

COVID-19 and Affordability for Applicable Large Employers

2020



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ALEs are required to offer minimum value, minimum essential, affordable coverage to all full-time employees. In 2021 that standard is 9.83%, which is higher than the 2020 standard of 9.78%.

Because employers rarely know an employee's household income, ALEs may meet the affordability requirement through one of three safe harbor options –

- the W-2 safe harbor,
- the rate of pay safe harbor, and
- the federal poverty level safe harbor

ALEs should keep in mind that once they meet the requirements of the safe harbor, if an employee is considered subsidy eligible, the employer would not face penalties under the employer mandate. Although it is rare, factors in an employee's personal financial and tax situation could render the coverage offered by the ALE unaffordable to the individual. Employers should only focus on meeting the safe harbor requirements.

Employers sometimes struggle to decide which safe harbor method is the right one for their employee population. Employers can use different safe harbors for different classes of employees, as long as the classes are based on a reasonable business decision. Common reasonable classifications would be geography (different locations of employees), hourly versus salary, and job classifications.

Employers that are struggling during the COVID-19 pandemic might be considering furloughs of employees (a furlough indicates the individual is still an employee because the employment relationship has not been terminated and there is an intent that they will return to work in the future) should keep in mind that if they move employees to COBRA and ask employees to pay the full COBRA premium during the furlough, that coverage is unlikely to be considered affordable. This could trigger ACA penalties for employers that use the measurement and lookback method for determining full time status. Furthermore, employers who lower employee's pay during the year or have employees take an unpaid furlough/leave of absence cannot calculate affordability using the rate of pay safe harbor.

Method	Wages / FPL	Monthly Premium Maximum
Rate of Pay	Federal minimum wage (\$7.25/hr)	\$92.17
Rate of Pay	\$12/hr	\$153.34
Rate of Pay	\$15/hr	\$191.68
FPL	2020 FPL – calendar year plan	\$104.52

W-2

Under the W-2 safe harbor, coverage is affordable if the employee's contribution for self-only coverage is less than 9.83% of their W-2 income for the current year. This determination looks at an employee's Box 1 income. Box 1 income shows total taxable wages, tips, and other compensation, but it does not include elective deferrals into retirement plans or Section 125 plans.

Practically speaking, the W-2 affordability determination is made after the calendar year ends although employers can make estimates based on an employee's annual salary. Unfortunately, employers cannot make any adjustment for unpaid leaves or large pre-tax contributions, which can increase the likelihood the employee's coverage will be unaffordable.

Employers that choose to use the W-2 method may not change the employee's contribution level, either the dollar amount or percentage during the calendar year, or during the plan year if the plan operates on a non-calendar year.

Rate of Pay

Under the rate of pay safe harbor, coverage is affordable for an hourly employee if the hourly employee's contribution for self-only coverage is less than 9.83% of the employee's lowest rate of pay during the calendar month, times an assumed 130 hours worked during a month. Employers should take care to understand that the rate of pay safe harbor has different considerations for hourly employees versus salaried employees, notably it cannot be used as a safe harbor for any salaried employee who has their wages reduced during the year or who has to take an unpaid furlough.

Employers sometimes overlook the fact that the 130 hours is the standard multiplier in the rate of pay formula and cannot be increased if the employee works more than 130 hours in the month. It also isn't increased or decreased for a month with fewer or more business days. An employee who works 40 hours a week during a 4 week month would actually work 160 hours in the month, but the multiplier for affordability would still be 130 hours. If an employee works one day in a month, he or she is considered to have worked the entire month (130 hours) for purposes of both the employee's share of the premium and assumed income for the calendar month. It is important to note that if a salaried employee's monthly salary is reduced during the year (even if due to a reduction in hours) the rate of pay method may not be used. Employers who reduce wages or implement unpaid furloughs due to COVID-19 will be unable to use this method for salaried employees. For hourly employees, the 130 hours is multiplied by the employee's lowest rate of pay during the calendar month. An employee who is forced to take unpaid leave due to COVID-19 would have an effective rate of pay of \$0 for that month.

This rate of pay method excludes tips and overtime and disregards any pay increase the employee may receive during the year. As a result, this method is not viable for commissioned or tipped employees, such as salespeople and hospitality workers with low base wages.

FPL

Under the federal poverty level (FPL) safe harbor, coverage is affordable if the employee's contribution for self-only coverage is less than 9.83% of FPL as of the start of the plan year for the state in which the employee lives. The FPL method does not look at the employees actual hours or pay, so it does not need to be adjusted for leaves of absence or changes in income.

FPL figures are released near the end of January, and an employer may use the FPL in effect within the six months before the start of the plan year. This allows an employer to set contributions during open enrollment for a calendar year plan, despite not having the upcoming year's FPL. Employers with employees in Alaska and Hawaii should take care to use the FPL for those states. The contiguous states have same FPL.

Which Method?

Employers are often left trying to decide which method is right for them and their employees. The W-2 method is the most flexible but least predictable and allows for no adjustments. The requirement to use Box 1 can lead to a significant decrease in an employee's pay if the employee makes large pre-tax contributions. It is also deflated if an employee takes a long unpaid leave of absence.

The rate of pay will underestimate income for full time employees (due to capping at 130 hours) and cannot be used for employees who are tipped or paid on commission due to low base wage. Its design makes affordability calculations easy for large groups of employees though, as it doesn't require calculations involving any employee's specific hours worked.

The FPL is the golden ticket method – an employee's hours and salary can change or drop with no impact on the affordability of the plan, because the affordability is based solely on the required affordability standard and the government's set FPL for the year. Using the 2021 calendar year affordability standard with the 2020 contiguous US FPL, an employee's premium cannot exceed \$104.52 per month.

