WHAT EMPLOYERS NEED TO KNOW RIGHT NOW ABOUT HEALTH CARE REFORM

Potential Employer Penalties under the Patient Protection and Affordable Care Act

Employers that do not meet the requirements of the Patient Protection and Affordable Care Act (PPACA) need to be concerned about several potential penalties. Two significant penalties include the excise tax, which can be as much as $100 per affected individual per day, and the penalties that larger employers must pay if they do not meet their employer-shared responsibility/play or pay obligations.

Excise Tax Penalties

The excise tax penalties apply to all plans, regardless of size. Since 2010, the IRS has said that employers and plan administrators should self-report any failure to comply with various group health plan requirements, including requirements related to COBRA, HIPAA, Mental Health Parity, and the comparable contribution requirement for health savings accounts (HSAs), using IRS Form 8928. With the passage of PPACA, numerous additional compliance responsibilities apply. Employers and plan administrators are now expected to self-report these compliance failures, too, using Form 8928. Historically enforcement of the filing requirement and collection of the excise tax has been light, but the IRS is now indicating that it expects employers to report failures and pay fines as applicable.

The excise tax is imposed on the plan sponsor, which generally is the employer. In the case of a multiemployer plan, the plan sponsor may be the employee organization, board of trustees, or committee. With COBRA and some PPACA violations, the tax may instead be imposed on the third-party administrator or insurer responsible for the failure.

Potential COBRA, HIPAA and related violations, which come with an excise tax of $100 per day per affected individual, include the failure to:

- Offer continuation (COBRA) coverage to a qualified beneficiary;
- Provide the required level of pediatric vaccine coverage;
- Comply with special enrollment requirements (and previously with the limitations on preexisting condition exclusions and the requirement to issue certificates of creditable coverage);

- Provide the required 48-hour and 96-hour hospital length of stay in connection with childbirth for mothers and newborns; and

- Provide parity in mental health and substance use disorder benefits.

Potential PPACA violations, which also come with an excise tax of $100 per day per affected individual, include:

- Preexisting condition exclusions
- Providing employer contributions for individual medical plans
- Discrimination against participants and beneficiaries based on health status
- Discrimination in coverage for services from certain health care providers
- Cost-sharing limitations on essential health benefits
- Eligibility waiting periods in excess of 90 days
- Failure to provide coverage for individuals participating in approved clinical trials (Non-Grandfathered Only)
- Imposing lifetime or annual dollar limits on essential health benefits
- Most rescissions of coverage
- Failure to provide first-dollar coverage for preventive health services (Non-Grandfathered Only)
- Failure to extend dependent coverage until age 26
- Summary of benefits and coverage failures
- Failure to meet health plan reporting requirements
- Failure to offer required health plan claim and appeals protections
- Failure to provide required patient protections relating to the selection of a primary care provider, coverage of emergency services, and access to pediatric, obstetrical and gynecological care providers (Non-Grandfathered Only)

If the HSA comparable contribution rules are violated, the tax is generally 35% of the aggregate amount contributed by the employer for the calendar year to the HSAs of all employees. Keep in mind that the comparable contributions requirements do not apply to employers that contribute to an HSA through a Section 125 plan.

The excise tax for violations of any of the group health plan (COBRA, HIPAA, PPACA, etc.) rules other than the comparable contribution requirements for HSAs often can be avoided.

- First, no excise tax is imposed during the period when the employer did not know, or exercising reasonable diligence would not have known, a plan failure existed.

- Second, once the failure is discovered, no excise tax will be imposed if the failure was due to reasonable cause and the failure is corrected within 30 days after the date on which the error became known or should have been known. For these purposes, “correction” means retroactively fixing the failure (to the extent possible) and putting any affected individual in the same financial position as he or she would have been if the failure had not occurred.

It is not entirely clear from the IRS instructions whether the form must be filed even if no tax is due because the failure was due to reasonable cause and corrected promptly. It is also unclear how to determine if a failure is due to reasonable cause.

The deadline for reporting the failure and paying the tax generally is the deadline for filing the plan sponsor’s federal income tax return. In the case of a multiemployer plan, the deadline is the last day of the seventh month following the close of the plan year. However, the deadline for reporting and paying the tax for violating the HSA comparable contributions requirements is the 15th day of the fourth month following the calendar year in which the non-comparable contributions were made. Plan sponsors may file Form 7004 to obtain an automatic six-month extension for filing Form 8928, but this will not extend the deadline for payment of the excise taxes.

If a plan sponsor fails to report and pay excise taxes when due, the IRS may assess penalties and interest, unless the failure to file and pay is due to reasonable cause and not willful neglect. The penalty for filing Form 8928 late is 5% of the unpaid excise tax for each month the form is late, up to a maximum of 25%. A separate penalty calculation applies for late payment of the excise tax, assuming the form has been filed. In addition, if the IRS discovers the failure during an audit, minimum penalties are significantly increased.

This new reporting obligation makes compliance with group health plan requirements more important than ever. To avoid self-reporting and excise taxes, plan sponsors should have procedures and processes in place that are designed to ensure compliance. If plan failures occur, the employer and other responsible parties should take action to correct the violation within 30 days.

Employer-Shared Responsibility/Play or Pay Penalties

Large employers will owe penalties if they do not meet the employer-shared responsibility/play or pay requirements. The IRS has recently issued a helpful Q and A that answers many questions about the potential play or pay penalties.

To avoid penalties, beginning in 2015 large employers (generally those with 100 or more full-time or full-time-equivalent employees in their controlled group) must offer health benefits to employees who work an average of 30 or more hours per week, or 130 hours per month. If an employer has a non-calendar year plan and can meet certain transitional rules, it can delay offering health benefits until the start date of its 2015 plan year.

Mid-size employers (those with 50 to 99 full-time or full-time equivalent employees in their controlled group) do not have to meet the play or pay requirements until 2016 as long as they keep their headcount, eligibility requirements, benefit levels, and employer contribution amount or percentage at essentially the same level it was on February 9, 2014. Employers taking advantage of this delay must certify to the IRS that they have met these requirements. Provided they meet certain transitional rules, if an employer has a non-calendar year plan, it may delay meeting the play or pay requirements until the start of its 2016 plan year.

To avoid all penalties, a large employer's plan must meet these requirements for 2015:

- Coverage must be offered to full-time employees (those who work an average of 30 or more hours per week). Coverage for dependent children must be offered. Coverage does not have to be offered to spouses.
- The plan must provide minimum essential coverage and it must be offered to at least 70% of full-time employees. (For 2016 and later years, the threshold will increase from 70% to 95%.) Minimum essential coverage is basic medical coverage – most plans will satisfy this requirement.
- The plan must provide minimum value. This means that the plan is expected to pay, on average, at least 60% of the cost of medical claims and include significant coverage for physicians and inpatient hospital services.
- The plan must be affordable to employees. Affordability is based upon the cost for single-only coverage under the lowest-cost plan that provides minimum value, regardless of what coverage the employee actually has. Affordability may be met under any of these criteria:

- The W-2 test, which requires that the employee's cost not exceed 9.5% of the employee's income as reported in Box 1 of the W-2;
- The rate of pay method, which requires that the employee's cost not exceed 9.5% of the lowest hourly rate paid to the employee, multiplied by 130 hours per month;
- The federal poverty line test, which requires that the employee's cost not exceed 9.5% of federal poverty rate (or about $93/month for 2015).

Employers may owe one of the two penalties, but never both. The first penalty, often called the "A" penalty, is based on whether the employer offers "minimum essential" (basic) coverage. If a large employer does not offer minimum essential coverage to at least 70% of its full-time employees in 2015, and at least one person receives a premium tax credit through the Federal Marketplace, the employer will owe a penalty of $166.67 per month ($2,000 per year) on **all** of its full-time employees – even those who were not offered coverage – less a certain number of excludable employees. The excludable number generally is 30, although for 2015 an employer with 100 or more full-time and full-time equivalent employees in 2014 may exclude 80 employees.

The second penalty, often called the "B" penalty, is based on whether the large employer offers coverage that is both "affordable" and "minimum value." If a large employer does not offer affordable, minimum value coverage to all of its full-time employees, the employer will owe a penalty of $250 per month ($3,000 per year) for each full-time employee who receives an Advanced Premium Tax Credit for coverage through a public Marketplace. The B penalty will never be more than the amount that the A penalty, if any, would have been, to provide employers with an incentive to offer at least minimum essential coverage.

Any penalty owed for 2015 will be billed by the IRS and will be due mid-2016.

About Cowden Associates, Inc.

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