AFFORDABILITY UNDER THE ACA

INFORMED ON REFORM

The Affordable Care Act (ACA) has three primary goals: expanding access to health care, along with improving the affordability and quality of health care. Because of affordability's central role in the law, it is a key factor in many of the law's provisions. With multiple provisions addressing affordability, there are times when the definition of affordability differs. This paper discusses the concept of affordability within the employer and individual mandates under the ACA.

Affordability and the employer mandate

The most commonly referenced definition of affordability under the ACA is included in the employer mandate. Under the mandate, large employers are required to offer "affordable," "minimum value" health coverage to at least 95% of their full-time employees and their child dependents up to age 26 or risk substantial penalties.

In this context, coverage is considered "affordable" if an employee's contribution to the cost of self-only coverage does not exceed an indexed threshold – 9.56% in 2018 and 9.86% in 2019 – of the employee's household income (see sidebar on next page). The employee contribution amount must also be included on annual required reporting (Forms 1094 and 1095).

If the coverage offered by an employer is deemed "unaffordable" or does not provide "minimum value" by ACA standards, employees may be able to receive a Federal Premium Assistance Tax Credit and/or a Cost Sharing Reduction Subsidy if they purchase a health plan from a public Marketplace (also known as an Exchange). This, in turn, may trigger financial penalties for the employer.

Together, all the way.®

Cigna®

Offered by: Cigna Health and Life Insurance Company, Connecticut General Life Insurance Company or their affiliates.

896869 b 06/18

Employer mandate safe harbors

Because employers don't typically have insight into their employees' household income, the Internal Revenue Service (IRS) established three safe harbor tests to determine whether the coverage offered is "affordable." An employee's required contribution for health coverage cannot exceed the indexed threshold – 9.56% in 2018 and 9.86% in 2019 – of one of the following.

Form W-2 Wages	The amount listed in Box 1 of the employee's Form W-2. For purposes of the safe harbor, wage adjustments are made for employees who did not work the entire year with the employer.
Rate of Pay	The hourly rate of pay for each qualified employee is multiplied by 130 hours.
Federal Poverty Line (FPL)	The FPL for a single individual. Because this safe harbor does not consider the employee's actual wages, it is the simplest of the safe harbors to calculate.

Employers may use one or more of these optional safe harbors when determining affordability for their employees.

Calculation considerations

In addition to the employee premium for self-only coverage, other employer contributions need to be considered when calculating an employee's total cost. These additional items were outlined in IRS Notice 2015-87.

What is INCLUDED in affordability calculations

- **Flex credits** that can be used to pay for premiums or other health care benefits (called "health flex contributions") will **lower** the employee's required contribution.
  - If flex credits are not restricted to qualified health care expenses or can be cashed out, then the amount cannot be included in the affordability calculation.
- **Health Reimbursement Account (HRA) contributions** that may be used to (1) pay plan premiums or (2) pay a combination of premiums and cost-sharing, and/or costs not covered by the health plan will **lower** the employee contribution. These contributions must also meet certain other specified conditions.
  - HRA contributions that cannot be used to pay premiums (i.e., HRAs that are restricted to cost-sharing, and/or costs not covered by the health plan) are not included in affordability calculations.
- **"Opt out" or "cash in lieu" payments** given to employees who decline the employer-sponsored health coverage will **increase** the employee's required contribution. The IRS considers these arrangements the equivalent of a salary reduction, since an employee would forego the additional payment to participate in the health plan.
  - Proposed regulations issued on July 8, 2016, provide that "eligible opt out" payments may be excluded (see *Eligible "opt out" payments*).*
- **Tobacco-related wellness incentives** for programs that include tobacco cessation will **lower** the employee's required contribution because it is assumed that each employee earns all incentives related to tobacco use. Incentives for other wellness program components not related to tobacco use do not count toward affordability (e.g., health assessments or biometric screenings).

What is EXCLUDED from affordability calculations

- **"Eligible 'opt out' or 'cash in lieu' payments"** are disregarded in calculating the employee's contribution if the payment is conditioned on the employee:
  - Declining to enroll in the employer-sponsored coverage, and
  - Providing reasonable evidence that the employee and all of their tax dependents have minimum essential coverage through another health plan other than individual market coverage (e.g., under a spouse's employer's plan).*
- **Health Savings Account (HSA) contributions** (from employer and/or employee)
- **Flex credits that are not health flex contributions**
- **HRA contributions if the HRA cannot be used to pay plan premiums**
- **Non-tobacco-related wellness incentives**

Example

Annual premium (employee share)	$3,600
Annual wellness incentive (tobacco-related)	$600
Annual premium health flex credits (employer contribution)*	$600
Total annual contribution for affordability purposes	$2,400
Employee salary (W-2 form safe harbor)	$35,000
Required contribution percentage	6.86%
Meets affordability requirement	✓

***Transition relief**

The IRS provided transitional relief in Notice 2015-87 effective until January 1, 2017 (or until an effective date is provided in final regulations) for plans that were in effect on or before December 16, 2015. This relief specifies what should be included when calculating an employee's required contribution.

- All flex credits will reduce the employee's required contribution, even if they may currently be used for non-health benefits or taken as cash; and
- Any "opt out" incentives or "cash in lieu" payments provided to employees who decline or waive health coverage will not be counted as increasing the employee's required contribution.

Affordability and the individual mandate

In addition to the employer mandate, the ACA also requires individuals to obtain and maintain health coverage or face financial penalties. This is known as the individual mandate. Under this mandate, individuals need to have minimum essential coverage which they may obtain through an employer-sponsored plan, an individual insurance policy, the public Marketplace, a government-sponsored plan such as Medicare or Medicaid, or a U.S.-issued expatriate plan.

Individuals are exempt from the individual mandate if the lowest-cost public Marketplace plan or employer plan offered is not affordable. To be considered "affordable" under the individual mandate, the lowest-cost self-only "Bronze" level plan available from the public Marketplace (reduced by any subsidy) or the lowest-cost employer-sponsored plan must not exceed an indexed threshold – 8.05% in 2018 – of an individual's household income. This threshold leaves a gap of more than 1.5% between the affordability standard under the employer mandate and the individual mandate.

The practical effect of this disparity is that an employer can comply with the employer mandate by offering affordable, minimum value coverage, but the cost of that coverage is still above the individual mandate's household income threshold. This creates a situation where it is possible for an employee (or his/her family members) to be exempt from the individual mandate, but not be eligible for public Marketplace subsidies for individual or family coverage (see Marketplace Subsidies sidebar). This is known as the "family affordability glitch."

Employer vs. individual mandate gap example

John Smith

- Household income: **$43,000**
- Household size: **1**
- Access to both employer-sponsored coverage and public Marketplace coverage

ABC Company

Offers **$3,800** self-only coverage to employees

= **8.84%** of John Smith's income

Employer mandate: ≤ 9.56% of income

✓ Meets employer mandate affordability threshold

✓ ABC Company meets affordability requirement of employer mandate

Individual mandate: ≤ 8.05% of income

✗ Does NOT meet individual mandate affordability threshold

✗ If John Smith declines coverage, he may be exempt from the individual mandate

Public Marketplace

Lowest-cost, self-only "Bronze" level plan is **$3,600**

= **8.47%** of John Smith's income

Individual mandate: ≤ 8.05% of income

✗ Does NOT meet individual mandate affordability threshold

✗ John Smith is not eligible for a subsidy because ABC Company is in compliance with the employer mandate*

✗ John Smith can choose not to purchase public Marketplace coverage and can claim an affordability exemption from the individual mandate

Subsidy eligibility through public Marketplace*

Individuals may be eligible for the Federal Premium Assistance Tax Credit to lower the cost of public Marketplace coverage if their household income is between 100% – 400% of the FPL, and they are:

- Not offered minimum essential coverage (MEC) by their employer, or
- Offered MEC, but the coverage does not comply with the employer mandate.

Individuals may also be eligible for a Cost-Sharing Reduction Subsidy if their income is at or below 250% of the FPL.**

**If the federal government ceases reimbursement payments of cost-sharing reductions (CSRs) to insurers, it does not eliminate the availability of CSRs. Insurers are required by law to offer them to qualified individuals.

Affordability – The ongoing balancing act

Affordability is a key ACA concept under both the employer and individual mandates. For employers, it will be increasingly important to monitor affordability requirements while continuing to balance the health and well-being needs of their employees. For individuals, affordability will continue to impact the cost and access to coverage types for both themselves and their families.

Employers should consult with their legal and tax professionals to ensure ongoing ACA compliance with their health plans. To learn more about the provisions covered throughout this paper and to stay up-to-date on any changes, visit **InformedOnReform.com**.