XXVIII. Shared Responsibility for Employers (Play or Pay Penalty Tax)

A. Introduction to Shared Responsibility for Employers (Play or Pay Penalty Tax)

Beginning in 2015,[1] certain large employers may be subject to a penalty tax (also called an "assessable payment") for (1) failing to offer minimum essential health care coverage for all full-time employees (and their dependents)—the subsection (a) penalty;[2] or (2) offering eligible employer-sponsored coverage that is not "affordable" (exceeds a specified percentage of the employee's household income) or does not offer "minimum value" (the plan's share of the total allowed cost of benefits is not at least 60%)—the subsection (b) penalty.[3]

The penalty tax is due if any full-time employee is certified to the employer as having purchased health insurance through an Exchange (discussed in Section XXI) with respect to which a premium tax credit is allowed or paid to the employee.[4] These requirements are also referred to as the employer shared responsibility provisions.

In July 2013, the IRS issued guidance[5] announcing a one-year delay in the application of the employer shared responsibility penalties (until 2015). The delay was prompted by IRS concerns about information reporting requirements under Code §§ 6055 (applicable to insurers, self-insuring employers, and other parties that provide health coverage) and 6056 (applicable to certain large employers with respect to health coverage offered to their full-time employees), which were scheduled to begin in 2014.[6]

---

1 The employer shared responsibility provisions are codified in Code § 4980H, which was added to the Code by the Patient Protection and Affordable Care Act, Pub. L. No. 111-148 (2010) (PPACA), as amended by the Health Care and Education Reconciliation Act, Pub. L. No. 111-152 (2010) (HCERA). Under Section 1513(d) of the PPACA, Pub. L. No. 111-148, § 1513(d), these provisions apply to months beginning after December 31, 2013. However, on July 2, 2013, the Treasury Department announced a one-year delay in application of the penalties under Code § 4980H. U.S. Department of the Treasury, Continuing to Implement the ACA in a Careful, Thoughtful Manner (July 2, 2013), available at http://www.treasury.gov/connect/blog/pages/continuing-to-implement-the-aca-in-a-careful-thoughtful-manner-.aspx (as visited Mar. 5, 2014). The delay was formally announced on July 9, 2013 in Notice 2013-45, 2013-31 I.R.B. 116.

2 Code § 4980H(a). Regulations have clarified the meaning of the parenthetical reference to "and their dependents"—see discussion in subsections D and E.

3 Code § 4980H(b).

4 Code §§ 4980H(a)(2) and (b)(1)(B). The determination of whether an employee is eligible for a premium tax credit is made under Code § 36B. To be eligible for a cost-sharing reduction, an individual must also be eligible for a premium tax credit. Therefore, although the statute appears to have two separate triggers for potential penalties, in reality at least one employee must qualify for a premium tax credit before the penalty can apply, and it does not matter if an employee also qualifies for a cost-sharing reduction.

5 Notice 2013-45, 2013-31 I.R.B. 116.

6 The Code § 6055 requirements are discussed in Section XXXVI.C. The Code § 6056 requirements are discussed in Section XXXVI.D. According to the IRS, because the information required by Code § 6056 is critical to administration of the employer shared responsibility penalties, it would have been "impractical" to determine liability for employer shared responsibility until the Code § 6056 reporting requirements begin. Consequently, the delay in the employer shared responsibility penalties is tied directly to the delay in the information reporting requirements.

Delay in Penalties Is a Reprieve, Not a Pardon. The delay announced in Notice 2013-45 came as a surprise and was welcomed by many employers. However, the delay is only temporary, and, given the complexity of the issues, employers have no time to waste. With the final regulations issued in February 2014, employers and advisors will need to adjust planning efforts to avoid and reduce penalties. Of particular importance are the rules for identifying full-time employees (discussed in subsection C), which require many employers to begin tracking employee status early in 2014.

In February 2014, the IRS issued final regulations on the employer shared responsibility provision,[7] finalizing provisions proposed in January 2013.[8] The final regulations generally incorporate many of the provisions in the proposed regulations and in previously issued guidance in various IRS Notices,[9] with some modifications and additional transition relief. Although the regulations are applicable for periods after December 31, 2014, employer may rely on them for periods before January 1, 2015.[10] The IRS has also issued questions and answers (Q&As) addressing various aspects of employer shared responsibility.[11]

1. Clarification of Periods During Which Code § 4980H Liability Does Not Apply—Limited Non-Assessment Periods

In various circumstances, the final regulations provide that an employer will not be subject to a penalty under Code § 4980H for a certain period of time. The term "limited non-assessment period" for certain employees is used to describe these periods.[12]

Specifically, an employer will not be subject to a penalty under Code § 4980H(a), and in certain cases Code § 4980H(b), with respect to an employee in the following circumstances:

- the transition rule for an employer's first year as an applicable large employer;[13]
- the application of Code § 4980H for the three full calendar month period beginning with the first full calendar month in which an employee is first otherwise eligible for an offer of coverage under the monthly measurement method;[14]
- the application of Code § 4980H during the initial three full calendar months of employment for an employee reasonably expected to be a full-time employee at the start date, under the look-back measurement method;[15]
- the application of Code § 4980H during the initial measurement period to a new variable-hour employee, seasonal employee, or part-time employee determined to be employed on average at least 30 hours of service per week, under the look-back measurement method;[16]
- the application of Code § 4980H following an employee's change in employment status to a full-time employee during the initial measurement period, under the look-back measurement method;[17] and
- the application of Code § 4980H to the calendar month in which an employee's start date occurs on a day other than the first day of the calendar month.[18]

The preamble notes that the relief from the penalty under Code § 4980H provided by the rules above does not affect an employee's eligibility for a premium tax credit.[19]

---

7 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543 (Feb. 12, 2014).

8 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 78 Fed. Reg. 217 (Jan. 2, 2013).

9 *See* IRS Notice 2012-58, 2012-41 I.R.B. 436; IRS Notice 2012-17, 2012-9 I.R.B. 430; IRS Notice 2011-73, 2011-40 I.R.B. 47; IRS Notice 2011-36, 2011-21 I.R.B. 792.

10 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8577 (Feb. 12, 2014).

11 Questions and Answers on Employer Shared Responsibility Provisions Under the Affordable Care Act (July 18, 2013), available at http://www.irs.gov/uac/Newsroom/Questions-and-Answers-on-Employer-Shared-Responsibility-Provisions-Under-the-Affordable-Care-Act (as visited Mar. 5, 2014).

12 Treas. Reg. § 54.4980H-1(a)(26).

13 Treas. Reg. § 54.4980H-2(b)(5). See subsection B for more details.

14 Treas. Reg. § 54.4980H-3(c)(2). See subsection C for more details.

15 Treas. Reg. § 54.4980H-3(d)(2)(iii). See subsection C for more details.

16 Treas. Reg. § 54.4980H-3(d)(3)(iii). See subsection C for more details.

17 Treas. Reg. § 54.4980H-3(d)(3)(vii). See subsection C for more details.

18 Treas. Reg. §§ 54.4980H-4(c) and 54.4980H-5(c). See subsections D and E for more details.

19 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8560 (Feb. 12, 2014).

2. Important Transition Relief in Final Regulations

The final regulations provide important transition relief, including relief to applicable large employers with fewer than 100 full-time employees (including full-time equivalent employees) during 2014—these employers will not be subject to Code § 4980H penalties until 2016 if they satisfy certain conditions to qualify for the relief. For complete details on this, and other forms of transition relief, see subsection F.

> **Employer Shared Responsibility Penalty Tax Is Not Deductible.** An assessable payment imposed under Code § 4980H is not deductible.*

* Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8567 (Feb. 12, 2014). (Pursuant to Code § 275(a)(6), regarding the nondeductibility of certain excise taxes, including those under chapter 43, an assessable payment imposed under Code § 4980H is not deductible.)

Health care reform authorizes states to apply for an "innovation waiver" from the employer shared responsibility penalty tax and certain other requirements for plan years beginning on or after January 1, 2017.[20] For more details about innovations waivers, see Section XXI.G.

In this Section, we address the following topics:

- How to determine whether an employer is an "applicable large employer" to whom the shared responsibility penalty tax may apply (subsection B);
- Who is considered a "full-time employee" for purposes of calculating the amount of the penalty tax (subsection C);
- How to calculate the penalty if the applicable large employer does not offer eligible employer-sponsored coverage to full-time employees and dependents—the subsection (a) penalty (subsection D);
- How to calculate the penalty even if the applicable large employer offers coverage to full-time employees and dependents, but the coverage either is unaffordable or does not provide minimum value—the subsection (b) penalty (subsection E);
- Transition rules with respect to the application of the penalties (subsection F);
- Rules relating to certification of the premium tax credit and the employer's payment of penalties (subsection G); and
- An analysis of the factors that may influence an applicable large employer's decision whether to play (to avoid the penalty) or to pay the penalty (subsection H).

B. Large Employers Are Potentially Subject to an Assessable Payment (Penalty Tax)

The penalty tax (or assessable payment) applies to "applicable large employers." An applicable large employer (ALE) for a calendar year is an employer who employed (along with members of its controlled group) an average of at least 50 "full-time employees" (including full-time equivalent employees) on business days during the preceding calendar year.[21]

> **"Applicable Large Employer" Status Also Significant for New Reporting Requirement.** An employer's status as an "applicable large employer" is not only relevant for purposes of Code § 4980H but also for purposes of a new reporting requirement under Code § 6056. This reporting requirement originally was to apply to coverage provided on or after January 1, 2014, but the IRS has delayed reporting for one year "to provide additional time for dialogue with stakeholders in an effort to simplify the reporting requirements"* For more on this reporting requirement, including the information that must be reported to the IRS and provided in written statements to full-time employees, see Section XXXVI.D.

* *See* Notice 2013-45, 2013-31 I.R.B. 116, Q/A-1.

[20] PPACA, Pub. L. No. 111-148, § 1332 (2010). President Obama has voiced support for legislation that would have made innovation waivers available beginning in 2014, but such legislation was not enacted. *See* White House fact sheet—The Affordable Care Act: Supporting Innovation, Empowering States (Feb. 28, 2011), available at http://www.whitehouse.gov/the-press-office/2011/02/28/fact-sheet-affordable-care-act-supporting-innovation-empowering-states (as visited Mar. 5, 2014).

[21] Code § 4980H(c)(2)(A); Treas. Reg. § 54.4980H-1(a)(4).

For purposes of determining whether an employer is an ALE subject to employer shared responsibility provisions, an employer must convert part-time employees into full-time equivalents (even though such individuals would not trigger the tax by receiving a premium subsidy).

Applicability of Rules for Employers With Employees in U.S. Territories. A letter issued by HHS to the Governors of U.S. territories (e.g., Puerto Rico, Guam) describing the applicability of the Exchange requirements under health care reform to their governments and residents also addresses Exchange-related tax provisions (including Code § 4980H).* While HHS acknowledges that territories have their own tax laws and must determine how those laws apply, it offers general "observations" based on its consultation with the Treasury. HHS states that the applicability of a tax provision depends on whether a territory's tax laws mirror or do not mirror the federal tax Code. While the employer shared responsibility penalty under Code § 4980H would not apply in either mirror or non-mirror territories, the stated reasoning is different. Mirror territories are generally not obligated to mirror excise tax provisions, and this penalty is considered an excise tax under the Code. Non-mirror territories have their own distinct tax codes and, thus, would not be subject to Code § 4980H (although such a territory could choose to enact a comparable provision under its own law).

It is important to note that while the HHS letter is not official guidance, it does provide helpful insight into the application of the Exchange-related tax provisions to U.S. territories, including Code § 4980H.

* *See* Information for the Territories Regarding the Affordable Care Act (Dec. 10, 2012), available at http://www.cms.gov/CCIIO/Resources/Files/Downloads/gov-letter-territories-12-10-2012.pdf (as visited Mar. 5, 2014).

1. Who Is the "Employer"?

Code § 4980H applies the controlled group test, meaning that all entities treated as a single employer under Code § 414(b), (c), (m), or (o) are treated as a single employer for purposes of § 4980H.[22] Thus, the employees of all employers within the controlled group are taken into account in determining whether any member of the controlled group is an ALE.[23] The regulations clarify that for a calendar year during which an employer is an ALE, the Code § 4980H standards generally are applied separately to each person that is a member of the controlled group comprising the employer (with each person referred to as an "applicable large employer member") in determining liability for, and the amount of, any assessable payment (see the discussion in subsections D and E regarding calculation of the penalties).[24]

For purposes of determining an ALE, the term "employer" also includes a predecessor employer and a successor employer.[25] The regulations reserve, and therefore do not address, the specific rules for identifying a predecessor employer (or the corresponding successor employer)—until further guidance is issued, reliance upon a reasonable, good faith interpretation of the statutory provision on predecessor (and successor) employer is permitted.[26] Note that although controlled group rules apply when determining if an employer is an ALE, Code § 4980H does not currently incorporate the separate line of business (SLOB) rules applicable under Code § 414(r). Thus, an employer could be affected by employer shared responsibility provisions even if the SLOB rules provide an exception for purposes of certain discrimination testing requirements.

22 Code § 4980H(c)(2)(C)(i); Treas. Reg. § 54.4980H-1(a)(16). The controlled group rules are discussed in detail in Section XXVIII.I of *Cafeteria Plans* (Thomson Reuters/EBIA, 1991-present, updated quarterly).

23 This rule prevents an employer from circumventing ALE status by setting up separate business entities and assigning fewer than 50 employees to each of them.

24 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8548 (Feb. 12, 2014). "Applicable large employer member" is defined in Treas. Reg. § 54.4980H-1(a)(5).

25 Treas. Reg. § 54.4980H-1(a)(16).

26 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8548 (Feb. 12, 2014).

Government entities (such as federal, state, local, or Indian tribal government entities) may be ALEs.[27] The regulations reserve on the application of the employer aggregation rules to government entities, as well as to churches or conventions or associations of churches. Until further guidance is issued, those entities may apply a reasonable, good faith interpretation in determining their status as an ALE.[28]

> **Example: Applicable Large Employer/Controlled Group.** For all of 2015 and 2016, Dean Corp. owns 100% of all classes of stock of Jimmy Corp. and Jean Corp. Dean Corp. has no employees at any time in 2015. For every calendar month in 2015, Jimmy Corp. has 40 full-time employees and Jean Corp. has 60 full-time employees. Corporations Dean, Jimmy, and Jean are a controlled group of corporations under Code § 414(b).
>
> Because Corporations Dean, Jimmy, and Jean have a combined total of 100 full-time employees during 2015, Corporations Dean, Jimmy, and Jean together are an ALE for 2016. Each of Corporations Dean, Jimmy, and Jean is an ALE member for 2016.*

* Treas. Reg. § 54.4980H-2(d), Example 1.

2. Who Is a Full-Time Employee?

The statute defines full-time employees as those who, with respect to any month, work at least 30 hours per week[29]—130 hours of service in a calendar month is treated as the monthly equivalent of at least 30 hours of service per week.[30] An "employee" is an individual who is an employee under the common-law standard.[31] A leased employee (as defined in Code § 414(n)(2)), a sole proprietor, a partner in a partnership, or a 2% S corporation shareholder is not each considered an employee.[32] Full-time equivalent employees are included (see discussion below), but employees who work outside the U.S. are excluded.[33]

"Hours of service" are used in determining whether an employee is a full-time employee and in calculating an employer's full-time equivalents. These rules are described in detail below in subsection C.

---

27 Treas. Reg. § 54.4980H-1(a)(23).

28 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8548 (Feb. 12, 2014).

29 Code § 4980H(c)(4)(A).

30 Treas. Reg. § 54.4980H-1(a)(21). This 130 hours of service monthly equivalency applies for the look-back measurement method and the monthly measurement method for determining full-time employee status (see subsection C) and, based on a fair reading of the regulations, an employer should also be able to use the 130-hour monthly equivalency to identify full-time employees for purposes of determining whether it is an ALE. Although not clear under the regulations, an employer should not be required to test an employee's full-time status using both the 30-hour weekly average and the 130-hour monthly equivalency. Rather, the employer should be able to apply the weekly average to some employees and the monthly equivalency to other employees, provided that it does so on a reasonable and consistent basis. Thus, an employee should be considered to be full-time only if the employee is credited with sufficient hours under the standard (30 hours per week or 130 hours per month) that the employer is applying to that employee. Further guidance on this would be welcome.

31 *See* Treas. Reg. § 31.3401(c)-1(b).

32 Treas. Reg. § 54.4980H-1(a)(15).

33 Treas. Reg. § 54.4980H-1(a)(24)(ii)(C).

Caution: Consequences of Misclassifying Workers. Significant tax consequences result if a worker is misclassified as an independent contractor and is subsequently reclassified as an employee—including liability for withholding taxes, interest and penalties, and potential disqualification of employee benefit plans. Section 530 of the Revenue Act of 1978 generally allows an employer to treat a worker as not being an employee for employment tax purposes (but not income tax purposes), regardless of the worker's actual status, unless the employer has no reasonable basis for such treatment or fails to meet certain specified requirements.* Significantly, the Section 530 relief does not apply to potential liabilities under Code § 4980H.† In response to the limitation on the relief under Section 530, commenters requested that the IRS formulate a similar provision in the final regulations under Code § 4980H. Citing concerns that the relief requested would serve to increase the potential for worker misclassification by significantly increasing the benefit of having an employee treated as an independent contractor, the IRS did not adopt this suggestion in the final regulations.‡ Thus, the stakes are now even higher in terms of adverse consequences resulting from worker misclassification.

* Revenue Act of 1978, Pub. L. No. 95-600 (Nov. 6, 1978). This relief has been extended several times since its original enactment in 1978.

† *See* Joint Committee on Taxation, "Present Law and Background Relating to Worker Classification For Federal Tax Purposes" (May 7, 2007).

‡ Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8568 (Feb. 12, 2014).

3. Full-Time Includes Full-Time Equivalents

For purposes of determining whether an employer is an ALE, "full-time" includes full-time equivalent employees.[34] Therefore, the employer must take part-time employees into account to determine whether it is an ALE.

No Penalty Tax for Part-Time Employees. Because of the requirement to count full-time equivalent employees,* an employer cannot avoid being treated as an ALE solely by making its workforce part-time. However, even if an employer is an applicable large employer, it will not necessarily be liable for the penalty tax. The penalty is calculated based only on true full-time employees (those who work 30 or more hours per week). Full-time equivalents are not used to calculate the amount of the penalty tax.

* Treas. Reg. § 54.4980H-1(a)(22).

The number of full-time equivalents the employer employed during the preceding calendar year are taken into account. All employees (including seasonal workers) who were not employed on an average of at least 30 hours of service per week for a calendar month in the preceding calendar year are included in calculating the number of full-time equivalents for that calendar month.[35] The approach for converting part-time employees to full-time equivalents includes two steps:

- Step 1: Calculate the aggregate hours of service in a month for employees who are not full-time employees for that month. (Do not include more than 120 hours of service for any employee.)
- Step 2: Divide the total hours of service from Step 1 by 120.[36]

The result is the number of full-time equivalent employees for the month.[37]

34 Code § 4980H(c)(2)(E).

35 Treas. Reg. § 54.4980H-2(c)(1).

36 Treas. Reg. § 54.4980H-2(c)(2).

37 In determining the number of full-time equivalents for each calendar month, fractions would be taken into account. For example, if in a calendar month employees who are not full-time employees work 1,260 hours, there would be 10.5 full-time equivalents for that month (1,260 ÷ 120 = 10.5). An employer may round the number of full-time equivalent employees for each calendar month to the nearest one hundredth. For example, an employer with a calculation of 30.544 full-time equivalent employees for a calendar month may round that number to 30.54 full-time equivalent employees. *See* Treas. Reg. § 54.4980H-2(c)(2).

4. Determining Applicable Large Employer Status

Status as an ALE is based on the number of full-time employees on "business days" during the preceding calendar year.[38] The reference to "business days" is not explained. For example, must an employer have the requisite number of full-time employees on all of the business days of the prior year, or on at least half[39] of those days? Is passing the threshold on just one business day enough to make the employer an ALE?

The IRS has provided a multi-step method for calculating the number of full-time employees during the preceding calendar year that does not distinguish between business days and non-business days.[40] Rather than looking at days, the method focuses on the number of full-time employees during each calendar month and then obtains an average number of full-time employees by dividing by 12. Specifically, the method entails the following steps:

- Step 1: Calculate the number of full-time employees (including seasonal workers) for each calendar month in the preceding calendar year.
- Step 2: Calculate the number of full-time equivalents (including seasonal workers) for each calendar month in the preceding calendar year (using the method described above).
- Step 3: Add the number of full-time employees and full-time equivalents obtained in Steps 1 and 2 for each month of the preceding calendar year.
- Step 4: Add up the 12 monthly numbers from Step 3 and divide the sum by 12. This is the average number of full-time employees for the preceding calendar year.[41]
- Step 5: If the number obtained in Step 4 is less than 50, then the employer is not an ALE for the current calendar year. If the number obtained in Step 4 is 50 or greater and the employer included seasonal workers in Step 1 and/or Step 2, the employer may then apply a special rule for seasonal workers. This rule is described below.

Note that the determination of ALE status is made retrospectively—employees would be counted in 2014 to determine applicable large employer status in 2015.[42]

> **Example: ALE With Full-Time Equivalent Employees.** During each calendar month of 2015, Nano has 20 full-time employees, each of whom averages 35 hours of service per week; 40 employees, each of whom averages 90 hours of service per calendar month; and no seasonal workers.
>
> Each of the 20 employees who average 35 hours of service per week count as one full-time employee for each calendar month. To determine the number of full-time equivalent employees for each calendar month, the total hours of service of the employees who are not full-time employees (but not more than 120 hours of service per employee) are aggregated and divided by 120. The result is that the employer has 30 full-time equivalent employees for each calendar month ($40 \times 90 = 3{,}600$, and $3{,}600 \div 120 = 30$). Because Nano has 50 full-time employees (the sum of 20 full-time employees and 30 full-time equivalent employees) during each calendar month in 2015, and because the seasonal worker exception is not applicable, Nano is an ALE for 2016.*

* Treas. Reg. § 54.4980H-2(d), Example 2.

38 Code § 4980H(c)(2); Treas. Reg. § 54.4980H-1(a)(4).

39 As a comparison, for purposes of applying the small employer exception under COBRA, an employer is considered to have normally employed fewer than 20 employees during a particular calendar year if it had fewer than 20 employees on at least 50% of its typical business days during that year. Treas. Reg. § 54.4980B-2, Q/A-5(b).

40 Treas. Reg. § 54.4980H-2(b)(1).

41 Fractional amounts are disregarded, meaning that the employer can round down to the next-lowest whole number after dividing by 12 (i.e., 49.9 equals 49 full-time employees).

42 Code § 4980H(c)(2) defines applicable large employer as one who employed at least 50 full-time employees on business days "during the preceding calendar year."

Important Transition Rules Relating to Applicable Large Employer Status for 2015. The regulations provide 2015 transition relief for certain ALEs with fewer than 100 full-time employees (including full-time equivalent employees). In addition, another transition rule allows employers to choose any period of six consecutive months in 2014 (rather than the entire calendar year) to determine their ALE status for 2015.* (Separate considerations apply for meeting the requirements of the seasonal worker exception, discussed below).

For a full discussion of these (and other) transition rules, see subsection F.

* Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8573, 8575–8576 (Feb. 12, 2014).

5. Disregarding Seasonal Workers in Certain Cases

Note: Seasonal Workers Must Be Counted. Code § 4980H(c)(2) generally requires the inclusion of seasonal workers in the ALE determination.* These workers may be excluded in certain cases, when determining ALE status, only if specified conditions are satisfied—see discussion below.

* Treas. Reg. § 54.4980H-2(b)(2).

The regulations define a "seasonal worker" as a worker who performs labor or services on a seasonal basis as defined by the Secretary of Labor[43] and retail workers employed exclusively during holiday seasons. Employers may apply a reasonable, good faith interpretation of the term "seasonal worker" and a reasonable good faith interpretation of the DOL regulation (including as applied by analogy to workers and employment positions not otherwise covered under the regulation).[44]

Compare: Seasonal Workers and Seasonal Employees. There are separate rules relating to seasonal employees in the context of applying the IRS safe harbors for determining full-time employee status to determine whether a penalty tax is payable (see subsection C).

An employer with 50 or more full-time employees can avoid ALE status if—

- the employer's workforce exceeds 50 full-time employees for 120 days or fewer[45] during the calendar year; and
- the employees in excess of 50 employed during such 120-day period were seasonal workers.[46]

This rule makes it easier to avoid ALE status where the employer's non-seasonal workforce (including full-time equivalents for part-time employees) is 50 or fewer employees.

43 This includes (but is not limited to) workers covered by 29 CFR § 500.20(s)(1).

44 Treas. Reg. § 54.4980H-1(a)(39).

45 The IRS has indicated that four calendar months will be treated as equivalent to 120 days. The four calendar months and the 120 days are not required to be consecutive. *See* Treas. Reg. § 54.4980H-2(b)(2).

46 Code § 4980H(c)(2)(B); Treas. Reg. § 54.4980H-2(b)(2).

Example: Seasonal Worker Exception. During 2015, Farmco has 40 full-time employees for the entire calendar year, none of whom are workers. In addition, Farmco also has 80 full-time workers who work from September through December 2015. Farmco has no part-time employees who would be counted as full-time equivalent employees during 2015.

Before applying the worker exception, Farmco has 40 full-time employees during each of eight calendar months of 2015 and 120 full-time employees during each of four calendar months of 2015, resulting in an average of 66.67 employees [(40 × 8) plus (120 × 4) divided by 12 equals 66.67].

However, Farmco can apply the seasonal worker exception because its workforce exceeded 50 full-time employees for only four calendar months (treated as the equivalent of 120 days) during 2015, and the number of full-time employees would be less than 50 during those months if seasonal workers were disregarded. Thus, Farmco is not an ALE for 2016.*

* Treas. Reg. § 54.4980H-2(d), Example 3.

Example: Seasonal Workers and Other Full-Time Equivalent Employees. Same facts as above example, except that Farmco has 20 full-time equivalent employees in August, some of whom are seasonal workers.

The seasonal worker exception described above does not apply if the number of an employer's full-time employees (including seasonal workers) and full-time equivalent employees exceeds 50 for more than 120 days during the calendar year. Because Farmco has at least 50 full-time employees for a period greater than four calendar months (treated as the equivalent of 120 days) during 2015, the exception does not apply. Farmco averaged 68 full-time employees in 2015: [((40 × 7) + (60 × 1) + (120 × 4)) ÷ 12 = 68.33]. And accordingly, Farmco is an ALE for calendar year 2016.*

* Treas. Reg. § 54.4980H-2(d), Example 4.

In the case of an employer that was not in existence on any business day during the preceding calendar year (see discussion below), the seasonal worker exception applies so that the employer will not be treated as an ALE if it reasonably expects (a) its workforce to exceed 50 full-time employees (including full-time equivalent employees) for 120 days or fewer during the current calendar year, and (b) the employees in excess of 50 employed during such 120-day period to be seasonal workers.[47]

6. New Employers: Special Rule for Employers Not in Existence in Preceding Year

If an employer was not in existence throughout the preceding calendar year, the determination of whether the employer is an ALE is based on the average number of full-time employees that the employer is reasonably expected to employ on business days in the current calendar year.[48]

[47] Treas. Reg. § 54.4980H-2(b)(2); Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8547–8548 (Feb. 12, 2014).

[48] Code § 4980H(c)(2)(C)(ii); Treas. Reg. § 54.4980H-2(b)(3).

Example: New Employer. Newbie Corp. is incorporated on January 1, 2016. On January 1, 2016, Newbie has three employees. However, prior to incorporation, Newbie's owners purchased a factory intended to open within two calendar months of incorporation and to employ approximately 100 full-time employees. By March 15, 2016, Newbie has more than 75 full-time employees.

Because Newbie can reasonably be expected to employ on average at least 50 full-time employees on business days during 2016, and actually employs an average of at least 50 full-time employees on business days during 2016, Newbie is an ALE (and an ALE member) for calendar year 2016.*

* Treas. Reg. § 54.4980H-2(d), Example 5.

The determination of whether a new employer is an ALE during its first calendar year is based on the employer's reasonable expectations at the time the business comes into existence—even if subsequent events cause the actual number of full-time employees (including full-time equivalent employees) to exceed that reasonable expectation.[49]

The regulations clarify that an employer is treated as not having been in existence throughout the prior calendar year only if the employer was not in existence on any business day in the prior calendar year.[50]

Determining New Employer Status. If an employer comes into existence on May 1 of Year 1, during Year 1 the employer's status as an ALE is determined based on the average number of employees that it is reasonably expected such employer will employ on business days in the current calendar year (Year 1). To determine the employer's status as an ALE for Year 2, the employer's status as an ALE is determined based on the number of employees that it employed on business days from May 1 through December 31 of Year 1 (rather than relying on the employer's reasonable expectations).*

* Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8547 (Feb. 12, 2014).

7. Employer's First Year as an Applicable Large Employer

Commenters noted that Code § 4980H should not apply to employers for a period of time after the end of the calendar year so that employers that are close to the 50 full-time employee (plus full-time equivalent employee) threshold, whose status may be affected by data from the final calendar months of the calendar year, have time to respond to becoming an ALE.[51] To address this concern, the final regulations provide, with respect to an employee who was not offered coverage at any point in the prior calendar year, that if the ALE offers coverage on or before April 1 of the first year in which the employer is an ALE, the employer will not be subject to a penalty (for January through March of the first year the employer is an ALE) under Code § 4980H(a) by reason of its failure to offer coverage to the employee for January through March of that year, and the employer will not be subject to a penalty (for January through March of the first year the employer is an applicable large employer) under Code § 4980H(b) if the coverage offered provides minimum value.[52]

However, if the employer does not offer coverage to the employee by April 1, the employer may be subject to the Code § 4980H(a) penalty for those initial calendar months in addition to any subsequent calendar months for which coverage is not offered, and if the employer offers coverage by April 1 but the coverage does not provide minimum value, the employer may be subject to the Code § 4980H(b) penalty for those initial calendar months (in addition to any subsequent calendar months for which coverage does not provide minimum value or is not affordable). This rule applies only during the first year for which an employer is an ALE—even if the employer falls below the 50 full-time employee (plus full-time equivalent employee) threshold for a subsequent year and then expands and becomes an ALE again.[53]

---

49 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8547 (Feb. 12, 2014).

50 Treas. Reg. § 54.4980H-2(b)(3); Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8547 (Feb. 12, 2014).

51 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8548 (Feb. 12, 2014).

52 The penalties under Code § 4980H(a) and Code § 4980H(b) are discussed in subsections D and E, respectively.

53 Treas. Reg. § 54.4980H-2(b)(5).

Example: First Year as an Applicable Large Employer. As of January 1, 2015, Growth Co. has been in existence for several years and did not average 50 or more full-time employees (including full-time equivalent employees) on business days during 2014. Growth Co. averages 50 or more full-time employees on business days during 2015, so that for 2016 Growth Co. is an ALE, for the first time. For all the calendar months of 2016, Growth Co. has the same 60 full-time employees. Growth Co. offered 20 of those full-time employees health care coverage during 2015, and offered those same employees coverage providing minimum value for 2016. With respect to the 40 full-time employees who were not offered coverage during 2015, Growth Co. offers coverage providing minimum value for calendar months April 2016 through December 2016.

For the 40 full-time employees not offered coverage during 2015 and offered coverage providing minimum value for the calendar months April 2016 through December 2016, the failure to offer coverage during the calendar months January 2016 through March 2016 will not result in penalties under Code § 4980H with respect to those employees for those three calendar months. For those same 40 full-time employees, the offer of coverage during the calendar months April 2016 through December 2016 may result in a penalty under Code § 4980H(b) with respect to any employee for any calendar month for which the offer is not affordable, and the employee receives a premium tax credit on the Exchange. For the other 20 full-time employees, the offer of coverage during 2016 may result in a penalty under Code § 4980H(b) for any calendar month if the offer is not affordable and the employee received a premium tax credit on the Exchange. For all calendar months of 2016, Growth Co. will not be subject to an assessable payment under Code § 4980H(a).*

* Treas. Reg. § 54.4980H-2(d), Example 6.

8. Employers Contributing to Multiemployer Plans

The preamble to the proposed regulations provided special rules for employers participating in multiemployer plans in view of such plans' unique operating structures.[54] The final regulations provided interim guidance (discussed below) intended to continue the special rules provided in the preamble to the proposed regulations, with some clarifications.[55]

The interim guidance under the final regulations applies to an ALE member that is required by a collective bargaining agreement (or an appropriate related participation agreement) to make contributions, with respect to some or all of its employees, to a multiemployer plan that offers, to individuals who satisfy the plan's eligibility conditions, coverage that is affordable and provides minimum value, and that offers coverage to those individuals' dependents. Under the interim guidance, the ALE member will not be treated, with respect to employees for whom the employer is required by the collective bargaining agreement (or appropriate related participation agreement) to make contributions to the multiemployer plan, as failing to offer the opportunity to enroll in minimum essential coverage to full-time employees (and their dependents) for purposes of the penalty under Code § 4980H(a), and will not be subject to a penalty under Code § 4980H(b).[56]

For purposes of determining whether coverage under the multiemployer plan is affordable, employers participating in the plan may use any of the affordability safe harbors discussed in subsection E.[57]

---

54 *See* Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 78 Fed. Reg. 217, 238 (Jan. 2, 2013).

55 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8576 (Feb. 12, 2014). Any future guidance that limits the scope of the interim guidance will be applied prospectively and will apply no earlier than January 1 of the calendar year beginning at least six months after the date of issuance of the guidance.

56 Whether the employee is a full-time employee is determined under Code § 4980H(c)(4), whether coverage is affordable (for purposes of the penalty under Code § 4980H(b)) is determined under Code § 36B(c)(2)(C)(i), and whether coverage provides minimum value (also for purposes of the penalty under Code § 4980H(b)) is determined under Code § 36B(c)(2)(C)(ii). Determination of full-time employee status is discussed in detail in subsection C, and the standards for affordability and minimum value are discussed in subsection E.

57 Coverage under a multiemployer plan will also be considered affordable with respect to a full-time employee if the employee's required contribution, if any, toward self-only health coverage under the plan does not exceed 9.5% of the wages reported to the qualified multiemployer plan, which may be determined based on actual wages or an hourly wage rate under the applicable collective bargaining agreement or participation agreement.

If a penalty were due under Code § 4980H, it would be payable by a participating ALE member and that member would be responsible for identifying its full-time employees for this purpose (which would be based on hours of service for that employer). If the ALE member contributes to one or more multiemployer plans and also maintains a single employer plan, this interim guidance applies to each multiemployer plan but not to the single employer plan.

C. Penalty Tax Hinges on Whether Employer Offers Coverage to Full-Time Employees

The penalty tax actually consists of two separate taxes. The first (discussed in subsection D) applies when the employer fails to offer full-time employees the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan.[58] The second (discussed in subsection E) applies when the employer offers minimum essential coverage under an eligible employer-sponsored plan to full-time employees, but the coverage is not affordable or does not provide minimum value.[59] Accordingly, both taxes hinge on whether an employer offers eligible employer-sponsored health coverage to "full-time employees," but the nature of the penalty will depend on the cost to employees and the terms of coverage. Final regulations published in February 2014 contain rules for identifying full-time employees.[60]

> **Employer Shared Responsibility Penalties Delayed Until 2015.** The IRS has announced that it will not apply the employer shared responsibility penalties until 2015.* This is one year later than the January 1, 2014 effective date stated in the statute.† However, an employer using the look-back measurement method described in this subsection to identify full-time employees for 2015 will need to start counting hours in 2014.

* Notice 2013-45, 2013-31 I.R.B. 116.

† Pub. L. No. 111-148, § 1513(d) (provisions apply for months after December 31, 2013).

1. Identifying "Full-Time Employees"

An applicable large employer's potential penalty tax liability is determined by reference to the number of full-time employees employed in a given month. The statute defines a full-time employee, with respect to any month, as "an employee who is employed on average at least 30 hours of service per week."[61]

> **30 Hours Per Week Equals 130 Hours Per Month.** While the statute defines "full-time" as 30 hours of service per week, the regulations permit an employer to treat 130 hours of service in a calendar month as the monthly equivalent of 30 hours of service per week, provided the employer applies this equivalency rule on a reasonable and consistent basis.*

* Treas. Reg. § 54.4980H-1(a)(21)(ii). This 130 hours of service monthly equivalency applies for the look-back measurement method and the monthly measurement method for determining full-time employee status (see discussion below). Although not clear under the regulations, an employer should not be required to test an employee's full-time status using both the 30-hour weekly average and the 130-hour monthly equivalency. Rather, the employer should be able to apply the weekly average to some employees and the monthly equivalency to other employees, provided that it does so on a reasonable and consistent basis. Thus, an employee should be considered to be full-time only if the employee is credited with sufficient hours under the standard (30 hours per week or 130 hours per month) that the employer is applying to that employee. Further guidance on this would be welcome.

Although the 30-hour threshold is the same as for purposes of determining whether an employer is an "applicable large employer" (ALE), there are important differences when employees are identified as full-time for purposes of determining whether employer penalties are applicable.

---

58 Code § 4980H(a). "Minimum essential coverage" and "eligible employer-sponsored plan" are defined by cross-reference to Code § 5000A(f). Minimum essential coverage is discussed in subsection D.

59 Code § 4980H(b). Affordability and minimum value are determined under Code § 36B, which describes when individuals may qualify to purchase subsidized health insurance coverage through an Exchange. The regulations provide three safe harbors for determining whether coverage is affordable. Treas. Reg. § 54.4980H-5(e). These safe harbors are discussed in subsection E.

60 Shared Responsibility for Employers Regarding Health Coverage, 26 CFR Parts 1, 54, and 301, 79 Fed. Reg. 8543, 8546–47 (Feb. 12, 2014).

61 Code § 4980H(c)(4).

