DOUGLAS • MCCARTY Insurance Services, LLC
An Employee Benefits Consulting Company

Legislative Report

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Control Group Rules

Starting in 2015, a large employer (over 100 full-time employees and full-time equivalents) will be subject a penalty under the federal health care reform law if it fails to provide a minimum value health benefit to all full-time workers.

The employer mandate (and the related penalties) apply to "applicable large employers." Under health reform rules, a large employer for a calendar year is an employer who employed an average of at least 50 "full-time employees" on business days during the preceding calendar year. For purposes of identifying whether an organization satisfies this definition, an employer must take into account full-time equivalent individuals by determining how many full-time workers would be required to perform the work done by part-time employees.

Federal law uses long-standing control group rules to combine employers for purposes of health reform, including with the need to count workers to determine if the employer has over 50 full-time employees and full-time equivalents. All "related" companies, as defined under the Tax Code, are treated as a single employer for purposes of health care reform, and the employees of all related employers within the controlled group are counted when determining whether the controlled group, treated as one, is a large employer. This means that some organizations that might otherwise escape application of the health reform mandate, could be drawn under the mandate as a result of control group relationships.

There are three types of controlled groups that are considered one employer for the purposes of the ACA employer mandate. The IRS defines, and provides example of, these three controlled groups in IRS Code § 414 (b) and 414 (c).

1. Parent-Subsidy Group: When one or more businesses are connected through stock ownership with a common parent corporation (such as a chain); and

- 80% of the stock of each corporation (except the common parent) is owned by one or more corporations in the group, and
- Parent Corporation must own 80% of at least one other corporation.

2. Brother-Sister Group: A group of two or more corporations, where five or fewer common owners own directly or indirectly a "controlling interest" of each group and have "effective control". A common owner must be an individual, a trust, or an estate.

- Controlling interest: Generally means 80% or more of the stock of each corporation (but only if such common owner own stock in each corporation); and
- Effective control: Generally more than 50% of the stock of each corporation, but only to the extent such stock ownership is identical with respect to such corporation.

3. Combined Group: A group consisting of three or more organizations that are organized as follows:

- Each organization is a member of either a parent-subsidiary or brother-sister group, and
- At least one corporation is the common parent of a parent-subsidiary, and is also a member of a brother-sister group

Penalty Calculation

For a calendar year during which an employer is a large employer, the penalties are generally applied separately to each member of the controlled group comprising the employer. A control group subject to the mandate has important planning opportunities to consider. Each part of the control group may now independently decide whether to pay or play, and based on that decision, possible penalty implications would be isolated to the member employer.

The penalty on employers not offering health coverage is $2,000 times the number of individuals employed by the applicable large-employer member (less a 30-employee reduction, 80 for 2015 only). If there are a number of separate employers within the control group, generally determined by separate tax ID numbers and separate corporate structures, then each entity will be allowed to subtract its proportionate share of the 30 employee reduction. If there are more than 30 separate entities within the control group, each part gets to subtract one employee when calculating the penalty.

Example

Employer Alpha and Beta are two separate companies but also are members of a single control group due to common ownership.

- Employer A has 40 full-time employees in each calendar month of 2015.
- Employer B employs 35 full-time employees in each calendar month in 2015.

Employer Alpha offers no group health plan for any calendar month of 2015, and at least one full-time employee receives tax credit assistance for a policy through the exchange.

Employer Beta sponsors a group health plan, and all full-time employees are eligible for affordable, minimum value coverage as generally required by the employer mandate.

Implications

There are 75 employees across the control group. The control group thus is a large employer subject to the health reform mandate, but Alpha and Beta are each allowed by their owner(s) to choose how to comply with health reform.

Employer Alpha decides not to "play," and is therefore subject to health reform penalty for 2015 of $48,000 determined as follows:

- Equal to 24 × $2,000 (40 employees reduced by 16 as Alpha's allocable share of the 30-employee offset.)

Employer Beta chooses to compliantly "play" by offering affordable minimal coverage and is therefore not subject to the $2,000 penalty for 2015. Beta is not responsible for the penalties of Alpha.

The segregated responsibility works both ways: Despite choosing to comply, if Employer Beta happened to offer someone "defective" coverage (the premium was not affordable as required and triggered a penalty), an assessment of $3,000 penalty would be charged to Employer Beta's tax ID number. Although special rules would allow Beta to assert it was within a 5% margin for error and thereby attempt to escape the penalty (if the situation is isolated enough), the main point is that, employer Alpha would not be charged for Beta's lapse in this example.

Common Ownership

If companies have common ownership, they will be considered one company for purposes of health reform. If they do not have common ownership, they should be treated as two or more separate companies. The federal tax code and regulations regarding retirement plans offer a good starting point. Those rules focus on percentages of common ownership – generally 80% for corporations and as low as 50% for smaller companies owned by individuals or family investors.

Separate Limited Liability Companies (LLCs), partnerships, or other such structures are not enough to make different entities not part of the same control group, nor would be separate Tax ID numbers. Ownership is the key issue – not company structure. Family attribution rules mean the ownership of a family member is sometimes treated as ownership by the main owner, increasing his or her share and increasing the risk of pulling in more companies into the controlled group and eliminating the possibility of some ownership transfers accomplishing health reform avoidance.

Also, even without common ownership, affected organizations need to be extremely careful about how they count or otherwise "share" workers as that may lead a federal agency to disregard the structure the employer believes it holds. In other words, the employer could inadvertently alter its structure, from an IRS perspective, by operating as an integrated firm through a sharing of employees.

Although insurance brokers cannot issue tax or legal advice about whether a controlled group or affiliated service group might exist and which entities are members, we strongly suggest -- if an employer thinks it might be separate enough from related businesses after reading some initial information -- the employer should obtain a formal tax or legal opinion specifically memorializing whether they are, or are not, actually a controlled group.

Helpful Links

Federal Register: Shared Responsibility for Employers Regarding Health Coverage

IRS discussion of control group rule

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