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Employee Benefits | Life Insurance | Risk Management

INSURANCE BRIEF

INSIDE THIS ISSUE:

Pay or Play Regulations

On Friday, December 28, 2012, the Internal Revenue Service (IRS) released a proposed Pay or Play Rule regulation. The proposed regulations incorporate guidance that was previously provided by the IRS on the Patient Protections and Affordable Care Act (PPACA) shared responsibility requirements, with some modifications. Specifically, the regulations include the provisions of Notice 2012–58 as well as many of the provisions of Notices 2011–36, 2011–73 and 2012–17.

The proposed regulations also contain guidance on additional issues associated with PPACA's shared responsibility requirements, notably they:

- Provide transition relief for non-calendar year plans;
- Expand the safe harbor options for determining whether an employer's health coverage is affordable; and
- Clarify how the shared responsibility penalty applies to members of a controlled group.

The IRS also released a series of questions and answers on the new regulation.

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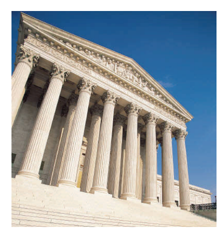
Transit Limits



The fiscal cliff legislation known as the American Taxpayer Relief Act of 2012 was signed into law on January 2, 2013. Included in this Act was an amendment to the Internal Revenue Code (IRC) Section 132(f) which provides for pre-tax treatment of transit benefits. Parity for transit and parking benefits has been extended until December 31, 2013. This raises the transit limit for 2013 to $240 from $125. This is welcome relief for BART riders travelling more than a few stops as the old limits were too low to cover their costs.

Although this amendment is retroactive to January 1, 2012, it is too late for employees to benefit from this increase for the 2012 year without the IRS issuing some form of transitional relief. The existing IRC requires that monies be withheld in the same month that they are expended. Furthermore, participants cannot use monies withheld in one Plan year for expenses incurred in a different Plan year.

The IRS has yet to announce whether a cost of living adjustment will be made for parking and transit for 2013. Stay tuned!

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Pay or Play Regulations *cont'd*

Effective Date: The new regulation is effective immediately. Employers can rely upon it until the final regulations are issued.

Key Provisions:

Transition relief for non-calendar year Plans. The proposed regulations provide transition relief for employers that, as of Dec. 27, 2012, offer health coverage under plans that operate on a non-calendar year basis. The regulations call these health plans "fiscal year plans." The proposed regulations note that this transition relief is provided because employers with fiscal year plans may have difficulty complying with PPACA's "pay or play" rules on Jan. 1, 2014. There are two components to the transition relief for fiscal year plans.

First, the transition relief applies with respect to employees who would be eligible for employer-sponsored coverage as of the first day of the fiscal plan year starting in 2014 under the plan's eligibility terms as in effect on Dec. 27, 2012. If these employees are offered affordable, minimum value coverage no later than the first day of the plan year starting in 2014, the employer will not be assessed a shared responsibility penalty with respect to these employees for any period in 2014 prior to the beginning of the plan year that starts in 2014 and runs into 2015.

Second, transition relief applies to employers that have a significant percentage of their employees who are eligible for or covered under one or more fiscal year plans with the same plan year. If an employer has at least one-quarter of its employees covered under a fiscal year plan (or if the employer offered coverage under the plan to at least one-third of its employees during the most recent open enrollment period before Dec. 27, 2012), the employer will not be subject to a shared responsibility payment with respect to any of its full-time employees until the first day of the plan year starting in 2014, provided that those full-time employees are offered affordable coverage that provides minimum value no later than that first day.

For example, if during the most recent open enrollment period before Dec. 27, 2012, an employer offered coverage to at least one-third of its employees under a plan with a plan year starting July 1, 2013, the employer could avoid liability for a shared responsibility payment if, by July 1, 2014, it expanded the plan to offer coverage satisfying PPACA's shared responsibility provisions to the full-time employees who had not been offered coverage.

Affordability safe harbor. In general, an employer's coverage is considered unaffordable under PPACA if the employee's required contribution for self-only coverage exceeds 9.5 percent of the employee's annual household income for the calendar year. The IRS recognizes that an employer will generally not know an employee's household income. Thus, in Notice 2011-73, the IRS outlined a safe harbor under which an employer could determine affordability based on whether the employee's required contribution exceeds 9.5 percent of his or her Form W-2 wages.

The proposed regulations provide additional guidance on the Form W-2 safe harbor and establish two additional safe harbors for determining affordability – the rate of pay safe harbor and the federal poverty line (FPL) safe harbor.

Rate of Pay Safe Harbor – Under this safe harbor, affordability is determined based on an employee's rate of pay. For salaried employees, the employer would use the employee's monthly salary to determine affordability. For hourly employees, the employer would multiply the employee's hourly rate of pay by 130 hours per month and determine affordability based on the resulting monthly wage amount. The employee's monthly contribution amount (for self-only coverage) is affordable if it is equal to or lower than 9.5 percent of the computed monthly wages.

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Regulatory Agenda of DOL and IRS

On December 24, 2012, the Department of Labor (DOL) updated its 2012 Semi-Annual Regulatory Agenda. Below is a chart showing those items which relate to health care and certain other employer benefits. Also included in the chart are items from the Internal Revenue Service (IRS) Business Plan. Projects added to the agendas since they were last published are shown in bold.

Guidance Project	IRS	DOL	Projected Date (DOL only)	On Agenda Since:
Guidance under §45R small employer health insurance credit as added by Patient Protection and Affordable Care Act (PPACA)	X			12/2012
Final regulations on cafeteria plans under §125	X			9/2008
Guidance under §223©(2)(C) on Health Savings Accounts (HSAs) regarding certain services required to be provided without cost sharing	X			12/2012
Regulations amending §1.419A-2T relating to collectively bargained welfare benefit funds	X			12/2012
Guidance on the employee retention credit under §1400R (for employers affected by hurricanes Katrina, Rita and Wilma)	X			11/2009
Regulations under §§3101(b), 3102(f), and 1401(b) on additional Medicare tax on employees and self-employed individuals, as added by PPACA	X			9/2011
Final regulations under §§4375-4377, as added by PPACA, regarding fees on insured and self-insured health plans to fund the Patient-Centered Outcomes Research Trust Fund	X			12/2012
Regulations under §4980G on interaction of §4980G and §125 with respect to comparable employer contributions to employees' HSAs	X			9/2008
Regulations on shared responsibility for employers regarding health coverage under §4980H, as added by §1513 of PPACA	X			12/2012
Regulations on the reporting requirements under §6056, added by PPACA	X			9/2011
Guidance relating to coverage of preventive services under PPACA		X	12/2012 (Proposed regulation)	12/2012
Incentives for nondiscriminatory wellness programs in group health plans		X	1/25/2013 (Comment period ends)	12/2012

CA In-

Pay or Play Regulations *cont'd*

FPL Safe Harbor – This safe harbor determines affordability based on the FPL for a single individual. If the employee's cost for self-only coverage under the employer's health plan does not exceed 9.5 percent of the FPL for a single individual, the coverage is considered affordable.

Controlled Group Rules. The proposed regulations provide that all members of a controlled group are combined for purposes of determining whether any member of the group is a large employer subject to ACA's shared responsibility provisions. However, the proposed regulations clarify that controlled group members are treated separately for purposes of determining whether an employer owes a penalty and the amount of the penalty. Thus, employers will not automatically be subject to a "pay or play" penalty just because an employer in their controlled group is subject to the penalty. Also, the penalty is computed separately for each member, taking into account that member's offer of coverage (or lack thereof) and based on that member's number of full-time employees.

Measurement Period Relief. The IRS noted that employers who wish to adopt a 12-month measurement period and a 12-month stability period will have "time constraints" due to the regulation just being released now. The transition rule allows an employer to adopt a shorter measurement period (such as six months) but keep the longer stability period (such as 12 months). To rely on this transition rule, the transition measurement period must be at least six months long, must begin no later than July 1, 2013 and must end no earlier than 90 days before the first day of the plan year beginning on or after January 1, 2014.

Large Employer Determination Relief. Some employers will be close to 50 full-time (and full-time equivalent) employees. These employers may need extra time to determine if they are subject to the Pay or Play Rule. The IRS has provided a transition rule for these employers. The transition rule allows an employer the option to determine its "large employer" status with respect to a period of at least six consecutive calendar months in the 2013 calendar year (rather than the entire 2013 calendar year). This will be very helpful for such employers.

De Minimis Rule. Employers have long been concerned that they could face a large penalty if they accidentally fail to cover just one full-time employee. The proposed regulations clarify that a large employer is liable for a penalty if the employer does not offer health coverage which is affordable and of value, or offers coverage to less than **95 percent** of its full-time employees (and dependent children), and at least one full-time employee receives a premium tax credit to help pay for coverage through an insurance exchange.

No Need to Offer Spousal Coverage. In order to avoid a Pay or Play Rule penalty, an employer must offer coverage to full-time employees and their "dependents." The regulation requires that coverage be offered to an employee's child who has not yet attained age 26. However, "dependent" does not include a spouse or, presumably, a domestic partner. Under a special transition rule, an employer does not need to offer dependent coverage in 2014, as long as it "takes steps" in 2014 to provide such coverage for the 2015 plan year.

Special Rule for Teachers and Employees on Unpaid Leave. One difficult question under the Pay or Play Rule had been how to determine an employee's hours of service when an employee was on unpaid leave (such as FMLA or USERRA leave) or when an employee worked for only a portion of the calendar year (such as a teacher who does not work during the summer). The regulation provides a special rule whereby an employer may ignore the period of the unpaid leave when averaging the hours, or, alternatively, provide a "credit" for hours worked during that time (even though no hours were, in fact, worked).

Educational institutions are subject to this general rule and an additional special rule. When such institutions have an

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Pay or Play Regulations *cont'd*

"employment break period" lasting at least four consecutive weeks (such as summer vacation), that period is ignored when determining an employee's hours of service. The IRS is still considering whether employers other than educational institutions may be subject to a similar rule.

Change in Employment Status. A new variable hour employee or new seasonal employee may sometimes have a change in employment status during the initial measurement period. For example, a seasonal employee may be "promoted" to full-time status. If so, the employer generally must treat the employee as a full-time employee by the first day of the fourth month following that change in status. Although this rule may not seem difficult, it likely will increase administrative complexity for employers. Now, employers (especially those with operations in multiple states and far-flung human resource departments) must regularly monitor each variable hour or seasonal employee's current status to determine if the status has changed to "full-time."

Rehired Employees. Many employers will hire an employee, have them work for a few months, terminate the employee, then rehire that employee a few weeks or months later. Does each rehire create a separate, new initial measurement period for that employee?

Under the new regulation, the answer is generally no, unless one of two exceptions apply. First, the employer can treat the rehired employee as a "new" employee if the person had a break in service of at least 26 weeks. Second, the employer may apply a "rule of parity" for a break which is less than 26 weeks. Under this rule of parity, an employee may be treated as a new employee if the employee's period of time with no credited service is at least four weeks long and is longer than the employee's immediately preceding period of employment. For example, suppose Employee B works for Client Co. for three weeks, then terminates employment. B is rehired 10 weeks later. Client Co. can treat B as a new employee because the 10-week period with no credited hours of service: (1) is at least four weeks long; and (2) is longer than the immediately preceding three-week period of employment. If a rehired employee cannot be treated as a "new" employee, the employee must be offered health plan coverage as soon as administratively practicable.

Anti-Abuse Rules. In a few places, the regulation imposes new "anti-abuse" rules. For example, an employer may not use an equivalency method for determining hours worked by an employee if the method would "substantially understate" an employee's hours of service. Similarly, the IRS specifically notes that an employer cannot have a single employee work 20 hours per week as the employer's "employee" and an additional 20 hours per week as the "employee" of a temporary staffing agency. The effect of such an arrangement, if it had been allowed, is that the employee would have been working "full-time" hours (40 hours per week) but would not have been any employer's "full-time" employee.

<u>What's Next</u>: Open items which are raised — but not answered — in the new regulation include: what type of coverage constitutes "minimum essential coverage"; how to determine "minimum value"; how the rules apply to "successor" employers; the exact definition of a "seasonal" employee; whether special rules should be created for "short-term" employees or "high-turnover" positions; whether special rules should apply for temporary staffing agencies; how exactly the Pay or Play Rule applies to employers who contribute to multiemployer plans; reporting requirements on the employer's health plan coverage; and how hours of service are calculated for certain industries (e.g., airline pilots and for colleges that pay professors based on course credits taught, not on hours worked).

We will continue to update you as regulations are published. Please contact your SML Account Team if you have any questions.