The FISCAL REPORT an informational update

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What We Do Know and What We Don't Know About the "Pay or Play" Employer Mandate

We have written numerous *Fiscal Report* articles on the various phases of the Patient Protection and Affordable Care Act (PPACA), otherwise referred to as federal health care reform. We have been able to provide you with information on the implementation of each phase as the details are made available. The most significant phase of the PPACA to local educational agencies (LEAs) is about to be upon us in just over a year—the "pay or play" employer mandate, referred to in PPACA as "employer shared responsibility," which takes effect in 2014. Details are still sketchy in some areas, so the purpose of this article is to lay out the different aspects of this phase of implementation, detailing what we do know, and honing in on what we don't yet know.

Applicable Large Employer

The first test is whether an LEA is an "applicable large employer" and therefore subject to the "pay or play" mandate. An "applicable large employer" is defined as an employer who employed an average of at least 50 full-time employees on business days during the preceding calendar year. So, for determining whether an LEA is an "applicable large employer" during 2014, the first year of this mandate, the number of full-time employees during 2013 would be the determining factor.

The Internal Revenue Service (IRS) has published preliminary guidance (Notice 2012-58), but as of yet, we do not have the final regulations. The preliminary guidance can be relied upon through the end of 2014. Based upon this, the 50-employee threshold is calculated on a monthly basis for the prior year as follows:

Step 1—Employees in that month who worked, on average, at least 30 hours per week or 130 hours in the month, would be counted as full time.

Step 2—For all other employees, including seasonal or temporary employees, add up the hours worked, not counting more than 120 hours for any one employee, for that month. Divide the result by 120 to determine the number of full-time equivalents (FTEs).

Step 3—Add up the FTEs from steps 1 and 2 for each month. Then add the months together and divide by 12, rounding the result down to the nearest whole number.

If the result is less than 50 FTEs, then the employer is not subject to the "pay or play" requirement. If the result is 50 FTEs or more, but only for 120 days or less during the year and only because of seasonal or temporary employees, then the employer is not subject to "pay or play." All other employers are subject to the "pay or play" requirement.

"Full-Time Employee" for Purposes of the Coverage Requirement

The next test is to determine which employees are "full time" and are therefore required to be provided coverage by LEAs starting in 2014. "Full-time" for this purpose is defined as at least 30 hours per week or 130 hours per month. For employees with varying hours, the IRS is allowing for a "standard measurement period" and a "stability period," which would each be of a particular length of time that LEAs can choose within IRS standards.

Employees with varying hours are employees that, as of their start date with the LEA, cannot reasonably be expected to work on average at least 30 hours per week for the "standard measurement period." For these ongoing employees, the LEA can determine the employee's status relative to "full time" by looking back for the chosen length of the "standard measurement period," which can be from three consecutive months to 12 consecutive months. If the employee averaged at least 30 hours per week during the "standard measurement period," then the employee is treated as full time during the subsequent "stability period" regardless of the number of hours worked during that period, as long as they remain an employee. The LEA would be required to offer health coverage to this employee during the "stability period," which is required to be at least six consecutive months and up to 12 consecutive months, but cannot be shorter than the "standard measurement period."

We would expect most LEAs to choose 12-month periods for the "standard measurement period" and the "stability period" because of the types of variable hour staff members that are typically employed—mostly certificated and classified substitutes—but also because of temporary workers that are often hired as well.

Minimum Essential Coverage

LEAs will be required to provide "minimum essential" coverage to all "full-time" employees as defined above starting in 2014. The "minimum essential" coverage is defined as a plan that covers at least 60% of the total allowed under the medical plan—in other words, the plan covers at least 60% of the actuarial value of the benefits provided, such as emergency services, prescription drugs, preventive care, etc.

We would expect that the types of plans already provided by LEAs would easily meet this requirement, but we advise that you check with your broker or carrier to be sure that the lowest coverage plan that employees can choose qualifies as "minimum essential" coverage.

Affordable Coverage

The "minimum essential" coverage offered to all "full-time" employees must also be "affordable," which means that the employee's cost cannot exceed 9.5% of household income. Since this is not measurable by employers, the IRS issued safe harbor guidance to allow for a different test: the employee's contribution to the premium for an employee-only plan cannot exceed 9.5% of the employee's W-2 wages for that year.

Potential Penalties

There are two types of potential penalties that LEAs can face for not meeting the mandates above. The penalties can apply if one or more employees purchase coverage through the California Health Benefit Exchange (Exchange) and receive a federal premium and cost-sharing subsidy. In order to qualify for a subsidy, the employee's household income cannot exceed 400% of the Federal Poverty Level, which depends on the size of the family. For 2012, 400% of the Federal Poverty Level for a family of one is $44,680 and for a family of five is $108,040.

If an LEA fails to provide coverage for at least one "full-time" employee, and that employee goes to the Exchange and receives a subsidy, the LEA would be subject to a penalty of $2,000 times the number of all FTEs in the LEA, minus the first 30 employees. This is the most Draconian of the two penalties—it is paid on all employees (minus the first 30) if even only one "full-time" employee was not offered coverage.

If an LEA provides coverage but the plan does not meet either the "minimum essential" test or "affordability" test above, and the employee purchases coverage through the Exchange and receives a subsidy, the LEA would be subject to a penalty of $3,000 times the number of employees who receive a subsidy, up to a maximum of $2,000 per FTE (minus the first 30).

The penalty amounts above are annualized, but assessed on a monthly basis. They will be indexed up each year after 2014.

What We Don't Know

There are significant unknowns that LEAs face in determining how to manage the upcoming costs of health care and the potential risk of paying penalties. While we have temporary guidance that we can rely on until the end of 2014, we are awaiting final regulations from the IRS. Comments on the temporary guidance were required by September 30, 2012, and the expectation is that we should have final regulations in the very near future.

LEAs can't assess the potential penalties because household income is not known, and that is the determining factor as to whether or not an employee would receive a subsidy when going to the Exchange for coverage. Would it make sense to cease employer coverage and provide some amount to employees to purchase coverage through the Exchange? The Exchange is well on its way to becoming operational, and we understand that the premiums will be based on age and whether or not the individual is a smoker, but we don't know yet what those premiums are estimated to be when the coverage requirement begins in 2014.

Meanwhile, LEAs need to be prepared to be able to make changes to their health benefits program as more information becomes available. We will continue to monitor these issues and keep you apprised but in the meantime, our advice still stands—avoid locking in health benefit language in collective bargaining contracts and individual employment contracts without reopeners for 2014 and beyond.

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