Employee Benefit Compliance Support Services

Benefit Comply

Compliance Alert

**IRS Increases ACA “Affordability” Percentage**

**Issue Date: August 2014**

On July 24, 2014, the IRS issued guidance in Revenue Procedure 2014-37 that increases the percentage from 9.5% to 9.56% effective in 2015 for purposes of determining the affordability of employer-sponsored group health coverage under the §4980H employer shared responsibility rules. This increased percentage will affect which applicable large employers may face potential penalties for failure to provide affordable coverage and which individuals may qualify for subsidized coverage through a public Marketplace.

**Background**

Under the employer shared responsibility rules, the employer must offer coverage that is affordable to avoid potential §4980H(b) penalties. In addition, individuals enrolling for coverage through a public Marketplace will not qualify for subsidized coverage if they are eligible for employer-sponsored group health coverage that is affordable.

Coverage is “affordable” if the employee contribution for employee-only (single) coverage does not exceed the required contribution percentage of household income.

*Note – Coverage is considered affordable for dependents as well, regardless of the contribution amount, as long as the employee-only (single) coverage is affordable.*

**Required contribution percentage**

Originally, for 2014, the required contribution percentage for determining affordability was set at 9.5%. This percentage is adjusted annually to reflect the excess of the rate of premium growth for the preceding calendar year over the rate of income growth for the preceding calendar year.

For 2015, as long as the employee contribution for employee-only (single) coverage does not exceed 9.56%, coverage will be deemed affordable for employees and any dependents eligible for coverage. The affordability will be indexed for future plan years.

**Employer safe harbors**

Affordability is based on an individual’s household income. A household, for purposes of determining eligibility for premium tax credits, includes any individuals for whom a taxpayer claims a personal exemption on the federal tax form. Household income is based on an individual’s modified adjusted gross income (MAGI).

An employer is unlikely to be able to determine an employee’s household income, so the IRS provided employers with three safe harbor methods. As long as coverage is affordable using one of the safe harbor methods, it is not necessary for the employer to determine employees’ actual household incomes.

* **Rate of Pay Safe Harbor** – Take the hourly rate of pay for each hourly employee and multiply that rate by 130 hours per month to determine a monthly “rate of pay.” The employee’s monthly contribution amount is affordable if it is equal to or lower than 9.56% of this computed monthly wage estimate, regardless of the number of hours the person actually works.
* **Federal Poverty Line Safe Harbor** - Coverage is affordable if the employee’s monthly contribution does not exceed 9.56% of the FPL for a single individual.
* **Form W-2 Safe Harbor** – Coverage is affordable if the employee’s monthly contribution does not exceed 9.56% of annual Form W-2 wages (as reported in Box 1). This is calculated retrospectively for the previous calendar year. To qualify for this safe harbor, the employee’s required contribution must remain a consistent amount or a consistent percentage of all Form W-2 wages during the year.

*NOTE – Subsidy eligibility will always be based on household income. However, if an individual qualifies for a subsidy because the employee contribution is deemed unaffordable using household income, but the employer can show that the coverage is affordable using one of the safe harbor methods listed above, the employer will avoid a penalty under 4980H(b) so long as the coverage also provides minimum value.*

**Examples**

The small change in the affordability percentage will make very little difference in which employer plans are considered affordable for an individual. Consider the following examples:

* For an employee with an annual household income of $30,000, an employer plan is considered affordable if the employee contribution for single coverage does not exceed:
  + $237.50 per month at 9.5%
  + $239.00 per month at 9.56%
* Or to look at it another way, if an employer requires a $200 per month contribution for single coverage, the plan is affordable for any employee with an annual household income of at least:
  + $25,236.16 at 9.5%
  + $25,104.60 at 9.56%

In other words, in the example of an employer who is charged $200 per month for single coverage, the percentage change will affect only employees with household incomes between $25,104.60 and $25,236.16. Obviously, this will be a very small number of employees.

**Summary**

Beginning in 2015, applicable large employers subject to the employer shared responsibility rules may need to make minor adjustments to contribution levels, at least for employee-only (single) coverage, to ensure that coverage is affordable to avoid potential penalties (Section 4980H(b) penalties).

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