# Department of the Treasury and the IRS Release Final Regulations on the Affordable Care Act's Employer Shared Responsibility Provisions

On February 10, the Department of the Treasury and the IRS issued final regulations, a fact sheet and a series of Questions and Answers on the Employer Shared Responsibility provisions under section 4980H of the Internal Revenue Code. The final regulations, while generally adhering to the structure and rules set forth in the proposed regulations, provide some significant changes to those rules and announce important transition relief that will affect all employers subject to the provisions.

The proposed regulations were published on December 28, 2012 and were summarized in our alert dated January 3, 2013. Last July, the Department of the Treasury announced that the effective date of the employer shared responsibility provisions would be delayed a year to January 1, 2015. These final regulations announce an additional one-year delay for employers with 50 to 99 full-time equivalent employees and provide added flexibility during the 2015 plan year for employers with 100 or more full-time equivalent employees.

## Structure Largely Unchanged

Applicable large employers (defined as employers with at least 50 full-time employees (including full time equivalents)) may be subject to an assessment under the employer shared responsibility provisions if they either fail to offer coverage to at least 95% of their full-time employees or offer coverage that is either not affordable or does not provide minimum value, and at least one of their full-time employees receives a premium tax credit to help pay for coverage purchased through a health insurance exchange (or marketplace). A full-time employee is an individual working on average at least 30 hours a week. Employers who are members of a controlled group, regardless of the size of their workforce, will be subject to the provisions so long as they collectively employ at least 50 full-time employees (including FTEs). The regulations refer to these employers as "applicable large employer members." The final regulations make no material changes in the affordability and minimum value standards discussed in the proposed regulations, but as described below, they do make changes to other important provisions.

## Notable Changes

While the final regulations adopt many of the rules set forth in the proposed regulations, they also clarify and change a number of rules on which comments were sought. The final regulations provide clarification on topics including:

- which hours count as hours of service;
- how to allocate assessable payments under 4980H among applicable large employer members who employ the same employee;
- how the 130 hours of service monthly equivalency standard should be applied;
- whether an employer's determination of a new hire's full-time status is reasonable is based on facts and circumstances;
- what factors to take into account when determining whether the employer, at the employee's start date, could not determine whether the employee was reasonably expected to average at least 30 hours of service a week during the initial measurement period;

- how temporary staffing firms determine whether their new employees are variable hour employees;
- the impact of changes in employment status on measurement and stability period calculations;
- application of the rules to multiemployer and single employer Taft-Hartley plans and MEWAs; and
- the applicability of 4980H in situations involving foreign operations and international employees.

The final regulations also make the following notable changes:

*Full-Time Employee Status.* The final regulations provide for two methods for measuring whether an employee has sufficient hours of service to be a full-time employee. First, the regulations retain the look-back measurement period introduced in the proposed regulations. Second, they add a monthly measurement period under which an employer determines each employee's status as a full-time employee by counting the employee's hours of service each month.

*Hours of Service.* The proposed regulations explain that an hour of service means each hour for which an employee is paid, or entitled to payment, for the performance of duties and each hour for which the employee is paid, or entitled to payment, for a period of time during which no duties are performed due to vacation, holidays, illness, incapacity and the like. The final regulations exempt from the hour of service definition any hour of service (a) performed by a bona fide volunteer, (b) provided as part of a federal or state work study program, (c) for which non-U.S. source income is earned, or (d) performed by an individual who is subject to a vow of poverty as a member of a religious order when the work is in the performance of tasks usually required of an active member of that order.

*Educational Organizations.* The final regulations also clarify certain issues related to employees of educational organizations. First, they confirm that full-time employees working only during the academic year will not lose their full-time status by virtue of not having hours of service throughout the year. They also retain the requirement that the organizations use a reasonable method of crediting hours of service in cases where compensation is not dependent on hours worked, but the final regulations also provide an optional method for determining an adjunct faculty member's hours of service. Educational organizations can allow credit for (a) 2¼ hours of service per week for each hour of teaching or classroom time and (b) an hour of service per week for each additional hour outside the classroom spent performing required duties, including providing office hours or attending faculty meetings.

*Coverage for Dependents.* The proposed regulations explain that in order to be deemed to be offering coverage, an employer must, among other things, provide coverage to dependents, which are defined as children under Code section 152(f)(1). The final regulations exempt foster children and stepchildren from the definition of dependent for purposes of determining whether an employer offers coverage under section 4980H. They also clarify that, for purposes of section 4980H, a child is a dependent through the end of the calendar month in which he or she turns age 26.

*Effective Opportunity to Accept or Decline Coverage.* The final regulations provide that an effective opportunity to decline coverage is not required for an offer of coverage that provides minimum value and is either offered at no cost to the employee or at a cost, for any calendar month, of no more than 9.5% of a monthly amount determined as 1/12 of the federal poverty line. Furthermore, the final regulations clarify that that an employee's evergreen election under its employer's plan constitutes an offer of coverage.

*Seasonal Employees*. The final regulations define a seasonal employee as an employee hired into a position for which the customary annual employment is six months or less. Customary annual employment means that an employee in the position usually works for a period of no more than six months and that the period begins each year in approximately the same part of the year.

*Rehire and Break-in-Service Rules*. The final regulations retain the rehire rules from the proposed regulations but reduce the length of the break-in-service required before a returning employee may be treated as a new employee from 26 weeks to 13 weeks, except that the 26-week break-in-service period will continue to apply to educational organizations. Although the proposed regulations sought comments on whether the averaging rules for special unpaid leaves and employment break periods available to educational organizations should be extended to other industries, the final regulations do not adopt this rule for any other industries.

## Transition Rules

Importantly, the final regulations adopt, with some modification, the transition rules in place in the proposed regulations with respect to (a) the application of section 4980H for the 2015 plan year to applicable large employers with non-calendar year plans, (b) shorter measurement periods for stability periods starting in 2015, (c) a shorter period for determining applicable large employer status for 2015, and (d) adding coverage for dependents for the 2015 plan year.

The final regulations also provide the following additional transition relief:

*Offer of Coverage for January 2015*. If an applicable large employer member offers coverage to a full-time employee no later than the first day of the first payroll period that begins in January 2015, the employee will be treated as having been offered coverage for January 2015.

*Applicable Large Employers with Fewer than 100 Full-Time Employees*. Applicable large employers with at least 50 but fewer than 100 full-time equivalent employees (including FTEs) are exempt from the requirements of section 4980H for all of 2015 plus, in the case of any non-calendar year plan that begins in 2015, the portion of the 2015 plan year that falls in 2016. In order to be eligible for this transition relief, during the period from February 9, 2014 through December 31, 2014 the employer must not (a) reduce the size of its workforce or the overall hours of service of its employees in order to satisfy the workforce size conditions or (b) eliminate or materially reduce the health coverage it offered as of February 9, 2014. Furthermore, the employer must certify that it qualifies for the transition relief on the forms it is required to file with the IRS under Code section 6056.

*Relief under section 4980H(a)*. For each calendar month during 2015 and any calendar months during the 2015 plan year that fall in 2016, an applicable large employer member that offers coverage to at least 70% of its full-time employees and, to the extent required, their dependents, will be deemed to be offering coverage and will not be subject to an assessable payment under section 4980H(a). The temporary reduction in the threshold from 95% to 70% gives applicable large employer members a cushion for the 2015 plan year to identify their full-time employees and establish policies for providing coverage to them. Applicable large employer members qualifying for this transition relief continue to be subject to a potential assessable payment under section 4980H(b) should the employer offer coverage that either is not affordable or does not

provide minimum value to an employee who receives a premium tax credit for coverage purchased on the exchange.

## Conclusion

The final regulations, through the detail provided and the transition relief offered, recognize that work schedules and hiring patterns are far from uniform, making application of a general set of principles challenging. In recognition of these challenges, the preamble to the final regulations states explicitly that the Treasury Department and the IRS anticipate that future guidance of general applicability will address open questions and principles that may need to be further developed.

If you wish to discuss how these final regulations impact your health care benefits, please contact a member of the employee benefits practice, the benefits consulting group or your usual Ropes & Gray advisor.