that this method is acceptable. Employers should not forget that other laws, like the Age Discrimination in Employment Act, may impact this design.

Q68: Is the employer required to consider its contribution level for spouse and child coverage when determining affordability?

A68: No. Only the cost of self-only (single) coverage matters, even if the employee has family coverage.

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Q69: May an employer use wellness incentives when determining affordability?

A69: When calculating affordability of employer coverage when incentives or penalties are offered through a wellness program, employers must assume each employee fails to satisfy the requirements of the wellness program, unless it is a non-discriminatory wellness program related to tobacco use. For nondiscriminatory tobacco use incentives, the affordability calculation can assume all employees earn the incentive or are not charged the penalty.

Q70: May an employer use HRA contributions or flex credits when determining affordability?

A70: When determining whether coverage is affordable, an employer may apply health reimbursement arrangement (HRA) contributions for the current year to reduce the employee's premium if those contributions may be used by employees to pay premiums (or for either premiums or cost-sharing).

An employer's flex contributions to a cafeteria plan can reduce the amount of the employee portion of the premium so long as the employee may not opt to receive the amount as a taxable benefit, the flex credit may be used to pay for the MEC, and the employee may use the amount only to pay for medical care.

If the flex contribution can be used to pay for non-health care benefits (such as dependent care), it could not be used to reduce the amount of the employee premium for affordability purposes. Furthermore, if an employee is provided with a flex contribution that may be used for health expenses, but may be used for non-health benefits, and is designed so an employee who elects the employer health plan must forego any of the flex plan's non-health benefits, those flex benefits may not be used to reduce the employee's premium for affordability purposes.

For plan years beginning before January 1, 2017, and for benefits adopted prior to December 16, 2015, an employer flex contribution that is not a health flex contribution because it may be used for non-health benefits but that may be used by the employee toward the amount the employee is otherwise required to pay for the health coverage, will be treated as reducing the amount of an employee's required contribution.

Furthermore, only for coverage for plan years beginning before January 1, 2017, an employer may reduce the amount of the employee's required contribution by the amount of a non-health flex contribution (other than a flex contribution made under a non-relief-eligible flex contribution arrangement) for purposes of information reporting on Line 15 of Form 1095-C. However, because treating a non-health flex contribution as reducing an employee's required contribution may affect the employee's eligibility for the premium tax credit, the IRS encourages employers not to reduce the amount of the employee's required contribution by the amount of a non-health flex contribution for purposes of information reporting. After reports have been submitted, if the employer is contacted by the IRS concerning a potential penalty relating to the employee's receipt of a premium tax credit, the employer will have an opportunity to respond and show that it is entitled to the relief described in the Notice, to the extent that the employee would not have been eligible for the premium tax credit if the required employee contribution had been reduced by the amount of the non-health flex contribution or to the extent that the employer would have qualified for an affordability safe harbor if the required employee contribution had been reduced by the amount of the non-health flex contribution.

An employer's non-health flex contribution will not be used to reduce the employee's premium for purposes of determining their eligibility for a tax credit.

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Q71: May an employer use HSA contributions when determining affordability?

A71: When determining whether coverage is affordable, an employer's contributions to a health savings account (HSA) may not be used to reduce the premium because HSA contributions may not be used by employees to pay their premiums.

Q72: What is "minimum value" coverage?

A72: Coverage is "minimum value" if the coverage is expected to pay at least 60% of covered claims costs. It must provide substantial coverage for inpatient hospital and physicians' services.

Fully insured plans provided to small groups must provide coverage at bronze level, or better. Bronze level is an actuarial value of approximately 60%, and those plans are automatically considered to provide minimum value.

The government has provided a calculator and several safe harbor plan designs to assist large insured plans and self-funded plans with their minimum value determinations.

Q73: May an employer use wellness incentives when determining minimum value?

A73: The employer may use non-smoking incentives when determining minimum value if non-smoking incentives are used to reduce cost-sharing (deductibles, coinsurance, copays, or the out-of-pocket maximum). If non-smoking incentives are available to reduce cost-sharing, essentially the employer may assume that all employees qualify for the non-smoker incentive. All other wellness incentives must be disregarded.

Q74: May an employer use HRA contributions when determining minimum value?

A74: When determining minimum value, an employer may apply HRA contributions for the current year if those contributions may only be used by employees for cost-sharing. (Cost-sharing generally means deductibles, coinsurance, or copays.)

Q75: May an employer use HSA contributions when determining minimum value?

A75: When determining whether coverage is affordable, an employer's contributions to an HSA may be considered as a first-dollar benefit.

Q76: What is the penalty for not offering affordable, minimum value coverage?

A76: The penalty is $250 per month ($3,000 per year, indexed) for each full-time employee who:

- Is not offered coverage that is both minimum value and affordable coverage, and
- Purchases coverage through a government Marketplace, and
- Is eligible for a premium tax credit/subsidy (so his household income must be below 400% of federal poverty line).

Example: Jones, Inc. has 55 full-time employees and eight part-time employees. Jones offers coverage that is minimum value for all employees, but which is not affordable for 10 of the full-time employees (nine of whom buy coverage through the Marketplace) and all of the part-time employees (all eight buy through the Marketplace). Seven of the nine full-time employees and six of the eight part-time employees who buy through the Marketplace qualify for a premium tax credit.

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Jones owes a penalty on each full-time employee who enrolls in a Marketplace plan and receives a premium tax credit, so Jones owes $21,000 ($250 per month for each of the seven full-time employees who receive a premium credit; the part-time employees are not counted).

Note that the first 30 (or 80) employees **do** count under this "inadequate coverage" penalty. Also, if the "no offer" penalty would be less expensive than the "inadequate coverage" penalty, the employer would pay the "no offer" penalty.

Q77: Does the employer owe a penalty if the employee declines affordable, minimum value coverage offered by the employer and buys coverage through the Marketplace instead?

A77: No. The employer simply has to **offer** affordable, minimum value coverage. (Specifically, the least expensive plan that provides minimum value coverage must be affordable based on the cost of self-only coverage.) If the employee chooses to obtain coverage through the Marketplace, he or she can, but the employee will not be eligible for a premium tax credit/subsidy and therefore the employer will not owe a penalty.

Q78: Does the employer owe a penalty if the employer offers minimum essential coverage that is not affordable and minimum value coverage to an employee who would be eligible for a premium tax credit/subsidy, but the employee chooses to enroll in the employer's plan?

A78: No. If the employee chooses to obtain coverage through his or her employer instead of through the Marketplace, the employee can, but he or she will usually not be eligible for a premium tax credit/subsidy and therefore the employer will not owe a penalty.

Q79: Is it possible for an employee to qualify for a premium tax credit/subsidy even though his or her employer offers affordable coverage?

A79: Yes. If the cost of self-only coverage through the Marketplace is more than 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) of an employee's actual household income, an employee could be eligible for the subsidy even though the coverage offered by his or her employer is affordable under one of the three safe harbors. This will be a fairly unusual occurrence but could happen because certain deductions are allowed when determining household income.

Q80: Must all plan options provide affordable, minimum value coverage?

A80: No. Only the lowest cost option that provides minimum value coverage needs to be affordable to avoid the penalty. An employer is free to offer other options that do not meet affordability.

Q81: Are there special rules for multiemployer plans?

A81: Yes. If the employer is required to make a contribution to a multiemployer plan with respect to some or all of its employees under a collective bargaining agreement or related participation agreement and the multiemployer plan offers affordable, minimum value coverage to eligible employees, the employer will be considered to have offered affordable, minimum value coverage. In addition to the three affordability safe harbors, coverage under a multiemployer plan is considered affordable if the employee's contribution toward self-only coverage does not exceed 9.5% (indexed to 9.56% in 2015, 9.66% in 2016, 9.69% in 2017, 9.56% in 2018, 9.86% in 2019, 9.78% in 2020, and 9.83% in 2021) of the wages reported to the multiemployer plan, based on either actual wages or an hourly wage rate under the bargaining agreement.

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Section 6 – Determining Which Full-Time Employees Must Be Offered Coverage to Avoid the No Offer and Inadequate Coverage Tests (Monthly Measurement Method)

An employer may use the monthly method or the look-back method to determine an employee's status as a full-time employee (or not). The monthly method is explained in this Section. The look-back method is explained in Section 7. An employer may use different methods for certain groups of employees – see Q&A 113 for details.

Q82: What is the monthly method?

A82: Under the monthly method the employer looks at each employee's actual hours of service each calendar month. As explained in Section 2, an hour of service generally is an hour for which the employee is paid for work, vacation, sick time, a holiday, jury duty, or paid leave. An employee is assumed to be full-time for the month if he or she works 130 hours (regardless of the actual length of the month). Under this method, at the end of the month the employer looks at the employee's actual hours for the month to determine whether the employee is full-time for the month.

> ***Example:*** Jack and Jim are both employed by Blue Sky Corp. and typically work 40 hours per week. Blue Sky uses the monthly method. Jack works at least 130 hours during January and February, is laid off during March, and works 130 or more hours during April through December. Jack must be considered a full-time employee for all months except March. Blue Sky may exclude Jack from the plan during March without paying a penalty.
>
> Jim worked at least 130 hours from January through May (and, in fact, worked 200 hours during May). Jim was on paid FMLA from June 1 through July 7 and on unpaid FMLA from July 8 through August 8. Jim returned to work full-time August 9 and worked at least 130 hours during August through September. Jim must be considered full-time and offered coverage or penalties will apply for January through June and August through December. Jim's extra hours during May are irrelevant. Paid FMLA counts toward hours worked; unpaid FMLA does not **for purposes of the monthly method**.

Q83: If an employer uses the monthly method, must it determine hours on a calendar month basis?

A83: The IRS recognizes that most pay periods are weekly or bi-weekly, rather than monthly, and will allow employers to look at hours on a current basis using the "weekly rule" method instead. Under this method, the employer chooses a work week that it will use consistently, such as from Sunday through Saturday. (In most cases, the simplest work week to choose would be the week used for payroll purposes.) The employer may then apply the work week method so that it includes either the first or the last day of the month. With this approach, some months will be treated as having four weeks (creating a monthly measure for full-time status for those months of 120 hours) and others will have five weeks (creating a monthly measure for full-time status for that month of 150 hours).

> ***Example:*** Widget Corp. uses the period of Sunday through Saturday as a week and includes the week that includes the first day of a calendar month and excludes the week that includes the last day of a calendar month (unless the last day of the calendar month occurs on a Saturday). Widget measures hours of service for the five weeks from Sunday, December 27, 2015, through

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Saturday, January 30, 2016, to determine an employee's full-time employee status for January 2016; for the four weeks from Sunday, January 31, 2016, through Saturday, February 27, 2016, to determine an employee's status for February 2016; and the four weeks from Sunday, February 28, 2016, through Saturday, March 26, 2016, to determine an employee's status for March 2016. For January 2016, Widget must treat an employee as full-time if the employee has at least 150 hours of service (30 hours per week × 5 weeks). For February 2016 and March 2016, Widget must treat an employee as a full-time employee if the employee has at least 120 hours of service (30 hours per week × 4 weeks).

Q84: How does an employer that uses the monthly (or weekly) method handle changes in employment status?

A84: Because this method is based on actual hours currently worked, if an employee moves from full-time to part-time status, the employer does not need to offer coverage once the employee drops below 30 hours per week for the month. If an employee moves from part-time to full-time, the employer will need to offer coverage by the first of the month after three full calendar months as an eligible employee.

Example: Beth works 20 hours a week for Popcorn, Inc**.** from January 1, 2016, through December 31, 2016. Beth is not eligible for, and is not offered, coverage in 2016. On January 1, 2017, Beth is promoted to a full-time supervisor position, and is eligible for coverage after completing 90 days as a supervisor. As of April 1, 2017, Popcorn offers affordable, minimum value coverage to Beth. Popcorn has met its obligations.

Q85: How does an employer that uses the monthly (or weekly) method handle leaves of absence?

A85: If the employee is on a paid leave of absence, he or she will have "hours of service" so coverage must be offered. If the employee is on an unpaid leave – including an FMLA or USERRA leave – he or she will not have hours of service and coverage does not have to be offered during this time.

Q86: How does an employer that uses the monthly (or weekly) method handle breaks in service?

A86: If an employee who does not work for an educational institution has a break in service because, for example, he or she has unpaid leave or his or her employment terminates, and the employee returns to work or is rehired within 13 weeks, the employee must be treated as a continuing employee, and no new waiting period can be imposed when he or she returns to work. Coverage must resume by the first of the month on or following the date he or she returns to work. If the break in service is more than 13 weeks, the employee can be treated as a new employee, subject to a new waiting period. Coverage does not have to be offered during the break in service period to satisfy play or pay requirements.

Example: Scott terminates his employment with Zero Corp. on June 25, 2017, and is rehired on August 26, 2017. Scott's coverage must resume as of September 1, 2017, because his break in service was less than 13 weeks.

If the employer wishes, it may use a shorter measurement period for short-term employees. The employer may use a break period equal to the employee's original period of employment (but not less than four weeks) instead of 13 weeks as the break period if the employee has a break in service during the first 13 weeks of employment. This is called the parity rule.

Example: Zero hires John on February 2, 2015. John resigns on March 27, 2015 (after 8 weeks of employment). John is rehired on June 1, 2015 (10 weeks after he resigned). Zero uses the parity rule. Because John's period of employment was less than his break in service, Zero does

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not have to offer coverage to John until he completes three full calendar months of employment after his rehire. (Note that while the play or pay rules use a maximum waiting period of the first of the calendar month on or following three months of employment, the waiting period rules use a maximum waiting period of 90 days.)

Q87: Are there special rules for employees of educational institutions?

A87: Yes. If an employee of an educational institution (whether public or private, and from primary through university level) has a break in service because, for example, he or she has unpaid leave, it is summer break, or his or her employment terminates, and the employee returns to work or is rehired within 26 weeks, the employee must be treated as a continuing employee, and no new waiting period can be imposed when he or she returns to work. Coverage must resume by the first of the month on or following the date he or she returns to work. If the break in service is more than 26 weeks, the employee can be treated as a new employee, subject to a new waiting period.

Example: Steve teaches full-time at Rose School. Steve does not work for Rose during summer break, which runs from May 27, 2015, through August 22, 2015. Steve's coverage must resume as of September 1, 2017, because his break in service was less than 26 weeks. Rose does not need to offer coverage to Steve during June, July, or August, since he worked less than 30 hours per week during those months and Rose has adopted the monthly measurement method. Rose does need to offer coverage to Steve from September through May.

If the employer wishes, it may use a shorter measurement period for short-term employees. The employer may use a break period equal to the employee's original period of employment (but not less than four weeks) instead of 26 weeks as the break period if the employee has a break in service during his or her first 26 weeks of employment. This is called the parity rule.

Example: Rose hires Jill as an aide on September 14, 2015. Jill resigns on December 29, 2015 (after 15 weeks of employment). Jill is rehired on May 30, 2016 (22 weeks after she resigned). Rose uses the parity rule. Because Jill's period of employment was less than her break in service, Rose does not have to offer coverage to Jill until she completes three full calendar months of employment after her rehire.

Note: Spring break and Christmas vacation often will be paid; paid hours of service are considered time worked even if the employee does not actually perform services during the week or month.

The IRS has determined some educational organizations are attempting to avoid these rules by using staffing agencies for certain roles, under the idea that staffing agency employees would be subject to the 13-week rehire rule. The IRS plans to propose amendments to regulations so that staffing agency employees providing services for educational organizations would be subject to the 26-week rule, not the 13-week rule. The amendments will apply as of the applicability date in the regulations.

Q88: Do the special rules for employees of educational institutions apply to employees who do not work directly for educational institutions, but whose work schedule is affected by the school year?

A88: No. The special 26-week break-in-service rule only applies to employees of educational institutions (as determined under IRS rules).

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Q89: Why would an employer choose to use the monthly or weekly method?

A89: Employers with workforces that work predictable numbers of hours may find the monthly method accurately determines which employees need to be offered coverage (or for whom penalties are due), with less record keeping than is involved in the look-back method. It also allows the employer to immediately adjust for changes from full-time to part-time, or to unpaid status. However, because this determination can only be made at the end of the month, if an hourly employee who is classified as not full-time unexpectedly works more than 130 hours in a month, the employer may owe a penalty for that month because coverage was not offered to the employee. Employers will need to consider the likelihood of unexpected overtime, the frequency of overtime, and whether it may make business sense to simply pay the penalty to meet short-term business needs.

Q90: If an employer chooses to use the monthly or weekly method, when does it start counting hours?

A90: Because this method looks at hours currently being worked, an employer with a calendar year plan and 100 or more employees would first count hours beginning January 1, 2015. A large employer with a non-calendar year plan would first begin counting hours as of the start of its 2015 plan year, assuming it qualifies for the transitional relief described in Q117.

Section 7 – Determining Which Full-Time Employees Must be Offered Coverage to Avoid the No Offer and Inadequate Coverage Tests (Look-Back Measurement Method)

Q91: What is the look-back method?

A91: Under the look-back method, the employer looks at how many hours the employee averaged during a look-back period called a “measurement period.” Once the employer determines whether or not the employee worked full-time during the measurement period, that determination generally will apply throughout the related stability period regardless of how many hours the employee actually works (unless the employee's employment ends).

Under the look-back period method, different processes apply to existing and new employees.

Q92: How does an employer use the measurement and stability period for existing employees?

A92: For existing employees (called ongoing employees in the rules), the employer looks at how many hours the employee averaged during a look-back period called a “standard measurement period.” Once the employer determines whether or not the employee worked full-time during the standard measurement period, that determination will apply throughout the related stability period regardless of how many hours the employee actually works (unless the employee's employment ends, or the employee moves to a part-time position and other conditions are met). To use this option:

- The employer must choose a “standard measurement period” of three to 12 months. The standard measurement period is the “look-back” period that is used to track the employee’s hours and determine how many hours he/she worked, on average, during the standard measurement period.

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- The employer must choose a start date for the standard measurement period. It can be January 1, the first day of the benefit period, a date near the start of open enrollment, or any other date the employer chooses.
- The employer must choose a stability period. The stability period is the period for which the employee is considered “full-time” or "not full-time," based on the average hours worked during the standard measurement period, regardless how many hours the employee actually works during the stability period. The stability period must be:
  - At least as long as the standard measurement period
  - Not more than 12 months
  - No longer than the standard measurement period if the employee is determined to not be full-time
  - At least six months if the employee is determined to be full-time
- The stability period must immediately follow the standard measurement period and any related administrative period (note that use of an administrative period cannot create gaps in coverage).
- Employers may use different standard measurement and stability periods and period start dates for these classes – and only these classes – of employees:
  - Collectively bargained and non-collectively bargained
  - Covered under different collective bargaining agreements
  - Hourly and salaried
  - Employees located in different states
  - Employees of different employers in a controlled or affiliated service group

Example: ABC Corp. chooses to use a six-month standard measurement period and a six-month stability period. ABC’s first standard measurement period will begin on July 1, 2014, and end on December 31, 2014, and its first stability period will run from January 1, 2015, through June 30, 2015.

Bill works: 29 hours per week in July 2014
30 hours per week in August 2014
28 hours per week in September 2014
28 hours per week in October 2014
26 hours per week in November 2014
33 hours per week in December 2014
35 hours per week in January 2015
32 hours per week in February 2015
30 hours per week in March 2015
33 hours per week in April 2015
31 hours per week in May 2015
28 hours per week in June 2015

Bill’s average is 29 hours per week during the July to December 2014 standard measurement period. He will not be considered a full-time employee for purposes of the play-or-pay penalties during the stability period (January to June 2015) even though he is regularly working more than 30 hours per week during that time.

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When January to June 2015 becomes the measurement period, the 35 + 32 + 30 + 33 + 31 + 28 hours worked will be averaged, and because Bill is full-time (31.5 hours per week) during that measurement period, he will be considered full-time for play-or-pay purposes from July to December 2015 even if his hours drop below 30 per week during that period, as long as he remains employed by ABC.

Note: Employers that have employees who work fluctuating schedules may find that using a 12-month standard measurement period will be advantageous as it gives a longer period to average hours.

Note: In many situations, it may be simplest to use:

- A stability period that is the same as the coverage period/plan year, since that is the period for which coverage needs to be offered to full-time employees
- A measurement period that ends shortly before the open enrollment period, so that the administrative period can be used to determine which employees averaged 30 or more hours, offer coverage to those employees, and have them enrolled by the next stability period
- An administrative period that is long enough to determine which employees should be offered coverage, run open enrollment, and notify providers who has elected coverage for the coming year

So, a calendar year plan might choose a stability period of January 1 to December 31, a measurement period of October 15 to October 14, and an administrative period of October 15 to December 31, with open enrollment from November 10 to November 30.

Note: The employer will need to track the employee's hours during the stability period, as that information will be needed to make the determination for the next standard measurement period.

See Appendix E for additional examples.

Q93: When is an employee considered an ongoing employee?

A93: An employee is considered "ongoing" once he or she has completed a full standard measurement period.

Q94: If the stability period must immediately follow the measurement period, how can an employer determine who should be offered coverage and get the employee enrolled?

A94: To give employers time to determine whether an employee is "full-time" during a standard measurement period, and to enroll the employee if he or she is eligible, employers may elect to use an administrative period.

When using an administrative period, these rules must be followed:

- The administrative period can include time at both the beginning and the end of the measurement period, but the total administrative period cannot be more than 90 days. (Under the rules, this is exactly 90 days, **not** three months.)
- The administrative period cannot reduce or lengthen the standard measurement period or stability period.

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- The administrative period must overlap the **prior** stability period. This means that employees who are full-time based on the prior standard measurement period must remain eligible through the end of the current stability period.
- The administrative period must adjoin the next measurement period.

Example: Yeller Co. has a calendar-year plan and open enrollment is from November 1 to November 30. Yeller chooses a 12-month stability period that begins each January 1 (to coincide with the plan year), a 12-month standard measurement period that begins each October 15 (to maximize the standard measurement period, but allow for the administrative period) and an administrative period that begins each October 15 (giving Yeller most of the month of October to determine who is eligible for open enrollment, November to conduct open enrollment and December to complete enrollment processing).

Jane averaged 32 hours per week during 2015 (the standard measurement period), and was provided minimum value, affordable coverage under Yeller's plan during 2016 (the stability period). Yeller determines that Jane averaged 28 hours per week from October 15, 2015, to October 14, 2016. This means that 1) Yeller does not have to offer coverage to Jane during the November 2016 open enrollment period to avoid penalties in 2017, and 2) Yeller must continue to offer Jane coverage through December 31, 2016 (the full 2016 stability period).

Q95: How does an employer measure new employees who are expected to work full-time?

A95: To avoid penalties, a new employee (other than a seasonal employee) who is reasonably expected to work 30 or more hours per week must be offered coverage with an effective date that is not later than the first of the month on or following completion of three calendar months of employment. If minimum value coverage is offered by the end of the three-month period, no penalty will be owed during the first three calendar months of employment (and the employee would be eligible to receive a premium tax credit/subsidy if he or she meets the requirements to receive a premium tax credit during the three-calendar-month period). If the employer does not offer acceptable coverage by the end of the third full calendar month to an employee who is reasonably expected to work 30 or more hours per week, the penalty will be due from the employee's start date. The monthly measurement period method will be used for the new, full-time employee until the employee has completed a full standard measurement period.

A new employee who is reasonably expected to work fewer than 30 hours per week does not need to be offered coverage (but his or her hours need to be tracked during the measurement periods).

Q96: How does an employer measure new employees who may or may not average 30 hours per week, or who are just hired for a season?

A96: Employers who hire variable-hour or seasonal employees may elect to use an "initial measurement period" to determine whether the employee is full-time during a subsequent stability period. No penalty is due during this initial measurement period, even if it is more than three calendar months and it is ultimately determined the employee averaged 30-plus hours and was therefore a full-time employee during this time.

Note: This method may only be used when the employer truly expects the employee's hours to fluctuate, or the employee is a seasonal employee. **The employer must use measurement and stability periods with its ongoing hourly employees, or with employees in the bargaining unit, to be eligible to use this method with new variable-hour or seasonal employees. An employer may not use the look-back method only with variable-hour and seasonal employees.**

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Q97: What is a "variable-hour employee"?

A97: A “variable-hour employee” is an employee who, as of his or her start date, is in a position for which the employer cannot reasonably anticipate whether the employee’s average hours will be above or below an average of 30 hours per week. An employer may **not** consider the likelihood that a variable-hours employee may terminate or be terminated during the initial measurement period.

When deciding if an employee’s hours are variable, the employer should consider:

- Whether the person the employee is replacing worked more or less than 30 hours per week
- Whether employees in comparable positions work more or less than 30 hours per week
- Whether the job was advertised as a full-time or part-time position

Q98: What is a "seasonal employee"?

A98: A “seasonal employee” is an employee who is hired for a position for which the customary annual employment is six months or less. Typically, the period for which work is available is about the same time each year.

> ***Example:*** Bob is hired to work as a ski instructor from November 1, 2015, through the end of March 2016. Bob is a seasonal employee. Bob works 50 hours per week from November 1, 2015, through March 28, 2016. Because Bob is a seasonal employee and Bob’s employer uses the look-back method, Bob does not need to be offered coverage during the initial measurement period.

Note: The seasonal measure is based on the customary period of employment. If one season runs unusually long and seasonal employees are asked to stay a bit longer, seasonal status may be continued. For example, if because of later than usual snowfall Bob is asked to stay through the end of April, Bob’s employer may still consider Bob a seasonal employee.

Note that a “seasonal worker” is not the same as a “seasonal employee.” The six-month measure of a seasonal employee is used when deciding if a particular worker is full-time and should be offered coverage. The 120-day “seasonal worker” measure is used when deciding if an employer is large enough for play or pay requirements to apply.

Q99: Are there special rules for employees of temporary staffing firms?

A99: There is no special rule that generally applies to employees of temporary staffing firms because there is so much variation between staffing firms. If the temporary staffing firm is the common-law employer, when deciding if a worker can be considered a variable-hour employee the firm should consider whether other similar employees of the staffing company have the right to reject assignments, if there are periods during which no assignments are available, if the worker is offered assignments of differing lengths, and whether the assignments typically are for less than 13 weeks. Educational institutions have special rules under the ACA relating to breaks in service. Generally, employees may be treated as a new employee after a break in service of at least 13 weeks. Educational institutions are held to a standard of 26 weeks, and under the measurement and look-back method, employees of educational institutions (whether public or private, and from primary through university level) cannot have breaks in service of *four to 26 weeks* counted against them when measuring hours. Employees of educational institutions who return to work after a break cannot be treated as a new employee unless the break is longer than 26 weeks. The IRS has determined some educational organizations are attempting to avoid

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these rules by using staffing agencies for certain roles, under the idea that staffing agency employees would be subject to the 13-week rehire rule.

The IRS plans to propose amendments to regulations so that staffing agency employees providing services for educational organizations would be subject to the 26-week rule, not the 13-week rule. The amendments will apply as of the applicability date in the regulations.

Q100: How does an employer determine if a new seasonal or variable-hour employee is full-time?

A100: To use the seasonal/variable-hour look-back option:

- An "initial measurement period" of three to 12 months must be chosen
- The stability period must be the same length as the stability period for ongoing employees
  - For new employees determined to be full-time, it must:
    - be at least as long as the initial measurement period
    - be at least six months long
  - For new employees determined not to be full-time, it must **not**:
    - be more than one month longer than the initial measurement period
    - exceed the remainder of the standard measurement period, plus any associated administrative period, in which the initial measurement period ends

Example: Because XYZ uses a 12-month stability period for ongoing employees, it must use a 12-month stability period for new hires. XYZ chooses an initial measurement period of 12 months for new variable hours and seasonal employees. Sally is hired May 10, 2015. Sally works in the after-school program, so she will work a few hours a day during the school year and as many as 50 hours per week during school vacations. She is on-call if the school closes due to bad weather. XYZ tracks Sally's hours from May 10, 2015, to May 9, 2016, and determines she averaged 32 hours per week during that time. Sally is offered coverage as of June 1, 2016. XYZ does not owe a penalty for Sally during the entire 12-month initial measurement period, even though it was more than the three-month period generally allowed and she actually averaged more than 30 hours per week because of this special option for variable employees.

Note: If an employer uses a three-month measurement period and needs to use a six-month stability period because the employee is full-time, the next measurement period (plus administrative period) must be adjacent to the end of the stability period.

Q101: May employers use an "administrative period" for new variable-hour and seasonal employees?

A101: Yes. As with ongoing employees, employers using measurement and stability periods may elect to add an administrative period to allow time to calculate hours and work through the enrollment process. When using an administrative period with new variable-hour and seasonal hires, these are the rules that must be followed:

- The administrative period cannot be more than 90 days.
- The administrative period can be split and applied both before and after the initial measurement period (to allow calculations based on calendar months), but the total administrative period cannot exceed 90 days.

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- The combined administrative period and initial measurement period cannot be longer than the last day of the first calendar month beginning on or after the first anniversary of the employee's start date. (That is, the calculation period cannot be more than 13 months plus a fraction of a month.)

Example: Smith, Inc. decides it needs a 60-day administrative period. This means that its initial measurement period cannot be more than 11 months. Smith chooses to use an initial measurement period of 11 months (rounded to the next calendar month) and a stability period of 12 months (which is at least as long as the measurement period and not more than one month longer, as explained above). On May 15, 2015, Smith hires Sam as an on-call lab tech and hires Lynn as an orderly who is expected to work 32 hours per week.

Because Sam is a "variable-hour employee," Smith will track Sam's hours from May 15, 2015, to April 14, 2016. Smith then has from April 15, 2016, to June 30, 2016, to determine if Sam is full-time, offer him coverage if he is full-time, and have his coverage start on (or before if it prefers) July 1, 2016. Smith will not owe a penalty for Sam during the 13-month initial measurement and administrative periods, even though it was more than three calendar months and Sam may have averaged more than 30 hours per week because of this special option for variable and seasonal employees.

Because Lynn has been hired into a job with steady hours, Smith must offer Lynn coverage effective on or before August 1, 2015, to avoid the penalty.

Q102: How does an employer transition new variable-hour or seasonal employees into ongoing employee status?

A102: Transitioning a new variable-hours or seasonal employee requires testing in both the initial measurement and subsequent standard measurement periods. If an employee is determined to be full-time in either period, he or she must be offered coverage for the full **applicable** stability period.

Example: Ridge, Inc. has chosen to use a 12-month standard measurement period for ongoing employees running from October 15 to October 14, an administrative period from October 15 to December 31, and a 12-month stability period running from January 1 to December 31. For new variable-hour employees, Ridge has chosen to use an 11-month initial measurement period that begins on the employee's start date and an administrative period that runs from the end of the initial measurement period until the end of the second calendar month beginning after the end of the initial measurement period. Ridge hires Tim on May 10, 2015, and cannot reasonably anticipate Tim's hours. Tim's initial measurement period runs from May 10, 2015, through April 9, 2016. Tim works an average of 32 hours per week during this initial measurement period. Ridge must offer Tim coverage for a stability period that runs from July 1, 2016, through June 30, 2017. Ridge must also test Tim's hours during its October 15, 2015, to October 14, 2016, standard measurement period. Tim works an average of 34 hours per week during this time. Tim must be offered coverage during the standard stability period of January 1, 2017, to December 31, 2017. Had Tim's hours dropped to 28 hours per week from October 15, 2015, to October 14, 2016, Ridge could terminate Tim's coverage as of June 30, 2017.

If, however, the employee is not full-time during the initial measurement period but is full-time during the first standard measurement period, the employee must be offered coverage beginning with the first standard stability period.

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Once a new variable hours or seasonal employee has completed an initial measurement and stability period, that status is irrelevant – they are simply treated as any other hourly employee going forward.

Q103: How does an employer transition a new full-time employee who is not a variable-hour or seasonal employee into ongoing employee status?

A103: The employer must use the monthly (actual hours worked) method until the end of the first standard stability period and offer coverage after that based on hours worked during the standard measurement period.

> ***Example:*** Virginia is hired as a full-time hourly employee on March 6, 2015. Virginia's employer, Case Co., has a standard stability period that runs from January 1 through December 31, a standard measurement period that runs from October 10 through October 9, and an administrative period that runs from October 10 through December 31.
>
> Virginia must be offered coverage by July 1, 2015. Case will begin measuring her hours using the monthly measurement period method on that date. (As a practical matter, Case will need to offer her coverage through December 31, 2016, unless she is laid off, goes on an unpaid leave, or is otherwise predictably going to work less than 130 hours in a calendar month. Note that while the play or pay rules use a maximum waiting period of the first of the calendar month on or following three months of employment, the waiting period rules use a maximum waiting period of 90 days.)
>
> Virginia's first standard measurement period will begin October 10, 2015, and will end on October 9, 2016. Case will use those results to determine if she averaged 30 hours per week during that measurement period and should be offered coverage for the January 1 through December 31, 2017, stability period.

Q104: What happens if an employee moves between full-time and not full-time status during a stability period?

A104: Unless the employee has a bona fide change in employment status (changes to a new part-time position), or the employee is a newly hired variable-hours or seasonal employee who transfers to a full-time position, the employee's status as full-time (30 hours per week) or not full-time (fewer than 30 hours per week) during the measurement period determines the employee's status during the subsequent stability period.

For there to be a bona fide change in employment status for an employee who is considered full-time who then transfers into a part-time position, a variety of requirements must be met to allow the employer to reclassify the employee as part-time.

- The employee must have been offered minimum value coverage while full-time from at least the first day of the month following the employee's initial three full calendar months of employment through the month that the change in status occurs (regardless of how long ago the employee's initial three full of calendar months of employment was),
- The new position must be classified as part-time; if the employee simply reduces hours but stays in the existing job, the employee must remain classified as full-time for the rest of the stability period, regardless of whether the employee requested or initiated the reduction in hours.

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- This rule only applies if for three months following the change to part-time status the employee averages less than 30 hours a week. The employer applies the monthly measurement period to this employee through the end of the first full measurement period and administrative period that would have applied had the employee remained under the applicable look-back measurement period.

If these requirements are met and documented, the employer may treat the employee as other than full-time, and move the employee to the monthly measurement period, as of the first day of the fourth month after the employee transfers to the part-time position.

If a new variable-hours employee moves into a full-time position during the initial measurement period, the employee must be offered coverage as of the first day of the fourth month after he/she moved to full-time status (or at the start of the next standard stability period, if that would cause him/her to be considered a full-time employee sooner).

Q105: What happens if an employee has a break in service?

A105: If an employee who does not work for an educational institution terminates employment and is rehired within 13 weeks or has an unpaid non-FMLA leave of absence and returns to work within 13 weeks, the employee's status as a full-time or a non-full-time employee will be reinstated when he or she returns to work. If he or she was full-time and covered by the plan, coverage must resume by the first of the month on or following the date he or she returns to work. If the break in service is more than 13 weeks, he or she can be treated as a new employee, subject to a new initial measurement period and waiting period.

> ***Example:*** Brett works for a travel agency and decides to take a six-week unpaid leave of absence to tour Africa. Brett's employer, World Travel, uses a March 1 through February 29 stability period, a May 1 through April 30 measurement period, and a March 1 through April 30 administrative period. Brett is considered full-time for the March 1, 2015, through February 29, 2016, stability period. Brett's unpaid leave is from June 1 through July 15, 2015. When Brett returns, his coverage must be reinstated not later than August 1, 2015. When counting Brett's hours during the May 1, 2015, through April 30, 2016, measurement period, Brett will have zero hours worked between June 1 and July 15, 2015.

If the employer wishes, it may use a shorter measurement period for short-term employees. The employer may use a break period equal to the employee's original period of employment (but not less than four weeks) instead of 13 weeks as the break period if the employee has a break in service during his or her first 13 weeks of employment. This is called the parity rule.

> ***Example:*** Allen worked for Silverstone for 6 weeks and quit. He was rehired 8 weeks later. Allen's employer does not need to reinstate Allen's coverage, and can treat him as a new employee.

Q106: Are there special rules for employees of educational institutions?

A106: Employees of educational institutions (whether public or private, and from primary through university level) cannot have breaks in service of four to 26 weeks counted against them when measuring hours. Employers may either disregard the breaks or assume the employee continued to work his or her usual schedule during summer break. The IRS has confirmed that there is no 501-hour limit on hours of service required to be credited to an employee on account of a continuous period of time during which the employee performs no service, if the hours would otherwise qualify as hours of service (such as for a leave of absence).

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The IRS has determined some educational organizations are attempting to avoid these rules by using staffing agencies for certain roles, under the idea that staffing agency employees would be subject to the 13-week rehire rule. The IRS plans to propose amendments to regulations so that staffing agency employees providing services for educational organizations would be subject to the 26-week rule, not the 13-week rule. The amendments will apply as of the applicability date in the regulations.

> ***Example:*** Paul is employed by Orchard School. Paul works 38 hours per week from September 7, 2014, through May 23, 2015, and then does not work and is not paid during the summer break. Paul goes back to work on September 7, 2015. Because Paul was off for 15 weeks, which is less than 26 weeks, Paul's coverage must be reinstated by October 1, 2015, if it lapsed. Also, for purposes of determining Paul's average hours of service per week for the measurement period, Paul is credited as having an average of 38 hours of service per week for the 15 weeks between May 24, 2015, and September 5, 2015.
>
> ***Note:*** Spring break and Christmas vacation often will be paid.

Q107: Are there similar rules for other industries that periodically have shutdowns?

A107: No, there are not. An employer other than an educational institution may treat periods when it shuts down or when work is unavailable as periods in which the employee worked no hours. This includes industries related to education that are affected by the school year – unless the employer is the actual educational institution, it can treat time off during the summer simply as time with no hours of service.

Q108: What happens if an employee takes a leave of absence during a stability period and the employer uses the look-back method?

A108: If the employee is on a leave other than a leave under FMLA, USERRA, or for jury duty, the 13- or 26-week break in service rule explained in Q&A 105 and Q&A 106 applies to any period of unpaid leave. (Paid leave is considered hours worked. See Q&A 13).

Coverage will continue during the leave, while the employee is in the stability period. Time for which the employee had no hours of service will count as zero for measurement period purposes.

> ***Examples:*** Wilson Inc. uses an October 15 through October 14 standard measurement period and a January 1 through December 31 standard stability period.
>
> Ruth is a full-time employee for purposes of the January 1 through December 31, 2015, standard stability period. Ruth takes an unpaid leave of absence (that is not FMLA, USERRA, or jury duty leave) from March 15, 2015, to May 15, 2015. Ruth must be offered coverage during her leave, since she is entitled to coverage during the 2015 stability period. When calculating Ruth's hours during the October 15, 2014, through October 14, 2015, measurement period, Ruth will have zero hours of service from March 15 to May 15, 2015.
>
> Don is a full-time employee for purposes of the January 1 through December 31, 2015, standard stability period. Don takes an unpaid leave of absence (that is not FMLA, USERRA, or jury duty leave) from March 15, 2015, through August 9, 2015. Don must be offered coverage during his leave because he is entitled to coverage during the 2015 stability period, but Don drops his coverage. Because Don's leave is over 13 weeks he has a break in service, and Wilson may treat Don as a new employee, with a new waiting period and initial measurement period, when he returns on August 10.

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An employee on FMLA, USERRA, or jury duty leave essentially must be treated as if he or she worked during the leave.

> ***Example:*** Amy works for a company that uses an April 1 through March 31 measurement period, an administrative period of April 1 through May 31, and a June 1 through May 31 stability period. Amy is considered full-time for the June 1, 2015, through May 31, 2016, stability period. Amy is on an FMLA leave from October 1 through December 31, 2015. Amy must be offered coverage during her FMLA leave (regardless whether the time is paid or unpaid). When applying Amy's April 1, 2015, through March 31, 2016, measurement period, Amy's employer will disregard the three months she was on FMLA leave and average her hours from April through September 2015 and January through March 2016 to see if she must be considered full-time for the June 1, 2016, through May 31, 2017, stability period.

Q109: What happens if an employee is laid off during a stability period (and the employer uses the look-back method)?

A109: The same rules apply as for a leave other than FMLA, USERRA, or jury duty leave (see the previous question). If the employee is in a stability period and considered full-time, coverage must be offered during the layoff. If an employee had no hours of service, the employee discontinued coverage and he returns to work within 13 weeks, coverage must be reinstated by the first day of the month following his return to work. The time on layoff will have zero hours of service for purposes of the measurement period. If the employee had no coverage and the layoff exceeds 13 weeks, the employee can be treated as a new employee, with a new waiting period and initial measurement period, when he returns. If the employee had coverage during the layoff, there is no reinstatement issue and he will have no hours of service to measure during the time he was laid off.

Q110: Must an employer use a calendar month for these calculations?

A110: No. An employer can track hours on a payroll period basis instead. The employer will need to adjust its measurement period for this, by including a full payroll period at the start or the end of the period.

> ***Example:*** Employer A's payroll period begins January 14, 2015. It can begin measuring as of January 14 as long as it includes the full payroll period, which includes December 31, 2014, (i.e., the measurement period ends January 12, 2015).

Q111: Must an employer use 30 hours as the definition of "full-time employee" for all purposes?

A111: No. If an employer wishes to use 40 hours as the definition of "full-time" for other benefits (such as group life or disability insurance), vacation, holidays, etc., it may. In fact, it can use an hours requirement to participate in the group health plan that is more than 30 hours, but it will be subject to penalties on employees who work more than 30 hours per week if it does and it is a "large" employer.

Q112: May an employer change its measurement and stability periods?

A112: Yes. However, it may only make the change as of the start of the period.

Q113: May an employer use monthly/weekly measurement periods for some employees and look-back periods for others?

A113: Yes. An employer may use different methods for different classes, but the only allowed classes are:

- Collectively bargained and non-collectively bargained

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- Employees covered under different collective bargaining agreements
- Hourly and salaried
- Employees located in different states
- Employees of different employers in a controlled group

This means that an employer may not limit use of look-back periods to variable-hour and seasonal employees.

Q114: What happens if an employee transfers between positions that use monthly and look-back measurement periods?

A114: The rules are complex, but essentially:

- An employee who was full-time under a look-back measurement approach will remain full-time through the end of the stability period.
- An employee who was not full-time under a look-back approach will move to the monthly measurement approach.
- An employee who was full-time under the monthly method must be treated as full-time if he would be full-time under either the monthly or look-back approach.
- An employee who was not full-time under the monthly measurement approach will be treated as full-time if he would have been full-time under the look-back approach (so the employee would need to reconstruct hours during the measurement periods)

Q115: What happens if the employer changes its measurement and stability periods or an employee transfers between positions with different periods?

A115: The rules are complex, but the basic principles are to move the employee to the method used by the new position as soon as possible, while preserving any existing stability period as a full-time employee.

Q116: What happens if an employee's pay falls short?

A116: Plan participants who have a low rate of pay, take an unpaid leave of absence, are paid based on commissions, are tipped employees, or who have a wage garnishment, might not earn enough at times to pay for their elections. Sometimes the pay shortage will be combined with or is the result of an event that causes a loss of benefit eligibility. Sometimes though, a participant will remain eligible for the plan. Employers are left to determine how to handle the pay shortage.

The IRS has not provided guidance or regulation for handling pay shortages without a loss of benefit eligibility. As a result, employers often refer to the rules provided for handling employee contributions during an employee's unpaid Family Medical Leave Act (FMLA) leave. There are three options that employers have during unpaid FMLA leave:

- Pre-payment
- Pay-as-you-go on an after-tax basis
- Catch-up salary reduction upon return from leave

These methods give employers some latitude when determining how to recoup a missed payment. In the context of a pay shortage, pre-payment is unlikely to be a viable option. Pay-as-you-go might be an option for some employees (who have savings or other sources of income) but the catch-up salary

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reduction is most likely the easiest method for an employer to administer. Employers may allow employees to make catch-up salary reduction payments over a period of time of their choosing.

As a best practice, employers should ensure that they have a written policy that is available to employees regarding pay shortages in relation to benefit elections. The written policy should be uniformly enforced for all employees. Employers may set a time limit for the employee to catch up on contributions before terminating coverage, as well as a maximum period of time over which employees may spread payments. Thirty or 60 days is likely to be a reasonable time limit to allow employees to make up missed payments. Employees should be allowed uniform periods of time to pay back missed contributions; for instance, management should not be given three months to pay back missed contributions when other staff members are only given one month (or vice versa).

Employers should also have a written policy regarding the order of benefit funding in case an employee has elected multiple benefits (such as health, life insurance, dental, or disability). It would be in many employers' best interest to require that health coverage be funded first for purposes of health care reform.

Section 8 – Effective Dates

Q117: When do these requirements go into effect?

A117: The requirements take effect in 2015 for employers that had 100 or more full-time or full-time equivalent employees in 2014. The requirements also apply beginning in 2015 for employers with 50 to 99 employees that do not meet the maintenance requirements. The maintenance requirements are that the employer be able to certify (on IRS reporting form 1094-C) that during the period beginning on February 9, 2014, and ending on the last day of the plan year that begins in 2015, the employer:

- Has not reduced the size of its workforce or the overall hours of service of its employees so that it could qualify for this delay, and
- Has not eliminated or materially reduced any coverage it had in effect on February 9, 2014. A material reduction means that:
  - The employer's contribution is either less than 95% of the dollar amount of its contribution for single-only coverage on February 9, 2014, **or** is a smaller percentage than the employer was paying on February 9, 2014;
  - A change was made to the benefits in place on February 9, 2014, that caused the plan to fall below minimum value; or
  - The class of employees or dependents eligible for coverage on February 9, 2014, has been reduced.

Employers with 50 to 99 employees that are newly offering coverage to some employees, or that only offer coverage to a few employees, are eligible for the delayed effective date as long as they don't make changes that would violate the maintenance requirements. Employers with 50 to 99 employees that have not previously offered any coverage are eligible for the delay.

An employer with 50 to 99 employees and a calendar year plan that does not meet the maintenance requirements will be subject to the play or pay requirements, and penalties, as of January 1, 2015. An employer with 50 to 99 employees and a non-calendar year plan that does not meet the maintenance requirements will be subject to the play or pay requirements, and penalties, at the start of its 2015 plan

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year if it meets the transition requirements described in Q&A 117. If it cannot meet both the maintenance and transition requirements, play or pay will apply as of January 1, 2015.

Examples:

- ABC Co. averages 105 full-time employees during 2014. ABC must comply with the play or pay requirements starting in 2015 or pay penalties.
- Master Co. averages 95 full-time employees during 2014. Master did not have a group health plan until May 1, 2014. Master does not have to comply with the play or pay requirements until 2016.
  Page Corp. averaged 60 full-time employees during 2014. Page has a July 1 plan year. On July 1, 2014, Page drops its minimum value PPO plan for a skinny plan that does not provide minimum value. Page qualifies for the plan year transition requirements and Page must pay penalties on employees who receive a premium tax credit starting July 1, 2015.
- Justice Co. averaged 125 full-time employees during late 2013 and early 2014. On March 31 Justice sells a division with 45 employees for a legitimate business reason. Justice averages 91 full-time employees over 2014, so Justice does not need to comply with the play or pay requirements until 2016.
- Quigley Co. averaged 80 full-time employees during 2014. Quigley has a calendar year plan. On September 1, 2014, Quigley changes its eligibility so that employees who work 25 to 30 hours per week are no longer eligible. Quigley must comply with the play or pay requirements starting January 1, 2015, or pay penalties.

See Q&A 30 for information on calculating full-time employees, including a special option for 2014.

Note: All of the employers in the controlled group must be combined when determining the employer's size.

Q118: Must non-calendar year plans meet the play or pay requirements as of January 1, 2015?

A118: Employers with non-calendar year plans do not need to comply until the start of the 2015 plan year if they meet the plan year transition rules. Under the plan year transition rules, the play or pay requirements do not apply until the start of the 2015 plan year if:

- The employer had a non-calendar year plan in place on December 27, 2012; and
- The employer has not moved the plan year to a later date since December 27, 2012, (e.g., didn't move from a July 1 to a December 1 plan year); and
- Any of these four criteria are met:
  - Actually covered one-fourth of **all** employees (full-time and part-time) on any day between February 10, 2013, and February 9, 2014;
  - Actually covered one-third of **full-time** employees (30+ hours/week) on any day between February 10, 2013, and February 9, 2014;
  - Offered coverage to one-third of **all** employees during the last open enrollment;
  - Offered coverage to half of **full-time** employees during the last open enrollment; and
- Affordable, minimum value coverage is offered to the applicable employees as of the start of the 2015 plan year.

It appears that the delay for non-calendar year plans will apply in 2016 to employers with 50 to 99 employees that have non-calendar year plans.

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Note: Despite the delay in the play or pay requirements, most of the other ACA requirements, such as the limits on waiting period, pre-existing condition limitations, and benefit maximums, were effective as of the start of the 2014 plan year.

Q119: What is a plan year?

A119: A plan year is the 12-month period used by the plan. The plan year may or may not be the same as the renewal date. Each employer should have a plan document, and that plan document should define the plan year. If the plan documents do not designate a plan year (or if there are no plan documents), and the plan files an IRS Form 5500, the plan year used for that filing generally will be the applicable plan year. If there is no plan document and no Form 5500 is filed, it is unclear which year should be used for ACA purposes. In similar situations, the next option is sometimes the deductible year and sometimes the policy year. Without clear rules, presumably either of these options will be acceptable, although the most conservative choice would be to comply as of the earliest possible date.

Section 9 – Exchange Notification "Employer Notice Program"

Q120: If an employee receives a subsidy or an advance premium tax credit from an Exchange, can an employer appeal this decision?

A120: Yes. However, this appeal will not determine if the employer owes an employer shared responsibility payment but could help prevent employees from erroneously obtaining an advance premium tax credit, which in turn could provide the employer with information about whether or not it might owe a penalty. By preventing employees from incorrectly obtaining the advance premium tax credit, employers could lessen the chance of being asked to provide further information to the IRS to prove they met their obligations under the employer shared responsibility requirements.

Under the Frequently Asked Questions Regarding The Federally-Facilitated Marketplace's (FFM) 2016 Employer Notice Program issued by the Centers for Medicare & Medicaid Services (CMS), the IRS has a system to notify employers when one of their employees enrolls in Exchange coverage and is eligible to receive advance payment of the tax credit. The Marketplace notice will identify the employee, that he or she is eligible for the tax credit, that this could trigger a penalty on the part of the employer, and that the employer may appeal the decision. Employers are prohibited from retaliating against an employee for going to the Exchange or receiving a tax credit.

The FFM has an Employer Appeal Request form, which *must* be submitted within 90 days of the date stated on the Marketplace notice. The form asks for basic information about the employer, provides a place to identify a secondary contact, and asks for the employer to explain why it is appealing the determination that the employee is eligible for premium assistance. The employer may include documents to support its appeal. Examples of documents that an employer may include with its appeal are contained in the FFM Employer Appeal Document Verification Guide.

Alternatively, the employer can send a letter requesting an appeal. An employer must submit an appeal with the following information:

- Business name
- Employer ID Number (EIN)
- Employer's primary contact name, phone number and address

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- The reason for the appeal
- Information from the Marketplace notice received, including date and employee information

Employers must then mail the appeal request form or letter and a copy of the Marketplace notice to:

Health Insurance Marketplace
Department of Health and Human Services
465 Industrial Blvd.
London, KY 40750-0061

Section 10 – Paying the Penalty

Q121: When is the penalty due?

A121: The penalty will be determined after the end of each calendar year, after employees have filed their federal tax returns.

In November 2017, the IRS indicated on its "Questions and Answers on Employer Shared Responsibility Provisions Under the Affordable Care Act" webpage that, in late 2017, it planned to issue Letter 226J to inform large employers of their potential liability for an employer shared responsibility payment for the 2015 calendar year. The IRS' determination of an employer's liability and potential payment is based on information reported to the IRS on Forms 1094-C and 1095-C and information about the employer's full-time employees that were allowed the premium tax credit.

The IRS will issue Letter 226J if it determines that, for at least one month in the year, one or more of a large employer's full time employees was enrolled in a qualified health plan for which a premium tax credit was allowed (and the large employer did not qualify for an affordability safe harbor or other relief for the employee).

Letter 226J includes:

- A brief explanation of section 4980H.
- An employer shared responsibility payment summary table itemizing the proposed payment by month and indicating for each month if the liability is under section 4980H(a) ("Penalty A") or section 4980H(b) ("Penalty B") or neither.
- An explanation of the employer shared responsibility payment summary table.
- An employer shared responsibility response (ESRP) form (Form 14764, "ESRP Response").
- An employee premium tax credit (PTC) list (Form 14765, "Employee Premium Tax Credit (PTC) List") which lists, by month, the employer's assessable full-time employees (individuals who for at least one month in the year were full-time employees allowed a premium tax credit and for whom the ALE did not qualify for an affordability safe harbor or other relief (see instructions for Forms 1094-C and 1095-C, Line 16), and the indicator codes, if any, the employer reported on lines 14 and 16 of each assessable full-time employee's Form 1095-C.
- A description of the actions the employer should take if it agrees or disagrees with the proposed employer shared responsibility payment in Letter 226J.
- A description of the actions the IRS will take if the employer does not respond timely to Letter 226J.
- A date by which the employer should respond to Letter 226J, which will generally be 30 days from the date of the letter.

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- The name and contact of the IRS employee to contact with questions about the letter.

When an employer responds to Letter 226J, the IRS will acknowledge the response with a version of Letter 227 to describe the further actions that the employer can take:

- **Letter 227-J** acknowledges receipt of the signed agreement Form 14764, ESRP Response, and that the penalty will be assessed. After the IRS issues this letter, the case will be closed. No response is required.
- **Letter 227-K** acknowledges receipt of the information provided and shows the penalty has been reduced to zero. After the IRS issues this letter, the case will be closed. No response is required.
- **Letter 227-L** acknowledges receipt of the information provided and shows the penalty has been revised. The letter includes an updated Form 14765 and revised calculation table. The employer can agree or request a meeting with the manager and/or appeals.
- **Letter 227-M** acknowledges receipt of information provided and shows that the penalty did not change. The letter provides an updated Form 14765 and revised calculation table. The employer can agree or request a meeting with the manager and/or appeals.
- **Letter 227-N** acknowledges the decision reached in appeals and shows the penalty based on the appeals review. After the IRS issues this letter, the case will be closed. No response is required.

If, after receiving Letter 227, the employer agrees with the proposed penalty, then the employer would follow the instructions to sign the form and return it with full payment in the envelope provided.

If, after receiving Letter 227, the employer disagrees with the proposed or revised shared employer responsibility payment, the employer must provide an explanation of why it disagrees or indicate changes needed, or both, on Form 14765. Then the employer must return all documents as instructed in the letter by the response date. The employer may also request a pre-assessment conference with the IRS Office of Appeals within the response date listed within Letter 227, which will be generally 30 days from the date of the letter.

If the employer does not respond to either Letter 226J or Letter 227, the IRS will assess the amount of the proposed employer shared responsibility payment and issue a notice and demand for payment.

Q122: How is the penalty paid?

A122: Although the penalty is calculated monthly, it will be paid annually. The penalty will not be included in any standard tax filing, but instead will be charged through a notice and demand for payment, Notice CP 220J, from the IRS.

Notice CP 220J will include a summary of the employer shared responsibility payment, payments made, credits applied, and the balance due, if any. If a balance is due, Notice CP 220J will instruct employers on how to make payment. For payment options, such as an installment agreement, employers should refer to Publication 594 “The IRS Collection Process.”

Employers are not required to make payment before receiving a notice and demand for payment.

Q123: Is there a statute of limitations on the IRS’ ability to collect the penalty amount?

A123: No, the IRS has stated that there is no applicable statute of limitations on the IRS’ ability to collect the penalty amount.

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Q124: What if an employer fails to file its Forms 1094-C and 1095-C?

A124: In late 2018, the IRS started issuing notices to assess penalties against employers that failed to file Forms 1094-C and 1095-C with the IRS or to furnish 1095-C forms to employees for the 2015 or 2016 tax year. The IRS calculates these penalty assessments based on the number of Form W-2s the employers filed with the IRS.

These penalties are separate from the employer shared responsibility penalties that are imposed for failing to offer coverage.

The IRS sends Letter 5699 to employers that did not file Forms 1094-C and 1095-C for a reporting year.

An employer has 30 days to respond to Letter 5699 using one of the following options:

1. The employer was an applicable large employer (ALE) for the tax years in question but filed its Forms 1095-C with a different entity.
2. The employer was an ALE for the tax years in question and is including the Forms 1094-C and 1095-C with its response to the Letter 5699.
3. The employer was an ALE for the tax years in question and will be filing the Forms 1094-C and 1095-C with the IRS by a specified date (not more than 90 days from the date on the Letter 5699).
4. The employer was not an ALE for the tax years in question.
5. Another reason with a statement explaining why the employer has not filed the Forms 1094-C and 1095-C and the actions the employer plans to take to remedy the situation.

If an employer fails to respond to Letter 5699 or fails to address any filing issues, then the IRS issues a penalty assessment using Letter 5005-A/Form 886-A.

The penalties for failing to file and furnish are indexed each tax year. Maximum penalties for failing to file a return or furnish a statement by tax year are:

2021	$560 per return	2018	$530 per return	2015	$250 per return
2020	$550 per return	2017	$530 per return		
2019	$540 per return	2016	$520 per return		

An employer who receives Letter 5699 should contact its attorney as soon as possible to file its response with the IRS by the deadline in the letter.

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Appendix A – Factors of Employment Status

These factors are considered when deciding if a person is a common-law employee or an independent contractor.

a) Where is the work performed?
   - If it must be performed on the hirer's worksite, that points toward the person being an employee.

b) How long will the relationship continue?
   - If the relationship is indefinite, that points toward the person being an employee.
   - If the relationship is just until the task is completed, or for a specific amount of time, that points away from the person being a common-law employee.

c) Who provides the tools and materials needed for the task?
   - If the hirer provides tools, computers, desks, uniforms, etc., that points toward the person being an employee.

d) Does the hirer have the right to require that the task be performed a certain way?
   - If the hirer has the right to require that tasks be performed in a certain order, or in a certain way, that points toward the person being an employee.
   - If the assignment is simply to get the task done by a certain date, that points away from the person being a common-law employee.

e) Does the hirer have the right to assign additional tasks?
   - If the hirer can add or remove tasks, that points toward the person being a common-law employee.
   - If additional tasks would need to be negotiated and/or an additional charge would apply, that points away from the person being a common-law employee.

f) Does the individual have discretion over when and how long to work?
   - If the hirer sets work hours, that points toward the person being a common-law employee.

g) The method of payment (hourly or daily, or only when the task is completed)
   - If the person is paid based on time (daily, hourly, weekly), that points toward the person being a common-law employee.
   - If the person is paid by the job, that points away from the person being a common-law employee.

h) Whether the work is part of the regular business of the hirer
   - If the person is doing work that is part of the hirer's core competency, that points toward the person being a common-law employee.

i) Whether employee benefits are provided
   - If employee benefits are provided, the person is invited to company events, or other perks are provided, that points toward the person being a common-law employee.

j) Whether the hirer provides training to the individual
   - If the hirer provides training, that points toward the person being a common-law employee.

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k) Whether expenses are reimbursed
   – If expenses are reimbursed, that points toward the person being a common-law employee.

l) Whether there is the possibility of making a profit or experiencing a loss
   – If the person will be paid a flat amount for the job, regardless how long it takes, that points away from the person being a common-law employee.

m) Is there a contract and what does it say?
   – What the person and the hirer think about their relationship carries some weight.

Typically, common-law employees receive W-2s and independent contractors receive 1099s but that is not a failsafe method of determining classification status. The IRS has a form that may be used to request a determination of status for tax purposes that may be of some help in reviewing a specific situation.

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Appendix B – Factors of Common-Law Employer Status

A court used these factors in the Microsoft cases when determining if the temporary agency, or the company that received the worker's services, was the common-law employer:

a) Whether the agency or the company recruited the worker
b) The extent of the training the company provides to the worker
c) The duration of the worker's relationship with the company
d) The company's right to assign additional projects to the worker
e) Whether the company may influence the relationship between the worker and the agency

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Appendix C – Sample Determination of Large Employer Status

If, for example, Employer A had the following **full-time** employees

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Employees	32	40	34	36	36	40	39	35	36	36	48	49

Employer A also had the following **part-time** employees:

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Employees	10	10	10	10	10	10	10	10	12	12	10	10
Total hours worked	840	800	882	840	840	845	840	850	1008	1066.4	840	840

The calculation of Employer A's employees would be:

January	32 full-time	+	7 full-time equivalents (840/120)	=	39 employees
February	40 full-time	+	6.67 full-time equivalents (800/120)	=	46.67 employees
March	34 full-time	+	7.35 full-time equivalents (882/120)	=	41.35 employees
April	36 full-time	+	7 full-time equivalents (840/120)	=	43 employees
May	36 full-time	+	7 full-time equivalents (840/120)	=	43 employees
June	40 full-time	+	7.04 full-time equivalents (845/120)	=	47.04 employees
July	39 full-time	+	7 full-time equivalents (840/120)	=	46 employees
August	35 full-time	+	7.08 full-time equivalents (850/120)	=	42.08 employees
September	36 full-time	+	8.4 full-time equivalents (1008/120)	=	44.4 employees
October	36 full-time	+	8.89 full-time equivalents (1066.4/120)	=	44.89 employees
November	48 full-time	+	7 full-time equivalents (840/120)	=	55 employees
December	49 full-time	+	7 full-time equivalents (840/120)	=	56 employees

Then add the monthly totals and divide by 12 (548.43/12 = 45.70, rounded down to 45)

Employer A is not a large employer for the next calendar year, and no penalty will apply if Employer A does not offer coverage.

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Appendix D – Sample Employer Statements Regarding Determining Full-Time Status for Purposes of the Employer-Shared Responsibility Requirements

Note: *This sample statement assumes a fairly common plan design, with a calendar year plan with a fall open enrollment period. It does not include all possible employer choices, some of which trigger additional options and requirements. The IRS has not prescribed a particular way for employers to document their choices; this statement takes one possible approach. To the extent these choices affect eligibility for coverage under the plan, the plan documents will need to be amended to reflect the eligibility rules.*

Employer A's plan is a calendar year plan that runs from January 1 through December 31. Until otherwise elected, Employer A elects to use measurement and stability periods as follows:

1) Employer A will use the monthly method for salaried employees. Full-time status for those employees will be determined at the end of each current month. Hours of service for salaried employees will use the weekly equivalency method (an employee will be credited with 40 hours of service for each calendar week in which he/she performed at least one hour of service).
2) For ongoing hourly employees, Employer A elects to use:
   a) A 12-month standard measurement period that will generally begin October 15 and end the following October 14.
   b) An administrative period that will begin October 15 and end December 31.
   c) A 12-month standard stability period that begins January 1 and ends on December 31.
3) For new hourly employees who are expected to work an average of 30 or more hours per week, Employer A will offer coverage to be effective the first day of the month after 60 days of employment
4) For new hourly employees who are expected to have variable hours, Employer A elects to use:
   a) An 11-month initial measurement period that will begin on the employee's start date and end 11 months later.
   b) A 30-day administrative period.
   c) A 12-month initial stability period that begins on the day after the administrative period ends.
   d) A transition method that recognizes that the employee's hours also will be measured beginning with the first standard measurement period that begins after the employee's start date, and that the standard stability period will immediately follow the standard measurement and administrative period.

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XYZ Company Policy for Identifying Full-Time Employees

SAMPLE

This policy will be used by XYZ Company, the Plan Sponsor of the XYZ Company Group Health Plan (Plan) to identify its full-time employees under the employer-shared responsibility requirement and to determine eligible employees under the XYZ Group Health Plan. All employees who are determined to be full-time employees with respect to a given period of time and who satisfy any other eligibility requirements stated in the Plan are eligible employees under the Plan during that period of time. This policy is intended to supplement and be considered a part of the Plan.

For purposes of this policy, the XYZ Company will:

1) Use the look-back measurement method with respect to all employees for purposes of identifying those employees who are full-time employees.
2) Use a 12-month standard measurement period beginning each November 1 and ending the following October 31.
3) Use a 12-month standard stability period beginning each January 1 and ending the following December 31.
4) Use a 61-day standard administrative period beginning each November 1 and ending the following December 31.
5) With respect to a new employee who is hired as a “part-time employee,” “variable-hour employee,” or “seasonal employee,” the initial measurement period will be the 12-month period beginning on the first day of the calendar month following the employee’s start date.
6) With respect to a new employee who is hired as a “part-time employee,” “variable-hour employee,” or “seasonal employee,” except as provided below, the initial stability period will be the 12-month period beginning on the first day of the second calendar month after the end of the initial measurement period.

Special Situations

1) If a full-time employee changes employment status to part-time during a stability period, and meets all of the criteria below, the employee will cease to be considered a full-time employee on the last day of the third calendar month after the change in employment status occurs. This section applies only if:

    a) The employee was offered minimum value coverage continuously during the period beginning on the first day of the calendar month following the employee's initial three full calendar months of employment and ending on the last day of the calendar month in which the change in employment status described in this section occurs;

    b) The employee has a change in employment status to a position or status in which the employee would not have reasonably been expected to be a full-time employee if the employee had begun employment in that position or status; and

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c) The employee actually is credited with less than 130 hours of service for each of the three full calendar months following the change in employment status.

A full-time employee who experiences a reduction in hours, but who does not experience a change in position, will continue to be considered full-time for the balance of the stability period.

2) If an employee is absent due to special unpaid leave, for purposes of determining an employee's average hours of service during a measurement period, the average hours of service for that measurement period will be determined by computing the average after excluding all periods of special unpaid leave during that measurement period. "Special unpaid leave" means unpaid leave that is subject to FMLA, subject to USERRA, or on account of jury duty.

Ongoing Employees

1) An ongoing employee who is determined to be a full-time employee during a standard measurement period will be considered a full-time employee, and therefore an eligible employee, for each calendar month during the standard stability period associated with that standard measurement period, unless special situation (1) described above applies.

2) An ongoing employee who is determined not to be a full-time employee during a standard measurement period will not be considered a full-time employee, and thus not an eligible employee, for any calendar month during the standard stability period associated with that standard measurement period.

New Employees

1) A new employee who is reasonably expected at his or her start date to be a full-time employee (and is not considered a seasonal, variable hour or part-time employee) is considered a full-time employee, and will be eligible for coverage under the Plan upon completion of the eligibility waiting period.

   Although no single factor is determinative, the following factors will be considered in determining whether a new employee is reasonably expected at his or her start date to be a full-time employee:

   a) Whether the employee is replacing an employee who was (or was not) a full-time employee.

   b) The extent to which hours of service of ongoing employees in the same or comparable positions have varied above and below an average of 30 hours of service per week during recent measurement periods.

   c) Whether the job was advertised or otherwise communicated to the employee or otherwise documented (for example, through a contract or job description) as requiring hours of service that would average 30 or more hours of service per week or less than 30 hours of service per week.

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Until a new employee who is hired as a full-time employee has been employed for an entire standard measurement period, the employee's status as full-time or not full-time will be determined, for purposes of the employer-shared responsibility requirement, based on actual hours worked each month. Unless XYZ Company expects the employee to work less than 130 hours during a calendar month (due, for example, to layoff or an unpaid leave that is not special unpaid leave), the employee will be considered full-time for purposes of eligibility for coverage under the Plan throughout the first standard measurement period. Once the employee has become an ongoing employee, the employee's status as a full-time employee and as an eligible employee will be determined under the provisions of this policy regarding ongoing employees.

2) A new employee who is considered a part-time employee, a seasonal employee, or a variable-hour employee will not be considered a full-time employee initially and will have hours of service measured over an initial measurement period and be treated as follows:

   a) Coverage will not be offered during the initial measurement period unless the employee transfers to a position that is considered full-time, as described in section (D), below.

   b) If a new employee who is a part-time employee, seasonal employee, or variable-hour employee is determined to be a full-time employee during the employee's initial measurement period based on the hours of service credited during the initial measurement period, the employee will be considered a full-time employee, and thus an eligible employee, for each calendar month during the employee's initial stability period.

   c) If a new employee who is a part-time employee, seasonal employee, or variable-hour employee is determined not to be a full-time employee during the employee's initial measurement period based on the hours of service credited during the initial measurement period, the employee will not be considered a full-time employee, and thus not an eligible employee, during the employee's initial stability period.

   d) If a new employee who is a part-time employee, seasonal employee, or variable-hour employee experiences a change in employment status before the end of the employee's initial measurement period such that if the employee had begun employment in that new status the employee would have reasonably been expected to be a full-time employee, the employee will be considered a full-time employee beginning on the first day of the calendar month after the change in the employee's employment status or, if earlier, at the beginning of the employee's initial stability period, if the employee is determined to be a full-time employee during the employee's initial measurement period, and coverage will begin on the first day of the fourth calendar month following the change in employment status.

   e) Once a new employee who is a part-time employee, seasonal employee, or variable-hour employee has been employed for an entire standard measurement period, the employee will be considered an ongoing employee, and the employee's status as a full-time employee will be determined by the provisions of this policy regarding ongoing employees, but subject to the following:

      1. If the employee is determined not to be a full-time employee for the standard measurement period that overlaps or immediately follows the employee's initial

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measurement period, the employee will continue to be considered a full-time employee for each calendar month during the Initial stability period, if the employee was determined to be a full-time employee during the employee's initial measurement period.

2. If the employee is determined to be a full-time employee for the standard measurement period that overlaps or immediately follows the employee's initial measurement period, the employee will be considered a full-time employee for each calendar month during the entire standard stability period associated with the employee's first standard measurement period, even though that standard stability period may overlap an Initial stability period associated with an initial measurement period during which the employee was determined not to be a full-time employee.

3. If the employee is considered a full-time employee during both the employee's Initial stability period and the employee's first standard stability period, the employee will be considered a full-time employee during any period between the end of the Initial stability period and the beginning of the employee's first standard stability period.

Rehired Employees
An employee who is terminated and rehired will be treated as a new employee upon rehire only if the employee was not credited with an hour of service with XYZ Company or any member of the controlled or affiliated group for a period of at least 13 consecutive weeks immediately preceding the date of rehire or, if less, a period of consecutive weeks that exceeds the greater of (a) four weeks, or (b) the number of weeks of the employee's immediately preceding period of employment. For purposes of applying these rehire rules, the duration of the period of employment immediately preceding a period during which an employee was not credited with any hours of service is determined after application to that period of employment of the rules on special unpaid leave, if and to the extent those rules are applicable.

Definitions
For purposes of this Policy, the following terms have the following meanings:

a) **"Full-time employee"** means an employee of the XYZ Company who is credited with an average of at least 30 hours of service per week during a measurement period. For this purpose, 130 hours of service in a calendar month is treated as the monthly equivalent of at least 30 Hours of Service per week.

b) **"Hour of service"** means (1) each hour for which an employee is paid, or entitled to payment, for the performance of duties for the employer, and (2) each hour for which an employee is paid, or entitled to payment, by the employer for a period of time during which no duties are performed due to vacation, holiday, illness, incapacity (including disability), layoff, jury duty, military duty, or leave of absence. Hours of service for all employees are credited using actual hours of service from records of hours worked and hours for which payment is made or due.

c) **"New employee"** means an employee who has been employed for less than one complete standard measurement period.

d) **"Ongoing employee"** means an employee who has been employed for at least one complete standard measurement period.

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e) **"Part-time employee"** means a new employee whom the employer reasonably expects to be employed on average less than 30 hours of service per week during the employee's initial measurement period, based on the facts and circumstances at the employee's start date.

The anticipated length of the employee's period of employment will not be considered.

f) **"Seasonal employee"** means a new employee who is hired into a position for which the customary annual employment is six months or less, occurring at approximately the same time each year.

g) **"Variable-hour employee"** means a new employee if, based on the facts and circumstances at the employee's start date, the employer cannot determine whether the employee is reasonably expected to be employed on average at least 30 hours of service per week during the initial measurement period because the employee's hours are variable or otherwise uncertain. For purposes of determining whether an employee is a variable-hour employee, the likelihood that the employee may terminate employment before the end of the initial measurement period will not be considered.

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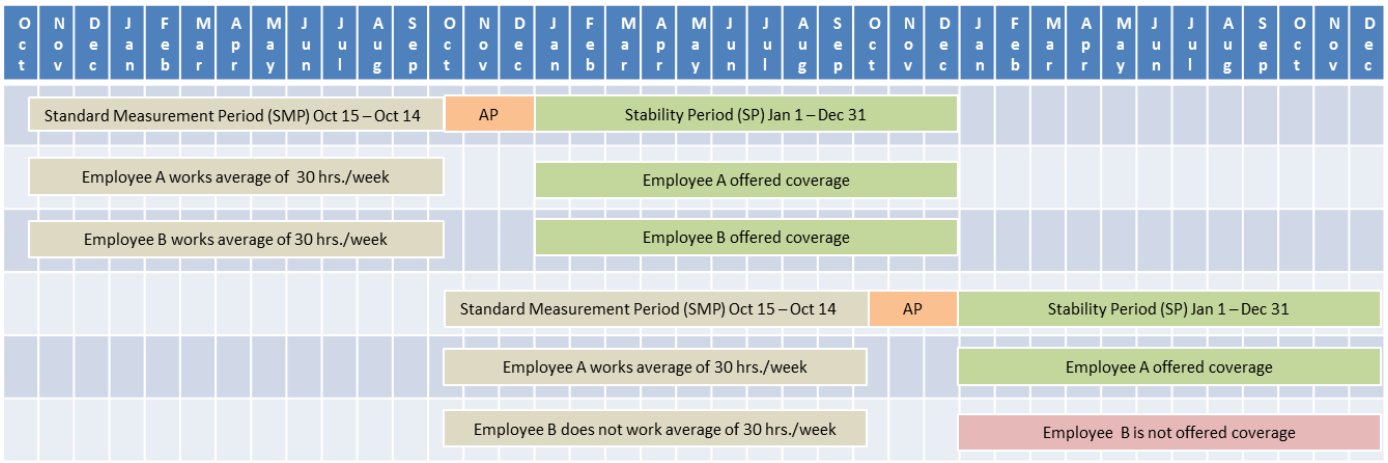
Appendix E – Examples of Measurement and Stability Periods

"Look-Back" Measurement/Stability Periods



Example: Employees A and B are measured during the "Standard Measurement Period" for ongoing employees. In year 1, both employees qualify for coverage due to hours worked.

Measurement periods start and end so that there is no break in coverage for those who qualify.

In year 2, employee A continues to qualify, but employee B does not qualify due to hours worked.

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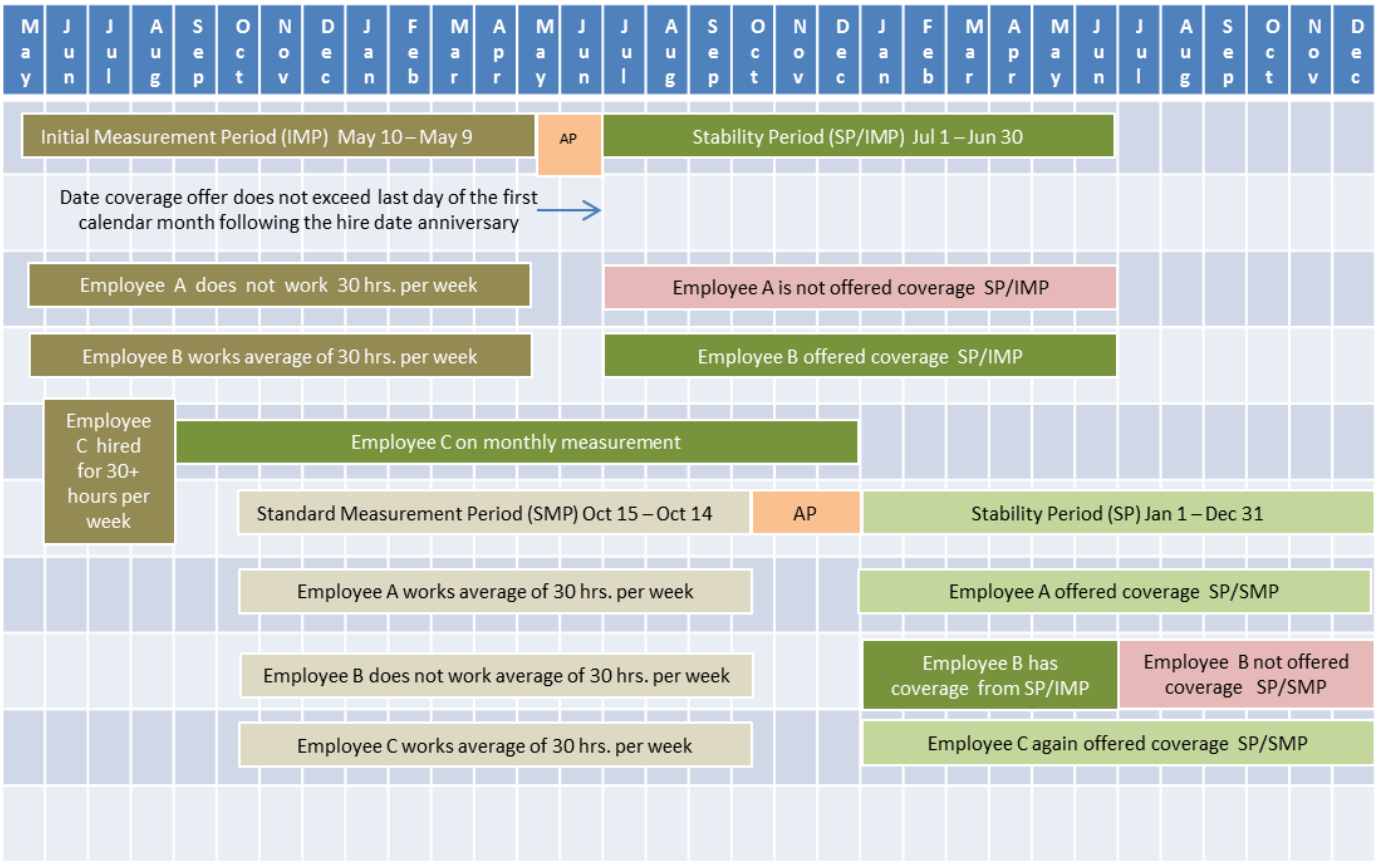
New Hires Become Ongoing Employees, Example 1



Example: Newly hired variable hour employees A and B are measured during an "Initial Measurement Period" – both qualify for coverage during a "Stability Period" associated with the Initial Measurement Period. Both employees are also measured during the "Standard Measurement Period" for ongoing employees.

Employee A continues to qualify for coverage based on hours worked during the "Standard Measurement Period." Employee B does not work 30 hours during the "Standard Measurement Period," but does not lose coverage until the "Stability Period" associated with the "Initial Measurement Period" ends.

Employee C is newly hired as a non-variable hour, full-time employee. Employee C must be offered coverage by the first day of the fourth calendar month of employment. Employee C will be on the monthly (actual hours) method until he completes one full Stability Period. C's hours also will be measured during the Standard Measurement Period.

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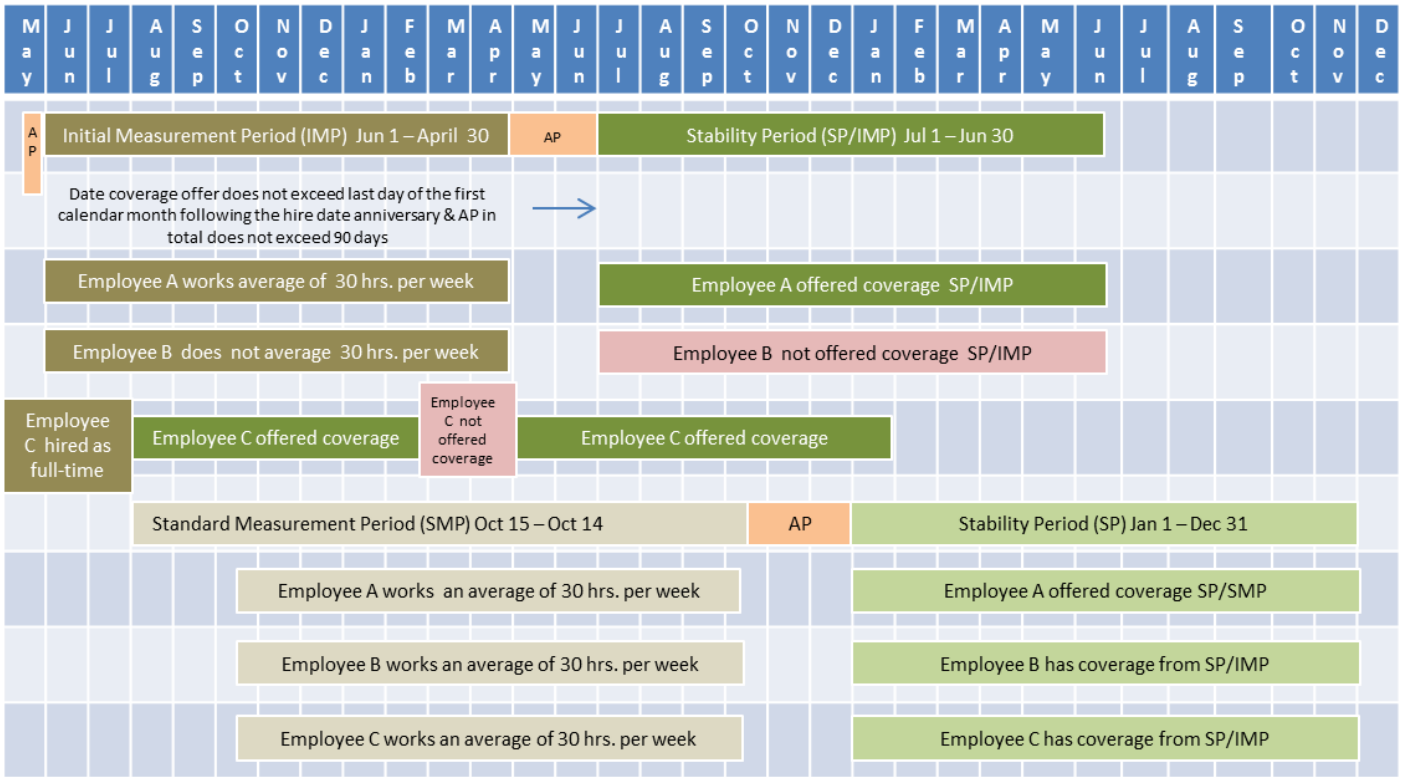
New Hires Become Ongoing Employees, Example 2



Example: Newly hired variable hour employees A and B are measured during an "Initial Measurement Period." Employee A qualifies for coverage, but employee B does not. Employee A is offered coverage during the "Stability Period" associated with the "Initial Measurement Period." Employee B is not offered coverage during the "Stability Period" associated with the "Initial Measurement Period."

Both employees are also measured during the "Standard Measurement Period" for ongoing employees.

Employee A continues to qualify for benefits based on hours worked during the "Standard Measurement Period." Employee B now qualifies during the "Standard Measurement Period" and is offered coverage for the "Stability Period" associated with the "Standard Measurement Period."

Employee C is hired to regularly work 35 hours per week. Employee C must be offered coverage by the first day of the fourth calendar month of employment. Employee C will be on the monthly measurement system until he completes one full Standard Stability Period. C's hours will be counted during the Standard Measurement Period. Employee C is laid off during March and April.

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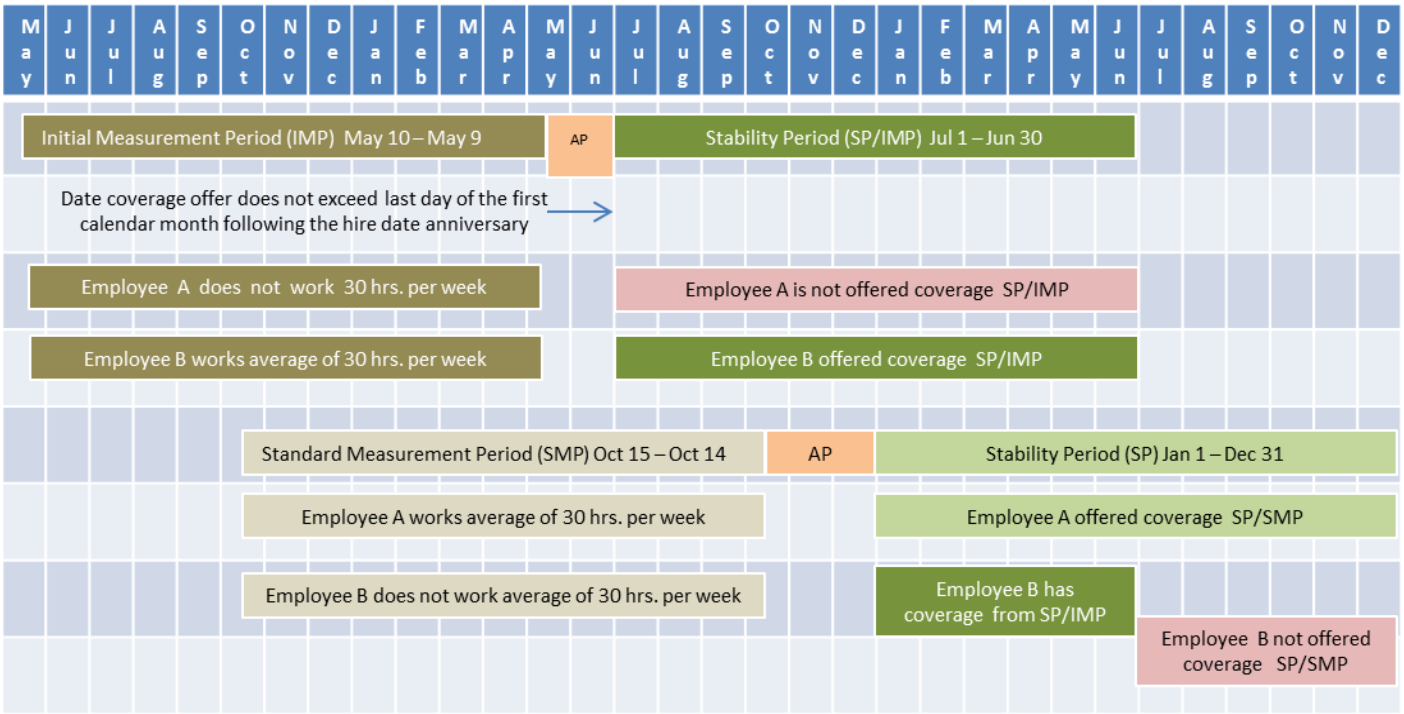
New Hires Become Ongoing Employees, Example 3



Example: Newly hired variable hour employees A and B are measured during an “Initial Measurement Period.” Employee A does not qualify for coverage but employee B does. Employee A is not offered coverage during the “Stability Period” associated with the “Initial Measurement Period.” Employee B is offered coverage during the “Stability Period” associated with the “Initial Measurement Period.”

Both employees are also measured during the “Standard Measurement Period” for ongoing employees.

Employee A now qualifies for coverage based on hours worked during the “Standard Measurement Period.” Employee B does not qualify during the “Standard Measurement Period,” but does not lose coverage until the “Stability Period” associated with the “Initial Measurement Period” is over.

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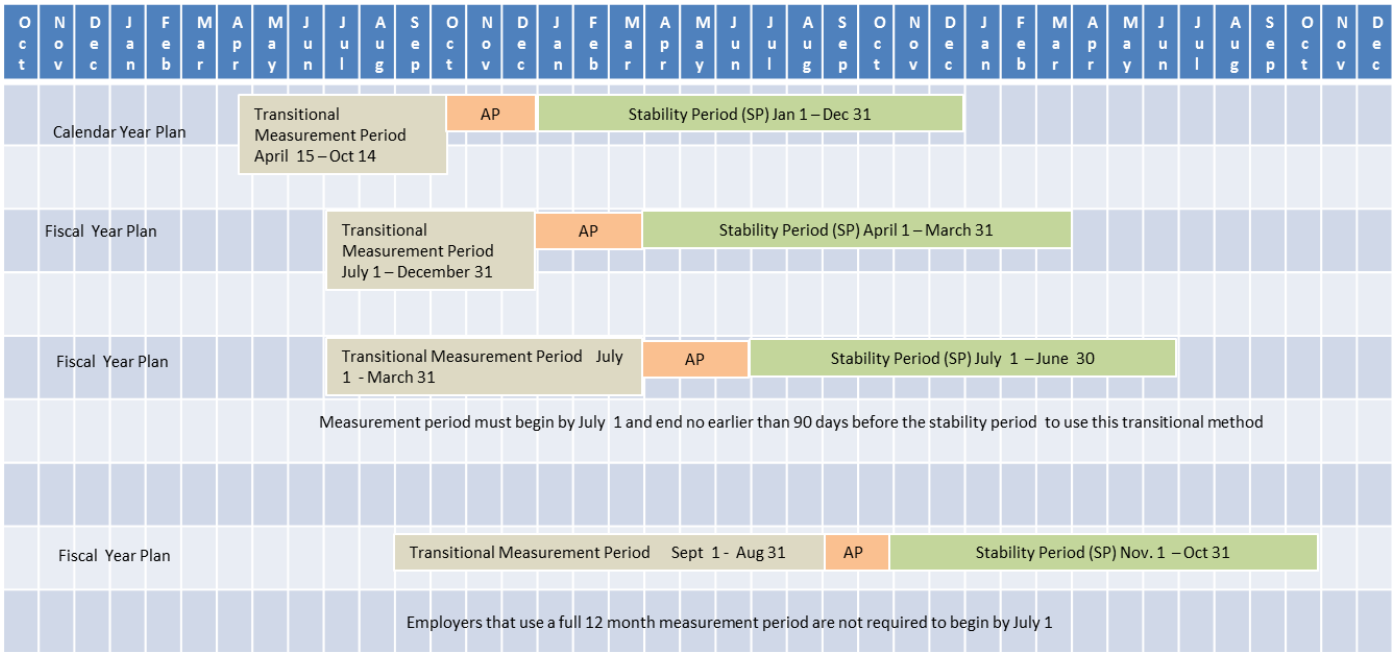
Transitional Measurement Periods for 2015 Only



For 2015, the ACA allowed for a shorter measurement period to apply to a longer stability period.

In order to use the shorter measurement period options, the measurement period must begin by July 1 and end no earlier than 90 days before the stability period.

If the renewal date is later in the year, a full 12-month measurement period had to be used.

Employees hired after the transitional measurement period begins are treated as new hires. A new variable hour/seasonal/part-time employee will begin a personal initial measurement period on their start date. A new employee reasonably expected to be full-time will use the monthly (actual hours) method until the first standard stability has elapsed; coverage must be offered by the first day of the fourth calendar month of employment (or as of the date the employer must comply, if later).

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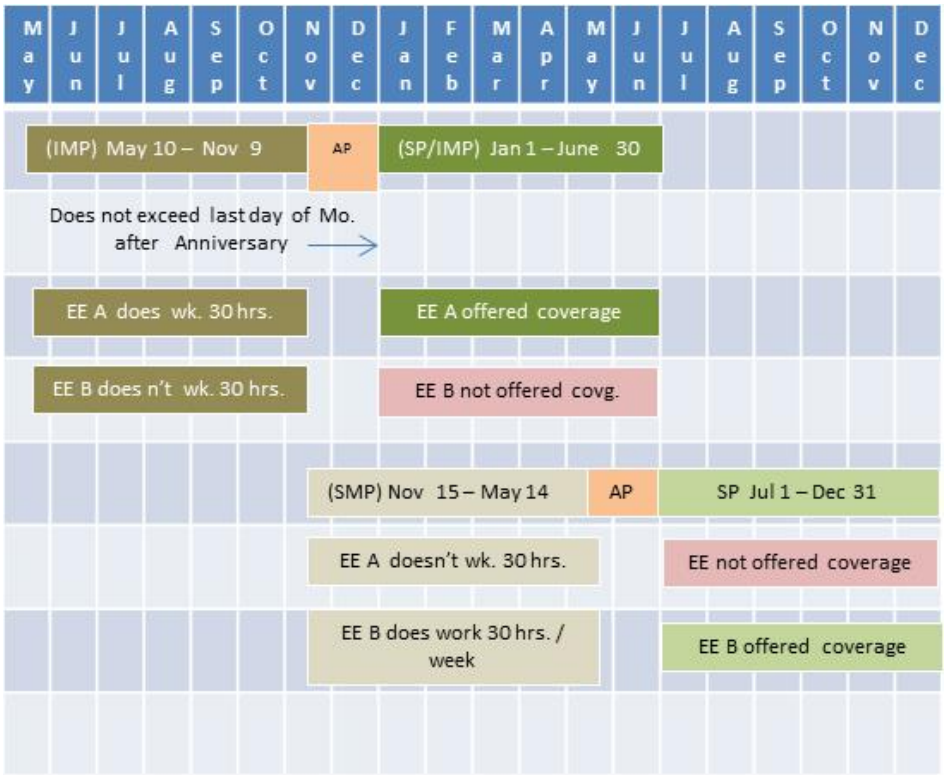
Using Periods Shorter Than 12 Months



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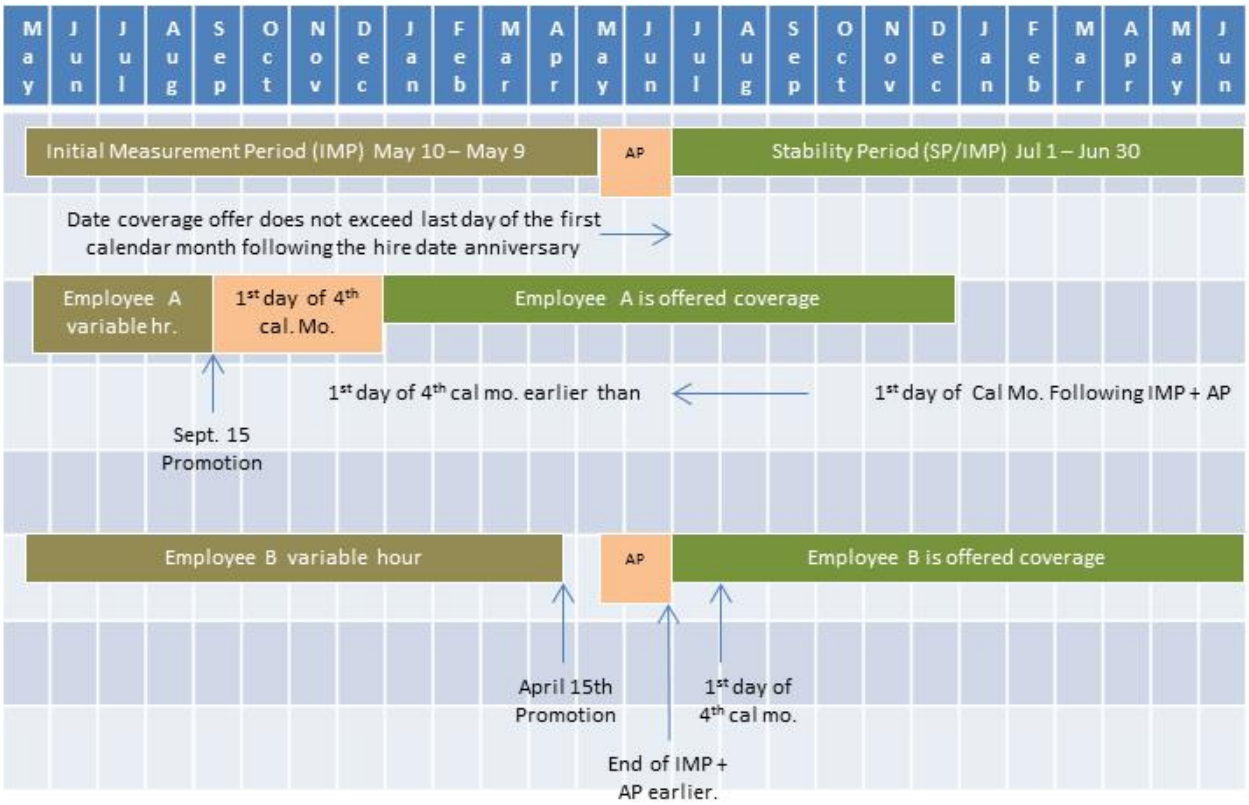
Example – Changing Employment during the Initial Measurement Period



If a “variable hour” employee becomes a full-time employee, coverage must be offered before the end of the first day of the fourth calendar month, or if earlier, the first day of the calendar month following the initial measurement period and any optional administrative period.

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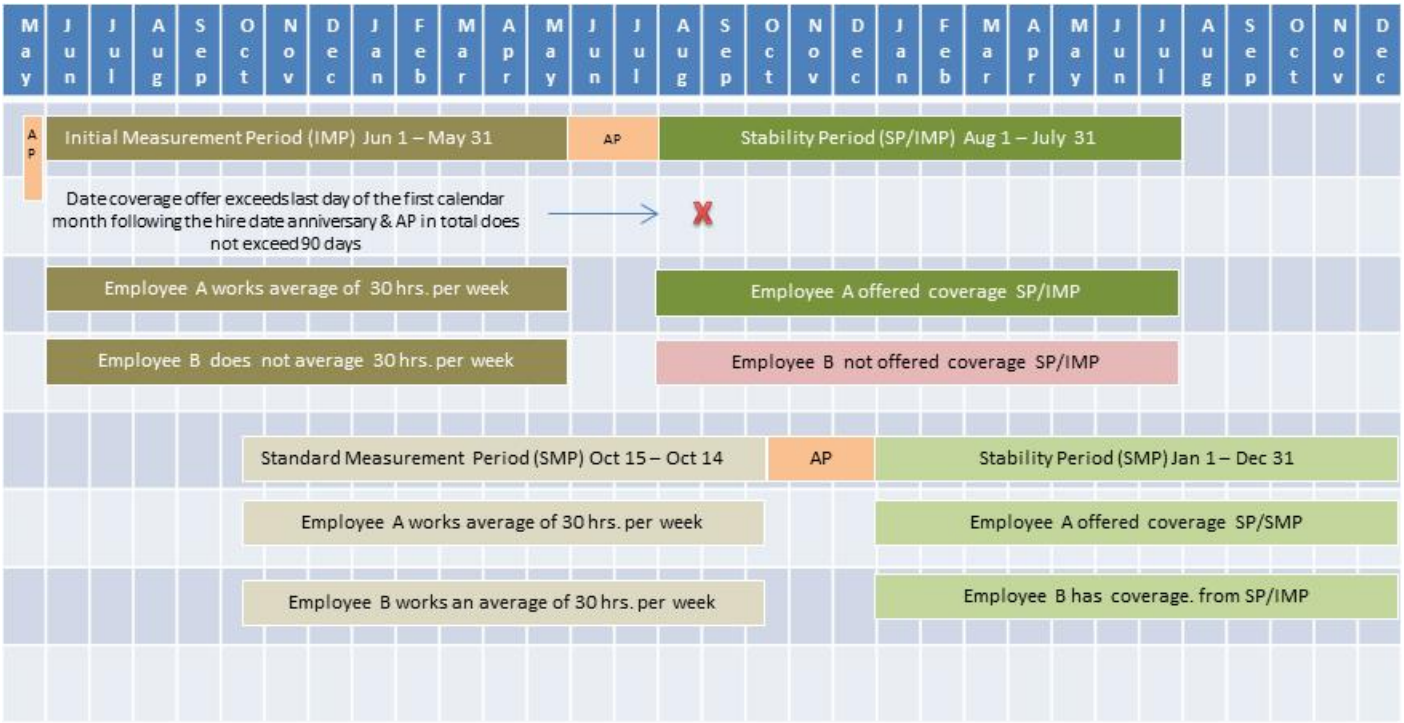
Total Initial Measurement and Administrative Period Limit



Employee hire date: May 15

The Administrative Period in this example is not allowed because the date coverage is offered (August 1) exceeds the last day of the first calendar month following the hire date (May 15) anniversary.

The last day of the first calendar month following the hire date (May 15) anniversary would be July 1.

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About United Benefit Advisors

United Benefit Advisors (UBA) is the nation's leading independent employee benefits organization with more than 200 offices throughout the United States, Canada, England, and Ireland. As trusted and knowledgeable advisors, UBA Partners collaborate with more than 2,000 fellow professionals to deliver expertise, thought leadership, and best-in-class solutions that positively impact employers and make a real difference in the lives of their employees and families. Employers, advisors and industry-related organizations interested in obtaining powerful results from the shared wisdom of our Partners should visit UBA online at www.UBAbenefits.com.

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