PPACA, HIPAA and Federal Health Benefit Mandates:

Practical Q&A

IRS Notice 2015-87 Provides Much Needed Guidance for Account-Based Plans and ACA Employer Shared Responsibility Requirement (IRC 4980H)[1] Part II

In IRS Notice 2015-87, the agencies provided further clarification on the impact of the Affordable Care Act (ACA) group health plan market reform provisions on account-based plans and much needed guidance on the Section 4980H employer shared responsibility requirements. In many cases, common benefit design practices for employer credits and opt-outs must be revisited prior to the next annual enrollment.

In this two part article we cover this important IRS guidance. Part I covered the impact of Notice 2915-87 on HRAs, FSAs and HSAs. This Part II covers the guidance related to the IRC 4980H excise tax and FSA carryover provisions.

Q10 Service Contract Act and Davis-Bacon Act Fringe Benefits

The McNamara-O'Hara Service Contract Act (SCA), the Davis-Bacon Act and the Davis-Bacon Related Acts (DBRA) require workers employed on some federal contracts to be paid prevailing wages and fringe benefits. The SCA and DBRA typically allow employers to satisfy the fringe benefit obligation by providing benefits of a sufficient dollar value. Usually, employers can select the benefit or benefits they provide. As an alternative, employers usually can satisfy their fringe benefit obligation by paying cash equal to the fringe benefit, or a combination of cash and benefits. If an employer provides SCA or DBRA fringe benefits by allowing employees to elect health coverage, but the employee declines coverage, the employer usually must pay the employee cash or provide benefits of an equivalent value.

Many employers noted that when employers satisfy their SCA or DBRA fringe benefit obligations by offering employees the option to enroll in the employer's health coverage, the amount that must be provided to employees who decline coverage as cash or other benefits is substantial. In addition, amounts that are available as cash payments or other benefits would not reduce the employee's required contribution for health coverage. Employers that satisfied their SCA or DBRA fringe benefit obligation by allowing employees to elect health coverage would also need to provide a significant additional subsidy to make the offer affordable and avoid Section 4980H(b) penalties. This subsidy would result in some employees receiving amounts significantly more than the SCA and DBRA requirements.

The IRS said it will continue to study the interaction of the SCA and DBRA with the employer shared responsibility rules. However, until the applicability date of further guidance and at least for plan years beginning before January 1, 2017, the amount of the employer's SCA and DBRA fringe benefit obligation that the employee can use to elect health coverage will reduce the employee's required contribution even if the employee can elect other benefits or cash.

Employers can also treat SCA and DBRA fringe benefit payments as reducing the employer's required contribution on Form 1095-C. However, the IRS encourages employers not to adjust Form 1095-C so that employees can qualify for premium tax credits. The IRS says that if the IRS contacts an employer regarding a possible excise tax under Section 4980H(b), the employer can respond and show that it was entitled to the relief and that it would have qualified for an affordability safe harbor if the employee's contribution had been reduced by the fringe benefit payment. Likewise, employees are not required to take fringe benefits into account as reducing their required contribution when determining premium tax credit eligibility.

The IRS is considering methods for reporting required contributions for employees subject to the SCA or DBRA, such as indicator codes. If adopted, these codes will not apply to plan years beginning *before* January 1, 2017.

Q11 Relief for Flex Credits, Opt-outs and Service Contract Act/Davis-Bacon Act Fringe Benefits

The IRS noted that the relief for health flex credits, opt-outs and SCA/DBRA fringe benefits will not affect most employees. However, employees who enrolled in the Marketplace, but did not receive the advance premium tax credit, may need more information from their employers to determine if they can claim the premium tax credit. Employers using the relief in the Notice should notify employees that they can obtain accurate information about their required contribution by calling the number listed on Form 1095-C. Regardless of how the employee obtains this information, the employee can obtain the premium tax credit if the required contribution is not affordable and the employee is otherwise eligible regardless of the information reported on that employee's Form 1095-C due to the relief.

Cost of Living Adjustments

Notice 2015-87 also provides cost of living adjustments for the employer mandate affordability safe harbors and excise taxes.

Q12 Good News: Affordability Safe Harbors Increased for Plan Years After 2014

Under the ACA, premium assistance is available if the employee's required contribution for employer coverage exceeds 9.5% of household income. For plan years after 2014, this 9.5% threshold is adjusted annually for cost of living changes. As a result, employees can obtain premium assistance for Marketplace coverage if the cost of employer coverage exceeds 9.56% of their household income for the 2015 plan year and 9.66% for the 2016 plan year.

Of course, employers do not know their employees' household income, so the IRS provided affordability safe harbors in its Section 4980H regulations. Under these safe

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harbors, the employer is deemed to provide affordable coverage if the employee's required contribution for single coverage is no more than 9.5% of the employee's rate of pay, employee's W-2 wages or the federal poverty line for a single individual. However, unlike the premium tax credit regulation, the employer mandate regulations did not provide any adjustment to the 9.5% threshold for the employer safe harbors. This resulted in an inconsistency where premium assistance was available only if the employee's contribution exceeded 9.56% of household income for the 2015 plan year, but the affordability safe harbor for employers was capped at 9.5%.

Due to this inconsistency, the IRS intends to amend the Section 4980H regulations so that the employer affordability safe harbors are adjusted with the premium assistance threshold annually. Thus, employers can use the 9.56% and 9.66% for the 2015 and 2016 plan years, respectively, when determining if coverage met the affordability safe harbors. Employers can also use the adjusted amount to determine whether coverage under a multiemployer plan is affordable under the IRS's interim guidance for multiemployer plan contributions.

The IRS also intends to amend the Section 6056 (i.e., Form 1095-C) regulations so that the threshold for qualifying offers of coverage is adjusted. Generally, an employer can use the qualifying offer method for reporting if the employee's required contribution for employee-only coverage does not exceed 9.5% of the mainland single federal poverty line. This change will be applicable back to December 16, 2015, and employers can rely on the adjusted amounts in applying the qualifying offer alternative reporting methods.

Q13 Not as Good News: Excise Taxes (Penalties) Also Increase

The ACA includes a $2,000 "sledgehammer" excise tax based on the employer's total number of full-time employees when an employee obtains a Marketplace subsidy because the employer did not offer minimum essential coverage to the employee and/or dependents (Section 4980H(a)). The ACA also assesses a $3,000 tackhammer tax for each full-time employee who obtains a Marketplace subsidy because the employer did not offer affordable, minimum value coverage (Section 4980H(b)). These penalties are adjusted annually after 2014. Accordingly, the sledgehammer penalty for the 2015 calendar year is $2,080 and $2,160 in 2016. The tackhammer penalty for the 2015 calendar year is $3,120 and $3,240 in 2016.

Leaves of Absence

Notice 2015-87 also includes highly anticipated guidance regarding the calculation of hours of service during a leave of absence.

Q14 No Hours of Service Credited After Termination

When determining if an employee is full time under the employer mandate, employers must include each "hour of service," which means each hour for which an employee is paid, or entitled to payment, for performing services, as well as each hour that the employee is paid, or entitled to payment by the employer, for a period when no duties are performed due to vacation, holiday, illness, incapacity, disability, layoff, jury duty, military duty or a leave of absence under Department of Labor (DOL) Regulation 2530.200b-2(a).

The DOL regulations are typically used to define hours of service for retirement plans, which has resulted in some confusion. The IRS clarified that the employer mandate regulations do not incorporate DOL Regulation 2530.200b-2(a)(2), which requires hours to be credited for certain periods when no duties are performed "irrespective of whether the employment relationship has terminated." Thus, an hour of service does not include any hours after an individual terminates employment.

Hours of Service Not Required Due to Payments from Certain Plans

Moreover, the IRS stated that it intends to incorporate the limitations in DOL Regulation 2530.200b-2(a)(2)(ii) and (iii). An hour of service for Section 4980H purposes does not include:

1. Hours of service associated with payments from a plan maintained solely to comply with workers' compensation, unemployment or disability insurance laws.
2. Hours for payments that solely reimburse employees for medical or related expenses incurred by the employee.

501-Hour Limit Does Not Apply (Except for Educational Organizations)

However, the IRS said it did not intend to incorporate the 501-hour limit on hours required to be credited during a single continuous period when the employee performs no duties if the hours otherwise qualify as hours of service

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(although the 501-hour limit still applies to an employee of an educational organization during employment breaks in a calendar year under Treas. Reg. 54.4980H-3(c)(6)(ii)(B)).

Employer Must Credit Hours for Short-term and Long-term Disability Payments

Hours that an employer must credit when no duties are performed must be credited regardless of the payment source. Employees must be credited with hours for short-term or long-term disability payments regardless of whether the employer pays directly or indirectly. For example, an employer must credit hours if it pays disability benefits directly through a trust or if paid by an insurer to which the employer paid premiums. However, the employer does not need to credit hours for payments if the employer did not contribute directly or indirectly. An arrangement that the employee paid for on an after-tax basis would be treated as an arrangement the employer did not contribute to and would not result in any hours of service. Moreover, employers need not credit hours to employees receiving workers' compensation payments from a state or local government.

Practice Pointer: *The IRS does not require hours of service to be credited when an employee receives disability payments based on his or her previous after-tax contributions. However, pre-tax contributions are considered to be made by the employer. Employers must credit hours of service for disability payments received under coverage that the employer paid for or allowed the employee to obtain on a pre-tax basis through its cafeteria plan.*

Q15 Potential New Rules for Hours of Service for Educational Organizations

The IRS's employer mandate regulations prohibit most employers from treating a rehired employee as new hire unless the employee had a break in service of at least 13 weeks. However, the IRS provided special rules for educational institutions to account for periods when employees might not be providing services, such as during summer break. Under those rules, employees of educational institutions must have a 26-week break in service before the employer can consider them a new hire under the employer mandate.

However, the IRS is aware of situations where educational institutions are trying to avoid this special rule by using third-party staffing agencies. The IRS intends to propose rules that apply the 26-week break in service requirement in circumstances where services are provided to one or more educational institutions even if the employer is not an educational organization. The IRS intends the rule to apply to employees providing services primarily to educational organizations who are not given a meaningful opportunity to work during the entire year. For example, the rule would apply to a cafeteria worker who is primarily placed to provide cafeteria services at educational organizations and is not given a meaningful opportunity to provide services during one or more months of the calendar year, such as during summer break. However, an employer that placed cafeteria workers at educational organizations would not apply the special rule to employees who are offered a meaningful opportunity to provide services during all months

(for example, by working at a hospital cafeteria during summer break).

The amendments will apply as of the applicability date in the regulations, but not earlier than the first plan year beginning after the date of the proposed regulations.

Q16 AmeriCorps Employees

Notice 2015-87 clarifies that participants in the AmeriCorps program are not employees of AmeriCorps or the grantee receiving assistance through AmeriCorps for which the participant is providing services for purposes of the employer shared responsibility rules of Section 4980H.

Q17 TRICARE Eligibility

The IRS clarified that for determining potential liability under Section 4980H and related information reporting under Section 6056, an offer of coverage under TRICARE for any month based on employment with an employer that results in TRICARE eligibility is treated as an offer of minimum essential coverage by that employer.

Q18 Applicable Large Employer (ALE) Status or ALE Member Status

The IRS noted that the aggregation rules under Section 414(b), (c), (m) and (o) that typically apply when determining if an employer is an ALE do not specifically address government entities. As provided in the preamble of the final employer mandate regulations, government entities can use a reasonable, good-faith interpretation of those aggregation rules to determine if it is an ALE or ALE member. The IRS noted this is of little consequence when government entities would independently be ALEs, with one of the few consequences being the allocation of any reduction of assessable payments under Section 4980H(a) or the cap on assessable payments under Section 4980H(b).

Q19 Separate EINs Required for Each ALE and ALE Member

The IRS clarified that each separate employer entity that is an ALE or ALE member, or that provides self-insured health coverage to employees, must use its own EIN for reporting purposes regardless of the aggregation rules. Thus, separate Forms 1094-C must be filed by each ALE member and each form must have a separate EIN. This is not changed by a government entity's use of a designated government entity (DGE) to file Forms 1094-C and 1095-C.

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EXAMPLE A state treats the state executive and its agencies, the judiciary and legislature as three separate employers. The executive, judiciary and legislature must each have separate EINs and file Forms 1094-C and 1095-C with the EIN of the applicable employer.

EXAMPLE Ten counties enter into agreements with a state government entity that the state agency will be the designated government entity for filing on behalf of each county. The state agency must file a 1094-C for each county, as well as itself. Each Form 1094-C will list the name and EIN of the state agency as the designated government entity and the name and EIN of the applicable county as the employer. The Forms 1094-C would be filed with the Forms 1095-C for each employee of that county, which would identify the county as the employer.

Q20 HSA Contributions and VA Coverage

Notice 2015-87 addressed the receipt of health care from the Department of Veterans Affairs (VA) and HSA contribution eligibility. As modified by the Surface Transportation Act, an individual receiving VA medical benefits can make HSA contributions if the medical benefits consist only of disregarded coverage, preventive care or hospital care or medical services under any law administered by the VA for service-connected disability. As a rule of convenience, the IRS will consider any hospital care or medical services received from the VA by a veteran who has a VA disability rating to be hospital care or medical services under a law administered by the VA for service-connected disability.

Additional Guidance on Health FSA Carryovers

The IRS modified the cafeteria plan rules to permit health FSA carryovers of up to $500 from year-to-year in Notice 2013-71. Notice 2015-87 provides updates based on common questions.

Q21 Carryover is Included When Determining if a Health FSA is Underspent for COBRA

The IRS clarified that the carryover must be included in determining whether COBRA coverage must be offered because the health FSA is underspent.

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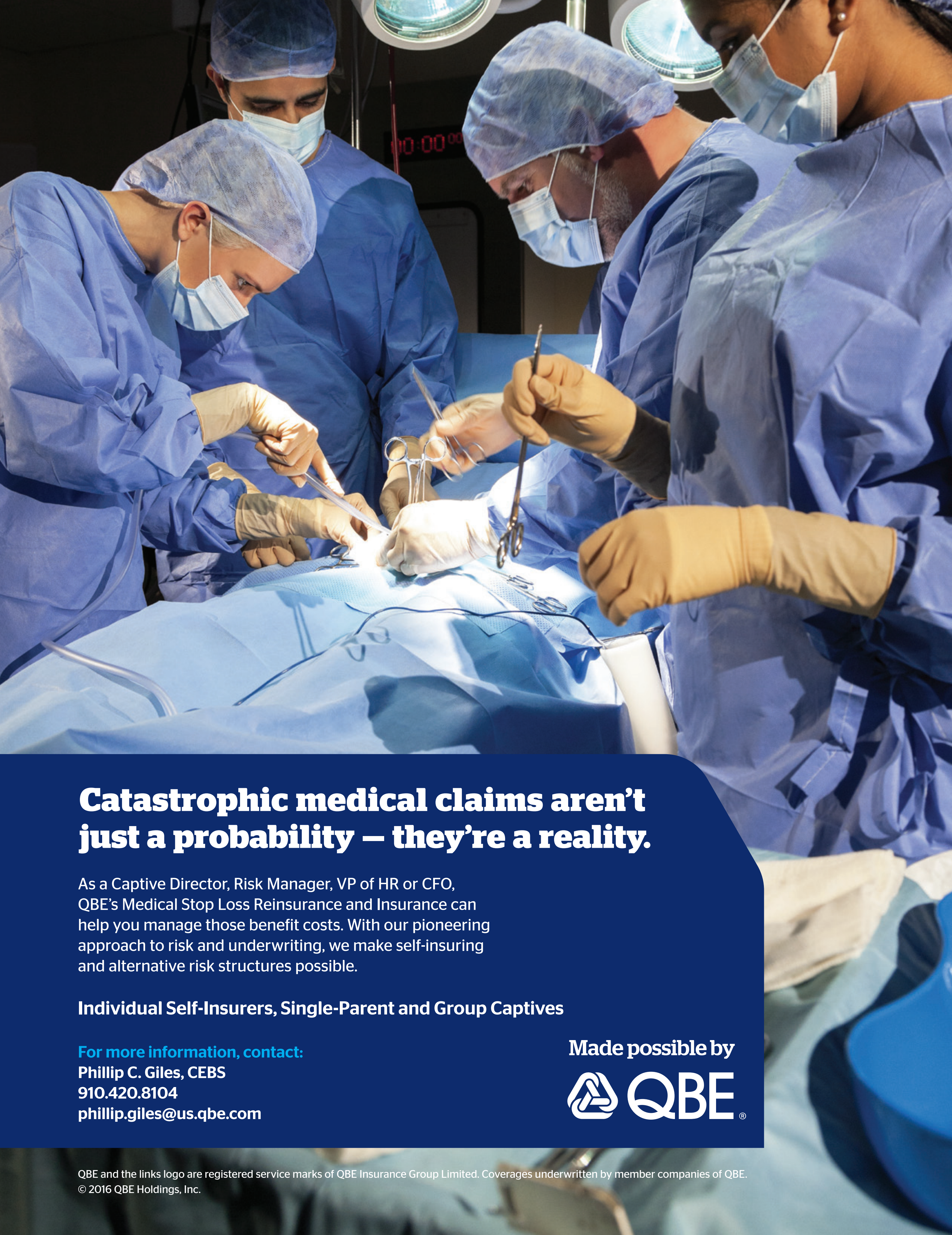
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EXAMPLE An employee can elect to contribute up to $2,500 to a calendar year health FSA and carries over $500 in unused benefits from the prior year. Thus, the maximum amount the employee can receive under the health FSA for the entire year is $3,000. When the employee terminates employment on June 30, he had submitted $1,100 of reimbursable expenses under the health FSA. As a result, the maximum benefit the employee receives for the remainder of the year is $1,900 (i.e., [$2,500 + $500] – $1,100]).

Practice Pointer: *The determination seems to hinge on when the qualifying event occurs. If it occurs prior to the end of the run-out period from the prior year, then it would appear that the carryover amount, which is not yet known, would not be a factor. However, if it occurs after the end of the run-out period, when the carryover is known, the carryover amount would be a factor. Additional guidance on the intended application of this rule would be welcome.*

Q22 Health FSA COBRA Premium Only Includes Salary Reductions and Employer Contributions

The IRS also clarified that the COBRA premium for a health FSA can only include the salary reduction election and non-elective employer contributions for the year, plus a 2% administrative fee. In other words, carryovers are not included when calculating the COBRA premium for a health FSA.

Q23 If COBRA is Elected, Carryover Continues Until Exhausted or COBRA Expires

Qualified beneficiaries who elected continuation coverage for their health FSAs must be provided with carryovers if similarly situated non-COBRA beneficiaries receive carryovers. However, the health FSA

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is not required to allow a COBRA beneficiary to elect additional salary reductions for the carryover period or provide employer contributions during the carryover period. The ability to carry over amounts is limited to the applicable COBRA continuation period (for example, 18 months due to termination of employment). The health FSA cannot charge a premium for the carryover in later years.

Practice Pointer: ***Employers that provide carryovers in their health FSAs should revise their COBRA notices to describe how the carryover impacts the premium and that amounts carried over will be available until exhausted or the COBRA period ends.***

Q24 Carryover Not Required if Employee Does Not Elect Health FSA for Next Year

The IRS also clarified that a health FSA can limit carryovers to individuals who elected to participate in the health FSA in the next year, even if a minimum salary reduction is required.

EXAMPLE An employer sponsors a health FSA that permits carryovers, but only if the employee participates in the health FSA during the next year. To participate in the health FSA, an employee must contribute at least $60 per year ($5 per month). At the end of 2015, Lou and Maureen each have $26 left in their health FSAs. Lou elects to contribute $600 to the FSA for 2016. Lou's $26 is carried over to the health FSA next year, giving Lou a $626 health FSA balance for 2016. However, Maureen does not elect to contribute to the health FSA in 2016, so she forfeits her $26 and has no health FSA balance for 2016.

Q25 Health FSAs Can Have a Maximum Carryover Period

The IRS stated that a health FSA can limit carryovers to a maximum period. For example, a health FSA can limit the ability to carry over unused amounts to one year.

Practice Pointer: ***If an employer wants to provide a maximum carryover period, it should check to see if a plan amendment is required and notify employees accordingly.***

The Affordable Care Act (ACA), the Health Insurance Portability and Accountability Act of 1996 (HIPAA) and other federal health benefit mandates (e.g., the Mental Health Parity Act, the Newborns and Mothers Health Protection Act, and the Women's Health and Cancer Rights Act) dramatically impact the administration of self-insured health plans. This monthly column provides practical answers to administration questions and current guidance on ACA, HIPAA and other federal benefit mandates.

Attorneys John R. Hickman, Ashley Gillihan, Carolyn Smith, and Dan Taylor provide the answers in this column. Mr. Hickman is partner in charge of the Health Benefits Practice with Alston & Bird, LLP, an Atlanta, New York, Los Angeles, Charlotte and Washington, D.C. law firm. Ashley Gillihan, Carolyn Smith and Dan Taylor are members of the Health Benefits Practice. Answers are provided as general guidance on the subjects covered in the question and are not provided as legal advice to the questioner's situation. Any legal issues should be reviewed by your legal counsel to apply the law to the particular facts of your situation. Readers are encouraged to send questions by email to Mr. Hickman at john.hickman@alston.com.

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