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Update on the PPACA – IRS Proposed Regulations on the Employer Mandate Tax

Introduction

On December 28, 2012, the IRS issued proposed regulations related to the employer mandate tax that was enacted by the Patient Protection and Affordable Care Act (PPACA) – Internal Revenue Code Section 4980H. That tax is effective in calendar year 2014.

In general, the proposed regulations are favorable for employers. There are reasonable interpretations of the law and attempts to ease administration of this very complex tax law. Given lead times necessary for making changes to health care plans for the 2014 calendar year, employers should begin examining the details of the proposed regulations early in 2013.

This report provides highlights of the proposed regulations.

Employee Determinations

Employee status will be determined under common law rules – the employer of a worker is the person who has the right to direct and control the rendition of the services.

- Under this standard, an employee leasing agency might not be considered the employer.
- Partners in partnerships, directors and 2% shareholders in S Corporations are not considered to be employees.
- The regulations appear to be intended to provide that the tax will not apply to expatriate employees.

Applicable Large Employer Determinations

The tax only applies to an employer with 50 or more full-time employee equivalents on business days in the preceding calendar year (an “applicable large employer”).

- Controlled group rules generally apply to determine if there are 50 employees.
- Employees working outside of the US are not counted. Thus, small US operations of foreign companies may be exempt.
- A transitional rule allows an employer to make its 2013 calculations on any period of at least six consecutive months, instead of the entire 2013 calendar year.

Determination and Imposition of the Tax

The tax will be applied separately to each member of a controlled group of companies. However, there is no liability of other controlled group members for non-payment of the tax.

- The tax will be applied to employers that otherwise are disregarded entities for tax purposes.

Full-Time Employee Determinations

The tax only applies with respect to employees who are "full-time employees". A full-time employee is one who averages 30 hours or more per week.

- For new employees who are not seasonal employees, a reasonable good faith determination must be made as to full-time employee status. Unless the employee is seasonal, the expected term of employment is not considered.
- Special rules are provided for seasonal employees and new employees who cannot reasonably be determined to be full-time (variable hour employees).
- A special look back rule is provided for determining if variable hour, seasonal and ongoing employees are "full-time employees".
    - The employer looks back to a previous "standard measurement period" (three to 12 months) to determine hours of service and full-time employee status.
    - The result (full-time or not full-time) is applied going forward for a "stability period" (minimum of six months, not more than 12 months, and not less than the measurement period).
- Special rules are being considered for employees of educational organizations, commissioned sales people, pilots and other professions.
- Special transitional rules can apply for determinations being made for the 2014 calendar year.

The First Tier Tax

The first tier of the tax is $2,000 for each full-time employee in excess of 30. To avoid the first tier tax, the employer must offer a medical plan that has minimum essential coverage (MEC) to all full-time employees and their dependents.

- The term dependent is being interpreted to only include an employee's children under age 26. Coverage does not have to be offered to spouses.
- This provision of the law will be satisfied if coverage is offered to 95% of the full-time employees.
- If there is a controlled group of corporations or other organizations, the 30 employee exemption is split among the controlled group members based on their full-time employee counts.

The Second Tier Tax

If the first tier tax does not apply, the second tier tax ($3,000) can apply for each full-time employee who opts out of the employer plan, obtains coverage through an Exchange, and is entitled to receive a premium tax credit or reduced cost-sharing. To receive a premium tax credit or reduced cost-sharing, the employee's household income must be between 100% and 400% of the federal poverty line.

However, the second tier tax cannot apply with respect to a full-time employee if (i) the employee is offered minimum essential coverage under an employer plan, (ii) the plan provides minimum value (i.e., the plan pays at least 60% of plan costs) and (iii) the cost to the employee for single coverage is "affordable" (i.e., the employee is not charged more than 9.5% of household income).

- The regulations clarify that it is only the employee's coverage that is examined for the second tier tax. Thus, the tax is not triggered if dependents are covered under an Exchange.
- There are three safe harbor methods an employer can use to determine if its plan will be

considered to be affordable. The is automatically deemed to be affordable if the amount being charged to an employee does not exceed 9.5% of either:

- The employee's taxable wages in Box 1 of the Form W-2,
- The employee’s standard rate of pay, or
- The federal poverty line (currently $11,170)

Form W-2 reporting

New Form W-2 reporting requirements will apply for the entire 2014 calendar year, beginning in January of 2015. Additional regulations are to be issued relating to Form W-2 reporting.

Transitional Rules

Other special transitional rules are provided for:

- Medical plans that do not operate on the basis of the calendar year.
- Cafeteria plan salary reduction election changes during 2014.
- Multi-employer plans.

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