Provisions of the Affordable Care Act Mandate in a Nutshell

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Commonly referred to as Obamacare, and the subject of considerable political wrangling, the Affordable Care Act (ACA), otherwise known as the Patient Protection and Affordable Care Act as amended by the Health Care Reconciliation Act of 2010, created an individual and employer mandate for health-care coverage. Failure to comply with the ACA will result in a "shared responsibility payment." While universal health-care coverage is the intended carrot under the ACA, the stick for noncompliance is the shared responsibility payment (which the Internal Revenue Code actual refers to as a penalty).

INDIVIDUAL MANDATE

As of 2014, each individual who is required to file a tax return and the filing individual's dependents must obtain "minimum essential coverage" (MEC) or else qualify for an exemption for each calendar month of noncoverage. IRC § 5000A(a). If the individual fails either to obtain minimum essential coverage or to qualify for an exemption for any month, the individual is required to make a shared responsibility payment when filing his or her federal income tax return. IRC § 5000A(b)(1).

Minimum essential coverage consists of (1) employer-provided coverage, (2) insurance purchased through the health insurance marketplace, or (3) coverage under government-sponsored plans, such as Medicare and Medicaid. Treas. Reg. §§ 1.5000A-1(b)(1), 1.5000A-2(a). An individual who obtains health-insurance coverage through any of these types of providers has satisfied the individual mandate, but must still report compliance. Treas. Reg. § 1.5000A-1(a).

If an individual has MEC for at least one day during a given month, the IRS will deem the individual to have MEC for the entire month. Treas. Reg. § 1.5000A-1(b)(1). To report full compliance with the individual mandate for the full year, the individual must check a box on his or her tax return (for example, line 61 on Form 1040). For individuals with MEC for the entire year, this is the extent of reporting compliance with the ACA.

An individual or any dependents who did not have MEC for the full year need to evaluate whether any exemptions apply. Some exemptions are obtained by filing a Marketplace exemption application while others are claimed when filing the tax return. Exemptions claimed when filing a tax return are reported on Form 8965, which is attached and filed with the individual's tax return. The exemptions most likely to affect the most individuals are individuals with no affordable coverage, households with income below the filing threshold (for example, the 2014 threshold is $10,150 for a single filer under age sixty-five and $20,300 for married people under age sixty-five filing jointly), and individuals with a "short coverage gap" of less than three months. Treas. Reg. § 1.5000A-3.

The ACA provisions [...] do affect a large number of individuals, especially Schedule C sole proprietors and medium-sized employers who may not be able to afford staff devoted to determine compliance.

For 2015, the hardship exemption applies if the lowest-priced coverage costs more than 8.05 percent of the household's income. Rev. Proc. 2014-37, § 5.03. For 2016, the percent of a household's income increases to 8.13 percent. Rev. Proc. 2014-62, § 2.03. "Household income" is the adjusted gross income from the individual's tax return plus any excludible foreign earned income and tax-exempt interest the individual receives during the taxable year. IRC § 5000A(c)(4)(B). Household income also includes the adjusted gross incomes of all dependents who are required to file tax returns. IRC § 5000A(a).

The short coverage gap exemption applies when an individual suddenly loses or terminates his or her health coverage. The exemption applies as long as the coverage gap is less than three months; however, because coverage for a single day counts as coverage for the entire month, partial months of noncoverage do not count and the exemption may still apply to actual noncoverage periods over the three-month threshold. As long as the total number of months deemed with noncoverage do not equal three months, this exemption applies. See, Treas. Reg. §§ 1.5000A-1(b)(1), 1.5000A-3(j)(2)(i). Only one short coverage gap exemption is allowed during the calendar year. If multiple short coverage gaps exist, the exemption applies only to the earliest gap. Treas. Reg. § 1.5000A-3(j)(2)(iii).

Certain low income individuals are allowed a refundable premium tax credit when enrolling in a qualified health plan through an exchange. IRC § 36B. (This provision was at issue in the U.S. Supreme Court decision in *King v. Burwell*.) To qualify for the premium tax credit, the individual must purchase health insurance through the exchange, have household income between 100 and 400 percent of the poverty line, be ineligible for coverage through an employer or government plan, not file a married filing separately return, and not be claimed as a dependent by another individual.

The shared responsibility payment is the lesser of (1) the sum of the monthly penalty amounts, or (2) the sum of the monthly national average "bronze plan" premiums for the shared responsibility family. IRC § 5000A(c)(1); Treas. Reg. § 1.5000A-4(a).

The code provisions and regulations setting forth how to compute the penalty are complicated. Stated simply, the shared responsibility payment for 2015 is the greater of (1) $325 per person for the year (or $162.50 per child under eighteen) up to a maximum penalty per family of $975, or (2) 2 percent of the individual's household income over the filing threshold. The penalty is capped at the national average premium for a bronze plan. For 2016, these amounts increase to the greater of (1) $695 per person for the year (or $347.50 per child under eighteen) up to a maximum penalty per family of $2,085, or (2) 2.5 percent of the household income over the applicable filing threshold, capped at the national average premium for a bronze plan. IRC § 5000A(c); Treas. Reg. § 1.5000A-4(b).

Unlike most other penalties in the Internal Revenue Code, the IRS is not permitted to file notices of liens or levy any property of the individual who fails to pay the shared responsibility payment. IRC § 5000A(g)(2)(B). Criminal prosecution is also not permitted. IRC § 5000A(g)(2)(A). The IRS, however, may intercept any tax refund due to the individual for failure to pay the penalty. Treas. Reg. § 1.5000A-5(b)(3). In other words, the IRS can only collect the shared responsibility payment if the individual is owed a refund.

EMPLOYER MANDATE

Beginning in 2015, the ACA also requires an "applicable large employer" to make an "assessable payment" (an excise tax) if any full-time employee is certified to the applicable large employer as having received "health care assistance," and the employer either (1) fails to offer health-care coverage to all its full-time employees, or (2) offers MEC under an employer-sponsored plan that is (a) not affordable or (b) fails to provide "minimum value." These provisions do not apply to an employer with fewer than fifty full-time employees (or full-time equivalents). IRC § 4980H(c)(2)(A); Treas. Reg. § 54.4980H-1(a)(4). The employer is not permitted to deduct the excise tax. IRC § 275(a)(6). There are quite a few exceptions and safe harbors that apply to determining compliance that cannot be addressed here.

The "assessable payment" depends on whether (1) the employer fails to offer health-care coverage to all full-time employees or (2) the employer fails to provide affordable or minimum value coverage. For the former, the 2015 assessable payment is $166.67 per month multiplied by the number of full-time employees during the month, reduced by an eighty-person threshold. After 2015, the threshold is reduced to thirty. For the latter situation, the assessable payment is $250 per month, multiplied by the number of full-time employees for any month who receive health-coverage assistance, reduced by the number of employees who were offered the opportunity to enroll in minimum essential coverage.

The IRS will notify employers if any employee received health-care assistance outside of employment and will inform the employer of potential liability with an opportunity to respond before any liability is assessed or notice and demand for payment made. Preamble to TD 9655, 02/12/2014, Q&A on Employer Shared Responsibility Provisions Under the Affordable Care Act, Q&A-27.

For 2016, employers with fifty or more full-time employees (or full-time equivalents) must now file an information return on Form 1095-C reporting the employer's 2015 compliance by reporting the health insurance that the employer offers to its full-time employees, and also requires that these employers furnish related statements to their employees. IRC § 6056; Treas. Reg. §§ 301.6056-1(m), 301.6056-2(b); Preamble to TD 9661, 3/10/2014. Failure to comply will likely trigger the failure to file information returns under section 6724.

While most individuals with regular wage employment and employers who do not fall into the fifty or more full-time employees category need not be concerned about the ACA provisions, these provisions do affect a large number of individuals, especially Schedule C sole proprietors and medium-sized employers who may not be able to afford staff devoted to determine compliance. The addition of the ACA to the Internal Revenue Code only increases the complexity of filing tax returns and costs of compliance. Counsel must remain mindful of the changing requirements under the ACA when advising businesses or individuals.

Jason Galek is certified as a specialist in taxation law by the State Bar of California Board of Legal Specialization. Galek represents individuals and business entities before the Internal Revenue Service, California Franchise Tax Board, Board of Equalization, all California state courts, all federal district courts, the U.S. Tax Court, and the U.S. Court of Federal Claims. He is treasurer of The Bar Association of San Francisco's Barristers Club and a member of the Bay Area Young Tax Lawyers Executive Committee.