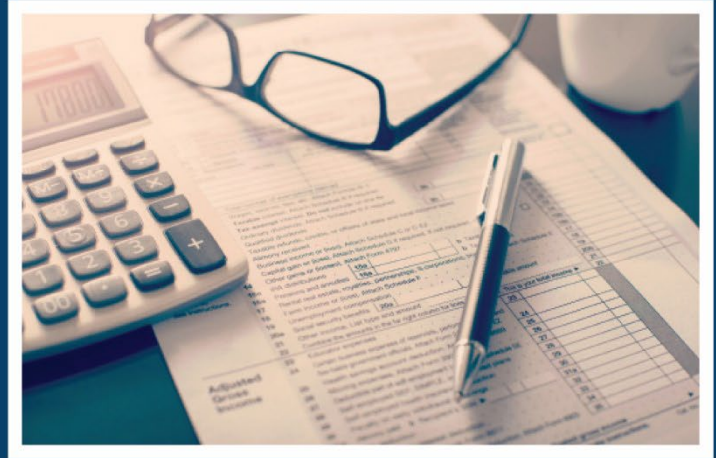


ACA AFFORDABILITY PERCENTAGE INCREASES FOR 2025



ACA Affordability Percentage Increases for 2025

On Sept. 6, 2024, the IRS released [Revenue Procedure 2024-35](#) to index the contribution percentage in 2025 for determining the affordability of an employer's plan under the Affordable Care Act (ACA). **For plan years beginning in 2025**, employer-sponsored coverage will be considered affordable under the ACA's "pay-or-play" rules if the employee's required contribution for self-only coverage does not exceed **9.02%** of their household income for the year. This percentage is an increase to the affordability threshold in 2024 which may give employers more flexibility when setting employee contribution levels for 2025.

Employer Shared Responsibility Rules

The ACA's pay or play rules require applicable large employers (ALEs) to offer affordable, minimum-value health coverage to their full-time employees (and dependents) or pay a penalty. The affordability of health coverage is a key point in determining whether an ALE will be subject to a penalty. An ALE's health coverage is considered affordable if the employee's required contribution to the plan does not exceed a certain percentage of the employee's household income for the taxable year. This percentage is adjusted annually based on health plan premium growth rates in relation to income growth rates.

In recent years, the affordability percentage has been adjusted to:

- 9.12% for plan years beginning in 2023
- 8.39% for plan years beginning in 2024
- 9.02% for plan years beginning in 2025

The affordability test applies only to the portion of the annual premiums for **self-only coverage** and does not include any additional cost for family coverage. Also, if an employer offers multiple health coverage options, the affordability test applies to the **lowest-cost option that provides minimum value**.

Because an employer generally will not know an employee's household income, the IRS has provided three optional affordability **safe harbors** that ALEs may use to determine affordability based on information that is available to them: the Form W-2 safe harbor, the rate of pay safe harbor and the federal poverty level safe harbor, as outlined below.

Form W-2 Safe Harbor

Under the Form W-2 safe harbor, an ALE may determine the affordability of its health coverage by reference only to an employee's wages from that ALE, instead of by reference to the employee's household income. For this purpose, "wages" is the amount that is required to be reported in **Box 1** of the employee's Form W-2.

An ALE satisfies the Form W-2 safe harbor with respect to an employee if the employee's required contribution for the calendar year for the ALE's lowest cost self-only coverage that provides minimum value during the entire calendar year (excluding COBRA or other continuation coverage except with respect to an active employee eligible for continuation coverage) **does not exceed 9.02% of that employee's Form W-2 wages** from the employer for the calendar year.

-Eligibility for the Form W-2 Safe Harbor

To be eligible for the Form W-2 safe harbor, the employee's required contribution must remain a consistent amount or percentage of all Form W-2 wages during the calendar year (or during the plan year for plans with non-calendar year plan years). Thus, an ALE may not make discretionary adjustments to the required employee contribution for a pay period. A periodic contribution that is based on a consistent percentage of all Form W-2 wages may be subject to a dollar limit specified by the employer.

-Timing of the Form W-2 Safe Harbor

ALEs determine whether the Form W-2 safe harbor applies after the end of the calendar year and on an employee-by-employee basis, taking into account W-2 wages and employee contributions.

-Partial-year Offers of Coverage

For an employee who was not offered coverage for an entire calendar year, the Form W-2 safe harbor is applied by:

- Adjusting the employee's Form W-2 wages to reflect the period when the employee was offered coverage; and
- Comparing the adjusted wage amount to the employee's share of the premium for the employer's lowest cost self-only coverage that provides minimum value for the periods when coverage was offered.

Specifically, the amount of the employee's compensation for purposes of the Form W-2 safe harbor is determined by multiplying the wages for the calendar year by a fraction equal to the number of calendar months for which coverage was offered over the number of calendar months in the employee's period of employment with the ALE during the calendar year. For this purpose, if coverage is offered during at least one day during the calendar month, or the employee is employed for at least one day during the calendar month, the entire calendar month is counted in determining the applicable fraction.

Rate of Pay Safe Harbor

The rate of pay safe harbor was designed to allow ALEs to prospectively satisfy affordability without the need to analyze every employee's wages and hours. **For hourly employees**, the rate of pay safe harbor allows an ALE to:

- Take the lower of the hourly employee's rate of pay as of the first day of the coverage period (generally, the first day of the plan year) or the employee's lowest hourly rate of pay during the calendar month;
- Multiply that rate by 130 hours per month (the benchmark for full-time status for a month); and
- Determine affordability for the calendar month based on the resulting monthly wage amount.

Specifically, the employee's monthly contribution amount (for the self-only premium of the employer's lowest cost coverage that provides minimum value) is affordable for a calendar month if it is equal to or lower than **9.02% of the computed monthly wages** (that is, the employee's applicable hourly rate of pay multiplied by 130 hours). The final regulations, unlike the proposed regulations, allow an ALE to use the rate of pay safe harbor even if an hourly employee's rate of pay is reduced during the year.

For salaried employees, monthly salary as of the first day of the coverage period would be used, instead of hourly salary multiplied by 130 hours. However, if the monthly salary is reduced, including due to a reduction in work hours, the rate of pay safe harbor may not be used.

Federal Poverty Line Safe Harbor

An ALE may also rely on a design-based safe harbor using the federal poverty line (FPL) for a single individual. Employer-provided coverage is considered affordable under the FPL safe harbor if the employee's required contribution for the calendar month for the lowest cost self-only coverage that provides minimum value does not exceed **9.02% of the FPL for a single individual** for the applicable calendar year, divided by 12.

ALEs may use any of the poverty guidelines in effect within six months before the first day of the plan year for purposes of this safe harbor. For reference, the last published 2024 FPL for a single individual of \$15,060 would result in a maximum employee contribution of **\$113.20** to be considered affordable under the FPL safe harbor (9.02% X \$15,060/12).

ACA Pay-or Play Penalty Calculations

Under the pay-or-play rules, an applicable large employer (ALE) is only liable for a penalty if at least one full-time employee receives a subsidy for Exchange coverage. This could be because the employer coverage does not provide minimum value and/or is considered unaffordable. The amount of the penalty will depend on whether or not the ALE offered coverage to at least 95% of its full-time employees (and dependents).

On Feb. 12, 2024, the IRS [released](#) updated penalty amounts for 2025 related to the employer shared responsibility (pay-or-play) rules under the Affordable Care Act (ACA). For calendar year 2025, the adjusted penalty amount for an ALE who did not offer coverage to substantially all of its' full-time employees (and dependents) is **\$2,900**. The adjusted penalty amount for an ALE who did offer coverage to substantially all of its' full-time employees (and dependents) is **\$4,350**. These are a decrease from the penalty amounts for the 2024 calendar year, which are \$2,970 and \$4,460, respectively.

This Legal Update is not intended to be exhaustive nor should any discussion or opinions be construed as legal advice. Readers should contact legal counsel for legal advice.
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