OEBB Health Care Reform Update

Affordability Provision: Determining the ACA's Employer Shared Responsibility Penalties

A presentation by Towers Watson for OEBB entities

March 19, 2015

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Today's discussion

- Welcome and Introductions
- The Shared Responsibility Provision
  - The "Pay" Penalty
  - The "Play" Penalty
- Affordability Rules — Subsidies and Employer Safe Harbors
  - Employer Safe Harbors
  - Composite Rates
  - Flex Credits
  - Examples
- Next Steps
- Questions?

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The Shared Responsibility Provision

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Shared Responsibility and Affordability Guidance

- Final regulations entitled "Shared Responsibility for Employers Regarding Health Coverage; Final Rule" were issued on February 12, 2014
  - These regulations established the pay or play rules related to measurement, reporting and potential penalties associated with full-time employees
  - Additional guidance has appeared in the form of IRS Notices and FAQs
- Final regulations entitled "Minimum Essential Coverage and Other Rules Regarding the Shared Responsibility Payment for Individuals" were issued on November 26, 2014
  - These regulations clarified certain definitions, including minimum essential coverage, and application of the pay and play penalties for employers for 2015 and 2016, as well as a safe harbor update for the affordability test
  - These regulations directly addressed the impact of flex credits for affordability determinations

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The Pay Penalty

- A large employer must offer coverage to 95% of its full-time employees to avoid the $2,000 “pay” penalty (note: the threshold is relaxed to 70% for the 2015 plan year)
  - For the 2015 OEBB plan year, a large employer means 100 or more full-time employee equivalents; beginning with the 2016 plan year a large employer means 50 or more full-time employee equivalents
  - The pay penalty for missing the threshold is $2,000 x the number of all full-time employees (if at least one full-time employee gets subsidized coverage in the exchange)
    - Threshold is calculated monthly and the penalty is pro-rated (≈$167/month)
    - The penalty is not based upon full-time employee equivalents; an employer can only be assessed penalties for full-time employees
    - An employer can subtract the first 80 full-time employees when calculating the pay penalty for 2015; this reverts to 30 beginning with the 2016 plan year
    - Example 1 (2015 plan year): An entity who offers coverage to fewer than 140 of its 200 full-time employees (140/200 = 70%) would be subject to an annual penalty of $240,000 [(200 – 80) x $2000 = $240,000]
    - Example 2 (2016 plan year): An entity who offers coverage to fewer than 190 of its 200 full-time employees (190/200 = 95%) would be subject to an annual penalty of $340,000 [(200 – 30) x $2000 = $340,000]

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The Play Penalty

- Employers who meet the minimum threshold for offering coverage to full-time employees avoid the "pay" penalty but may still be subject to the $3,000 "play" penalty
- The play penalty occurs if:
  - A full-time employee is not offered coverage and gets subsidized coverage in the exchange; or
  - A full-time employee is offered coverage that either does not meet a minimum value requirement or an affordability test and the employee gets subsidized coverage in the exchange
    - Minimum Value — The plan must have an actuarial value of at least 60% (All OEBB plans meet this requirement)
    - Affordability — The cost for single only coverage for the least expensive option should not cost the employee more than 9.5% of his or her household income (please see slide #10 for a discussion of affordability safe harbors)
- The play penalty is $3,000 ($250/month) for each affected full-time employee who obtains subsidized coverage through an exchange

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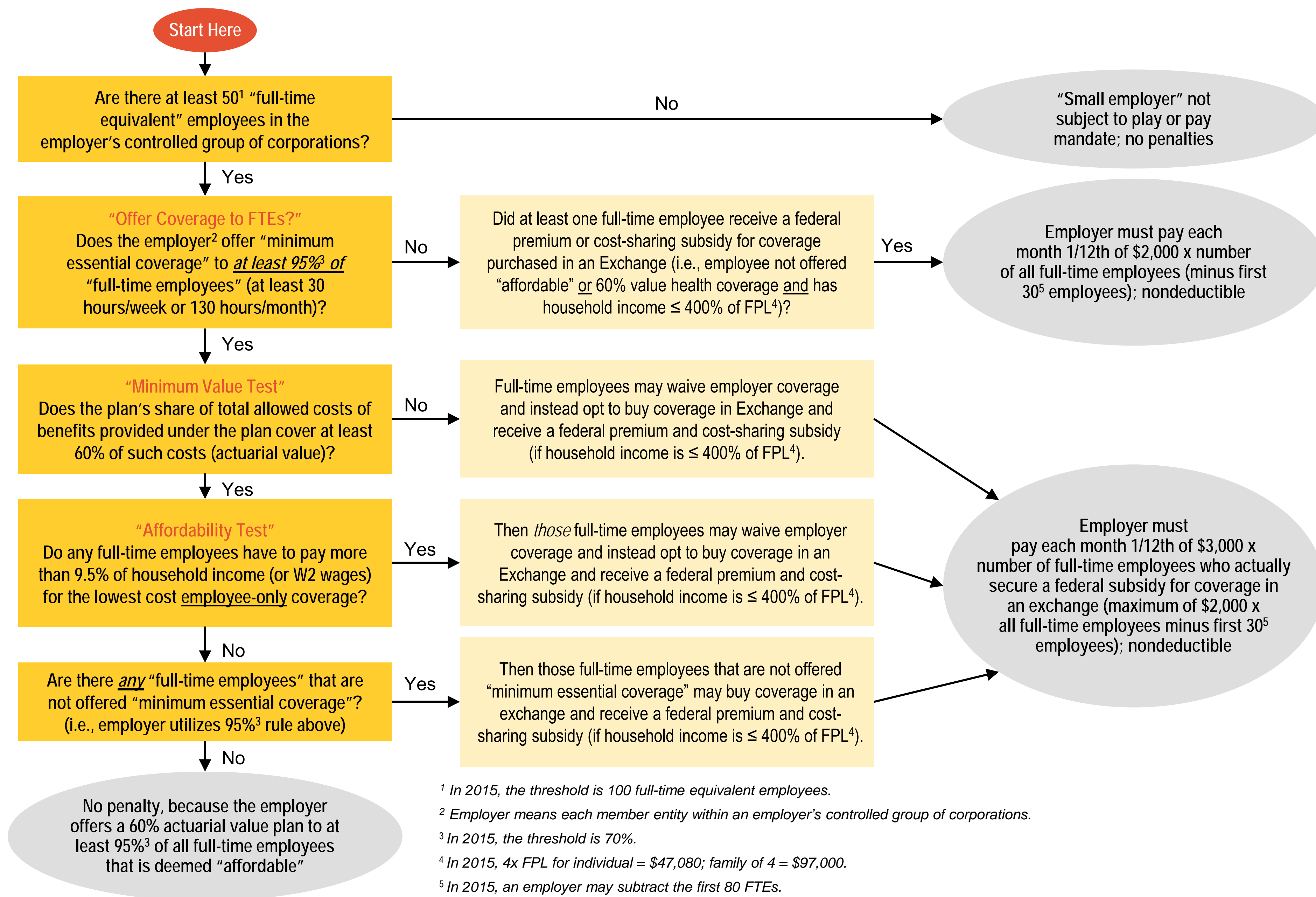
The Pay or Play Penalty Roadmap



[1] *In 2015, the threshold is 100 full-time equivalent employees.*

[2] *Employer means each member entity within an employer's controlled group of corporations.*

[3] *In 2015, the threshold is 70%.*

[4] *In 2015, 4x FPL for individual = $47,080; family of 4 = $97,000.*

[5] *In 2015, an employer may subtract the first 80 FTEs.*

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Passing the Affordability Test

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The Affordability Rules

- **Affordability when Determining Subsidy Eligibility** — Affordability is based upon whether the individual has access to minimum essential coverage within an indexed percentage of their household income (9.56% in 2015). Household income is generally adjusted gross income.
  - Household income is typically based upon individual's prior tax year but changing circumstances (e.g., loss of employment) can be taken into account
- Affordability can be satisfied by offering a plan option that is considered affordable, even if the employee does not elect that plan option
  - This means that an entity that enables employees to select from the full array of OEBB plans will be able to use the plan with the lowest employee only premium contributions (OEBB Plan H) for purposes of determining if the plan is "affordable"
  - Also, the affordability test looks at the premium contribution requirement for **employee-only coverage**, even if the entity has a tiered rate structure and the employee selects family coverage
  - In other words, the separate cost of dependent coverage doesn't impact an employer for affordability purposes (but see The Affordability Rules — Composite Rates)

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The Affordability Rules — Subsidies and Employer Safe Harbors

- **Affordability Safe Harbors for Employers to Avoid Penalties** — An employer may avoid potential penalties through three affordability safe harbors. These safe harbors remain calculated at 9.5% and did not rise to 9.56% for 2015 (this value is not indexed in the statute).
    1. W-2 — Based on current year; will not take pre-tax exclusions into account
    2. Rate of Pay — Avoids pre-tax exclusion problem; Salaried employees' rate of pay fixed at beginning of year and cannot be lowered; Hourly employees' rate of pay determined as (hourly rate x 130 hours/month) and hourly rate can fluctuate
    3. Federal Poverty Limit — Based on current year

- An employer may use the same safe harbor for all its employees or vary the use of safe harbors based upon any "reasonable category of employees" provided the employer does so on a uniform and consistent basis for all employees within a particular category
    - "Reasonable category of employees" can generally be based upon: specific job categories, nature of compensation (hourly/salaried), geographic location or similar bona fide business criteria

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Safe Harbor Test I: Form W-2 Safe Harbor

- An employer satisfies the W-2 safe harbor if:
  - The employee is offered a plan for which the required annual premium contribution for employee-only coverage is less than 9.5% of that employee's wages for the calendar year, as reported in Box 1 of Form W-2
- Notes:
  - Box 1 of the Form W-2 excludes elective deferrals that an employee makes into an IRC § 401(k) plan or § 403(b) plan and also excludes amounts that an employee elects to contribute on a pre-tax basis for qualified benefits under a cafeteria plan
  - Box 1 of the Form W-2 reflects earnings for a calendar year even though OEBB plan years run October – September
  - If used, an entity will need to rely on the 2015 W-2 for purposes of establishing affordability in connection with the 2015 reporting requirements (estimate for testing prior to year end)

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Safe Harbor II: Rate of Pay Safe Harbor

- An employer satisfies the rate-of-pay safe harbor if the employee is offered a plan for which the monthly premium contribution for employee-only coverage is less than 9.5% of his or her **monthly pay**
  - For *hourly* employees, the monthly pay amount = Employee hourly rate of pay x 130 hours
  - For *salaried* employees, monthly salary is used
- Solely for this purpose, an employer may use any reasonable method for converting payroll periods to monthly salary
- An employer can use the rate of pay safe harbor even if an hourly employee's rate of pay is reduced during the year. The employee's required contribution may be based on the lower of the employee's hourly rate as of the beginning of the year or the employee's rate of pay for the calendar month multiplied by 130 hours.
- A reduced rate of pay during the year cannot be applied to salaried employees. In other words, the rate of pay for a salaried employee is fixed as the beginning of the year.
- In contrast to the W-2 safe harbor, the rate of pay safe harbor doesn't exclude elective pre-tax deferrals

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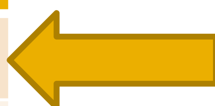
Safe Harbor Test III: Federal Poverty Level (FPL) Safe Harbor

- An employer satisfies the FPL safe harbor if:
  - The employee is offered a plan for which the monthly premium for employee-only coverage is less than 9.5% of the Federal Poverty Level for a single individual, divided by 12
  - The final regulations clarified that with the FPL safe harbor, employers can use the guidelines in effect six months prior to the beginning of the plan year in order to give employers enough time to establish premium amounts in advance of the plan's open enrollment period
- 2015 Poverty guidelines for the 48 contiguous states and the District of Columbia:

Persons in the family/household	Poverty guideline
1	$11,770
2	15,930
3	20,090
4	24,250



- 9.5% of $11,770 = $1,118.15
- $1,118.15 / 12 = $93.18

- If the employee's contribution for the lowest cost option is less than $93.18 per month for employee only coverage, the entity will satisfy the FPL Safe Harbor

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The Affordability Rules — Composite Rates

- Composite vs. tiered rating:
  - Employers that use composite rating need to pay special attention to the affordability rules
  - With the tiered rating structure, the affordability will be assessed on the employee-only cost of coverage for the lowest plan option
  - With composite rates, the full composite rate will be used to determine whether the plan is considered affordable
  - What does this mean?
    - Employees who are at the lower end of the pay scale are more likely to have an unaffordable premium contribution if the entity uses a composite premium rate structure
    - OEBB entities should consider moving to a tiered rating structure to better meet affordability rules

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The Affordability Rules — Flex Credits

- Flex credits can be applied towards the affordability calculation if all of the following are true:
  - The employee does not have the option to take the flex credit as a taxable benefit (i.e., cash)
  - The flex credit may be used to purchase minimum essential coverage
  - The flex credit may only be used to pay for benefits providing medical care under Internal Revenue Code §213
- The November 26, 2014 regulations view a combination of flex credits and an opt-out waiver credit as the ability to take the flex credit as a taxable benefit
  - This means employers providing an opt-out waiver credit may not count flex credits toward their affordability calculations; it does not matter if the opt-out waiver credit is only a portion of the overall flex credit
  - The IRS has informally indicated that it is considering whether the value of the opt-out waiver credit should be *added* to the cost of employee-only coverage for affordability calculation purposes
- Employers should be careful to limit the use of flex credits to benefits providing medical care (e.g., medical, dental, vision, HCFSA)

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The Affordability Rules — Examples

Example 1
Entity A offers all OEBB plans. Plan H is the lowest cost plan, and the employee only premium amount is $353 per month. Entity A provides $500 per month in flex credits that may be used toward the purchase of medical, dental, vision and HCFSA coverage. Entity A does not provide an opt-out waiver credit for any full-time employee who waives coverage.
Affordability Concerns
• The lack of an opt-out waiver credit means that Entity A's flex credits do count toward lowering the cost of medical coverage for affordability calculation purposes
Affordability Calculation
• Because the $500 fully covers the cost for single only coverage for Plan H, the employee's premium share is $0/month
• The coverage is automatically affordable under the FPL safe harbor because the employee premium share is less than $92/month (9.5% of 2015 FPL is ≈$92.18/month which is greater than $0/month)

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The Affordability Rules — Examples

Example 2

Entity B uses a composite rate structure and offers all OEBB plans. Plan H is the lowest cost plan option with a premium of $841. Entity B provides $900 per month in flex credits that may be used toward the purchase of medical, dental, vision and HCFSA coverage. Entity B does not provide an opt-out waiver credit for any full-time employee who waives coverage.

Affordability Concerns

- The lack of an opt-out waiver credit means that Employer B's flex credits do count toward lowering the cost of medical coverage for affordability calculation purposes

Affordability Calculation

- Because the $900 fully covers the cost for single only coverage for Plan H, the employee's premium share is $0/month
- The coverage is automatically affordable under the FPL safe harbor because the employee premium share is less than $92/month (9.5% of 2015 FPL is ≈$92.18/month which is greater than $0/month)

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The Affordability Rules — Examples

Example 3

Entity C offers all OEBB plans. Plan H is the lowest cost plan, and the employee only premium amount is $353 per month. Entity C provides $500 per month in flex credits that may be used toward the purchase of medical, dental, vision and HCFSA coverage. Entity C provides a $100 per month opt-out waiver credit for any full-time employee who waives coverage.

Affordability Concerns

- The opt-out waiver credit means that Entity C's flex credits do not count toward lowering the cost of medical coverage for affordability calculation purposes

Affordability Calculation if Opt-Out Credit Does Not Count

- According to the affordability calculation rules, the employee's premium share for Plan H (single only coverage) is $353/month
- The coverage is affordable for an individual with approximately $44,589 in annual compensation using the W-2 or Rate of Pay safe harbors (FPL is not available)
  - ($353/.095) x 12 = $44,589

Affordability Calculation if Opt-Out Credit Does Count (based upon informal IRS guidance)

- According to the affordability calculation rules, the employee's premium share for Plan H (single only coverage) is $453/month
- The coverage is affordable for an individual with approximately $57,221 in annual compensation using the W-2 or Rate of Pay safe harbors (FPL is not available)
  - ($453/.095) x 12 = $57,221

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The Affordability Rules — Examples

Example 4

Entity D uses a composite rate structure and offers all OEBB plans. Plan H is the lowest cost plan option with a premium of $841. Entity D provides $900 per month in flex credits that may be used toward the purchase of medical, dental, vision and HCFSA coverage. Entity D provides a $100 per month opt-out waiver credit for any full-time employee who waives coverage.

Affordability Concerns

- The opt-out waiver credit means that Entity D's flex credits do not count toward lowering the cost of medical coverage for affordability calculation purposes

Affordability Calculation if Opt-Out Credit Does Not Count

- According to the affordability calculation rules, the employee's premium share for Plan H (single only coverage) is $841/month
- The coverage is affordable for an individual with approximately $106,232 in annual compensation using the W-2 or Rate of Pay safe harbors (FPL is not available)
  - ($841/.095) x 12 = $106,232

Affordability Calculation if Opt-Out Credit Does Count (based upon informal IRS guidance)

- According to the affordability calculation rules, the employee's premium share for Plan H (single only coverage) is $941/month
- The coverage is affordable for an individual with approximately $118,863 in annual compensation using the W-2 or Rate of Pay safe harbors (FPL is not available)
  - ($941/.095) x 12 = $118,863

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Next Steps

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Next Steps

- Perform the affordability tests based on the lowest premium cost plan for employee-only coverage you offer using each of the safe harbor tests:
  - Form W-2 safe harbor
  - Rate of Pay safe harbor
  - Federal Poverty Level safe harbor
- If you determine that you cannot pass the affordability test under any of the safe harbors, consider whether you are offering all of the OEBB plans (included option G/H).
- If you are using composite premium rates and you don't pass the affordability test, retest using the employee-only rate of the tiered rate structure for the lowest cost OEBB plan. If you pass using the tiered rates, consider using the tiered rate structure for all employee groups for the next plan year.
- If you are using flex credits toward the purchase of coverage and cannot pass the affordability test under any of the safe harbors, discontinue the use of an opt-out waiver credit.

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Questions

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