Health Insurance Reform: Pay or Play Mandate – Who Must Comply?

By Bill Balek, Director of Legislative Affairs, ISSA (Jan. 15, 2013)

A major emphasis of the Affordable Care Act is reducing the number of uninsured individuals, and the employer "pay or play" mandate is one of several new laws aimed at expanding coverage. Although this new law does not require you, as an employer, to provide health coverage to your employees, beginning on January 1, 2014, if you are a large employer you must choose to "**play**" (offer "minimum essential coverage" to all of your full-time employees) or "**pay**" (owe a potential excise tax if you do not offer "minimum essential coverage"). As a general rule, the "pay or play" mandate applies to you for a calendar month if you employed an average of at least 50 full-time equivalent employees (FTEs) on business days in the prior calendar year.

Moreover, the IRS has issued proposed regulations and Q&As that provide additional guidance intended to help employers determine whether they are subject to the pay or play mandate beginning in 2014 and, if so, how to comply. This article is the first in a series of articles that address the details of this latest guidance. This particular article addresses the question: who is subject to the pay or play mandate and when will the rules take effect.

What "Large Employers" are Subject to the Pay or Play Mandate?

If you employ at least 50 full-time equivalent employees ("FTEs") on average during the prior year, you are covered by the pay or play mandate. The guidance clarifies that you will average your number of employees across the calendar months in the prior calendar year to test whether you meet this threshold. Thus, in order to determine your FTE count, you must first determine your number of FTEs for each calendar month which is equivalent to: (1) each employee who works more than 30 hours per week ("full-time"), plus (2) the total number of hours worked during a month by employees who are not full-time (but not in excess of 120 hours for any such employee) divided by 120 (retaining any fractions). Then you must total the FTE count for each calendar month and divide by 12. If you equal or exceed 50, you are subject to the pay or play mandate. In calculating this final number, you will disregard any fractions – thus, if your final average is 49.9, you would round down to 49.

If you are close to meeting the threshold for the 2013 look-back year, you may be able to qualify for special transition relief that allows you to use any 6-consecutive month period during 2013, rather than the whole year. This may allow you the time to apply the measurement period, have several months to analyze the results, determine whether you need to offer a plan, and then choose and establish a plan.

The guidance clarifies that:

- "Employee" for purposes of the mandate means common law employee, which is a concept based on direction and control and is the same as the definition used for purposes of ERISA (it is not the same as the FLSA definition).
- A partner in a partnership (or member in an LLC taxed as a partnership), a sole proprietor, and a 2% or more s-corporation shareholder are not treated as "employees."
- The leased employee rules (which treat leased employees as employees of the service recipient for certain purposes) do not apply.
- The mandate may apply, regardless of whether you are for-profit, non-profit or a government entity (federal, state, local or Indian tribal).
- Special provisions address how to determine the average number of employees for the year and how to count salaried employees who may not clock their hours.
- There are no special rules for high turnover positions (they must still be counted).
- Special anti-abuse provisions have been included for temporary staffing agencies (defined as an entity that is the common law employer of the workers providing services to its clients) in an attempt to deter employers from using temporary staffing agencies to avoid their pay or play obligations (the IRS has asked for comments on whether special safe harbors or other special provisions are needed to address temporary staffing issues).

What If I Employ Seasonal Workers?

This new guidance continues to provide a special rule for seasonal workers, which allows you to avoid the pay or play mandate if you exceed the 50 FTE threshold for 120 days or fewer during the look-back year solely because of seasonal workers. The guidance allows you to use either the 120 days or a four calendar month period for purposes of this special rule. The guidance defines "seasonal worker" as including a worker who performs labor or service on a seasonal basis, retail workers employed exclusively during holiday seasons and, pending further guidance, any other reasonable, good faith interpretation of the statutory definition as adopted by the employer (any such interpretation should be made with the assistance of legal counsel).

Do I Need to Count Employees of Related Organizations?

For purposes of determining whether you meet the threshold to become subject to the pay or play mandate, you must include all employees of all members of your controlled group or affiliated service group (unless you are a governmental entity or church, in which case special exemptions may apply). Thus, if you are part of a larger group of entities with common ownership or you are a subsidiary or parent company, you need to consult with your legal counsel to determine which, if any, of the employees of these other entities must be combined with yours in determining if you meet the threshold.

However, the guidance clarifies that imposition of the penalties will be determined on an individual member basis. Therefore, a member of a controlled group of corporations (or

affiliated service group) that offers health coverage to its own full-time employees and dependents will not be subject to penalties because other members in its controlled group (or affiliated service group) do not offer health coverage to their respective full-time employees. Furthermore, if penalties are imposed on you for not providing health coverage to your employees, then calculation of any penalty will be based on the number of full-time employees employed by you and not by the total number of full-time employees of your controlled group or affiliated service group.

Do I Need to Count My Non-U.S. Workforce?

The guidance clarifies that, in counting hours of service for purposes of determining FTEs, generally only work performed in the U.S. will need to be counted. Thus, if you have fewer than 50 FTEs in the U.S., you should not be subject to the pay or play rules. The guidance further clarifies this point by stating that if you employ workers outside the U.S., regardless of whether they are U.S. citizens, you should generally be able to exclude them.

If I'm a New Employer, Am I Exempt?

No. If you were not in existence during the entire preceding calendar year, you are still subject to the pay or play mandate if it is "reasonably expected" that you will employ an average of at least 50 FTEs on business days during the current calendar year. Note that the IRS is seeking comments on whether to offer safe harbors or presumptions to assist new employers, so additional relief may be included in the final regulations.

Do I Need to Count the Employee of Businesses that I Acquire?

The guidance clarifies that you must count the employees of predecessor employers in determining whether you meet the threshold for the pay or play mandate (the regulations state that rules similar to those used for employment taxes will likely apply to determine the meaning of successor and predecessor – in the meantime, a reasonable, good faith interpretation should be used). Also note that you may have successor liability for any penalties owed by these companies.

Effective date of Pay or Play Rules: Under the original health care reform laws, the pay or play mandate would take effect on January 1, 2014, regardless of whether your plan year or insurance policy operates on a fiscal year. This has been a significant concern for employers who will be renewing plans or policies in 2013 and locking in the terms of their plans and policies until mid-2014. These employers feared that if later guidance was issued that concluded that their current coverage did **not** meet the minimum requirements under the pay or play rules, they would be unable to renegotiate their current insurance contracts and forced to pay penalties.

However, the guidance offers you transition relief if you have group health coverage on December 27, 2012 through a plan that operates on a fiscal year. You will not be subject to the pay or play rules until the first fiscal year beginning in 2014 if either (a) the employee in question was eligible to participate in the plan under its terms as of December 27, 2012 (regardless of whether the employee actually enrolled), or (b) the plan (along with any other plans with the same fiscal year) was offered to at least 1/3 of your full-time and part-time employees at the most recent open enrollment, or (c) the plan (along with any other plans with

the same fiscal year) covered at least ¼ of your employees, looking at any day between October 31, 2012 and December 27, 2012 (it is not clear in the guidance whether this includes both full-time and part-time employees, but we assume it does). The transition relief is **only** available if you offer affordable coverage that provides minimum value to those full-time employees as of the first day of the plan year beginning in 2014 and the employee was not eligible for coverage under any group health plan that had a calendar year plan year.

Thus, for example, an employer who offers coverage under a plan with a plan year ending June 30, 2014 to at least 1/3 of its employees (thus satisfying the transition relief) may wait until July 1, 2014 to expand the plan to offer coverage satisfying the pay or play rules. This is welcome relief for sponsors of fiscal year plans.

Special Rules for Cafeteria Plans: Also note that if you sponsor a cafeteria plan that has a non-calendar year plan year, the guidance offers transitional relief for your employees who have elected to pay pre-tax through the cafeteria plan for the cost of their group health coverage or who chose not to make a pre-tax salary reduction election for group health coverage through the cafeteria plan. Although these elections generally must be irrevocable for the entire plan year unless the employee experiences certain family status change or HIPAA special enrollment events, the guidance permits you to allow an employee participating in your cafeteria plan during the plan year beginning in 2013 to make a one-time election to revoke or change his or her election with respect to group health coverage under the cafeteria plan (presumably, in order for him or her to purchase coverage through an Exchange, but there is no requirement that you verify this).

You may also allow an employee who chose not to pay for pre-tax premiums through the cafeteria plan to elect mid-year to pay the cost of group health coverage through the cafeteria plan (in order for him or her to avoid the individual responsibility payment). You must amend your cafeteria plan by December 31, 2014 to allow for such revocation, changes and mid-year elections, and such amendment may be retroactive.