BREAKING NEWS

For Immediate Release:

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Employee Benefits
MMA Western Edition

IRS RELEASES FREQUENTLY ASKED QUESTIONS INDICATING THE ASSESSMENT OF POTENTIAL PENALTIES FOR 2015

Executive Summary:

- The Internal Revenue Service (IRS) recently updated its website on the Employer Shared Responsibility Payment (i.e., Employer Mandate) through a set of frequently asked questions (FAQs).
- The FAQs explain that the IRS intends to begin sending "inquiries" to employers who may owe penalties for either a failure to offer substantially all of their Full-Time employees Minimum Essential Coverage (MEC), or to employers who may owe penalties for failure to offer Minimum Value or affordable coverage to their Full-Time employees.
- The inquiries, which will be titled **Letter 226J**, will be sent "**in late 2017**" to Applicable Large Employers (ALEs) that may owe a penalty payment to the IRS for calendar year 2015.
- ALEs that receive Letter 226J will only have **30 days** to respond to the letter, and the letter will contain information on how ALEs may respond to the letter either by agreeing with, or appealing, the proposed penalty.

Introduction

The Internal Revenue Service (IRS) recently updated its website on the Employer Shared Responsibility Payment (i.e., Employer Mandate) through a set of frequently asked questions (FAQs). Questions 55 through 58 provide guidance for employers who may receive a penalty inquiry this year. The IRS letters will be sent "**in late 2017**" to Applicable Large Employers (ALEs) that may owe a penalty payment to the IRS for calendar year 2015. ALEs are defined as any employer who averages 50 or more Full-Time and/or Full-Time Equivalent employees in the previous calendar year.

Background

Beginning in 2015, the Employer Mandate assessed penalties on ALEs who either failed to offer "substantially all" of their Full-Time employees Minimum Essential Coverage, or failed to offer affordable, Minimum Value coverage, to Full-Time employees. Both penalties are contingent upon an employee receiving a premium tax credit to help purchase coverage through the Health Insurance Marketplace (i.e., Exchange).

The two potential penalties (both non-deductible for tax purposes) that could apply to an ALE, in 2015, were:

- **Failure to offer "substantially all" Full-Time employees coverage** – If an employer failed to offer "substantially all" of its Full-Time employees Minimum Essential Coverage, a penalty of $2,080 per Full-Time employee minus 80 Full-Time employees could be assessed, if at least one employee received a premium tax credit for Exchange coverage.

- **Failure to offer Minimum Value or affordable Coverage to a Full-Time employee** – An employer who failed to offer Minimum Value or affordable coverage could be assessed a penalty of $3,120 for each Full-Time employee who received a premium tax credit for Exchange coverage.

Some ALEs may be entitled to transition relief from these penalties for the 2015 calendar year.

IRS Penalty Process

The IRS will be sending **Letter 226J** to employers, which will represent the proposed penalty assessment against the employer. The IRS will issue a Letter 226J to any ALE that the IRS has determined that, for at least one month in the year, at least one of the ALE's Full-Time employees was enrolled in subsidized coverage through the Exchange, and the ALE did not qualify for any relief from the penalties.

The letter will include the following:

- a brief explanation of the penalty provisions

- a table itemizing the proposed penalty by month, and whether the liability is under the "failure to offer substantially all" provision or the "failure to offer Minimum Value/affordable coverage" provision

- two new IRS Forms:
  - Form 14764 – An Employer Mandate Response form, that will allow an employer to respond to the potential penalty liabilities;
  - Form 14765 – Employee Premium Tax Credit List which will list all Full-Time employees who received subsidized Exchange coverage, and for whom the ALE did not qualify for a safe harbor (or other relief)

- a description of the actions the ALE should take if it agrees, partially agrees, or disagrees with the proposed payment amount in Letter 226J; and

- a description of the actions the IRS will take if the ALE does not respond in the time indicated (**generally 30 days** from the date of the Letter 226J).

The letter will also contain the name and contact information of a specific IRS employee that the ALE should contact if it has questions about the letter.

Employer Responses to Letter 226J

ALEs will have an opportunity to contest any proposed penalties. The process for an ALE to contest the penalty is as follows:

- An ALE will respond, in writing, to Letter 226J, either agreeing with the proposed penalty amount, partially agreeing with the proposed penalty amount, or disagreeing with all of the proposed penalty amount.

- The IRS will then acknowledge and provide an ALE a response with one of five versions of **Letter 227** (which, in general, acknowledges the ALE's response and describes further actions the ALE may need to take).

- If the ALE receives its Letter 227, and it disagrees with the proposed or revised penalty, it may request a pre-assessment conference with the IRS Office of Appeals. The ALE should follow the instructions provided in Letter 227 and Publication 5 for requesting a conference with the IRS Office of Appeals. A conference should be requested in writing, by the response date shown on Letter 227, which generally would be **30 days** from the date of Letter 227.

If the ALE does not respond to either Letter 226J or Letter 227, the IRS will assess the amount of the proposed penalty provided in Letter 226J.

The IRS will then issue a notice and demand for payment (**Notice CP 220J**). This Notice will include a summary of the penalty and it will reflect payments made, credits applied, and balances due, if any. The notice will instruct the ALE on the process to make a payment. ALEs will not be required to include the penalty on any tax return that they file or to make payment before notice and demand for payment is made. ALEs may have the ability to make installment payments, as described in Publication 594.

Summary

Employers should also be prepared to respond to any IRS penalty letters and continue to prepare for 2016 and 2017 reporting (in 2018).

The IRS determines the proposed penalty liabilities based on an employer's Forms 1094-C and 1095-C, along with information received from the Exchange regarding an individual's receipt of a premium tax credit. ALEs who have consistently offered affordable, Minimum Value coverage to Full-Time employees should be prepared to appeal any proposed penalties. This may include providing payroll records and documentation regarding how offers of coverage were made. ALEs may also want to consider the information they need to appeal penalties for later years, in the case they receive a Letter 226J for any future years.

Employers that receive Letter 226J should carefully consider whether they have a basis for an appeal, by reviewing its records of the employee in question (who received the premium tax credit), and whether that employee was a Full-Time employee for each month for which the penalty is proposed. Also, an employer may need to demonstrate to the IRS the measurement method for its seasonal and variable hour employees, and whether those employees would be considered Full-Time employees during their stability period.

Employers have a very limited timeframe to respond to Letter 226J, and depending on mailing delays and internal routing, it is critical for employers to consider advanced planning in anticipation of these proposed penalty letters.

Employers may also receive subsidy notification letters from the Exchange during the year, and should be diligent in appealing those letters if there is a basis in doing so. Employers should maintain the appeal letters sent back to the Exchange, as they also could be used to respond to Letter 226J.

Employers, in responding to and receiving Letter 226J, should avoid violating ACA Section 1558, which prohibits employers from retaliating against employees who receive premium tax credits. Prohibitions include the discharge or discrimination against an employee because the employee received a premium tax credit. Employers who violate Section 1558 may be required to reinstate the employee to his or her former position (and provide back pay) and may be subject to compensatory damages, costs, and expenses (including attorneys' fees) incurred by the employee in connection with the bringing of a complaint.

Employers that have questions regarding Letter 226J or IRS response letters should consult with qualified benefits counsel so that the relevant facts and circumstances can be reviewed.