The Affordable Care Act:
A Guide for Independent Schools

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February 2015
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I. General Overview

The Patient Protection and Affordable Care Act of 2010 (the “ACA”) is intended to make healthcare affordable and accessible for more Americans. To that end, it requires large employers to provide affordable coverage for employees and provides for those who do not work for large employers by creating state-specific insurance marketplaces (the “Exchange”) and government subsidies. On the flip side, the ACA requires all individuals to carry insurance, thus widening the pool of healthy and young participants, with the idea of reducing the cost of coverage for everyone.

This new approach to healthcare has been a sea change for both employers and their employees. In the past, an independent school that chose to maintain a health plan was subject to certain laws such as the Employment Retirement Income Security Act (ERISA) and the Health Insurance Portability and Accountability Act (HIPAA). However, the decision of whether to offer a health plan in the first place was always up to the school itself. Now, if the school is a large employer, it must offer coverage or pay penalties. In addition, the school should expect most of its workforce to accept its offer of coverage because individuals must now carry coverage or pay a tax penalty. Just as the employer has little choice about the matter, the same is true for their employees.

While these requirements seem straightforward, administering ACA-compliant health plans is not always intuitive. This guide explains your obligations as an employer, including requirements particular to educational institutions, as well as the new requirements faced by your employees. Understanding these requirements is vital to avoiding penalties and administering your plan in a way that makes sense for your employees.

II. The Employer Mandate

Under the ACA, beginning in 2015, large employers must offer affordable healthcare coverage that meets federal government minimum value requirements to their full-time employees and their children or face penalties. Understanding this requirement means first understanding whether a given school counts as a large employer under the ACA and therefore must provide insurance for its employees. For schools that are considered to be large employers, the next question is who counts as a full-time employee to whom such an offer of coverage must
be given. To answer this question, this section explains how employers are required to calculate hours under the ACA.

A. Who Is a Large Employer?

Under the ACA, an applicable large employer ("Large Employer") is an entity that employed 50 or more full-time and full-time equivalent ("FTE") employees during the preceding year. The concept of the FTE employee is relevant only when your school is determining whether it is a Large Employer; it does not come into play when you are determining who is full-time for purposes of offering coverage.

To determine whether your school is a Large Employer under the ACA, the law requires you to count full-time and FTE employees by month in the preceding year, add those numbers together, and divide by 12. Any employee who works 130 hours or more in a month is considered one full-time employee. Any employee who works 120 hours or more in a month is considered one FTE employee. For all employees who work fewer than 120 hours, employers should add those hours together and divide by 120. For example, if two employees worked 60 hours each in a month, add 60 and 60, divide by 120, and count those two employees as one FTE employee. Add the number of full-time employees and the number of FTE employees to reach a total for each month; add those totals together, and divide by 12. If the result is 50 or more employees, your school is considered a Large Employer.

1. Controlled Group Rules

The ACA applies the controlled group test, meaning that all entities with common ownership that are treated as a single employer under Tax Code § 414(b), (c), (m), or (o) are treated as one entity for the purposes of counting employees. Many employers have run the controlled group test in the context of their retirement plan. If your school is part of a larger organization such as a church or if it runs other entities such as a daycare, it is worth consulting an attorney to determine whether employees from related organizations must be counted to determine your status under the ACA.

2. Independent Contractors

Another common pitfall in ACA compliance appears when employers treat certain workers as independent contractors when they should actually be treated as employees. It is possible that, as a result of such misclassification, an employer could be subject to the ACA without realizing it.
Now is a good time to take a look at any independent contractors on your payroll to determine whether they are classified appropriately. For more information on that topic, see this piece from the IRS.

3. Transition Relief for 2015

Note that, for 2015, there is some transition relief for employers with fewer than 100 employees. Employers with fewer than 100 full-time and FTE employees during business days in 2014 will not need to comply with the employer mandate until 2016 as long as the following apply: (1) they have not reduced their workforce for the purpose of using such transition relief; (2) they have not eliminated or materially reduced health coverage offered as of February 9, 2014 (the publication date of the final regulations for the employer mandate); and (3) during ACA reporting in spring 2016, they certify on a prescribed form that they meet the eligibility requirements set forth above.

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 Large Employer status for 2015.

B. Who Is a Full-Time Employee?

The ACA requires employers to offer health coverage to their full-time employees, but determining who those employees are can get tricky. An employee is “full-time” for ACA purposes if he or she works on average at least 30 hours per week or 130 hours per month.

To count hours of service, employers should count the actual hours of service for hourly employees. For non-hourly employees, employers may count actual hours or use equivalencies and credit eight hours for each day worked or 40 hours for each week worked. An acceptable alternative to measuring hours per week is to measure hours per month, counting 130 or more as full-time.

Employers must count all hours for which an employee is paid, including vacation and paid leave. Employers must also count unpaid hours related to Family and Medical Leave Act (FMLA) leave, jury duty, and military leave. In addition, schools may not count break periods of more than four consecutive weeks (i.e., summer vacation) against employees. To deal with special leaves and break periods, employers must either exclude such time when averaging hours or credit employees during such leave time with the number of hours the employee worked on a weekly
basis during the rest of the look-back period. For example, if an employee is paid for working 35 hours a week throughout the look-back period, but takes two weeks of unpaid FMLA during that time, the school may count those weeks either as regular weeks or not include those weeks at all within the calculation. The FMLA time may not be used against the employee when determining if the employee is a full-time employee.

Some schools have become concerned about guidance in the final regulations related to counting hours for adjunct faculty. Because compensation for such individuals is not directly tied to the number of hours worked, universities were concerned that the days-worked equivalency (eight hours) would overstate actual hours, but tracking actual hours would be administratively burdensome. In response, until further guidance is issued, the IRS has identified a reasonable option to track hours by crediting 2.25 hours of service for each hour of teaching or classroom time. This method is optional and is generally appropriate only in a university setting. Schools should consider whether the time teachers spend preparing lesson plans or grading is captured by their hour-counting method. However, generally speaking, if a teacher is given time during the school day to complete these tasks, there should be no need to use an equivalency such as the adjunct faculty counting method.

The real problem with counting hours is determining what time period to use for doing so. The ACA was written to require tracking hours on a monthly basis, but in practice this would create an administrative nightmare as employers scrambled to count hours and employees bounced on and off insurance plans based on their hours during the preceding month. This method is known as the “monthly counting method.” Because the government recognized the administrative issues with this method, the IRS provided an alternative framework for determining full- and part-time status.

Under this alternative, employers can look back over a period of preceding months (known as the “look-back period”) to determine how an employee should be classified for a set number of months going forward (known as a “stability period”). Employers will calculate hours during the look-back period, and then the employee will be considered as either full-time or part-time for the duration of the stability period. Employers can choose the number of months they use for the look-back period (between three and 12 months) and for the stability period (between six and 12 months). However, the stability period for full-time employees cannot be shorter than the look-back period, and the stability period for part-time employees cannot be longer than the look-back period. In addition, employers must choose one look-back period for all employees in the same
broad categories (e.g., salaried and hourly workers can be considered two different categories with different look-back periods). To simplify the process, most employers will choose both a 12-month look-back period and a 12-month stability period. The regulations also allow for an administrative period of up to 90 days between these two time frames so that employers can calculate hours and provide an open enrollment period.

Implementing a look-back/stability period is easier to understand by example. To determine who must be covered for a plan year beginning January 1, 2015, an employer could choose a look-back period of October 15, 2013, to October 14, 2014. The employer would count hours for each employee and divide by the number of weeks per year to determine whether the employee averaged 30 hours or more per week. Then, the employer would offer insurance through open enrollment at some time between October 15, 2014, and December 31, 2014. Beginning on January 1, 2015, all employees who worked more than 30 hours per week during the look-back period would be considered full-time until December 31, 2015. In October 2015, the employer would go through the hour-counting process again.

The IRS has created a special transition rule that will allow employers to use a look-back period for the 2015 plan year that is only six months long, while still using a stability period of 12 months. This is a limited transition rule that is available only for the 2015 plan year (which will apply to counting hours in 2014).

1. **Ongoing Employees**

   This system is relatively straightforward for employees who started working with you before the beginning of your look-back period (“ongoing employees”). For ongoing employees, employers must measure hours based on the look-back/stability periods they choose for each category of employees.

2. **New Employees**

   A problem arises with new employees. If you hire a new employee after the beginning of your look-back period and that employee is expected to work 30+ hours per week, then he or she must be classified as “full-time” from his or her start date and offered coverage within 90 days of hire (or the applicable waiting period for your plan). After the employee’s first year, he or she will be treated as an ongoing employee, and his or her hours should be measured in the same manner as those of other employees.
However, there are special cases when you hire new employees you do not expect to work more than 30 hours per week for an extended period of time. These include “variable hour” (part-time) and “seasonal” employees. For these workers, the regulations allow for an “initial measurement period” of no more than 13 months during which coverage does not need to be offered. The employer should pick a look-back/stability period for the employee of up to 12 months and offer coverage by the end of the 13-month period.

An employee can be treated as a variable hour employee if the employer cannot determine at the employee’s start date whether he or she is reasonably expected to be employed on average at least 30 hours of service per week during the initial measurement period (generally 12 months) because his or her hours of service are variable or otherwise uncertain. Factors to consider include whether the employee is replacing a full-time employee, the extent to which employees in the same or comparable positions are full-time employees, and how the job was advertised. You should tread carefully when considering whether an employee hired for a temporary position can be classified as a variable hour employee. If there is a definite end date to this person’s employment and, based on his or her hours and length of service, the employee will not average 30 hours per week over a 12-month initial measurement period, he or she can be considered variable hour. However, you cannot consider an employee to be variable hour because he or she is expected to work more than 30 hours per week but the project duration is uncertain or because this particular position experiences high turnover rates.

A seasonal employee is an employee in a position that is offered each year and the customary annual employment is six months or less. Like variable hour employees, seasonal employees do not need to be offered coverage until they have completed 13 months with the company and the employer has had the chance to count their hours over a 12-month period.

3. Re-hired Employees

Re-hired employees should be treated as ongoing employees, with their time measured using the standard look-back/stability periods, unless they have not worked for the school for a period of at least 26 weeks before their re-hire. In that case, you can treat them as new employees. Note that this requirement is different for schools than for other employers. While most employers can treat re-hires as new employees after only 13 weeks, educational institutions may only do so after 26 weeks.
4. COBRA Coverage

The look-back/stability measurement method will alter the way you administer continuation coverage for employees who experience a reduction in hours. Remember, an employee keeps his or her full-time or part-time status for the duration of the stability period no matter what happens with his or her hours during that time. So, using our example from above, an employee who worked 40 hours per week from October 15, 2013, to October 14, 2014 (the look-back period), will be considered full time from January 1, 2015, to December 31, 2015 (the stability period), even if the employee reduces his or her schedule to part-time in 2015. Although in the past this employee’s continuation coverage would have become available at the time of the reduction in hours, beginning in 2015, continuation coverage must be offered at the end of the stability period when he or she actually loses coverage.

C. Meeting the Affordability Requirement

One aspect of the ACA that many employers struggle with is the requirement not only to offer health coverage to employees but to do so at an affordable price. If an employee’s share of the premium for employer-provided coverage would cost the employee more than 9.5 percent of his or her annual household income, the coverage is not considered affordable for that employee.

Before you review the details of the affordability requirement, you need to keep a few things in mind: First, affordability is based on single-employee coverage. That is the only premium amount employers must consider. An employer could offer single-employee coverage at no cost and family coverage for $1,000 per month, and this would be considered affordable for all employees. Second, remember that employers need to offer only one affordable option. It is becoming common practice, for example, for employers to offer one high-deductible plan and one regular plan. The reason is that the high-deductible plan will generally have lower premiums, while the regular plan offers more coverage. As long as an employer’s lowest-cost plan satisfies the affordability requirement for single-employee coverage, the employer has complied with the ACA.

Because employers generally do not know their employees’ household incomes, employers can use one of three affordability safe harbors created by the government that are based on information the employer will have available. If an employer meets the requirements of any of these safe harbors, the offer of coverage will be deemed affordable for purposes of the ACA.
The three affordability safe harbors are (1) the Form W-2 wages safe harbor, (2) the rate of pay safe harbor, and (3) the federal poverty line safe harbor.

The Form W-2 wages safe harbor allows an employer to determine affordability based on Box 1 of an employee’s Form W-2 (“Wages, Tips, and Other Compensation”). As long as the premium amount charged to the employee does not exceed 9.5 percent of the amount reported for that employee in Box 1, the offer is deemed affordable. However, there are a few problems with this approach. First, the IRS has made it clear that this safe harbor is based on current year wages. In other words, an employer cannot look at the most recent Form W-2 to set premium prices for the following year. In addition, Box 1 excludes amounts the employee elects to contribute to certain benefits, such as a 401(k) plan or pre-tax health plan premium payments. So, even if the employer can guess at the value of Box 1 before the year begins because the employee will be paid on a salaried basis, the employee’s benefit elections could change that amount. For these reasons, the Form W-2 wages safe harbor is generally not practical.

The rate of pay safe harbor treats coverage as affordable if the employee contribution for a month does not exceed 9.5 percent of the employee’s hourly rate of pay multiplied by 130. Some employers with low turnover rates have decided to adopt this method based on their lowest-paid hourly worker’s rate.

However, the federal poverty line safe harbor may be the easiest to administer. It generally treats coverage as affordable if the employee contribution for the year does not exceed 9.5 percent of the federal poverty line for a single individual for the applicable calendar year. That means that, in 2015, any premium amount that is $93 per month or less will be considered affordable.

**D. Meeting the Minimum Value Requirement**

In order to avoid penalties under the ACA, employer-sponsored coverage must also meet minimum value. The good news is that this standard is fairly easy to meet. A health plan meets minimum value if, on an actuarial basis, it is designed to pay at least 60 percent of the total cost of medical services offered under the plan. Generally, this is not a calculation the plan sponsor can make, but it should be made and certified to you by your broker or insurance company.

**E. Penalties for Noncompliance**

The ACA requires employers to provide affordable coverage that meets minimum value or pay one of two penalties for noncompliance. Under the law, there is a large penalty and a small
penalty. Your school will be assessed one of these penalties only if one of your employees goes to the Exchange and is awarded a subsidy from the government to help pay for his or her insurance.

The larger penalty will apply if one full-time employee goes to the Exchange and gets a subsidy and your school has not offered qualified coverage to at least 95 percent of its full-time employees (or 70 percent for 2015 only). The penalty will be $2,000 per full-time employee minus the first 30 employees (or minus the first 80 employees for 2015 only) for failure to offer affordable coverage to a sufficient percentage of employees. If coverage is offered to avoid the larger penalty, it is still possible that an individual full-time employee whose coverage fails to be affordable or to meet minimum value or who is misclassified and not offered coverage could go to the Exchange and receive a subsidy. In that case, your school would be subject to a smaller penalty of $3,000 for that employee only.

F. Reporting Requirements

The ACA requires Large Employers to file information returns with the IRS and provide statements to their full-time employees about the health insurance coverage offered. The IRS will use this information to administer penalties under both the employer mandate and the individual mandate. Beginning in 2016, Large Employers must file information returns with the IRS and furnish statements to employees to report information about their offers of health coverage to their full-time employees in 2015. An employer can satisfy the reporting requirements by filling out a general transmittal form with information about the employer and the kind of coverage it offered (Form 1094-C), as well as an employee statement for each full-time employee, describing the coverage he or she carried during each month of the year (Form 1095-C).

Employers who offer self-insured coverage have additional reporting requirements and should contact their legal counsel to discuss compliance.

III. The Individual Mandate

Beginning January 1, 2014, all individuals are required to carry “minimum essential” healthcare coverage or pay a penalty. Minimum essential coverage includes an employer-sponsored health plan or a plan on the Exchange that is at least bronze level of the marketplace insurance plans. The penalty will be assessed when individuals file tax returns the following year. The fee for failing to carry insurance in 2014 will be the greater of $95 per uncovered family
member or 1 percent of household income; the fee in 2015 will be the greater of $325 per person or 2 percent of household income; and the fee after that will be the greater of $695 per person or 2.5 percent of household income. The maximum penalty is the national average premium for a bronze plan.

Many employees do not understand the requirement to carry insurance or how costly the penalties will be. However, public understanding should greatly improve in 2015 after the filing of individual tax returns for the 2014 year. Employers should expect employees who do not currently participate in their plan and new hires to join their plan at an increased rate.

IV. Other Requirements

In addition to the requirements of the employer and individual mandates, the ACA also created additional requirements that schools need to understand.

A. Grandfathered Plans

To help ease compliance burdens for companies that planned to continue offering substantially similar coverage despite cost increases, the ACA allows a group health plan that was created on or before March 23, 2010, to maintain “grandfathered” status, which exempts the plan from some compliance requirements. Plans or policies may lose their grandfathered status if they make certain significant changes that reduce benefits or increase costs to consumers. A health plan must disclose in its plan materials whether it considers itself to be a grandfathered plan and must also advise consumers how to contact the U.S. Department of Labor or the U.S. Department of Health and Human Services with questions.

B. New Health Plan Prohibitions

The ACA also created new prohibitions for health plans. As of January 1, 2014, group health plans cannot require a waiting period for an otherwise qualified participant to join the plan that exceeds 90 days. A three-month time frame cannot be substituted for 90 days, so many plans have chosen a two-month or 60-day waiting period.

In addition, health plans cannot have limits on lifetime or annual medical costs for “essential health benefits.” Grandfathered plans are not exempt from any of the requirements in this subsection.
C. **Nondiscrimination**

Though it is rarely discussed right now, the ACA contains a nondiscrimination provision that prohibits fully insured group health plans from discriminating in favor of highly compensated individuals. Such a requirement was previously in place for self-insured plans but has seldom been enforced. The current problem with this provision is that no one knows how to determine whether a plan is actually discriminatory. Although the ACA initially required compliance with the nondiscrimination rules for insured plans for plan years beginning on or after September 23, 2010, the IRS has announced that compliance with the rules will not be required until the agencies have issued regulations or other guidance regarding the rules. For this reason, schools that offer varying eligibility, prices, or quality of coverage to employees should be mindful of these rules and watch for regulations.

D. **Automatic Enrollment**

In addition to the individual penalty for failure to carry health coverage, another way the ACA attempts to boost enrollment in employer-sponsored health plans is to require employers with 200 or more employees to automatically enroll new employees in healthcare coverage. Healthcare reform amends the Fair Labor Standards Act (FLSA) to require certain large employers to (1) automatically enroll new full-time employees in one of the employer’s health benefit plans and (2) automatically continue the enrollment of current employees.

This requirement applies to employers that (1) are subject to the FLSA, (2) have more than 200 full-time employees, and (3) have one or more health benefit plans. Employers must provide “adequate notice” of the health insurance enrollment to employees, and employees must be given an opportunity to opt out of coverage.

The ACA did not specify an effective date for the automatic enrollment requirement. However, the U.S. Department of Labor has indicated that employers are not required to comply with this requirement until final regulations are issued and applicable — and that such regulations are not expected to be promulgated in time to implement the automatic enrollment provisions by 2015.