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# The ACA's Affordability Safe Harbor Percentage Plummets for 2024

The IRS released Revenue Procedure 2023-29 on August 23, 2023, which set the 2024 affordability safe harbor percentage for employer-provided medical coverage to 8.39%. This is an annually indexed amount and a sharp decrease from 2023's 9.12% safe harbor percentage.[1] This affordability percentage affects both: (1) individuals' eligibility for subsidies in the public health insurance marketplace (the "Marketplace"), and (2) the employer affordability safe harbors used to avoid potential employer mandate penalties.

This Alert is relevant for any applicable large employer (ALE) as defined under the Affordable Care Act (ACA) and provides a summary of the ACA's employer mandate penalties and the three available employer affordability safe harbors, as well as a description of how the 8.39% affordability safe harbor percentage will affect setting employee contributions for the 2024 plan year.

## A Summary of the ACA's Employer Mandate Penalties

The ACA's employer mandate penalties are indexed annually and only apply to ALEs that fail to meet certain minimum standards for offering medical coverage to full-time (FT) employees. A discussion of how to determine ALE and FT employee status is beyond the scope of this Alert.

### IRC §4980H(a) "no offer" penalty

This penalty applies when an ALE fails to offer minimum essential coverage (MEC) to at least 95% of its FT employees for a calendar month and at least one FT employee obtains subsidized coverage in the Marketplace for that month. Most employer-provided medical coverage qualifies as MEC. For the purposes of avoiding this penalty,

[1] The current methodology measures premium growth against income growth. This is the second significant decrease in a row and indicates that the gap in growth rates continues to narrow.

## Highlights

### In a nutshell

- The 2024 ACA affordability safe harbor is 8.39%. This is the second sharp decrease in the last two years.
- The 8.39% limit will generally lower the amount ACA applicable large employers are permitted to charge FT employees for medical coverage and avoid the IRC §4980H(b) "inadequate offer" employer mandate penalty.
- This Alert includes a discussion of the ACA's employer mandate penalties and affordability safe harbors (including examples of each).

### Recommended employer action

Applicable large employers – as defined under the ACA – should review their 2024 employee medical coverage contribution strategies to limit their risk of employer mandate penalties.

it does not matter if the offer of coverage is affordable or if the coverage satisfies the ACA's minimum value requirements.[2]

The 2024 §4980H(a) annual penalty amount is $2,970 ($247.50/month).[3] The penalty calculation multiplies this amount by all of the ALE's FT employees for the given month minus the 30 FT employee exclusion amount.[4]

Example

An ALE fails to offer MEC to at least 95% of its 127 FT employees in April 2024, and at least 1 FT employee qualifies for a Marketplace subsidy that month. The total §4980H(a) penalty risk is:

$247.50 × (127 - 30) = $24,007.50 for April 2024

## IRC §4980H(b) "inadequate offer" penalty

This penalty applies when an ALE offers MEC to at least 95% of its FT employees but fails to offer affordable and/or minimum value coverage to one or more FT employees who obtain a subsidy in the Marketplace. This penalty determines affordability solely on the required employee contribution toward employee-only coverage for the employer's lowest cost medical plan option offered to the FT employee that provides minimum value, regardless of which coverage option an employee actually elects or if they waive coverage.

The 2024 §4980H(b) annual penalty amount is $4,460 ($371.67/month).[5] Unlike the §4980H(a) penalty, this penalty only applies to the FT employee(s) that trigger the penalty that month.

Example

An ALE offers MEC to 100% of its FT employees for the entire 2024 calendar year, but the offer of coverage does not meet the employer's chosen affordability safe harbor for some of them. Assume that 5 FT employees who were offered unaffordable coverage obtain Marketplace subsidies in April 2024. The total §4980H(b) penalty risk is:

$371.67 × 5 = $1,858.35 for April 2024

**Did you know?** An ALE does not get credit for offering coverage to a FT employee unless the employee can also enroll his or her natural and adopted children up to age 26, as applicable.

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[2] In general, minimum value means the plan pays at least 60 percent of the expected total allowed cost of benefits for the plan year and includes coverage for hospital and physician services.

[3] See Revenue Procedure 2023-17.

[4] The 30 FT employee exclusion amount applies as a single combined limit for related legal entities that must be counted together when determining ALE status (known as an aggregated ALE group). A group member's proportion of the group's total FT employees determines its share of the exclusion amount. For example, if a member has 50% of the aggregated ALE group's FT employees, it can exclude 15 FT employees from its own penalty calculation (50% × 30 = 15).

[5] See Revenue Procedure 2023-17.

# The Employer Affordability Safe Harbors

## Brief background

The trigger for potential employer mandate penalties is whether a FT employee obtains a Marketplace subsidy during a given month. An individual who enrolls in medical coverage, or who waives affordable employer medical coverage that meets the ACA's minimum value requirements, is generally ineligible for a Marketplace subsidy. The subsidy affordability calculation measures the offer of coverage against the individual's household income. At a high level, household income is adjusted gross income from all sources[6] reported on the taxpayer's federal personal income tax return after certain adjustments.

The ACA provides employers with three safe harbors (one has two subparts) that qualify as affordable offers of coverage for the purposes of avoiding the employer mandate penalties. These safe harbors do not require an employer to have any knowledge of an employee's household income. The three safe harbors are:

1. Federal poverty line;
2. Form W-2; and
3. Rate of Pay.

While uncommon, the use of household income for Marketplace subsidy eligibility purposes makes it possible for an individual to qualify for a Marketplace subsidy even though their employer offered coverage that met an affordability safe harbor. The safe harbor still prevents a FT employee from triggering an employer mandate penalty in this situation.

## The 2024 affordability safe harbor percentage and other general employer affordability safe harbor notes

The most recent affordability safe harbor percentages used to determine Marketplace subsidy eligibility and the employer affordability safe harbors are below.

| Calendar Year | Affordability Percentage |
|---|---|
| 2022 | 9.61% |
| 2023 | 9.12% |
| 2024 | 8.39% |

The following notes apply broadly to all three available employer affordability safe harbors:

- Safe harbor calculations – An affordability calculation uses the employee cost for the lowest cost employee-only minimum value plan the employee could have elected. It makes no difference if the employee waives coverage, enrolls a spouse and/or dependents, or enrolls in a more expensive plan option.

  **Wellness Programs:** If wellness incentives affect the employee contribution toward medical coverage, the employer must treat all employees as tobacco-free and failing all other incentives when performing employer affordability calculations. It does not matter which standards an employee actually satisfies.

[6] This includes a spouse's income if the spouses file a joint tax return, as well as investment, rental, and/or other business income. Please note that various losses and/or other deductions can lower household income below the taxable compensation amounts reported by employers.

- Plan year – Affordability calculations use the affordability percentage in effect at the beginning of the plan year. For example, a plan with a July 1, 2023 – June 30, 2024 plan year will use 9.12% for the entire plan year for affordability calculation purposes.

- Classes of employees – The regulations allow an employer to define and apply different safe harbors to different classes of employees. The regulations indicate the categories must be reasonable, and the same safe harbor must apply to all employees within a class. Reasonable classifications include the following:

  - Hourly and salaried employees;

  - Union (i.e., collectively bargained) and non-union employees;

  - Employees working in different geographic locations; and

  - Employees in different job categories (e.g., corporate and retail).

## Federal poverty line (FPL) safe harbor

Under the FPL safe harbor, coverage is affordable for plan years beginning in 2024 if the employee's share of the premium does not exceed 8.39% of the individual FPL amount for the calendar year divided by 12. The U.S. Department of Health & Human Services (HHS) publishes the FPL amounts annually. There is one set of FPL amounts for the continental United States. Separate and higher FPL amounts apply to Alaska and Hawaii.

Since the FPL amounts are usually not available from HHS for a given year before late January or early February of that year, the rules allow plans to use the individual FPL amount in effect six months prior to the start of the plan year. Calendar year plans effectively have little choice but to rely on the prior year's FPL amount.

An employer with a non-calendar plan year that begins within six months of the month HHS releases the current year FPL amounts can choose between using the prior or current year individual FPL amount for affordability calculation purposes. The FPL amounts historically increase year-over-year, so employers generally prefer to use the current year FPL amount when feasible. For open enrollment and other plan administrative reasons, it is generally difficult for employers with plan years beginning before April to take advantage of the current year individual FPL amount. An employer with a plan year beginning more than six months after the month HHS releases the data must use the current year FPL amount.

If an employer's plan satisfies this safe harbor, employers should rely on it in lieu of the others since it is automatic and does not rely on employee wages or hours worked. However, this safe harbor usually results in lower permitted employee contribution amounts than the others.

Example 1

The 2023 individual FPL amount is $14,580. For a plan year beginning on January 1, 2024, an offer of coverage is affordable if the monthly employee cost of employee-only coverage is $101.93 or less.

($14,580 × 8.39%) = $1,223.26 annually

($1,223.26 ÷ 12) = $101.93/month[7]

Example 2

Purely as a hypothetical, assume HHS releases the 2024 FPL amounts on January 27, 2024, and the individual amount increases to $15,640. An employer sponsors a plan with a plan year beginning on July 1, 2024. Using the

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[7] We generally recommend rounding affordability answers down.

hypothetical 2024 individual FPL amount, coverage is affordable for the July 1, 2024 – June 30, 2025 plan year if the monthly employee cost of employee-only coverage is $109.34 or less.

($15,640 × 8.39%) = $1,312.19 annually

($1,312.19 ÷ 12) = $109.34/month

The employer could rely on the 2023 FPL amount instead, since that was still in effect six months before the July 1, 2024 plan year began, but $109.34/month is obviously greater than $101.93/month.

## Form W-2 safe harbor

Under the Form W-2 safe harbor, coverage is affordable for plan years beginning in 2024 if the employee's share of the premium does not exceed 8.39% of wages reported in Box 1 of the employee's 2024 IRS Form W-2. Box 1 reports taxable compensation minus all pre-tax benefit deductions.

Employers can estimate Form W-2 earnings when pricing coverage, but actual affordability will not be certain until the end of the year and the actual W-2 is issued (i.e., Employers will not issue their 2024 Forms W-2 before January 2024). The W-2 safe harbor is an all-or-nothing approach. An employer cannot rely on the W-2 safe harbor for part of the Form 1095-C reporting year and use a different safe harbor for the rest of the reporting year for the same employees. This may affect some employers with non-calendar year plans.

Example 1 below is probably the most familiar Form W-2 safe harbor calculation. It uses an actual or estimated W-2 amount as a benchmark to forecast the maximum employee-only contribution an employer can charge and fit within the safe harbor for employees at or above that Box 1 compensation amount.

Example 1

Using a Form W-2, Box 1 compensation amount of $18,000, an offer of coverage is affordable if the monthly employee cost of employee-only minimum value coverage is $125.85 or less.

($18,000 × 8.39%) ÷ 12 = $125.85/month

Example 2 follows the safe harbor calculation in the regulations, using actual Box 1 W-2 wages for the year. Employers should follow this approach when appealing a later challenge from the IRS that an offer of coverage did not meet the Form W-2 safe harbor for a particular FT employee. The Form W-2 safe harbor calculation pro-rates the Box 1 wages if the months worked exceed the months an employer offered coverage. This will apply if the plan has a waiting period or if the employer does not employ the employee for the entire calendar year.

Example 2

An employee's actual 2024 Form W-2, Box 1 compensation is $23,444.53. The employee worked and the employer offered coverage for all 12 months. The monthly employee cost for the lowest cost employee-only minimum value medical plan is $140.

Wages: $23,444.53 × (12 offered ÷ 12 worked) = $23,444.53

Annual Cost: $140 × 12 = $1,680

$1,680 ÷ $23,444.53 = 7.17%

Coverage is affordable because 7.17% is less than 8.39%

## Rate of pay safe harbor

The Rate of Pay safe harbor has two subparts for hourly and non-hourly employees, described below. This safe harbor bases the rate of pay on the employee's gross base rate of pay. This amount does not exclude any employee contributions toward benefits, but it does not account for bonuses, commissions, or tips. This safe harbor is impractical for employees that receive a significant amount of their compensation from those sources.

**Hourly employees**

Under the Rate of Pay safe harbor for hourly employees, coverage is affordable for plan years beginning in 2024 for a particular month if the employee's share of the premium for the lowest cost employee-only minimum value plan option does not exceed 8.39% of 130 paid hours multiplied by the lower of:

- The employee's hourly rate as of the first day their offer of coverage is effective during the plan year (the first day of the plan year for most employees); or
- The employee's hourly rate for that particular month.

Employers must multiply the applicable rate of pay by 130 hours regardless of the actual number of hours the employee works during any given month.

Example 1

An employer maintains a calendar year plan. On January 1, 2024, the employee's hourly rate is $12. The employee's hourly rate increases to $13.50 as of July 1st. An offer of coverage is affordable if the monthly employee cost of employee-only coverage is $130.88 or less.

(130 × $12) × 8.39% = $130.88 for all months

The increase to $13.50 does not apply, because the employee's hourly rate as of the first day of the plan year (the first day the offer of coverage was effective) remains the lowest applicable rate for calculation purposes.

Example 2

An employer maintains a calendar year plan. On January 1, 2024, the employee's hourly rate is $12. The employee's hourly rate decreases to $10 from June – August and then returns to $12 beginning in September. An offer of coverage is affordable if the monthly employee cost of employee-only coverage is equal to or less than the following calculated amounts:

(130 × $12) × 8.39% = $130.88 for January – May and September – December

(130 × $10) × 8.39% = $109.07 for June – August

**Non-hourly employees ("salaried employees")**

Under the Rate of Pay safe harbor for salaried employees, coverage is affordable for plan years beginning in 2024 if the employee's share of the premium does not exceed 8.39% of the employee's gross monthly salary as of the first day their offer of coverage is effective during the plan year. For most employees, this will be the first day of the plan year.

Employers sponsoring non-calendar year plans will use the gross monthly salary applicable to the plan year beginning in 2024. This safe harbor is not available for a salaried employee if the employee's monthly salary decreases during the plan year (e.g., Due to an unpaid leaves of absence, demotion, etc.).

Example

An employer maintains a calendar year plan. On January 1, 2024, the employee's monthly gross salary throughout the year is $3,000. An offer of coverage is affordable if the monthly employee cost of employee-only coverage is $251.70 or less.

$3,000 × 8.39% = $251.70/month

## Form W-2 versus Rate of Pay safe harbor

The Rate of Pay safe harbor often appears more attractive than the Form W-2 safe harbor for planning purposes, because affordability under the Form W-2 safe harbor may not be certain for a number of employees until after the end of the calendar year. However, there are still situations where the Form W-2 safe harbor is or may be preferable:

- Although Form W-2, Box 1 excludes pre-tax benefit deductions while the Rate of Pay safe calculation uses gross monthly pay, the Rate of Pay safe harbor calculation for hourly employees is fixed at 130 hours. The Form W-2 safe harbor may produce better results for employees who work significantly more hours than this per month, even accounting for payroll deductions.
- The Rate of Pay safe harbor does not include bonuses, commissions, tips, or overtime pay. If these forms of compensation make up a significant portion of an employee's pay, the Form W-2 safe harbor should produce better results.
- The Rate of Pay safe harbor is not available for salaried employees whose gross monthly salary decreases during the plan year.

# About the author

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