Informal IRS Comments Help Clarify the Employer Penalty

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Annually, the American Bar Association's Joint Committee on Employee Benefits ("JCEB") meets with representatives from the IRS and Treasury for a question and answer ("Q&A") session. While the responses are informal and cannot be relied upon, they provide helpful clarification on a number of issues. In this year's meeting, the agency highlighted the employer shared responsibility provisions under Code § 4980H, as described below.

Large Employer Determination

IRS officials stated that for purposes of determining large employer status (whether the employer is subject to Code § 4980H), the statute requires employers to use 120 hours as full-time. In other words, each employee who works at least 120 hours in a month counts as one full-time employee ("FTE"). Employees who worked less than 120 hours in a month are counted as a fraction where the numerator is the employees' actual hours worked and the denominator is 120. This response has caused some confusion as, under a fair reading of statutory provisions and final regulations, full-time status is based on 30 hours of service in a week or 130 hours a month. Those working less than 30 hours of service a week are considered full-time equivalents. Regardless of which approach used, the net result remains the same. (Q/A-24)

Variable Hour and Seasonal Employees

The comments of agency officials in Q/A-25 contain various helpful hints in understanding the appropriate categorization of an employee.

Employment contract terms and variable status. The terms of an employment contract can be relevant in terms of how many hours a week an employer expects an employee to work for a specified period. If the employer does not know if the hours are going to be above 130 hours in a month, the employer can treat the employee as a variable hour employee.

Additional clarification on the definition of a seasonal employee. An employee is seasonal if his/her position tends to be reoccurring and is tied to a specific season. Examples include a lifeguard or ski instructor, but the FAQ clarifies that the definition is not limited to an individual whose job is affected by weather. Therefore, a seasonal employee may include a summer associate in a law firm or someone who works during a peak season in a hotel.

Short-term, non-seasonal employees. An employer cannot treat a non-seasonal, short-term employee who is hired to work 40 hours a week, but only for a 6 month period, as a part-time employee because the average hours over a year are 20 hours per week. An employer always has until the beginning of the fourth month to get an employee who is reasonably expected to be full-time as of his/her start date on the plan. If the employee is a non-seasonal, short-term FTE employed for two months, the employer will not need to bring that employee on the plan.

Measurement Periods

Look Back Measurement Period

The length of the initial and standard measurement period ("IMP" and "SMP") must generally be the same, subject to a limited exception. In using the look back measurement method, the length of the stability periods that are tied to the SMP and the IMP must be the same. The guidance clarifies a special rule for new employees. Under this special rule, the IMP may be a month shorter than the initial stability period. This means the employer can use an 11-month IMP with a 2½ month administrative period and a 12 month initial stability period. Other than this special one-month rule, the measurement period (IMP and SMP) must be the same length. (Q/A-26)

Monthly Measurement Period

In an example, the agency is asked how the penalty would be applied in the case of an FTE who was not eligible for the employer's plan for his/her first calendar year of employment due to failure to satisfy a substantive eligibility requirement (for example, the employee had not obtained the required professional license). As of the first day of the second calendar year, the employee satisfies this eligibility requirement. The IRS responded that as long as the employee is brought onto the coverage by the first day of the fourth month in the second year, the employer gets a pass for the first 3 months of the second year. However, there is no pass for the first year. (Q/A-27)

Different Measurement Methods

In what was a confusing question posed to the IRS, the agency restated that an employer may apply either the monthly measurement method or the look back measurement method. However, one cannot apply two different methods to the same category of employees and certainly not to the same individual. (Q/A-29)

Counting Hours – On Call Employees

The IRS states that if an employee is getting paid for on-call hours, if the employee is required to remain on the employer's premises or if the employee is subject to "sort of severe restrictions" on what the employee can do, even where the employee receives a reduced hourly rate, the employee must receive credit for all hours of service for the on-call time. There is no concept of partial hours. (Q/A-28)

For notes from the Q&A session, visit:
http://www.americanbar.org/content/dam/aba/events/employee_benefits/2014_irs_qa.authcheckdam.pdf