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ACA Mandates—Different Measures of Affordability

Several key reforms under the Affordable Care Act (ACA) measure the affordability of employer-sponsored health coverage. Effective for 2014, the affordability of an employer's plan may be assessed in the following three contexts:

- The **shared responsibility penalty** for applicable large employers (also known as the pay or play rules or the employer mandate);
- An exemption from the tax penalty imposed on individuals who fail to obtain health insurance coverage (also known as the **individual mandate**); and
- The **premium tax credit** for low-income individuals to purchase health coverage through an ACA Exchange.

Although all of these ACA mandates involve an affordability determination, the test for affordability varies for each provision. This Legislative Brief summarizes the different measures of affordability for these key ACA mandates.

On July 24, 2014, the Internal Revenue Service (IRS) released Revenue Procedure 2014-37 (Rev. Proc. 2014-37) to index the ACA's affordability contribution percentage for 2015. For plan years beginning in 2015:

- Employer-sponsored coverage will generally be considered affordable under **both the pay or play rules and the premium tax credit eligibility rules** if the employee's required contribution for self-only coverage does not exceed **9.56 percent** of the employee's household income for the year. However, applicable large employers using an affordability safe harbor **may have to continue using a contribution percentage of 9.5 percent** to measure their plan's affordability in 2015.
- Coverage is unaffordable for purposes of **the individual mandate exemption** if it exceeds **8.05 percent** of household income.

OVERVIEW

ACA MANDATE	SUMMARY	AFFORDABILITY MEASURE FOR EMPLOYEES	AFFORDABILITY MEASURE FOR FAMILY MEMBERS
Employer Shared Responsibility Penalty	Applicable large employers that do not offer health coverage to their full-time employees and dependents, or offer coverage that is either unaffordable or does not provide minimum value, may be subject to a penalty.	Coverage is affordable if the employee portion of the premium for the lowest-cost, **self-only coverage** that provides minimum value does not exceed **9.5 percent of an employee's W-2 wages, rate-of-pay income or the federal poverty level for a single individual**.	Coverage is affordable if the employee portion of the premium for the lowest-cost, **self-only coverage** that provides minimum value does not exceed **9.5 percent of an employee's W-2 wages, rate-of-pay income or the federal poverty level for a single individual**. The cost of family coverage is not taken into account.

Individual Mandate	Most individuals must obtain health coverage for themselves and their family members or pay a penalty. However, individuals who lack access to affordable minimum essential coverage are exempt from the individual mandate.	Coverage is affordable if the required contribution for the lowest-cost, **self-only coverage** does not exceed **8 percent of household income** (**adjusted to 8.05 percent for plan years beginning in 2015**).	Coverage is affordable if the required contribution for the lowest-cost **family coverage** does not exceed **8 percent of household income** (**adjusted to 8.05 percent for plan years beginning in 2015**).
Premium Tax Credit	The premium tax credit helps eligible individuals and families purchase health insurance through an ACA Exchange. Employees (and their family members) who are eligible for coverage under an employer-sponsored plan that is affordable and provides minimum value are not eligible for ACA's premium tax credit.	Coverage is affordable if the employee's cost for **self-only coverage** does not exceed **9.5 percent of household income** (**adjusted to 9.56 percent for plan years beginning in 2015**).	Coverage is affordable if the employee's cost for **self-only coverage** does not exceed **9.5 percent of household income** (**adjusted to 9.56 percent for plan years beginning in 2015**). The cost of family coverage is not taken into account.

EMPLOYER SHARED RESPONSIBILITY PENALTY

Under the ACA's "pay or play" requirements, applicable large employers (ALEs) that do not offer health coverage to their full-time employees and dependents, or offer coverage that is either unaffordable or does not provide minimum value, may be subject to a penalty. An ALE is one with **50 or more full-time employees**, or an equivalent combination of full-time and part-time employees.

> The employer penalty provisions were set to take effect on Jan. 1, 2014. However, in July 2013, the Treasury announced that **the employer penalties and related reporting requirements would be delayed for one year, until 2015**. Therefore, no penalties will apply to any employers for 2014. Smaller ALEs may also be eligible for an additional one-year delay.

On Feb. 12, 2014, the IRS published final regulations on the employer shared responsibility rules. These regulations finalize provisions in proposed regulations released on Jan. 2, 2013. Under the final regulations, **ALEs that have fewer than 100 full-time employees (including full-time equivalents, or FTEs) generally will have an additional year, until 2016, to comply with the pay or play rules.** ALEs with 100 or more full-time employees (including FTEs) must comply with the pay or play rules starting in 2015.

Affordability Determination

Affordability of health coverage offered by an ALE is a key point in determining whether the employer will be subject to a pay or play penalty. Coverage is considered affordable if the employee's portion of the **self-only premium** for the employer's lowest-cost coverage that provides minimum value does not exceed **9.5 percent** of the employee's household income for the tax year (**adjusted to 9.56 percent for plan years beginning in 2015**). This determination applies regardless of whether the employee is eligible for another level of health plan coverage, such as family coverage. Thus, **the cost of family coverage is not taken into account** to determine whether an employer's health plan is affordable for purposes of the pay or play penalty.

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Because employers may be largely unaware of the income levels of their employees' family members, they could find it difficult to assess whether the coverage they offer would be considered affordable. To address this issue, the IRS provided **three affordability safe harbors** that allow an employer to determine the affordability of its health coverage without knowing an employee's household income, as follows:

- *Form W-2*—Under the Form W-2 safe harbor, an employer compares the cost of self-only health coverage to an employee's wages from that employer that are required to be reported in Box 1 of the employee's Form W-2 to determine whether the cost exceeds 9.5 percent of income.
- *Rate-of-Pay*—Under the rate-of-pay safe harbor, affordability is determined by comparing the cost of self-only coverage to an employee's rate of pay. For salaried employees, the employer uses 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.
- *Federal Poverty Level*—The federal poverty level (FPL) safe harbor measures affordability based on the FPL for a single individual in effect within six months before the first day of the plan year.

Note that these affordability safe harbors **specifically reference 9.5 percent** as the required contribution. Thus, based on a literal reading of the affordability safe harbor rules, applicable large employers using any of the affordability safe harbors in 2015 will measure their plan's affordability using a required contribution of 9.5 percent (instead of the adjusted 9.56 percent). The IRS may issue guidance in the future to address this disconnect.

INDIVIDUAL MANDATE

Beginning in 2014, the ACA requires most individuals to obtain acceptable health coverage for themselves and their family members or pay a penalty. Because this provision has the effect of "requiring" individuals to have coverage, it is often referred to as the "individual mandate." The decision to delay the employer mandate penalties does not affect the individual mandate's effective date.

The penalty will be assessed against an individual for any month during which he or she does not maintain minimum essential coverage (MEC), beginning in 2014 (unless an exemption applies). The requirement applies to individuals of all ages, including children. MEC includes coverage under:

- A government-sponsored program (such as coverage under Medicare or Medicaid, CHIP, TRICARE and certain types of veterans' health coverage);
- An eligible employer-sponsored plan (including COBRA and retiree coverage);
- A health plan purchased in the individual market; or
- A grandfathered health plan.

MEC also includes any other types of coverage that HHS designates or when the sponsor of the coverage follows a process to be recognized as MEC. However, MEC does not include specialized coverage, such as coverage only for vision or dental care, workers' compensation, disability policies or coverage only for a specific disease or condition.

Affordability Exemption

The ACA includes a number of exemptions from the individual mandate. Under one of these exemptions, individuals who **lack access to affordable MEC** are not subject to the individual mandate penalty. This exemption avoids making an individual pay a tax penalty if his or her only health coverage option is unaffordable.

On Feb. 1, 2013, the IRS issued a proposed rule on the individual mandate's affordability exemption. The proposed rule would implement the following affordability measures for employees and family members:

- Coverage is unaffordable to an employee who is eligible to purchase coverage through his or her employer if the required contribution for the lowest-cost, **self-only coverage** would be more than **8 percent of household income (adjusted to 8.05 percent for plan years beginning in 2015).**
- For family members who are eligible to purchase coverage through an employer-sponsored plan, coverage is unaffordable if the required contribution for the lowest-cost, **family coverage** would exceed **8 percent of household income (adjusted to 8.05 percent for plan years beginning in 2015).**

Thus, unlike the employer shared responsibility penalty and the premium tax credit, the individual mandate's measure of affordability for family members takes into account the cost of family coverage.

Under the individual mandate's exemption rules, the required contribution for self-only coverage under an employer-sponsored plan may cost less than 8 percent (8.05 percent in 2015) of household income, while the required contribution for family coverage under the same employer plan may cost more than 8 percent (8.05 percent in 2015) of household income. In this case, the employee is not exempt from the individual mandate, while the employee's spouse and other dependents would be exempt.

PREMIUM TAX CREDIT

The ACA created a premium tax credit to help eligible individuals and families purchase health insurance through an Exchange. By reducing a taxpayer's out-of-pocket premium costs, the credit is designed to make coverage through an Exchange more affordable. To be eligible for the premium tax credit, a taxpayer:

- Must have household income for the year between 100 and 400 percent of FPL for the taxpayer's family size;
- May not be claimed as a tax dependent of another taxpayer; and
- Must file a joint return, if married.

In addition, to receive the premium assistance, a taxpayer must enroll in one or more qualified health plans through an Exchange. Also, the taxpayer **cannot be eligible for MEC** (such as coverage under a government-sponsored program or an eligible employer-sponsored plan). Employees who may enroll in an employer-sponsored plan, and individuals who may enroll in the plan because of a relationship with an employee, are generally considered eligible for MEC if the plan is affordable and provides minimum value.

Affordability Determination

Employees (and their family members) who are eligible for coverage under an employer-sponsored plan that is affordable and provides minimum value are not eligible for the premium tax credit. To determine an employee's eligibility for a tax credit, the ACA provides that employer-sponsored coverage is considered affordable if the employee's cost for **self-only coverage** does not exceed **9.5 percent** of the employee's household income for the tax year (**adjusted to 9.56 percent for plan years beginning in 2015**).

On Feb. 1, 2013, the IRS released a final rule to confirm that an employer-sponsored plan is affordable for family members if the portion of the annual premium the employee must pay for **self-only coverage** does not exceed **9.5 percent of the taxpayer's household income** for the tax year (**adjusted to 9.56 percent for plan years beginning in 2015**). Thus, the affordability determination for families is **based on the cost of self-only coverage**, not family coverage.

MORE INFORMATION

Please contact Clarke & Company Benefits, LLC for more information on the ACA's employer shared responsibility penalty, premium tax credit or individual mandate requirements.

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