

# IRS Employer Health Plan Coverage Affordability Considerations

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## Quick Facts

- Recently, the Internal Revenue Service (IRS) significantly decreased the affordability percentage from 9.12% in 2023 to 8.39% in 2024.
- Under the Affordable Care Act (ACA) employers must offer coverage to employees that is “affordable” or risk facing penalties.
- Employers have the option to use one of three IRS affordability safe harbors to provide more predictability when determining whether the coverage will be considered affordable.

## Background

In [Revenue Procedure 2023-29](#), the IRS significantly decreased the affordability percentage from 9.12% in 2023 to 8.39% in 2024. This is the lowest that the affordability percentage has been since its inception, and the first time it has ever been below 9%. This percentage determines which applicable large employers (ALEs) may face penalties under §4980H(b) for failure to offer affordable coverage as well as which individuals may qualify for subsidized coverage through a public Exchange. It is important to understand whether coverage offered under an employer-sponsored group health plan is “affordable.” When setting plan contribution rates, employers must consider IRS employer affordability safe harbors, the various elements that play into the determination of the employee contribution, and the penalties associated with failing to offer affordable coverage.

Under §4980H (employer mandate), applicable large employers (50 or more full-time equivalents (FTEs)) must offer coverage to full-time employees that is affordable to avoid potential §4980H(b) penalties. In addition, individuals enrolling for coverage through a public Exchange will not qualify for subsidized coverage (premium tax credits) if they are eligible for employer-sponsored group health plan coverage that is affordable.

Coverage is considered “affordable” if the required employee contribution does not exceed a set percentage (8.39% in 2024) of household income.

- For employees, coverage is affordable if the required employee contribution for the lowest cost minimum value plan for employee-only (single) coverage is affordable.
- For spouses and dependents, coverage is affordable if the required employee contribution for the lowest cost minimum value plan for family coverage is affordable.

Coverage is also considered “affordable” under §4980H(b) requirements if the employee contribution satisfies at least one of three available safe harbors (i.e., federal poverty level (FPL), rate of pay, or Form W-2).

## Required Contribution Percentage

In 2014, the required contribution percentage for determining affordability was set at 9.5%. The percentage is adjusted annually. See the applicable percentages for each year in the table below.

Affordability Percentage										
Year	2024	2023	2022	2021	2020	2019	2018	2017	2016	2015
Rate	8.39%	9.12%	9.61%	9.83%	9.78%	9.86%	9.56%	9.69%	9.66%	9.56%

## Application

Effective for plan years beginning on or after January 1, 2024, the percentage to be used in affordability calculations is 8.39%. For calendar year plans, the 8.39% applies beginning in January 2024, but for a non-calendar year plan that renews midyear the 8.39% will begin when the plan year begins. For example, employers with a plan year that starts in September will apply the 8.39% beginning in September 2024.

The decrease in the affordability percentage (from 9.12% in 2023 to 8.39% in 2024) may require ALEs to lower employee contributions for employee-only (single) coverage for the 2024 plan year to meet the affordability requirements under §4980H(b). Note that employers are not required to offer affordable coverage to spouses and dependents; however, this lower affordability percentage might allow more spouses and dependents to qualify for subsidized individual health coverage through a public Exchange when the cost for the family to participate in the employer's plan is deemed unaffordable.

## Affordability Safe Harbors

An employer is unlikely to know the employee's household income. When setting employer contribution rates, employers have the option to use one of three IRS affordability safe harbors to provide more predictability when determining whether the coverage will be considered affordable. So long as minimum value coverage is affordable under one of the three recognized safe harbors, the employer will be considered in compliance for purposes of avoiding a potential penalty under §4980H(b). Keep in mind that the use of the employer safe harbor does not change an individual's possible eligibility for subsidies (which is tied to household income).

An employer may choose to apply any of the safe harbors for any reasonable category of employees, provided it does so on a uniform and consistent basis for all employees in a category. The regulations provide that reasonable categories generally include specified job categories, nature of compensation (hourly or salary), geographic location, and similar bona fide business criteria. In addition, an employer may use different affordability safe harbors for each reporting year; the only rule is that if the Form W-2 safe harbor is used, it must be used for all 12 months of a particular calendar year because it considers Box 1 wages for the same calendar year. The employer is not required to choose the safe harbor until the employer is preparing Forms 1094-C and Forms 1095-C, but many employers use the safe harbors to set employer contributions for the year. Each safe harbor is described below, using the applicable 2024 affordability percentage.

### Federal Poverty Level Safe Harbor

Coverage offered to an employee is affordable if the employee's cost for single coverage does not exceed 8.39% (in 2024) of the FPL for a single individual. "Federal Poverty Line" (or FPL) refers to any of the poverty guidelines (updated periodically in the Federal Register by the Secretary of Health and Human Services) in effect within six months before the first day of the plan year of the ALE

member's health plan. The FPL is typically updated in late January, so a calendar year plan will generally rely upon the FPL of the previous year, while plans beginning in February or later can rely upon the current year's FPL. Therefore:

- For a 2024 calendar year plan, \$101.93/month or less meets the safe harbor ( $\$14,580 \times 8.39\% / 12$ ).
- For a 2024 non-calendar year plan, a slightly higher amount per month will be affordable due to being able to use the 2024 FPL guidelines.

**TIP:** When determining which affordability safe harbor to use, employers should first consider the FPL safe harbor because it is the simplest and guarantees affordability for all employees. If the FPL safe harbor is not met, then the employer should consider the rate of pay or Form W-2 safe harbor.

### Rate of Pay Safe Harbor

For an **hourly employee**, the employee's monthly contribution for single coverage is affordable if it does not exceed 8.39% (in 2024) of the employee's hourly rate multiplied by 130.

- The calculation uses the employee's rate of pay as of the first day of the coverage period unless the rate of pay is reduced, in which case the lower amount is used.
- 130 (to match the definition of full-time) is used in the calculation even if the employee works more or less than 130 hours during a calendar month. Therefore, this safe harbor protects the employer even in situations in which the employee's hours may be less than full-time and the employer remains obligated to continue offering coverage during the stability period. However, it might also require a lower monthly employee contribution than required under the Form W-2 safe harbor for employees who regularly work 40 or more hours per week.

For a **non-hourly employee**, the coverage is treated as affordable if the employee's required contribution for single coverage does not exceed 8.39% (in 2024) of the employee's monthly salary as of the first day of the coverage period (instead of 130 multiplied by the hourly rate of pay)—provided that if the monthly salary is reduced, including due to a reduction in work hours, this safe harbor is not available. **NOTE** – This safe harbor cannot be used for tipped employees or for employees who are compensated solely based on commissions.

### Example

An employer has full-time hourly employees paid \$14/hour and up. So long as employee contributions for the lowest cost minimum value plan do not exceed \$152.69/month ( $130 \times \$14 \times 8.39\%$  in 2024), the coverage will be considered affordable.

### W-2 Safe Harbor

Under this safe harbor, the employee's annual contribution for single coverage is affordable if it is  $\leq 8.39\%$  (in 2024) of the employee's Form W-2 Box 1 wages. Application of this safe harbor is determined after the end of the calendar year, taking into account the employee's annual W-2 wages (as reported in Box 1) and the employee contribution for the full calendar year (e.g., employee's 2024 Box 1 wages and employee contributions during 2024). Box 1 is used to report taxable wages, bonuses, tips, and other compensation paid by the employer, as defined in Code §3401(a). It does not include non-taxable employee benefits, such as pre-tax contributions to a 401(k) plan or pre-tax cafeteria plan salary reductions. When using this in advance of the plan year to set employer contributions, the employer would have to base affordability on an estimate of Box 1 wages for the year.

To use this method, an employee's required contribution must remain a consistent amount or a consistent percentage of all Form W-2 wages during the year.

### Examples

An employee is full-time from January through December and is offered minimum value coverage that costs the employee \$200/month for single coverage (\$2,400 for the year). This coverage will be affordable for any employees that have Box 1 W-2 wages of \$28,605.48 or more ( $\$2,400 / 8.39\%$  in 2024).

Employer expects that all full-time employees will have at least \$30,000 or more reported in Box 1 during the year. So long as the employee contributions for single coverage do not exceed \$2,517 for the year or \$209.75/month ( $\$30,000 \times 8.39\%$  in 2024), the coverage will be affordable for those considered full-time all 12 months.

### Affordable and Not Affordable at the Same Time

Subsidy eligibility for coverage through a public Exchange will always be based on household income. That being the case, if an individual qualifies for a tax subsidy because the employee contribution is deemed unaffordable using household income, but the employer can show that the coverage is affordable using one of the three safe harbor methods mentioned above, the employer will not be liable for a penalty under §4980H(b).

Consider the following example:

- The employer determines that the lowest rate of pay for hourly employees is \$12/hour. Using the rate of pay safe harbor, the employer decides to set employee contributions for single coverage at \$130.88 ( $130 \text{ hours} \times \$12/\text{hour} \times 8.39\% = \$130.88$ ).
- One of the employer's full-time employees earns about \$1,600/month but also makes a \$300/month alimony payment. Household income for subsidy purposes is based on an individual's household adjusted gross income (AGI), and alimony payments are an "above the line" deduction that reduces an individual's AGI. Consequently, this individual's monthly household income equals \$1,300, and the employee's required contribution for single coverage (\$130.88) equals 10.06% of household income.
- This employee might qualify for a subsidy when purchasing individual health insurance through a public Exchange, but the employer would face no liability under §4980H(b) due to meeting the rate of pay safe harbor.

### Determining the Required Employee Contribution

The required employee contribution considers the amount an employee is required to contribute toward employee-only (single) coverage under the lowest cost minimum value coverage offered by the employer. In addition to the amount the employee is required to contribute toward the monthly premium, several other things may impact the employee contribution reported on Line 15 of Form 1095-C for purposes of the affordability calculation as set forth below.

#### HSAs

Contributions to a health savings account (HSA), which are not available to pay for the insurance premium, do not affect affordability.

#### HRAs

Contributions to a health reimbursement arrangement (HRA) are typically not available to reimburse the premium (they are more often designed to offset plan cost-sharing), and so employer

contributions may count toward determining minimum value, but do not impact the employee contribution for purposes of determining affordability.

### Flex Credits

Flex credits (or defined contributions) restricted to health coverage (e.g., medical, dental, vision, or health FSA) will decrease the employee contribution; but flex credits that can be used for non-health coverage do not decrease the employee contribution.

For example, an employer makes \$300/month available via flex credits and the employee's cost for single medical coverage is \$500/month:

- If the flex credit may be used only toward the medical, dental or vision premiums, or contributed to a health FSA, the monthly employee contribution for affordability purposes is \$200 (\$500 minus \$300).
- However, if in addition to the options mentioned above, the employee may use the \$300 toward life, disability and dependent care assistance program (DCAP) expenses or taken as cash, the monthly employee contribution for affordability purposes is \$500.

### Opt-Out Incentives (Cash-in-Lieu)

If the employee has the option to either receive medical coverage or receive an amount as taxable cash (an opt-out or waiver incentive), this cash option may need to be considered for purposes of affordability.

- If the credit is available to any employee who waives coverage (i.e., an unconditional opt-out), the opt-out incentive should be used in calculating affordability for all eligible employees.
- If the opt-out credit is limited only to employees who show proof of other non-individual health insurance and who also attest to all family members having minimum essential coverage (i.e., an "eligible opt-out arrangement"), then the credit would not be considered for any employees, whether they enroll in the employer's plan or receive the opt-out credit.

For example, an employee cost for health coverage is \$125/month, but there is an opt-out credit of \$50/month:

- If the opt-out credit is available to any employee who waives coverage, the employee contribution for affordability purposes is \$175 (\$125 + \$50). Note that there is transition relief allowing employers to disregard the opt-out amount for opt-out arrangements in place prior to December 2015 which have not substantially changed since that time.
- If the opt-out credit is only available to those employees who prove coverage for themselves and family members under another employer's group health plan (e.g., through a spouse), the employee contribution for affordability purposes is \$125.

### Wellness Incentives

Affordability is determined assuming the individual fails to satisfy any wellness requirements unless it is tobacco related.

For example, a required employee contribution for the month is \$200 and the potential wellness incentive reduces the cost to \$150:

- Coverage is "affordable" so long as \$200 (not \$150) does not exceed 8.39% (in 2024) of the employee's household income if the wellness incentive is NOT tobacco related.

- Coverage is “affordable” so long as \$150 does not exceed 8.39% (in 2024) of the employee’s household income if the wellness incentive IS tobacco related.

## Setting Employer Contributions

It is not always financially advantageous to the employer to ensure that the coverage offered is affordable to ALL full-time employees. Employers should consider the §4980H(b) penalty for a full-time employee receiving a subsidy. The employer contribution for employees who enroll in the employer’s plan may be more than the employer would be required to pay as a penalty under §4980H(b).

Furthermore, the §4980H(b) penalty applies only to those full-time employees who waive employer-sponsored coverage, enroll in subsidized coverage through a public Exchange and qualify for a premium tax credit). Therefore, if an employee voluntarily enrolls in unaffordable employer-sponsored coverage or does not qualify for a tax subsidy toward coverage through a public Exchange after waiving the employer’s coverage, the employer will not face a penalty. Keep in mind that employees who are eligible for Medicare or Medicaid will not qualify for a tax subsidy.

Additionally, it is important to understand that there is nothing under §4980H rules that requires a uniform contribution rate across all categories of employees; rather, affordability is considered on an employee-by-employee basis. The employer could choose to contribute differently to different categories of employees or based on a percentage of salary. However, anytime the employer sets different contribution rates for different categories of employees, nondiscrimination rules, which restrict the ability to offer favor to highly compensated individuals on a tax-favored basis, must be considered.

## Summary

When applicable large employers set employer contributions for health coverage, and there are many variables that may affect the strategy chosen. The IRS has simplified things a bit by allowing employers to use one of three employer affordability safe harbors as opposed to having to guess at an employee’s household income. Employers also need to consider how other benefits and incentives offered may affect the employee contribution amount for purposes of calculating affordability. It is important to weigh the risk of a potential penalty under §4980H(b) for some employees versus choosing to set the employer contribution at a higher rate for lower-paid employees.

Employers are not required to offer affordable coverage to spouses and dependents, and may require employees to contribute up to 100% of the premium cost for coverage for spouses and dependents. If the required employee contribution for spouses and dependents is not affordable based on the family’s household income, the employer will not face any risk of §4980H penalties, but such spouses and dependents may then qualify for subsidized individual health coverage through a public Exchange.

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