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The Top 10 Changes Made to the 2012 Proposed Rule Under the Affordable Care Act's Employer Shared Responsibility Rules by Recently Issued Final Regulations

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The Treasury Department and Internal Revenue Service recently issued final regulations (available at http://op.bna.com/dlrcases.nsf/id/kpin-9g8snn/$File/2014-03082_PI.pdf) implementing the employer shared responsibility provisions of the Affordable Care Act. For "applicable large employers" — i.e., those with an average of 50 or more full-time and full-time equivalent employees on business days during the prior calendar year — these are perhaps the Act's most important provisions. The final regulations provide employers with the answers to two key questions: What's this requirement going to cost? And, what changes do I need to make to my group health plan(s) to come into compliance?

The Act's employer shared responsibility provisions take the form of amendments to the Internal Revenue Code. Specifically, the Act added new Code Section 4980H, which provides that an applicable large employer is subject to an assessable payment if one or more full-time employees is certified to the employer as having received an applicable premium tax credit or cost-sharing reduction and either:

- The employer fails to offer to its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer sponsored plan; or
- The employer offers its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan but the coverage fails to meet requirements for affordability and minimum value.

The employer shared responsibility rules were originally slated to go into effect beginning January 1, 2014, but enforcement was delayed for one year to January 1, 2015 by IRS Notice 2013-45 (available at: http://www.irs.gov/pub/irs-drop/n-13-45.pdf). In a series of notices issued in 2011 and 2012, the Treasury Department and IRS offered proposals and invited public comments on issues relating to the definition of terms such as "employer," "employee," and "hour of service." The proposals also included an approach to use an optional look-back measurement method for determining full-time employee status, and an affordability safe harbor. Taking into account the comments received in response to this series of notices, the Treasury Department and the IRS released a proposed regulation on December 28, 2012.

While the final regulations make many welcome and important refinements, they break little new ground. The basic regulatory structures implementing the Act's employer shared responsibility rules as set out in proposed regulations and earlier guidance (discussed in our January 16, 2013 client advisory) remain intact. The final regulations instead (i) fix glitches in the proposed regulations, (ii) provide some important clarifications of certain provisions of the proposed regulations, and (iii) extend and expand the transition rules that were originally offered in the preamble to the proposed regulations.

Set out below are ten changes made in the final regulations that (in our view) are among the most important:

Item No.	Proposed Regulations	Final Regulations
1.	*Definition of "seasonal employee"* The proposed regulations did not supply a definition of "seasonal employee." Instead, they provided (consistent with Notice 2012–58) that employers could apply a reasonable, good faith interpretation of the term through 2014.	Treas. Reg. § 54.4980H-1(a)(38) defines the term "seasonal employee" to mean, "an employee who is hired into a position for which the customary annual employment is six months or less."
2.	*Exclusions from definition of "Hour of Service" for volunteers* The proposed regulations did not include specific exclusions for volunteers.	Treas. Reg. § 54.4980H-1(a)(24) (definition of hour of service) excludes hours of service of bona fide volunteers. Under Treas. Reg. § 54.4980H-1(a)(7) the term "bona fide volunteer" means an employee of a government entity or an organization described in section 501(c) that is exempt from taxation under section 501(a) whose only compensation from that entity or organization is in the form of — (i) Reimbursement for (or reasonable allowance for) reasonable expenses incurred in the performance of services by volunteers; or (ii) Reasonable benefits (including length of service awards), and nominal fees, customarily paid by similar entities in connection with the performance of services by volunteers.
3.	*Clarification of whether and when an employer can test compliance month-by-month vs. under the look-back measurement method* The proposed regulations provided for the testing of ongoing, new variable hour, and new seasonal employees under the "look-back measurement method." But the scope of the look-back measurement method was not clear.	Treas. Reg. § 54.4980H-3 clearly delineates and provides rules for two options for testing compliance with Code § 4980H: (i) The "monthly measurement method" under Treas. Reg. § 54.4980H-3(c); and (ii) The "look-back measurement method" under Treas. Reg. § 54.4980H-3(d). Treas. Reg. § 54.4980H-3(e) provides rules that permit the use of different methods for different categories of employees (i.e., salaried vs. hourly, employees in different states and collectively bargained vs. non-collectively bargained), and also sets forth rules for changing from one method to the other.
4.	*Definition of "part-time employee"* The proposed regulations did not define the term "part-time" employee.	Treas. Reg. § 54.4980H-1(a)(32) defines "part-time employee" to mean "a new employee who the applicable large employer member reasonably expects to be employed on average less than 30 hours of service per week during the initial measurement period, based on the facts and circumstances at the employee's start date." Part-time employees are tested along with new variable hour and new seasonal employees under the provisions of the look-back measurement method dealing with the initial

		measurement periods. Once a part-time employee has been employed for a full standard measurement period, he or she is tested as an "ongoing employee."
5.	*Rules for stability periods that are longer than the associated measurement period* The proposed rules governing the application of the look-back measurement method include a minor glitch under which there could be a period of time between the stability period associated with the initial measurement period and the stability period associated with the first full standard measurement period during which a variable hour employee or seasonal employee has been employed. The preamble to the final regulations notes that "[t]his generally may occur in cases in which a new employee begins providing services a short period after the beginning of the standard measurement period that would apply to the employee if the employee were an ongoing employee." (79 Fed. Reg. p. 8,559)	Treas. Reg. § 54.4980H-3(d)(1)(vi) furnishes the following solution to this conundrum: "To prevent this administrative period from creating a period during which coverage is not available, the administrative period must overlap with the prior stability period, so that, during any such administrative period applicable to ongoing employees following a standard measurement period, ongoing employees who are enrolled in coverage because of their status as full-time employees based on a prior measurement period must continue to be covered through the administrative period."
6.	*Hours of service for adjunct faculty* The preamble to the proposed regulations acknowledged that hours of service of adjunct faculty pose certain challenges, but no special rule or accommodation was included. Instead, the preamble provided (78 Fed. Reg. p. 225) that: "Until further guidance is issued, employers of employees … must use a reasonable method for crediting hours of service that is consistent with the purposes of section 4980H. A method of crediting hours would not be reasonable if it took into account only some of an employee's hours of service with the effect of recharacterizing, as non-fulltime, an employee in a position that traditionally involves more than 30 hours of service per week."	The preamble to the final rule includes the following safe harbor (79 Fed. Reg. p. 8,552): "The Treasury Department and the IRS have determined that, until further guidance is issued, one (but not the only) method that is reasonable for this purpose would credit an adjunct faculty member of an institution of higher education with (a) 2¼ hours of service (representing a combination of teaching or classroom time and time performing related tasks such as class preparation and grading of examinations or papers) per week for each hour of teaching or classroom time (in other words, in addition to crediting an hour of service for each hour teaching in the classroom, this method would credit an additional 1¼ hours for activities such as class preparation and grading) and, separately, (b) an hour of service per week for each additional hour outside of the classroom the faculty member spends performing duties he or she is required to perform (such as required office hours or required attendance at faculty meetings)."

7.	*Break-in-service rules* Prop. Treas. Reg. § 54.4980H-3(e) provided a rule under which "for purposes of Code § 4980H, an employee who resumes providing services to (or is otherwise credited with an hour of service for) an applicable large employer after a period during which the employee was not credited with any hours of service may be treated as having terminated employment and having been rehired, and therefore may be treated as a new employee upon the resumption of services only if the employee did not have an hour of service for the applicable large employer *for a period of at least 26 consecutive weeks*." (Emphasis added.) The proposed regulations also provided for a rule of parity that was not changed by the final regulations. Under that rule, an employee may be treated as having terminated employment and having been rehired after at the greater of (i) four consecutive weeks during which the employee was not credited with any hours of service, or (ii) a period that exceeds the most recent period of service.	Treas. Reg. § 4980H-3(c)(4)(v) reduces the 26 consecutive week period for employers other than educational organizations to 13 consecutive weeks. The 26 consecutive week period rule is retained for educational organizations.
8.	*Definition of Dependent* Noting that Code § 4980H does not define the term "dependent," the proposed regulations define an employee's dependent "as an employee's child (as defined in section 152(f)(1)) who is under 26 years of age. A child attains age 26 on the 26th anniversary of the date the child was born." Code § 152(f) defines the term to include biological children, stepchildren, adopted children, and foster children.	Treas. Reg. § 4980H-1(a)(12) defines the term "dependent" to mean: "[A] child (as defined in section 152(f)(1) but excluding a stepson, stepdaughter or an eligible foster child (and excluding any individual who is excluded from the definition of dependent under section 152 by operation of section 152(b)(3))) of an employee who has not attained age 26."
9.	*Proposed regulations — transitional relief* The preamble to the proposed regulations includes transition guidance addressing: (i) The application of Code section 4980H to applicable large employers with fiscal year plans; (ii) Salary reduction elections for accident and health plans provided through cafeteria plans with non-calendar year plan years beginning in 2013; (iii) For purposes of determining full-time employee status, measurement periods for stability periods starting in 2014; (iv) The application of Code section 4980H to applicable large employer members participating in multiemployer plans;	The final regulations make these changes: (i) The relief for fiscal year plans — which the preamble to the final regulation refers to as "non-calendar year plans" — was extended and expanded, and a new option (based on coverage and offers of coverage for full-time employees only) was added; (ii) The relief for salary reduction elections was clarified in Notice 2013-71, but the final regulations made no further changes; (iii) For purposes of determining full-time employee status, a shorter measurement period is permitted; (iv) The application of Code section 4980H to applicable large employer members participating in multiemployer plans is extended and clarified;

	(v) The determination of applicable large employer status for 2014; (vi) The application of Code section 4980H to an offer of coverage to a full-time employee's dependents; and (vii) For purposes of determining full-time employee status, variable hour employee determinations.	(v) The rules governing the determination of applicable large employer status for 2014 are extended, and new rules were added under which offers of coverage in the first year of applicable large employer status need not commence until April 1 (rather than January 1); (vi) The transition rule relating to offers of dependent coverage is extended; and (vii) The transition rule for determining full-time employee status and variable hour employee determinations are extended.
10.	*New transitional relief*	The preamble to the final regulations added two important, new transition rules: (i) For employers that meet the conditions below and have fewer than 100 full-time employees (including full-time equivalents) in 2014, the employer shared responsibility rules are delayed until the first day of the 2016 plan year. To be eligible for this relief, an employer will be required to certify that it meets the following conditions: • The employer must employ on average at least 50 full-time employees (including full-time equivalents) but fewer than 100 full-time employees (including full-time equivalents) on business days during 2014; • During the period beginning on February 9, 2014 and ending on December 31, 2014, the employer may not reduce the size of its workforce or the overall hours of service of its employees in order to qualify for the transition relief (other than for bona fide business reasons); and • During the period beginning on February 9, 2014 and ending on the last day of the 2015 plan year, the employer does not eliminate or materially reduce the health coverage, if any, it offered as of February 9, 2014. (ii) Under the proposed regulations, an employer is deemed to have failed to make an offer of coverage to its full-time employees if it does not offer health coverage or offers coverage to fewer than 95% of its full-time employees and (unless the employer qualifies for the 2015 dependent coverage transition relief) the dependents of those employees. For 2015 (and for any calendar months during a non-calendar year plan year beginning in 2015 that fall in 2016), the 95% threshold is lowered to 70%.

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