# Affordability for Employers—Determining Which Safe Harbor to Use

## What is Affordability?

The Affordable Care Act's employer shared responsibility provision (so-called "employer mandate" or "play-or-pay") requires that applicable large employers offer health coverage to their full-time employees. If a full-time employee receives a government subsidy for individual insurance through a Marketplace (Exchange) due to employer's failure to offer adequate coverage at work, the employer may be assessed either one of two types of penalties. A large penalty may apply if the employer did not offer coverage to at least 95% of all full-time employees. If the employer did offer coverage, but the coverage did not meet standards for minimum value and affordability, a smaller penalty may apply.

Affordability is simply based on the employee contribution requirement for self-only coverage divided by the employee's "income." The maximum allowable percentage is based on plan year as adjusted for inflation:

- For plan year beginning in 2015: 9.56% of income.
- For plan year beginning in 2016: 9.66% of income.

The IRS regulations on play or pay allow the employer to define the employee's "income" using any of three different safe harbor methods. Employers may use any one of the methods, or use different methods for different classes of employees as long as the chosen method is applied uniformly to the class.

## What are the Affordability Safe Harbors?

Eligibility for a Marketplace subsidy is based on an individual's household income and other factors. Most employers won't have access to an employee's actual household income, so the regulations allow an employer to define "income" using any of three different safe harbor methods. Extensive details are available at https://www.federalregister.gov/documents/2014/02/12/2014-03082/shared-responsibility-for-employers-regarding-health-coverage.

- Federal Poverty Line
- Rate of Pay
- W-2 Wages

## How does an employer decide which safe harbor to use?

There are pros and cons to each safe harbor depending on the employer and employee demographics. See our comparison charts later. Considerations when deciding which safe harbor to apply:

- Employer Budget
- Employer Support in Payroll and Benefits Administration
- Base Salary for Lowest Paid Employees (Hourly and Salary)
- Hourly Employee Turnover
- Hourly Employees that Consistently Work 40 Hours per Week
- Hourly Employees that are now Full Time, Mostly due to 30 Hours per Week
- Hourly Employees with "Busy" Seasons and Overtime Opportunities

## When reporting 2016 data on 1094/1095-C, how does an employer determine which safe harbor was used for cost-sharing, if not known?

Someone had to set the cost sharing (employee contribution rates) before the plan year started (e.g., at renewal). The employer will need to do an analysis to determine which safe harbor was used and/or which one may be most advantageous for the highest number of employees. See details in our comparisons later. Also review the information in the previous question. ThinkHR cannot do this for employers.

## Federal Poverty Line (FPL)

- Annual income is defined as the mainland FPL amount for a single-member household. For 2015 plan years (and 2016 plan year if start date is before 1/26/2016), the FPL amount is $11,770. For 2016 plan years starting 1/26/2016 or later, the FPL amount is $11,880.
- Example: For the plan year beginning January 1, 2016, coverage is automatically deemed affordable if the employee’s self-only cost does not exceed $94.74 per month ($11,770 X 0.0966)/12 months).
- The employee’s actual earnings, or any changes in earnings, are not relevant when using the FPL safe harbor method.
- The FPL is updated annually in late January. For details, go to [https://aspe.hhs.gov/poverty-guidelines](https://aspe.hhs.gov/poverty-guidelines).
- Employers may use the most recently published poverty guidelines as of the first day of the plan year of the applicable large employer member's health plan. Employers are permitted to use the guidelines in effect up to six months prior to the first day of the plan year, so as to provide employers with adequate time to establish premium amounts in advance of the plan's open enrollment period.

## Rate of Pay

- For hourly employees, income is defined as the employee’s hourly rate times 130 hours per month (regardless of the number of hours actually worked).
- Example: For plan year beginning January 1, 2016, if the employee’s hourly rate is $11, coverage is automatically deemed affordable if the employee’s self-only cost does not exceed $138.13 per month ($11 X 130 hours) X 0.0966).
- The rate of pay method does not require monitoring actual earnings or hours worked, as long the employee’s hourly rate (e.g., $11/hour) does not reduce.
- For salaried employees, the rate of pay method is more difficult to use so we do not recommend it.

## W-2 Wages

- Income is defined as the amount reported in Box 1 of the employee’s Form W-2 for the current year. (Note that pretax § 125 contributions and § 401(k) or § 403(b) deferrals are not included in Box 1, so this method may understate the employee’s actual income.) This method can be the most difficult to administer of the three safe harbor options since Box 1 wages must be monitored monthly during the current year to ensure affordability.
- Employers using the W-2 Wages safe harbor method often asked whether they can adjust the contribution during the year to ensure that the employee’s cost always meets the affordability threshold. Employer health plans usually are part of a cafeteria plan subject to rules under Section 125 of the Internal Revenue Code which generally restrict changes after the plan year starts. Therefore, to accomplish the employer’s objective, care must be taken in the language of the cafeteria plan document.
    - The self-only coverage contribution amount (e.g., employee’s payroll deduction amount) should be set forth in the 2016 plan document as 9.66% of W-2 Box 1 monthly wages but not to exceed $X.
        - For instance, if employer wants to set the employee contribution amount at $150/month, the contribution described in the plan would be 9.66% of W-2 Box 1 monthly wages but not to exceed $150 per month.
    - To implement this type of contribution, the payroll administrator needs to monitor the amount being captured for Box 1 reporting with each payroll cycle. (Although the affordability threshold only needs to be met on a monthly basis, most employers use weekly, bi-weekly or semi-monthly payroll cycles.)

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| Federal Poverty Line (FPL) | | | | |
|---|---|---|---|---|
| Plan Year | % of "Income" | Annual FPL* | Max "Affordable" Monthly Cost | Details |
| 2015 | 9.56% | $11,770 | $93.77 | |
| 2016 | 9.66% | $11,880 | $95.63 | |
| 2017 | 9.69% | TBD | TBD | Look for new FPL in mid-Jan |
| *Employers are permitted to use the guidelines in effect up to six months prior to the beginning of the plan year. Caution! FPL is updated annually in mid-January; i.e., for a calendar-year health plan, use the prior year's FPL chart. | | | | Current FPL Guide |

| Rate of Pay | | | | |
|---|---|---|---|---|
| Source | Hourly Wage | PY2016 Max "Affordable" Monthly Cost | PY2017 Max "Affordable" Monthly Cost | |
| Federal Minimum Wage | $7.25 | $91.05 | $91.33 | |
| Highest State Min Wage | $10.00 | $125.58 | $125.97 | |
| Sample 1 | $12.00 | $150.70 | $151.16 | |
| Sample 2 | $15.00 | $188.37 | $188.96 | |
| Maximum "Affordable" Monthly Cost = Hourly Wage x 130 hours x 9.66% (PY2016) or 9.69% (PY2017) | | | | |
| Rate of Pay is based on 30 hours per week/130 hours per month regardless of hours actually worked. This method is good for employers that want to charge more than the FPL method allows, and their hourly workforce fluctuates and/or generally only works 30 hours/week. | | | | |

| W-2 Wages / Comparison Only | | | | |
|---|---|---|---|---|
| Source | Hourly Wage | PY2016 Max "Affordable" Monthly Cost | PY2017 Max "Affordable" Monthly Cost | |
| Federal Minimum Wage | $7.25 | $121.40 | $121.78 | |
| Highest State Min Wage | $10.00 | $167.45 | $167.97 | |
| Sample 1 | $12.00 | $200.94 | $201.56 | |
| Sample 2 | $15.00 | $251.17 | $251.95 | |
| W-2 Wages is based on actual earnings reported in Box 1 of the W-2 each month. Box 1 excludes pretax contributions (e.g., deductions from pay for health coverage, and 401(k) and 403(b) plans) which reduce "income." | | | | |
| If the employer ONLY has full-time employee that work at least 40 hours per week, then the employer would use 40 hours in the calculations instead of 30. This is merely a sample calculation to assist employers with comparing "projected" W-2 Wages to the Rate of Pay when determining which safe harbor to use. | | | | |
| 40 x 4.33 weeks = 173.34 hours in a month | | | | |
| Monthly Cost = Hourly Wage x 173.34 x 9.66% or 9.69% | | | | |