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HEALTH CARE REFORM RECAP - SUMMER 2013

Determining Applicable Large Employer and Full-Time Employee Status: How Employers Can Avoid "Pay or Play" Penalties

INTRODUCTION

Under the Affordable Care Act ("ACA"), "applicable large employers" are required to offer affordable medical coverage to full-time employees and their dependent children, or pay a penalty for failure to offer affordable coverage. This requirement, sometimes called the "employer mandate" or "pay or play", becomes effective for plan years beginning on and after 1/1/2014.

DETERMINING APPLICABLE LARGE EMPLOYER STATUS

An "applicable large employer" will employ 50 or more full-time or full-time equivalent employees. For many employers, determining whether they are a large or small employer will be easy. However, some employers may fluctuate monthly from 50 or over to fewer than 50 employees, depending on open positions or seasonal demands on the business.

An employer's "applicable large employer" status for a calendar year is determined on a month-to-month basis based on the previous calendar year. For 2014, an employer will use months in calendar year 2013, but will be able to use just six consecutive months under a transitional rule. The "counting" rule will then revert to a full 12 months in future years.

For this "middle" group of employers whose size may fluctuate just over or just under 50 full-time or full-time equivalent employees, knowing how and who to count is critical to determining if they will be subject to the large employer mandate and potentially subject to penalties for not offering affordable insurance coverage to full-time employees. To make this determination, follow these steps:

- Count all employees on a month-to-month basis, regardless of benefits eligibility. Count full-time employees, part-time employees and certain seasonal employees (see below). Don't count independent contractors or temporary employees hired from an outside agency. Do count temporary employees to whom your business issues a W-2.
- Each full-time employee working 30 or more hours per week is counted as one employee.

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Part-time employees are converted to full-time equivalent employees:

Count the total hours worked by your part-time employees in a month and divide by 120, then round down to a whole number. For example, 1,360 part time hours in a month/120 = 11.33, which is 11 full-time equivalent employees for that month.

- Each seasonal employee is included in the months of employment as one employee if he/she works 30 hours or more, but can be excluded if he/she works no more than 120 days in a year, which need not be consecutive days.
- Add 2, 3, and 4 together and divide by 12 (or 6 if the transitional rule is used). Round down to a whole number. If the average is 50 or more, the employer is subject to the employer mandate.

Remember that employers who are members of a controlled group are treated as single employers, and must include all the employees from the member companies when determining "applicable large employer" status.

I'M AN APPLICABLE LARGE EMPLOYER, NOW WHAT?

More Counting!

And, of course, the counting rules for complying with the employer mandate ("playing" rather than "paying") are different from the applicable large employer counting rules, because the focus now is on identifying full-time employees to whom an applicable large employer must offer affordable medical coverage in order to avoid a penalty.

HOW TO COUNT HOURS

It's important to note that some employees you now classify as part-time, per diem, temporary or seasonal could be ACA-full-time employees if they average at least 30 hours based upon hours worked, not hours scheduled. Hours "worked" are determined as follows:

For hourly employees, include hours paid for work performed and hours paid for periods during which no work is performed (vacation, sick, holiday, jury duty, paid leave).

For salaried employees, credit 8 hours for each day for which the employee is credited with at least one hour of service, or credit 40 hours per week for each week in which the employee is credited with at least one hour of service (useful to avoid understating hours if an employee works partial weeks but more than 8 hours per day worked).

DETERMINING FULL-TIME STATUS – ONGOING EMPLOYEES

Proposed regulations set out a safe harbor method for determining who is an ACA-full-time *ongoing* (i.e., not new) employee:

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There is a standard measurement period prior to the beginning of the plan year during which a large employer will count hours and determine which employees, on average, work at least 30 hours per week – that is, which employees are “ACA-full-time” – and must be offered medical coverage for the coming plan year so that the large employer avoids the “no offer” penalty.

A standard measurement period can be up to 12 months (typically ending in time for open enrollment), but can be 6 months for 2014 and 12 months for subsequent plan years.

Immediately following the standard measurement period there may be an administrative period (of no more than 90 days) during which a large employer will offer coverage for the coming plan year to any employee determined to be ACA-full-time during the standard measurement period. That coverage must become effective no later than the 1st day of the coming plan year.

Finally, there is a stability period (of no more than 12 months, typically the plan year) during which a large employer will continue to treat employees as ACA-full-time or not, based on the determination made during the standard measurement period, regardless of their average weekly hours during the stability period (whether more, or less, than during the measuring period).

DETERMINING FULL-TIME STATUS – NEW EMPLOYEES

Full-Time at the Start

For a new employee hired with the expectation he/she will work an average of at least 30 hours per week and is not seasonal (that is, someone hired as an ACA-full-time employee), there is no measurement or administrative period. That employee must be offered coverage that **becomes effective** no later than 90 days following his/her date of hire.

Variable Hour or Seasonal Employees

For a newly-hired variable hour or seasonal employee, the process works a bit differently, because the initial measuring period is specific to each employee, and runs for a period of up to 12 months, generally from the employee’s date of hire.

“Variable hour employee” means an employee for whom, as of his/her date of hire, it can’t be determined that he/she is reasonably expected to work an average of at least 30 hours per week.

“Seasonal employee” has not yet been defined in regulations, but for 2014, large employers are permitted to use a “reasonable good faith” definition. *The “120 day rule” described above for use in determining applicable large employer status does not apply to determining which employees must be offered coverage (at least not as of this writing – stay tuned for future regulations).*

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If during that initial, employee-specific measurement period the new employee works on average at least 30 hours per week, then at the end of the measurement period the employee is deemed an ACA-full-time employee and, during the administrative period, must be offered coverage that **becomes effective** no later than the first day of the month that begins on or immediately after the 13-month anniversary of his/her date of hire.

If a new variable hour employee has a material change in employment status during the initial measuring period such that if he/she had been initially hired into the new position he/she would have been treated like an ACA-full-time employee from date of hire, then the initial, employee-specific measurement period ends for that employee and he/she must be offered coverage that will become effective no later than 90 days following the change in status to ACA-full-time.

Temporary Employees

New full-time temporary employees (who work at an ACA-full-time rate but for limited duration) generally must be treated like any other ACA-full-time employee (*i.e.*, offered coverage that **becomes effective** no later than 90 days following date of hire), regardless of whether they will be employed for the entire standard measurement period.

For the 2014 plan year, there is some leeway to treat full-time temporary employees as variable hour employees, and thus subject them to an initial, employee-specific waiting period. However, for the 2015 plan year (and thereafter), new full-time temps **cannot** be treated as new variable hour employees just because they may not be employed for the entire standard measurement period. Large employers may decide it is “cleaner” to adopt the 2015 rule for 2014.

EXAMPLE

The ABC Company wants to determine if it is an “applicable large employer” for the Affordable Care Act employer mandate, and if so, to whom it may need to offer medical coverage in 2014. Since its insurance contract shows only 47 eligible employees, ABC has always been treated as a small employer, but now is unsure whether that will continue to be true for purposes of the employer mandate.

The first step it takes is to review its payroll register, time and attendance system or HRIS system to determine how many individuals it employs and for how many hours. ABC does this **for each month in a 6 consecutive month period** during 2013. One month’s analysis is shown in Chart 1 (*on next page*).

An analysis of one summer month shows that ABC employs 93 employees. Of those, 47 employees work 40 hours per week and have always been offered medical coverage. Another 29 employees are part-time, but have flexible hours each week. There are 7 employees hired from June to September to cover for vacations and there are 10 temporary employees from a leasing company working on a long-term IT project.

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CHART 1

Employee Classification	Total Hours This Month	Calculation	Employees/Full-time Equivalent Employees
47 Full-time Employees	N/A	N/A	47
29 Part-Time Variable Hour Employees	3100	3100/120 Hours	25 full-time equivalent employees
7 Summer Employees	NA - work fewer than 120 days each year		0
7 Temporary Leased Employees	NA - not ABC's common law employees		0
TOTAL FULL-TIME AND FULL-TIME EQUIVALENT EMPLOYEES THIS MONTH		47 + 25	72

ABC determines the number of full-time and full-time equivalent employees for each of the 6 months and averages them. Its 6-month average is 68 full-time and full-time equivalent employees.

Now that ABC Company knows it is an applicable large employer for purposes of the 2014 employer mandate, it knows it will have to offer its full-time employees medical coverage. The next step is to determine how many of the part-time variable hour and seasonal employees will be eligible for medical coverage. First, ABC determines the appropriate measurement period to count the hours of these employees. ABC has chosen a 6 consecutive month period beginning April 15, 2013, as its look-back measurement period to determine which of the variable hour and seasonal employees average **30 hours** or more per week and must be offered medical coverage, regardless of whether ABC considers 30 hours full-time. This calculation is done individually **for each employee**. Four employees are profiled below. The ABC Company's plan year (which it has also chosen as its stability period) begins January 1st and its annual open enrollment period is November 1st – 30th. It has chosen an administrative period which runs from October 15th – December 31st.

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CHART 2

Employee Name	April-May hrs worked	May-June hrs worked	June-July hrs worked	July-Aug hrs worked	Aug-Sept hrs worked	Sept-Oct hrs worked	Total Hours	Average Hours Worked During the Measurement Period
John Smith	90	100	160	160	90	77	67	26.03
Mary Allen	120	110	160	160	120	110	780	30
Tom Jones	55	120	120	160	120	75	650	25
Sue Brown	75	75	120	160	75	75	580	22.3

Based on the 6-month measurement period, the only employee of these four who must be offered medical coverage for January 1st is Mary Allen. She must be treated as a full-time employee for the entire 2014 stability period, regardless of whether her average hours dip below 30 per week during the stability period.

On October 15, 2013, ABC begins a 12-month measurement period for its on-going employees to determine who must be offered coverage for the 2015 stability period/plan year. And during 2014, it is continually evaluating its new employees to determine who is hired for at least 30 hours per week and who is hired as a variable hour or seasonal employee and can be evaluated during his or her own initial measurement period.

REMINDERS

Although this Recap focuses on a large employer’s obligation to offer medical coverage to full-time employees and their dependent children, it’s important to note that there is a second prong to the pay or play rules: *the coverage offered must also be affordable* or the employer will be subject to a different monetary penalty. Affordability of coverage will be the subject of a future update once there is more guidance from Washington.

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