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The Affordable Care Act—Countdown to Compliance for Employers, Week 36: Hacking the Affordable Care Act's $100/Day Penalties for Insurance Market Reform Violations

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Particularly with the issuance of **final regulations** under the Affordable Care Act's employer shared responsibility rules, employers have been concerned—justifiably—with the pay-or-play penalties. Human resource, finance, even senior management personnel of affected employers (i.e., generally, those employers who employed an average of at least 50 full-time employees on business days during the preceding calendar year) want to know, what's this going to cost me, and what does it mean for the maintenance and operation of our group health plans?

But the penalties imposed under Internal Revenue Code section 4980H (the provision of the Code where the pay-or-play penalties live) are not the only penalties imposed by the Act. The Act's insurance market reforms apply to, and potentially impose penalties on, state-licensed insurance carriers ("health insurance issuers" in the parlance of the Act) in the individual and group markets, as well as group health plans, irrespective of the size of the sponsoring employer or employee organization. These reforms include limits on waiting periods, a ban on rescissions, extension of dependent coverage to age 26, the obligation to issue summaries of benefits and coverage, and many more. (A comprehensive listing of the Act's insurance market reforms prepared by the National Association of Insurance Commissioners is available at **here**.)

The Act's insurance market reforms took the form of amendments to the Public Health Service Act, which generally apply to health insurance issuers and to self-funded, non-federal governmental group plans, but not to group health plans. Following a pattern first established with the health care continuation rules enacted by the Consolidated Budget Reconciliation Act of 1985 (COBRA), Congress incorporated the Act's insurance market reforms into both the Internal Revenue Code and ERISA. The effect of this incorporation is to extend the rules to employer-sponsored group health plans.

Where group health plans are concerned, the most worrisome penalty for violation of the ACA insurance market reforms is the $100 per day penalty imposed during the "noncompliance period" by Internal Revenue Code Section 4980D. The noncompliance period is the period that begins on the date the failure first occurs, and ends on the date the failure is corrected. The penalty is imposed "with respect to each individual to whom such failure relates." Importantly, the tax may be abated upon a showing of "reasonable cause" (e.g., if the person otherwise liable for such tax did not know or if exercising reasonable diligence would not have known that such violation existed). Relief is denied, however, where a failure is due to willful neglect. Code Section 4980D penalties must be self-reported on IRS Form 8928. This self-reporting requirement already applies to infractions involving violations of COBRA, HIPAA or Health Savings Account comparable contributions, among others. The revised Form 8928 is available **here**, and the accompanying instructions may be accessed **here**.

Too many employers have simply assumed that their carrier (in the case of fully-insured plans) or their third-party-administrator (in the case of self-funded plans) has handled compliance with the Act's insurance market reforms. In most—but not all—instances their reliance is likely warranted. In recent weeks we have encountered a spate of violations involving the failure of a small group to offer certain mandated essential health benefits (pediatric dental), failure to offer the proper alternative standard under a wellness program (not an insurance market reform issue, but the same conundrum), and the failure to adopt the prescribed limit on waiting periods, among others.

So what is an employer to do?

The regulators have yet to provide rules specific to the waiver of penalties in the case of a violation of the Act insurance market reforms that involves reasonable cause. But under provisions of the Code relating to the filing of information returns generally, penalties may be waived where the violation is due to reasonable cause and not willful neglect. (These rules are found in Internal Revenue Code §§ 6721 and 6724.) Typically, this requires a taxpayer to submit a Statement of Reasonable Cause asking that the penalties be waived. Where an employer discovers an insurance market reform violation, it could file IRS Form 8928 along with a Statement of Reasonable Cause.

Under the existing rules (Treas. Reg. §301.6724-1), to qualify for a waiver, an employer must establish that the failure is due to reasonable cause and is not due to willful neglect. The employer must also demonstrate that it "acted in a responsible manner both before and after the failure occurred."

- To establish that the cause is "reasonable," the employer must demonstrate that either there are significant mitigating factors with respect to the failure, or the failure arose from events beyond the filer's control. (Mitigating factors include, but are not limited to "the fact that prior to the failure the filer was never required to file the particular type of return or furnish the particular type of statement with respect to which the failure occurred.")
- The employer must also establish that it acted in a responsible manner both before and after the failure occurred. This means, among other things, that the correction is made promptly. Correction is considered prompt if it is made within 30 days after the date the violation is discovered or on the earliest date thereafter on which a regular submission of corrections is made.

As explained above, relief is denied where the failure to comply results from willful neglect. Whether ignorance of a insurance market reform rule constitutes willful neglect is not clear—at least not to us. While certain of these rules go back to 2010, others did not take effect until January 1, 2014. Presumably, an employer that first became aware of a violation in, say, 2014, would be able to qualify for a waiver based on reasonable cause. Whether the result would be the same in, say, 2018, is less than clear.

Authors