Internal Revenue
bulletin

Bulletin No. 2014–9
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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 2014–7, page 539.

This revenue ruling provides guidance on the amount of the life insurance reserves taken into account under § 807 of the Internal Revenue Code for a variable contract where some or all of the reserves are accounted for as part of a life insurance company's separate account reserves. Rev. Rul. 2007–54 is modified and superseded and Rev. Rul. 2007–61 is obsoleted.

T.D. 9655, page 541.

TD 9655 includes final Treasury regulations providing guidance under section 4980H of the Internal Revenue Code, as added by the Patient Protection and Affordable Care Act. Section 4980H generally provides that an applicable large employer may be subject to an assessable payment if the employer does not offer minimum essential health coverage to its full-time employees (and their dependents), or if the employer offers its full-time employees (and their dependents) minimum essential health coverage that is not affordable. The regulations affect applicable large employers, defined under section 4980H as employers that employed on average at least 50 full-time employees (including full-time equivalents) on business days during the preceding calendar year.

Notice 2014–10, page 605.

Notice 2014–10 provides relief from the individual shared responsibility payment required under section 5000A of the Internal Revenue Code for months in 2014 in which individuals have, under Medicaid and chapter 55 of Title 10, U.S.C., limited-benefit health coverage that is not minimum essential coverage.

Notice 2014–12, page 606.

Resident populations of the 50 states, the District of Columbia, Puerto Rico, and the insular areas for purposes of determining the 2014 calendar year (1) state housing credit ceiling under section 42(h) of the Code, (2) private activity bond volume cap under section 146, and (3) private activity bond volume limit under section 142(k) are reproduced.

Rev. Proc. 2014–16, page 606.

Rev. Proc. 2014–16 provides the procedures by which a taxpayer may obtain the automatic consent of the Commissioner of Internal Revenue to change to certain methods of accounting for amounts paid to acquire, produce, or improve tangible property, as well as to change to a reasonable method described in § 1.126A–1(f)(4) for self-constructed assets. The revenue procedure also provides the procedures for changing to a permissible method of accounting under section 263A(b)(2) and § 1.263–3(a)(1) for certain costs related to real property acquired through foreclosure or another similar transaction. Finally, the revenue procedure modifies section 3.09 of the APPENDIX to Rev. Proc. 2011–14 regarding a change to the method of accounting described in Rev. Proc. 2011–43 for taxpayers in the business of transporting, delivering, or selling electricity.

Rev. Proc. 2014–20, page 614.

This revenue procedure provides a safe harbor under which the Internal Revenue Service will, under certain, defined circumstances, treat indebtedness that is secured by 100 percent of the ownership interest in a disregarded entity that holds real property as indebtedness that is secured by real property for purposes of § 108(c)(3)(A) of the Internal Revenue Code. This revenue procedure will assist taxpayers with so-called "mezzanine" financing in workouts and similar circumstances.

Finding Lists begin on page ii.
Index for July through February begins on page iv.

Department of the Treasury
Internal Revenue Service

The IRS Mission

Provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions and Other Related Items, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.
This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The last Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the last Bulletin of each semiannual period.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 108.—Income from Discharge of Indebtedness

For the scope and procedures for a safe harbor under which the Internal Revenue Service will, under certain, defined circumstances, treat indebtedness that is secured by 100 percent of the ownership interest in a disregarded entity that holds real property as indebtedness that is secured by real property for purposes of § 108(c)(3)(A) of the Internal Revenue Code. See Rev. Proc. 2014–20, page 614.

Section 162.—Trade or business expenses

Procedures are provided by which a taxpayer may obtain the automatic consent of the Commissioner of Internal Revenue to change to the methods of accounting provided in §§ 1.162–3 and 1.162–4 of the Income Tax Regulations and §§ 1.162–3T and 1.162–4T of the temporary regulations (T.D. 9564). See Rev. Proc. 2014–16, page 606.

Section 263A.—Capitalization and inclusion in inventory costs of certain expenses

Procedures are provided by which a taxpayer may obtain the automatic consent of the Commissioner of Internal Revenue to change to a reasonable method described in § 1.263A–1(f)(4) for self-constructed assets and to change to a permissible method of accounting under section 263A(b)(2) of the Internal Revenue Code and § 1.263A–3(a)(1) for certain costs related to real property acquired through foreclosure, by deed in lieu of foreclosure, or in another similar transaction. See Rev. Proc. 2014–16, page 606.

Section 446.—General rule for methods of accounting

Procedures are provided by which a taxpayer may obtain the automatic consent of the Commissioner of Internal Revenue to change to the methods of accounting provided in §§ 1.162–3, 1.162–4, 1.263(a)–1, 1.263(a)–2, and 1.263(a)–3 of the Income Tax Regulations and §§ 1.162–3T, 1.162–4T, 1.263(a)–1T, 1.263(a)–2T, and 1.263(a)–3T of the temporary regulations (T.D. 9564). In addition, procedures are provided by which a taxpayer may obtain the automatic consent of the Commissioner of Internal Revenue to change to a reasonable method described in § 1.263A–1(f)(4) for self-constructed assets and to change to a permissible method of accounting under section 263A(b)(2) of the Internal Revenue Code and § 1.263A–3(a)(1) for certain costs related to real property acquired through foreclosure, by deed in lieu of foreclosure, or in another similar transaction. Finally, modifications are made to section 3.09 of the APPENDIX of Rev. Proc. 2011–14 regarding a change to the method of accounting described in Rev. Proc. 2011–43, 2011–37 I.R.B. 326, for taxpayers in the business of transporting, delivering, or selling electricity. See Rev. Proc. 2014–16, page 606.

Section 807.—Rules for certain reserves

Rev. Rul. 2014–7

ISSUE

What is the amount of the life insurance reserves taken into account under section 807 of the Internal Revenue Code for a variable contract where some or all of the reserves are accounted for as part of a life insurance company's separate account reserves?

FACTS

Situation 1. IC is a life insurance company as defined in section 816(a) and is the issuer of Contract A. Contract A provides for the payment of variable annuity benefits computed on the basis of a recognized mortality table and the investment experience of *IC*'s segregated asset account (separate account). *IC* bears the mortality risks with regard to the contingencies involved in the variable annuity benefits. Contract A neither provides any "supplemental benefits" (as defined in section 807(e)(3)(D)) nor involves any "qualified substandard risks" (as defined in section 807(e)(5)(B)).

Contract A is a "variable contract" as defined in section 817(d) and an "annuity contract" under section 817(g). *IC*'s reserves for Contract A are "life insurance reserves" as defined in section 816(b).

For taxable years 2012 and 2013, the amounts of end-of-year tax reserves determined under section 807(d)(2) for Contract A are $8,000 and $10,000, respectively.

The 2012 and 2013 end-of-year net surrender values determined under section 807(e)(1) for Contract A are $7,840 and $9,830, respectively. The amounts taken into account by *IC* with regard to Contract A in determining its 2012 and 2013 end-of-year statutory reserves within the meaning of section 807(d)(6) are $8,050 and $10,045, respectively. None of *IC*'s statutory reserves is attributable to any deferred or uncollected premium.

Situation 2. The facts are the same as Situation 1, except that Contract A provides a minimum guaranteed death benefit in addition to variable annuity benefits. *IC* bears the mortality risks and investment risks with regard to the contingencies involved in the provision of the death benefit.

For taxable years 2012 and 2013, the end-of-year tax reserves determined under section 807(d)(2) for Contract A are $8,155 and $10,165, respectively. The 2012 and 2013 end-of-year net surrender values determined under section 807(e)(1) for Contract A are $8,000 and $10,000, respectively. The amount taken into account by *IC* with regard to Contract A in determining its 2012 and 2013 end-of-year statutory reserves within the meaning of section 807(d)(6) are $8,210 and $10,215, respectively.

If Contract A had not provided the minimum guaranteed death benefit, the 2012 and 2013 end-of-year tax reserves determined under section 807(d)(2) would have been $8,000 and $10,000, respectively.

LAW AND ANALYSIS

Section 803(a) provides that life insurance company gross income is the sum of (i) premiums, (ii) net decreases in certain reserves under section 807(a), and (iii) other amounts generally included by a taxpayer in gross income. Section 805(a)(2) authorizes a deduction for the net increase in certain reserves under section 807(b). In calculating the change in reserves for a variable contract, the increase or decrease in the reserves due to appreciation and depreciation of separate account assets is removed. *See* section 817(a).

Section 807(c) sets forth the items taken into account in determining the net decrease or net increase in reserves under section 807(a) and (b). Among the items taken into account are "life insurance reserves" (as defined in section 816(b)).

For purposes of determining a life insurance company's income or deduction from a change in reserves, section 807(d)(1) provides that the amount of the life insurance reserves for any contract is the greater of— (i) the contract's net surrender value, or (ii) the contract's tax reserve determined under section 807(d)(2). However, the life insurance reserves for a contract cannot exceed the "statutory reserves" (as defined in section 807(d)(6)).

Section 807(d)(2) provides that the amount of the tax reserve for any contract is determined using— (i) the tax reserve method applicable to the contract, (ii) the greater of the applicable Federal interest rate or the prevailing State assumed interest rate, and (iii) the prevailing commissioners' standard tables for mortality and morbidity adjusted as appropriate to reflect the risks (such as substandard risks) incurred under the contract which are not otherwise taken into account. The tax reserves determined under section 807(d)(2) reflect all of the benefits (including the net surrender value) payable under the contract.

Section 807(e)(1) provides generally that the net surrender value of "any contract" is determined with regard to any penalty or charge that would be imposed on surrender, but without regard to any market value adjustment on surrender. The net surrender value represents the current contractual cash benefit payable under a contract.

Except as otherwise provided in special rules under section 807(e)(3) and (5) (relating to qualified supplemental benefits and qualified substandard risks), the comparison of the tax reserve and the net surrender value is made on an aggregate benefit basis. *See* H. Rep. No. 432, Pt. 2, 98th Cong., 2d Sess. 1414 (1984); S. Prt. 169, Vol. I, 98th Cong. 2d Sess. 540 (1984).

Section 807 makes no distinction between a fixed (non-variable) contract and a variable contract. For both fixed and variable contracts, a life insurance company determines its income or deduction from a change in reserves using the amounts of its life insurance reserves determined under section 807. *See also* section 817(a) (referring to "the sum of the items described in section 807(c)").

Section 817(c) requires a life insurance company to account separately for the income, exclusion, deduction, asset, reserve, and other liability items attributable to variable contracts. If a variable contract contains a guarantee (for example, a minimum death benefit), section 817(d) (flush language) requires an insurance company to account for the excess of obligations under the guarantee over the obligations under the contract without regard to the guarantee as part of the company's general account, and not as part of the company's separate account.

In both Situation 1 and Situation 2, the end-of-year tax reserves determined under section 807(d)(2) for Contract A— (i) exceed the end-of-year net surrender value of the Contract, but (ii) are less than the end-of-year statutory reserves for the Contract. Accordingly, under section 807(d)(1), the amount of the end-of-year life insurance reserves taken into account under section 807 for Contract A in both Situations is the amount of the end-of-year tax reserves determined under section 807(d)(2). In Situation 1, the amounts of the 2012 and 2013 end-of-year life insurance reserves for Contract A are $8,000 and $10,000, respectively. In Situation 2, the amounts of the 2012 and 2013 end-of-year life insurance reserves for Contract A are $8,155 and $10,165, respectively.

In Situation 2, *IC* is required under section 817(d) to account for the excess of its obligations under Contract A with the minimum death benefit over its obligations under the Contract without the death benefit as part of the company's general account reserves. Pursuant to section 817(c), *IC* accounts for its remaining obligations under the Contract A as part of the company's separate account reserves. Accordingly, for end-of-year 2012, *IC* accounts for the $155 excess of its obligations under Contract A with the minimum death benefit ($8,155) over its obligations under the Contract without the death benefit ($8,000) as part of the company's general account reserves. *IC* accounts for the remaining $8,000 as part of its separate account reserves. For end-of-year 2013, *IC* accounts for the $165 excess of its obligations under Contract A with the minimum death benefit ($10,165) over its obligations under Contract A without the death benefit ($10,000) as part of the company's general account reserves. *IC* accounts for the remaining $10,000 as part of its separate account reserves.

This revenue ruling provides guidance only with regard to the determination under section 807(d) of the amount of the life insurance reserves for a variable contract when some or all of the reserves are accounted for as part of a life insurance company's separate account reserves.

HOLDING

Under section 807(d)(1), the amounts of the end-of-year life insurance reserves for Contract A in both Situation 1 and Situation 2 are the amounts of the tax reserve determined under section 807(d)(2). Thus, in Situation 1, the amounts of the 2012 and 2013 end-of-year life insurance reserves for Contract A are $8,000 and $10,000, respectively. In Situation 2, the amounts of the 2012 and 2013 end-of-year life insurance reserves for Contract A are $8,155 and $10,165, respectively.

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 2007–54 is modified and superseded. Rev. Rul. 2007–61 is obsoleted.

DRAFTING INFORMATION

The principal author of this revenue ruling is David Remus of the Office of the Associate Chief Counsel (Financial Institutions & Products). For further information regarding this revenue ruling, contact Mr. Remus at (202) 317-6995 (not a toll-free number).

TD 9655

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Parts 1, 54, and 301

Shared Responsibility for Employers Regarding Health Coverage

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations providing guidance to employers that are subject to the shared responsibility provisions regarding employee health coverage under section 4980H of the Internal Revenue Code (Code), enacted by the Affordable Care Act. These regulations affect employers referred to as applicable large employers (generally meaning, for each year, employers that had 50 or more full-time employees, including full-time equivalent employees, during the prior year). Generally, under section 4980H an applicable large employer that, for a calendar month, fails to offer to its full-time employees health coverage that is affordable and provides minimum value may be subject to an assessable payment if a full-time employee enrolls for that month in a qualified health plan for which the employee receives a premium tax credit.

DATES: *Effective date*: These regulations are effective February 12, 2014.

Applicability Dates: For dates of applicability, see section XVI of this preamble, §§ 54.4980H–1(b), 54.4980H–2(f), 54.4980H–3(i), 54.4980H–4(h), 54.4980H–5(g), and 54.4980H–6(b).

FOR FURTHER INFORMATION CONTACT: Kathryn Johnson or Shad Fagerland, (202) 317-6846 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

Sections I through IV of the preamble ("Background") describe section 4980H, including previously issued guidance under section 4980H, as well as related statutory provisions. Sections V through XIV of the preamble ("Explanation and Summary of Comments") describe the comments received on the proposed regulations and explain amendments to the proposed regulations. Section XV of the preamble ("Transition Relief and Interim Guidance") provides certain transition relief and interim guidance under section 4980H, and section XVI of the preamble provides information on the effective date for and reliance on these final regulations.

I. *Shared Responsibility for Employers (Section 4980H)*

A. *In general*

Section 4980H was added to the Code by section 1513 of the Patient Protection and Affordable Care Act, Public Law 111–148 (124 Stat. 119 (2010)), was amended by section 10106(e) and (f) of the Patient Protection and Affordable Care Act, was further amended by section 1003 of the Health Care and Education Reconciliation Act of 2010, Public Law 111–152 (124 Stat. 1029 (2010)), and was further amended by the Department of Defense and Full-Year Continuing Appropriations Act, 2011, Public Law 112–10 (125 Stat. 38 (2011)) (collectively, the Affordable Care Act). Section 1513(d) of the Affordable Care Act provides that section 4980H applies to months beginning after December 31, 2013; however, Notice 2013–45 (2013–31 IRB 116), issued on July 9, 2013, provides transition relief for 2014 with respect to section 4980H.

Section 4980H applies only to applicable large employers. An applicable large employer with respect to a calendar year is defined in section 4980H(c)(2) as an employer that employed an average of at least 50 full-time employees on business days during the preceding calendar year. For purposes of determining whether an employer is an applicable large employer, full-time equivalent employees (FTEs), as well as full-time employees, are taken into account. As set forth in section 4980H(c)(2)(E), the number of an employer's FTEs is determined based on the hours of service of employees who are not full-time employees. Under section 4980H(c)(2)(C), the determination of whether an employer that was not in existence in the preceding calendar year is an applicable large employer is based on the average number of employees that it is reasonably expected the employer will employ on business days in the current calendar year.

Section 4980H generally provides that an applicable large employer is subject to an assessable payment if either (1) the employer fails to offer to its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage (MEC) under an eligible employer-sponsored plan and any full-time employee is certified to the employer as having received an applicable premium tax credit or cost-sharing reduction (section 4980H(a) liability), or (2) the employer offers its full-time employees (and their dependents) the opportunity to enroll in MEC under an eligible employer-sponsored plan and one or more full-time employees is certified to the employer as having received an applicable premium tax credit or cost-sharing reduction (section 4980H(b) liability). Section 4980H(c)(4) provides that a full-time employee with respect to any month is an employee who is employed on average at least 30 hours of service per week.

An employer may be liable for an assessable payment under section 4980H(a) or (b) only if one or more full-time employees are certified to the employer as having received an applicable premium tax credit or cost-sharing reduction. The assessable payment under section 4980H(a) is equal to the number of all full-time employees (excluding 30 full-time employees) multiplied by one-twelfth of $2,000 for each calendar month, while the assessable payment under section 4980H(b) is based on the number of full-time employees who are certified to the employer as having received an applicable premium tax credit or cost-sharing reduction with respect to that employee's purchase of health insurance for the employee on an Affordable Insurance Exchange (Exchange[1]) multiplied by one-twelfth of $3,000 for each calendar

[1]An Exchange is also referred to in other published guidance as a Marketplace.

month. In no case, however, may the liability under section 4980H(b) exceed the maximum potential liability under section 4980H(a). Generally, liability under section 4980H(b) may arise because, with respect to a full-time employee who has been certified to the employer as having received an applicable premium tax credit or cost-sharing reduction[2], the coverage[3] offered by the employer is not affordable within the meaning of section 36B(c)(2)(C)(i) or does not provide minimum value (MV) within the meaning of section 36B(c)(2)(C)(ii). An employee's receipt of a premium tax credit under section 36B (premium tax credit) with respect to coverage for a dependent only will not result in liability for the employer under section 4980H.

B. *Previously issued guidance*

During 2011 and 2012, the Treasury Department and the IRS published four notices, each of which outlined potential approaches to future guidance under section 4980H and requested public comments: (1) Notice 2011–36 (2011–21 IRB 792) (addressed the definition of the terms *employer*, *employee*, and *hour of service* and requested comments on an approach to use an optional look-back measurement method for determining full-time employee status); (2) Notice 2011–73 (2011–40 IRB 474) (requested comments on a health coverage affordability safe harbor for employers under section 4980H using Form W-2 wages); (3) Notice 2012–17 (2012–9 IRB 430) (provided that the look-back measurement method and the Form W-2 affordability safe harbor will be incorporated into upcoming proposed regulations and requested comments on a potential approach for determining the full-time employee status of new employees under section 4980H); and (4) Notice 2012–58 (2012–41 IRB 436) (provided guidance and reliance on approaches for ongoing employees and new employees who are reasonably expected to be full-time employees and requested comments on a revised optional method for determining the full-time employee status for new employees with variable hours and new seasonal employees). Public comments were submitted in response to each of the four notices.

Taking into account all the comments received in response to this series of notices, on December 28, 2012, the Treasury Department and the IRS released a notice of proposed rulemaking (REG–138006–12, 78 FR 218). Written and electronic comments responding to the notice of proposed rulemaking were received. The comments are available for public inspection at www.regulations.gov or upon request. A public hearing was conducted on April 23, 2013. After consideration of all of the comments and testimony, the proposed regulations are adopted as amended by this Treasury decision. The amendments are discussed in this preamble.

After the issuance of the proposed regulations, on July 9, 2013, the Treasury Department and the IRS issued Notice 2013–45, which provides as transition relief that no assessable payments under section 4980H will apply for 2014. Notice 2013–45 also provides transition relief for 2014 for the section 6056 information reporting requirements for applicable large employers and the section 6055 information reporting requirements for providers of MEC.

The preamble to the proposed regulations provides transition relief that allows flexibility for individuals to make changes in salary reduction elections for accident and health plans provided through section 125 cafeteria plans for non-calendar cafeteria plan years beginning in 2013. The scope of this transition relief was clarified in section VI of Notice 2013–71 (2013–47 IRB 532), issued on October 31, 2013.

II. *Minimum Essential Coverage, Minimum Value and Affordability (Sections 5000A and 36B)*

MEC, MV and affordability are defined under Code provisions other than section 4980H, but all relate to the determination of liability under section 4980H, and accordingly are summarized briefly in this section of the preamble (but are more fully described in other cited guidance). Specifically, for purposes of section 4980H, an employer is not treated as having offered coverage to an employee unless the coverage is MEC. Moreover, under section 36B, an individual who is offered employer coverage but instead purchases coverage under a qualified health plan within the meaning of section 1301(a) of the Affordable Care Act on an Exchange may be eligible for a premium tax credit if the household income of the individual's family falls within certain thresholds and the coverage offered by the employer either does not provide MV or is not affordable. While an individual may purchase coverage under a qualified health plan on an Exchange without regard to whether the individual is eligible for a premium tax credit, an employer's potential liability under section 4980H is affected by the individual's purchase of coverage on an Exchange only if the individual receives a premium tax credit.

A. *Minimum essential coverage (MEC)*

MEC is defined in section 5000A(f) and the regulations under that section. Section 5000A(f)(1)(B) provides that MEC includes coverage under an eligible employer-sponsored plan. Under section 5000A(f)(2) and § 1.5000A–2(c)(1), an eligible employer-sponsored plan is, with respect to any employee, (1) group health insurance coverage offered by, or on behalf of, an employer to the employee that is either (a) a governmental plan within the meaning of section 2791(d)(8) of the Public Health Service Act (PHS Act) (42 U.S.C. 300gg–91(d)(8)), (b) any other plan or coverage offered in the small or large group market within a State, or (c) a grandfathered health plan, as defined in section 5000A(f)(1)(D), offered in a group market, or (2) a self-insured group health plan under which coverage is offered by, or on behalf of, an employer to the employee. Section 5000A(f)(3) and regulations thereunder provide that MEC does not include coverage consisting solely of excepted benefits described in section

[2] For simplicity, references in this preamble to full-time employees certified as having received a premium tax credit include full-time employees receiving the premium tax credit or the cost-sharing reduction because, in connection with Exchange coverage, only individuals who qualify for the premium tax credit can qualify for a cost-sharing reduction.

[3] For purposes of this preamble, the term "coverage" means MEC.

2791(c)(1), (c)(2), (c)(3), or (c)(4) of the PHS Act or regulations issued under these provisions. See § 1.5000A–2(g).

B. *Minimum value (MV)*

If the coverage offered by an employer fails to provide MV, an employee may be eligible to receive coverage in a qualified health plan supported by the premium tax credit. Under section 36B(c)(2)(C)(ii), a plan fails to provide MV if the plan's share of the total allowed costs of benefits provided under the plan is less than 60 percent of those costs.

Section 1302(d)(2)(C) of the Affordable Care Act provides that, in determining the percentage of the total allowed costs of benefits provided under a group health plan, the regulations promulgated by the Secretary of Health and Human Services (HHS) under section 1302(d)(2) of the Affordable Care Act apply. HHS published final regulations under section 1302(d)(2) of the Affordable Care Act on February 25, 2013 (78 FR 12834). On May 3, 2013, the Treasury Department and the IRS published a notice of proposed rulemaking (REG–125398–12, 78 FR 25909) that adopts the HHS rules and provides additional guidance on MV. The HHS regulations at 45 CFR 156.20 define the percentage of the total allowed costs of benefits provided under a group health plan as (1) the anticipated covered medical spending for essential health benefits (EHB) coverage (as defined in 45 CFR 156.110(a)) paid by a health plan for a standard population, (2) computed in accordance with the plan's cost sharing, and (3) divided by the total anticipated allowed charges for EHB coverage provided to the standard population. In addition, 45 CFR 156.145(c) provides that the standard population used to compute this percentage for MV (as developed by HHS for this purpose) reflects the population covered by typical self-insured group health plans. The HHS regulations describe several options for determining MV, including the MV Calculator (available at http://cciio.cms.gov/resources/regulations/index.html). Alternatively, a plan may determine MV through one of the safe harbors being established by HHS and the IRS. For plans with nonstandard features that are incompatible with the MV Calculator or a safe harbor, 45 CFR 156.145(a)(3) provides that the plan may determine MV through an actuarial certification from a member of the American Academy of Actuaries after the member performed an analysis in accordance with generally accepted actuarial principles and methodologies. Under proposed § 1.36B–6(f)(4), an actuary performing an actuarial certification for a plan with nonstandard features must use the MV Calculator to determine the plan's MV for plan coverage the MV calculator measures. The actuary adds to that MV percentage the result of the actuary's analysis of nonstandard features. Finally, 45 CFR 156.145(a)(4) provides that a plan in the small group market satisfies MV if it meets the requirements for any of the levels of metal coverage defined at 45 CFR 156.140(b) (bronze, silver, gold, or platinum).

C. *Affordability*

Under section 36B(c)(2)(B) and (C), an employee is not eligible for subsidized coverage for any month in which the employee is offered health coverage under an eligible employer-sponsored plan (as defined in section 5000A(f)(2)) that provides MV and that is affordable to the employee. Coverage for an employee under an eligible employer-sponsored plan is affordable if the employee's required contribution (within the meaning of section 5000A(e)(1)(B)) for self-only coverage does not exceed 9.5 percent of the taxpayer's household income for the taxable year. See section 36B(c)(2)(C)(i) and § 1.36B–1(e).

III. *Reporting Requirements for Applicable Large Employers (Section 6056)*

Section 6056, enacted by the Affordable Care Act, directs an applicable large employer to file a return with the IRS that reports, for each employee who was a full-time employee for one or more months during the calendar year, certain information described in section 6056(b) about the health care coverage the employer offered to that employee (or, if applicable, that the employer did not offer health care coverage to that employee). Section 6056 also requires applicable large employers to furnish, by January 31 of the calendar year following the calendar year for which the return must be filed, a related statement described in section 6056(c) to each full-time employee for whom information is required to be included on the return. On September 5, 2013, the Treasury Department and the IRS released a notice of proposed rulemaking (REG–136630–12, [78 FR 54996]) providing guidance under section 6056, including a description of and request for comments on certain simplified reporting methods under consideration by the Treasury Department and the IRS.

IV. *The 90-Day Limit on Waiting Periods (Public Health Service Act Section 2708)*

Section 2708 of the PHS Act[4] provides that, for plan years beginning on or after January 1, 2014, a group health plan or health insurance issuer offering group health insurance coverage may not apply any waiting period that exceeds 90 days. Section 2704(b)(4) of the PHS Act, section 701(b)(4) of ERISA, and section 9801(b)(4) define a waiting period to be the period that must pass with respect to an individual before the individual is eligible to be covered for benefits under the terms of the plan. Section 2708 of the PHS Act does not require the employer to offer coverage to any particular employee or class of employees, but prevents an otherwise eligible employee (or dependent) from waiting more than 90 days before coverage becomes effective.

Notice 2012–59 (2012–41 IRB 443), and parallel guidance issued by the Department of Labor (DOL) and HHS[5], provide temporary guidance on compliance

[4]The Affordable Care Act adds section 9815(a)(1) to the Code and section 715(a)(1) to the Employee Retirement Income Security Act (ERISA) to incorporate the provisions of part A of title XXVII of the PHS Act into the Code and ERISA, and to make them applicable to group health plans and health insurance issuers providing health insurance coverage in connection with group health plans. The PHS Act sections incorporated by these references are sections 2701 through 2728.

[5]See Department of Labor Technical Release 2012–02 and HHS FAQs issued August 31, 2012.

with section 2708 of the PHS Act and provide that this temporary guidance remains in effect at least through the end of 2014.

On March 21, 2013, the Treasury Department, DOL, and HHS (the Departments) issued a notice of proposed rulemaking (REG–122706–12, 78 FR 17313) providing guidance under section 2708 of the PHS Act. In the preamble to the proposed regulations under section 2708 of the PHS Act, the Departments state that, in their view, the proposed regulations are consistent with, and no more restrictive on employers than Notice 2012–59 (and the parallel guidance issued by DOL and HHS) and further state that the Departments will consider compliance with the proposed regulations as compliance with section 2708 of the PHS Act at least through the end of 2014.

Under the section 4980H final regulations, there are times when an employer will not be subject to an assessable payment with respect to an employee although the employer does not offer coverage to that employee during that time. However, the fact that an employer will not owe an assessable payment under section 4980H for failure to offer coverage during certain periods of time does not, by itself, constitute compliance with section 2708 of the PHS Act during that same period.[6]

Explanation and Summary of Comments

V. *Determination of Status as an Applicable Large Employer*

A. *In general*

Section 4980H applies only to employers that are applicable large employers. Section 4980H(c)(2)(A) provides that the term *applicable large employer* means, with respect to a calendar year, an employer that employed an average of at least 50 full-time employees on business days during the preceding calendar year. Section 4980H(c)(2)(E) provides that solely for purposes of determining whether an employer is an applicable large employer, an employer shall, in addition to the number of full-time employees for any month otherwise determined, include for such month a number of employees determined by dividing the aggregate number of hours of service of employees who are not full-time employees for the month by 120. For purposes of the proposed regulations and these final regulations, these additions to the number of full-time employees made solely for the determination of status as an applicable large employer are referred to as full-time equivalent employees (FTEs).

An applicable large employer may consist of multiple related entities (such as corporations) due to the application of the aggregation rules. Each such entity is referred to in this preamble and the final regulations as an *applicable large employer member*.

Commenters requested that the threshold for status as an applicable large employer be increased to various numbers of full-time employees (including FTEs) greater than 50. The final regulations do not adopt this suggestion as a permanent rule because it is inconsistent with the statutory definition of applicable large employer in section 4980H(c)(2). But see section XV.D.6 of this preamble for 2015 transition relief for certain applicable large employers with fewer than 100 full-time employees (including FTEs). Additional comments received on the definition of applicable large employer and modifications to the rules related to the determination of status as an applicable large employer contained in the proposed regulations are described in this section V of the preamble.

B. *Rules for employers not in existence in preceding year*

Section 4980H(c)(2)(C)(ii) provides that in the case of an employer that was not in existence throughout the preceding calendar year, the determination of whether such employer is an applicable large employer for the current calendar year is based on the average number of employees that it is reasonably expected such employer will employ on business days in the current calendar year.

The final regulations clarify that an employer is treated as not having been in existence throughout the prior calendar year only if the employer was not in existence on any business day in the prior calendar year. For example, if an employer comes into existence on May 1 of Year 1, during Year 1 the employer's status as an applicable large employer is determined based on the average number of employees that it is reasonably expected such employer will employ on business days in the current calendar year (Year 1). To determine the employer's status as an applicable large employer for Year 2, the employer's status as an applicable large employer is determined based on the number of employees that it employed on business days from May 1 through December 31 of Year 1 (rather than relying on the employer's reasonable expectations).

Commenters requested that an employer not in existence in the prior calendar year be granted a safe harbor under which an employer would not be an applicable large employer until a certain period of time has passed after the employer begins operations or until a certain period of time has passed after a new employer employs at least a specified number of full-time employees. One commenter opposed the adoption of a safe harbor that would delay the applicable large employer determination for new employers. The final regulations do not adopt such a safe harbor.

However, other aspects of section 4980H and the final regulations may address the concern raised by commenters that new employers will have difficulty establishing a group health plan in the first months of operation. In particular, under the final regulations, the determination of whether a new employer is an applicable large employer during its first calendar year is based on the employer's reasonable expectations at the time the business comes into existence, even if subsequent events cause the actual number of full-time employees (including FTEs) to ex-

[6]The Departments expect to issue final regulations in the near future with respect to section 2708 of the PHS Act. As stated in the proposed rules, the Departments will consider compliance with the proposed regulations under section 2708 of the PHS Act as compliance with section 2708 of the PHS Act through at least 2014 and, to the extent final regulations are more restrictive on plans and issuers, the final regulations will not be effective prior to January 1, 2015. 78 FR 17317 (March 21, 2013).

ceed that reasonable expectation. Section 54.4980H–2(b)(3). Also, for purposes of the liability calculation under section 4980H(a), with respect to a calendar month, the number of full-time employees of an applicable large employer member is reduced by that member's allocable share of 30. Section 54.4980H–4(e). This reduction could be particularly significant for a new employer with a number of full-time employees that does not exceed 30 by a large number for certain calendar months (and that for some calendar months may be below 30), circumstances which the Treasury Department and the IRS anticipate would characterize many new employers. Also, under the look-back measurement method if an employee is reasonably expected at his or her start date to be a full-time employee (and is not a seasonal employee) and is otherwise eligible for an offer of coverage, an employer that sponsors a group health plan that offers coverage to the employee by the first day of the calendar month immediately following the conclusion of the employee's initial three full calendar months of employment will not be subject to an assessable payment under section 4980H(a) (and section 4980H(b) if the coverage offered provides MV) for those three calendar months by reason of its failure to offer coverage to the employee for the initial three full calendar months of employment. Section 54.4980H–3(d)(2)(iii). See also § 54.4980H–3(c)(2) for a similar rule under the monthly measurement method that applies based on when an employee first becomes otherwise eligible for an offer of coverage. An employer is also not subject to an assessable payment under section 4980H with respect to an employee for the first calendar month of the employee's employment if the employee's start date is other than the first day of the calendar month. See § 54.4980H–4(c) and § 54.4980H–5(c).

C. *Seasonal workers*

Section 4980H(c)(2)(B) provides that an employer is not considered to employ more than 50 full-time employees if (1) the employer's workforce exceeds 50 full-time employees for 120 days or fewer during the calendar year, and (2) the employees in excess of 50 employed during such 120-day period are seasonal workers. For this purpose, the proposed regulations define the term *seasonal worker* as a worker who performs labor or services on a seasonal basis as defined by the Secretary of Labor, including (but not limited to) workers covered by 29 CFR 500.20(s)(1) and retail workers employed exclusively during holiday seasons. The proposed regulations further provide that employers may apply a reasonable, good faith interpretation of the term *seasonal worker* and a reasonable good faith interpretation of 29 CFR 500.20(s)(1) (including as applied by analogy to workers and employment positions not otherwise covered under 29 CFR 500.20(s)(1)).

Commenters requested that other employees with seasonal employment who are not excluded under the seasonal worker exception nonetheless be excluded for purposes of determining applicable large employer status. However, given the specific statutory reference to seasonal workers as part of a more limited exception, there is no statutory authority for such a broad exclusion. Accordingly, the final regulations adopt the provisions of the proposed regulations with certain clarifications in response to comments.

With respect to the reference to retail workers employed exclusively during the holiday seasons, commenters requested clarification of the specific events or periods of time that would be treated as holiday seasons. The final regulations do not indicate specific holidays or the length of any holiday season for this purpose, as these will differ for different employers. Retail workers employed exclusively during holiday seasons often are seasonal workers and therefore are generally excludible on that basis, if the employer otherwise meets the conditions of the seasonal worker exception.

The proposed regulations apply the seasonal worker exception set forth in section 4980H(c)(2) based on the prior calendar year. One commenter requested that the seasonal worker exception apply to new employers. The final regulations adopt this suggestion, so that in the case of an employer that was not in existence on any business day during the preceding calendar year, the seasonal worker exception applies so that the employer will not be treated as an applicable large employer if it reasonably expects (1) its workforce to exceed 50 full-time employees (including FTEs) for 120 days or fewer during the current calendar year, and (2) the employees in excess of 50 employed during such 120-day period to be seasonal workers.

D. *Application of employer aggregation rules to determination of status as an applicable large employer*

Section 4980H(c)(2)(C)(i) provides that, for purposes of determining whether an employer is an applicable large employer, all persons treated as a single employer under section 414(b), (c), (m) or (o) are treated as one employer. Comments were received both in favor of and opposed to this aggregation rule; however, the rule is explicitly set forth in the statute and is thus retained. While the final regulations therefore incorporate this rule, they also provide, consistent with the proposed regulations, that the determination of any potential assessable payment under section 4980H(a) or (b) is made separately for each entity (referred to as an applicable large employer member) that together with other entities is treated as the applicable large employer. For a discussion of the determination of any potential liability under section 4980H, see section X of this preamble.

The final regulations continue to reserve on the application of the employer aggregation rules under section 414(b), (c), (m) and (o) to government entities, as well as to churches or conventions or associations of churches (as defined in § 1.170A–9(b)). Until further guidance is issued, those entities may apply a reasonable, good faith interpretation of section 414(b), (c), (m) and (o) in determining their status as an applicable large employer.

E. *Predecessor employers*

Section 4980H(c)(2)(C)(iii) provides that, for purposes of determining whether an employer is an applicable large employer, any reference to an employer includes a reference to any predecessor of the employer. As with the proposed regulations, the final regulations reserve with respect to specific rules for identifying a predecessor employer (or the corresponding successor employer). The Treasury

Department and the IRS continue to consider development of rules for identifying a predecessor employer (or the corresponding successor employer), and until further guidance is issued, taxpayers may rely upon a reasonable, good faith interpretation of the statutory provision on predecessor (and successor) employers for purposes of the applicable large employer determination. For this purpose, use of the rules developed in the employment tax context for determining when wages paid by a predecessor employer may be considered as having been paid by the successor employer (see § 31.3121(a)(1)–1(b)) is deemed reasonable.

F. *Administrative period*

As set forth in section XV.D.3 of this preamble, the Treasury Department and the IRS have concluded that transition relief for the 2015 applicable large employer determination is appropriate because employers will be becoming familiar with the applicable large employer determination method and applying it for the first time with respect to 2014 (to determine their status for 2015).

In addition, commenters suggested that section 4980H should not apply to employers for a period of time after the end of the calendar year so that employers that are close to the 50 full-time employee (plus FTE) threshold, whose status may be affected by data from the final calendar months of the calendar year, have time to respond to becoming an applicable large employer. To address this concern, the final regulations provide, with respect to an employee who was not offered coverage at any point in the prior calendar year, that if the applicable large employer offers coverage on or before April 1 of the first year in which the employer is an applicable large employer, the employer will not be subject to an assessable payment (for January through March of the first year the employer is an applicable large employer) under section 4980H(a) by reason of its failure to offer coverage to the employee for January through March of that year, and the employer will not be subject to an assessable payment (for January through March of the first year the employer is an applicable large employer) under section 4980H(b) if the coverage offered provides MV. However, if the employer does not offer coverage to the employee by April 1, the employer may be subject to a section 4980H(a) assessable payment for those initial calendar months in addition to any subsequent calendar months for which coverage is not offered, and if the employer offers coverage by April 1 but the coverage does not provide MV, the employer may be subject to a section 4980H(b) assessable payment for those initial calendar months (in addition to any subsequent calendar months for which coverage does not provide MV or is not affordable). This rule applies only during the first year for which an employer is an applicable large employer (even if the employer falls below the 50 full-time employee plus FTE threshold for a subsequent year and then expands and becomes an applicable large employer again).

G. *Full-time equivalent employees*

Full-time equivalent employees are included in the applicable large employer determination. See § 54.4980H–2(c). A commenter suggested that the final regulations provide rounding rules for the monthly FTE calculation. The number of FTEs for each calendar month in the preceding calendar year is determined by calculating the aggregate number of hours of service for that calendar month for employees who were not full-time employees (but not more than 120 hours of service for any employee) and dividing that number by 120. The proposed regulations and these final regulations provide that in determining the number of FTEs for each calendar month, fractions are taken into account. In response to a request for a rounding rule, the final regulations provide, as an option, that an employer may round the resulting monthly FTE calculation to the nearest one hundredth. For example, an employer with a calculation of 30.544 FTEs for a calendar month may round that number to 30.54 FTEs.

H. *Application of employment break period rules and special unpaid leave rules to determination of applicable large employer status*

The proposed regulations and these final regulations provide a method for determining full-time employee status, referred to as the look-back measurement method, under which employers may determine the status of an employee as a full-time employee during a subsequent period (referred to as the stability period), based upon the hours of service of the employee in a prior period (referred to as the measurement period). See § 54.4980H–3(d). The proposed regulations and these final regulations also provide a method under which special unpaid leave and employment break periods during a measurement period are not treated as a period during which zero hours of service are credited when applying the look-back measurement method. See § 54.4980H–3(d)(6). Commenters suggested that these rules be extended to the applicable large employer determination calculation so that periods during which an employee experiences special unpaid leave or an employment break period would not be counted as periods of zero hours of service, as counting those periods in that manner brings down the average hours of service for the employee (which will reduce the full-time employee and FTE counts). Because the statute explicitly provides the method for determining applicable large employer status, including counting employees who do not average 30 hours of service per week, the final regulations do not adopt this suggestion.

VI. *Hours of Service*

The identification of an employer's full-time employees and FTEs for purposes of determining its status as an applicable large employer, and of an employer's full-time employees for purposes of determining any potential liability under section 4980H, is based on each employee's hours of service. The following section discusses the rules for determining an employee's hours of service.

The final regulations adopt the general definition of hours of service set forth in the proposed regulations. However, as discussed in sections VI.B and VI.C of this preamble, the final regulations include further rules to clarify or modify the application of the rules for crediting hours of service to address various situations raised in the comments.

A. *General definition of hours of service*

Section 4980H(c)(4)(B) provides that the Secretary of the Treasury, in consultation with the Secretary of Labor, will prescribe such regulations, rules and guidance as may be necessary to determine the hours of service of an employee, including rules for the application of section 4980H to employees who are not compensated on an hourly basis. In consultation with the Secretary of Labor, the Treasury Department and the IRS formulated rules set forth in the proposed regulations that generally were based on the definition of the term *hour of service* for purposes of the rules related to the crediting of hours of service under a qualified retirement plan (see 29 CFR 2530.200b–2(a)), with certain modifications.

Specifically, the proposed regulations define an *hour of service* to mean each hour for which an employee is paid, or entitled to payment, for the performance of duties for the employer, and each hour for which an employee is paid, or entitled to payment by the employer for a period of time during which no duties are performed due to vacation, holiday, illness, incapacity (including disability), layoff, jury duty, military duty or leave of absence (as defined in 29 CFR 2530.200b–2(a)).

For employees paid on an hourly basis, an employer is required to calculate actual hours of service from records of hours worked and hours for which payment is made or due. For employees paid on a non-hourly basis (such as salaried employees), an employer may calculate the actual hours of service using the same method as for hourly employees, or use a days-worked equivalency crediting the employee with eight hours of service for each day for which the employee would be required to be credited with at least one hour of service, or a weeks-worked equivalency whereby an employee would be credited with 40 hours of service for each week for which the employee would be required to be credited with at least one hour of service. The proposed regulations prohibit use of these equivalencies, however, in circumstances in which their use would result in a substantial understatement of an employee's hours of service in a manner that would cause that employee not to be treated as a full-time employee.

Comments were received on the days-worked and weeks-worked equivalency methods. Commenters requested that the number of hours of service credited under the equivalency methods be increased from eight hours per day or 40 hours per week to 10 hours per day or 45 hours per week, consistent with equivalency methods contained in regulations issued by DOL. See 29 CFR 2530.200b–3(e). The higher equivalency amounts under the DOL regulations are intended to provide an expansive standard for the number of hours an employee is credited with for purposes of eligibility, vesting and accrual of benefits in a pension plan. In the context of section 4980H, an equivalency of eight hours per day or 40 hours per week is more appropriate.

Commenters requested clarification of the circumstances under which an employee must be credited with service under the equivalency methods. Specifically, commenters asked whether an employee must have actually worked one hour of service in a day or week to be credited with eight or 40 hours of service respectively for that period. The equivalency methods contained in the proposed regulations provide that hours must be credited for any day or week in which the employee would otherwise be required to be credited with one hour of service if treated as an hourly employee. As described previously in this section VI.A, under the service crediting method applicable to hourly employees, an hourly employee must be credited with hours of service for certain hours in which no services are performed but with respect to which payment is made or owed by the employer (such as certain hours of paid leave). Accordingly, the equivalency methods do not require that an employee have actually worked an hour of service in a day or week to be credited with eight or 40 hours of service with respect to that day or week. This approach is the same as the equivalency rule for crediting hours of service under an employee pension benefit plan under DOL regulations at 29 CFR 2530.200b–3(e).

The preamble to the proposed regulations states that an employer may change the method of calculating non-hourly employees' hours of service for each calendar year. At one commenter's request, this rule has been added to the text of the final regulations. As set forth in the proposed and final regulations, an employer is not required to use the same method of calculating a non-hourly employee's hours of service for all non-hourly employees, and may apply different methods of calculating a non-hourly employee's hours of service for different categories of non-hourly employees, provided that the categories are reasonable and consistently applied. An employer may change the method of calculating a non-hourly employee's hours of service for one or more categories of non-hourly employees for each calendar year as well.

One commenter asked whether an employer is required to calculate hours of service using all three hours of service calculation methods provided for non-hourly employees (actual hours and two equivalencies), and if an employer is required to classify the employee as a full-time employee if the employee would have such status under any of the methods. The regulations indicate that the equivalency methods are optional, and that an employer choosing to use equivalencies may determine hours of service using one of the equivalency methods. Accordingly, employers are not required to use more than one method of determining hours of service for any particular employee.

Commenters requested that the equivalency methods be expanded to include employees who are compensated on an hourly basis. Because employers are required to maintain records of hours worked in the case of employees who are compensated on an hourly basis, and because use of the equivalency methods could in some cases understate or overstate the number of hours actually worked by such employees, the final regulations do not adopt this suggestion.

One commenter requested that the anti-abuse rule prohibiting the use of an equivalency method if the result is to substantially understate an employee's hours of service in a manner that would cause the employee not to be treated as a full-time employee be expanded to also prohibit the use of an equivalency method if the result is to understate hours of service for a substantial number of employees (even if no given employee's hours of service are understated substantially and even if the understatement would not cause the employee to not be treated as a full-time employee). This expanded rule could affect the calculation of FTEs as part of the applicable large employer determination. For example, if an employer had 100 non-hourly employees who each worked two days per week for 10 hours each day, the employer could not use the days-worked equivalency because that would result in 400 fewer hours of service being included in the FTE calculation for each week, even though the understatement would not affect the employees' treatment as full-time employees (because these employees are not full-time employees, regardless of the use of equivalencies). The final regulations adopt this suggestion.

B. *Exclusions from definition of hour of service*

Commenters requested that hours of service performed in certain capacities not be counted as an hour of service. The final regulations adopt the following changes in response to these comments.[7]

1. Volunteer Employees

Commenters requested that hours of service performed in the capacity of a volunteer for a government entity or tax-exempt organization not be counted as hours of service for purposes of section 4980H. Under the definition of hour of service outlined in these regulations, an hour of service is generally defined as an hour for which an employee is paid or entitled to payment. Accordingly, hours worked by a volunteer who does not receive (and is not entitled to receive) compensation in exchange for the performance of services are not treated as hours of service for purposes of section 4980H.

Commenters noted, however, that some volunteers receive compensation in the form of expense reimbursements, stipends, contributions to employee benefit plans, or nominal wages. Local governments, for instance, noted that many volunteer firefighters or other emergency responders are paid a salary or an hourly wage, generally at a rate lower than the rate paid to non-volunteers performing services in a similar capacity. Other volunteer firefighters or emergency responders may receive expense reimbursements or other fees each time they respond to a call. Commenters generally expressed concern that volunteer service would be discouraged if volunteer hours were required to be counted when determining whether the individual is a full-time employee for purposes of section 4980H.

In response to these concerns, the final regulations provide that hours of service do not include hours worked as a "bona fide volunteer." For this purpose, the definition of "bona fide volunteer" is generally based on the definition of that term for purposes of section 457(e)(11)(B)(i), which provides special rules for length of service awards offered to certain volunteer firefighters and emergency medical providers under a municipal deferred compensation plan. For purposes of section 4980H, however, bona fide volunteers are not limited to volunteer firefighters and emergency medical providers. Rather, bona fide volunteers include any volunteer who is an employee of a government entity or an organization described in section 501(c) that is exempt from taxation under section 501(a) whose only compensation from that entity or organization is in the form of (i) reimbursement for (or reasonable allowance for) reasonable expenses incurred in the performance of services by volunteers, or (ii) reasonable benefits (including length of service awards), and nominal fees, customarily paid by similar entities in connection with the performance of services by volunteers.

2. Student Employees

Commenters from educational organizations requested that special rules apply for determining the hours of service of employees who are also students of an educational organization. These comments generally fell into two categories. First, commenters expressed concern about the impact of section 4980H on federal work study programs under which a student receives financial aid in the form of a federally subsidized work assignment. Commenters posited that if educational organizations were required to aggregate hours of service performed by the student employee in the context of the work study program with hours of service performed by the student employee for the educational organization in other capacities (for example, a non-work study position with the campus bookstore) in determining whether the student is a full-time employee for purposes of section 4980H, it could discourage educational organizations from hiring students in other capacities in addition to their work study positions. Second, commenters requested that hours of service performed for an outside employer by students through an internship or externship program sponsored by an educational organization not be counted as hours of service for the outside employer for section 4980H purposes. The commenters suggested that, without such an exception, outside employers would be discouraged from offering internships or externships to students, which could have a detrimental impact on the educational system.

The federal work study program, as a federally subsidized financial aid program, is distinct from traditional employment in that its primary purpose is to advance education. See 34 CFR 675. To avoid having the application of section 4980H interfere with the attainment of that goal, the final regulations provide that hours of service for section 4980H purposes do not include hours of service performed by students in positions subsidized through the federal work study program or a substantially similar program of a State or political subdivision thereof. However, the final regulations do not include a general exception for student employees. All hours of service for which a student employee of an educational organization (or of an outside employer) is paid or entitled to payment in a capacity other than through the federal work study program (or a State or local government's equiva-

[7]Commenters also raised issues related to the application of the hour of service definition to certain categories of employees whose hours of service are particularly challenging to identify or track or for whom the final regulations' general rules for determining hours of service may present special difficulties. See section VI.C of this preamble.

lent) are required to be counted as hours of service for section 4980H purposes.

With respect to internships and externships, services by an intern or extern would not count as hours of service for section 4980H purposes under the general definition of hours of service contained in the regulations to the extent that the student does not receive, and is not entitled to, payment in connection with those hours. However, excluding hours of service for which interns or externs receive, or are entitled to receive, compensation from the employer from the definition of hours of service for section 4980H purposes would be subject to potential misuse through labeling positions as internships or externships to avoid application of section 4980H. The final regulations do not adopt a special rule for student employees working as interns or externs for an outside employer, and, therefore, the general rules apply, including the option to use the look-back measurement method, as appropriate, or the monthly measurement method.

3. Members of Religious Orders

A commenter requested clarification about whether members of religious orders must be treated as full-time employees of their orders for purposes of section 4980H. As noted in section VI.C of this preamble, the Treasury Department and the IRS continue to consider additional rules for the determination of hours of service for purposes of section 4980H with respect to certain categories of employees whose hours of service are particularly challenging to identify or track or for whom the final regulations' general rules for determining hours of service may present special difficulties, including hours worked by members of religious orders for the orders to which they belong. Until further guidance is issued, a religious order is permitted, for purposes of determining whether an employee is a full-time employee under section 4980H, to not count as an hour of service any work performed by an individual who is subject to a vow of poverty as a member of that order when the work is in the performance of tasks usually required (and to the extent usually required) of an active member of the order.

C. *Application of hours of service to certain employees*

Commenters requested guidance on the application of the hours of service definition to certain categories of employees whose hours of service are particularly challenging to identify or track or for whom the final regulations' general rules for determining hours of service may present special difficulties.

The Treasury Department and the IRS continue to consider additional rules for the determination of hours of service for purposes of section 4980H with respect to certain categories of employees (including adjunct faculty, commissioned salespeople, and airline employees), and certain categories of hours associated with work by employees (including layover hours (for example, for airline employees) and on-call hours). The regulation authorizes the promulgation of such rules through additional guidance, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b)).

Until further guidance is issued, employers of adjunct faculty, employers of employees with layover hours, including the airline industry, and employers of employees with on-call hours, as described in sections VI.C.1 through VI.C.3 of this preamble, respectively, are required to use a reasonable method of crediting hours of service that is consistent with section 4980H. Further, employers of other employees whose hours of service are particularly challenging to identify or track or for whom the final regulations' general rules for determining hours of service may present special difficulties, such as commissioned salespeople, are required to use a reasonable method of crediting hours of service that is consistent with section 4980H.

A method of crediting hours is not reasonable if it takes into account only a portion of an employee's hours of service with the effect of characterizing, as a non-full-time employee, an employee in a position that traditionally involves at least 30 hours of service per week. For example, it is not a reasonable method of crediting hours to fail to take into account travel time for a travelling salesperson compensated on a commission basis. Paragraphs C.1 through C.3 of this section VI of the preamble describe methods of crediting hours of service that are (or are not) reasonable to use with respect to adjunct faculty, layover hours, including for airline industry employees, and on-call hours. The examples of reasonable methods provided are not intended to constitute the only reasonable methods of crediting hours of service. Whether another method of crediting hours of service in these situations is reasonable is based on the relevant facts and circumstances.

1. Adjunct Faculty

Commenters raised issues relating to adjunct faculty who receive compensation for teaching a certain number of classes (or credits) and whose compensation is not based on the actual time spent on non-classroom activities such as class preparation, grading papers and exams, and counseling students. Comments from employers generally suggested that the hours of service equivalencies for non-hourly employees (eight hours per day or 40 hours per week) were too high for this purpose, but that counting actual hours would be administratively burdensome. These commenters suggested various methods for permitting assumptions for hours of service that would be applied for each task completed, for example, a set number of hours of service per week per class or credit taught by an adjunct faculty member. Comments from employees and their representatives included two very different types of suggestions. Some suggested that any assumption be set sufficiently high and be subject to robust periodic review so as not to fail to attribute adequate hours of service for the work performed. Others suggested that the assumption be set at a relatively moderate level that would avoid giving undue incentives for institutions to reduce adjunct faculty members' teaching assignments to avoid full-time employee status.

In addition, comments from adjunct faculty members and educational organizations requested the adoption of a method whereby an adjunct faculty member would be treated as a full-time employee for purposes of section 4980H only if the faculty member were assigned a course load that was equivalent to (or, as requested in some comments, at least 75 percent of) the average course load assigned to faculty members who are treated as full-time employees by the particular educational organization or academic department. The course loads assigned to other faculty members may be a relevant factor in an employer's determination of the number of hours of service to be credited to an adjunct faculty member. However, the course loads of faculty treated as full-time employees may vary considerably, making implementation of the proposed approach very difficult to administer.

Until further guidance is issued, employers of adjunct faculty (and of employees in other positions that raise analogous issues with respect to the crediting of hours of service) are required to use a reasonable method for crediting hours of service with respect to those employees that is consistent with section 4980H. With respect to adjunct faculty members of an educational organization who are compensated on the basis of the number of courses or credit hours assigned, the commenters noted that a wide variation of work patterns, duties, and circumstances apply in different institutions, academic disciplines, and departments, and apply to different courses and individuals, and that this might factor into the reasonableness of a particular method of crediting hours of service in particular circumstances.

Various commenters also suggested, however, that, in the interest of predictability and ease of administration in crediting hours of service for purposes of section 4980H, regulations specify a multiple that might be applied to credit additional hours of service for each credit hour or hour of classroom time assigned to the adjunct faculty member. Commenters suggested a number of possible multiples that might be used for this purpose. After reviewing these comments, the Treasury Department and the IRS have determined that, until further guidance is issued, one (but not the only) method that is reasonable for this purpose would credit an adjunct faculty member of an institution of higher education with (a) 2 1/4 hours of service (representing a combination of teaching or classroom time and time performing related tasks such as class preparation and grading of examinations or papers) per week for each hour of teaching or classroom time (in other words, in addition to crediting an hour of service for each hour teaching in the classroom, this method would credit an additional 1 1/4 hours for activities such as class preparation and grading) and, separately, (b) an hour of service per week for each additional hour outside of the classroom the faculty member spends performing duties he or she is required to perform (such as required office hours or required attendance at faculty meetings).

Although further guidance may be issued regarding these matters, the method described in the preceding paragraph may be relied upon at least through the end of 2015. To the extent any future guidance modifies an employer's ability to rely on that method, the period of reliance will not end earlier than January 1 of the calendar year beginning at least six months after the date of issuance of the guidance (but in no event earlier than January 1, 2016). This extended period of reliance is provided so that if the method described in the preceding paragraph is modified or replaced, employers will have sufficient time to make necessary adjustments. Of course, employers may credit more hours of service than would result under the method described in the preceding paragraph and also may offer coverage to additional employees beyond those identified as full-time employees under that method.

2. Layover Hours for Airline Industry Employees and Others

Commenters noted that pilots and flight attendants often are required, as a practical matter, to remain overnight between flights at a location other than their residence. The Treasury Department and the IRS continue to consider additional rules for the determination of hours of service, including layover hours, for purposes of section 4980H with respect to certain categories of employees whose hours of service are particularly challenging to identify or track or for whom the final regulations' general rules for determining hours of service may present special difficulties. Until further guidance is issued, with respect to categories of employees whose hours of service are particularly challenging to identify or track or for whom the final regulations' general rules for determining hours of service may present special difficulties, employers are required to use a reasonable method for crediting hours of service that is consistent with section 4980H.

With respect to layover hours, it is not reasonable for an employer to not credit a layover hour as an hour of service if the employee receives compensation for the layover hour beyond any compensation that the employee would have received without regard to the layover hour or if the layover hour is counted by the employer towards the required hours of service for the employee to earn his or her regular compensation. For example, if an employer requires that an employee perform services for 40 hours per week to earn full salary, and credits "layover hours" towards the 40 hours, then it would not be reasonable for the employer to fail to credit the layover hours as hours of service.

For layover hours for which an employee does not receive additional compensation and that are not counted by the employer towards required hours of service, it would be reasonable for an employer to credit an employee in the airline industry with 8 hours of service for each day on which an employee is required, as a practical matter, to stay away from home overnight for business purposes (that is, 8 hours each day (or 16 hours total) for the two days encompassing the overnight stay). The employee must be credited with the employee's actual hours of service for a day if crediting 8 hours of service substantially understates the employee's actual hours of service for the day (including layover hours for which an employee receives compensation or that are counted by the employer towards required hours of service). Other methods of counting hours of service may also be reasonable, depending on the relevant facts and circumstances.

3. On-call Hours

Commenters requested that "on-call" hours, for which an employee has been directed by the employer to remain available to work, not be treated as hours of service unless the employee is directed to perform services. The commenters noted that a variety of compensation structures may apply to on-call hours. In some cases, employees are paid a reduced hourly wage for on-call hours. In other cases, employees are not paid additional compensation for on-call hours but are required to remain on call periodically as a condition of employment.

The Treasury Department and the IRS continue to consider additional rules for determining hours of service for purposes of section 4980H with respect to certain work arrangements, including on-call hours, or categories of employees whose hours of service are particularly challenging to identify or track or for whom the final regulations' general rules for determining hours of service may present special difficulties. Until further guidance is issued, employers of employees who have on-call hours are required to use a reasonable method for crediting hours of service that is consistent with section 4980H. It is not reasonable for an employer to fail to credit an employee with an hour of service for any on-call hour for which payment is made or due by the employer, for which the employee is required to remain on-call on the employer's premises, or for which the employee's activities while remaining on-call are subject to substantial restrictions that prevent the employee from using the time effectively for the employee's own purposes.

VII. *Identification of Full-Time Employees*

A. *In general*

Section 4980H(c)(4) defines the term *full-time employee* to mean, with respect to any month, an employee who is employed on average at least 30 hours of service per week. The final regulations provide two methods for determining full-time employee status—the monthly measurement method (described in section VII.B of this preamble) and the look-back measurement method (described in section VII.C of this preamble).

The final regulations reiterate that the requirements for use of the look-back measurement method and the monthly measurement method prescribe minimum standards for the identification of full-time employees. Employers may always treat additional employees as eligible for coverage, or otherwise offer coverage more expansively than would be required to avoid an assessable payment under section 4980H, subject to compliance with any nondiscrimination or other applicable requirements.

1. Thirty-Hour Threshold

Commenters requested that the 30 hours of service per week threshold be increased as part of the final regulations, either generally or as applied with respect to certain positions or industries. Because the statute is explicit that the threshold for status as a full-time employee is an average of 30 hours of service per week, the final regulations do not adopt these suggestions.

Other commenters pointed to employees whose hours of service are restricted by federal or other law, arguing that in such cases a lower threshold should be applied to determine whether the employee is a full-time employee. In particular, airline pilots explained that federal aviation law restricts the number of hours that a pilot may fly, resulting in many pilots averaging fewer than 30 hours of service per week despite having what may be considered a full-time position within the standards of the industry. However, section 4980H contains no exceptions from the requirement that an employee average at least 30 hours of service per week to be a full-time employee. Accordingly, the 30 hours of service threshold is not adjusted for any particular industry or position of employment in the final regulations. However, see the discussion of the application of hours of service to certain employees at section VI.C of this preamble.

2. Monthly Equivalency

The proposed regulations provide that, for purposes of determining full-time employee status, 130 hours of service in a calendar month is treated as the monthly equivalent of at least 30 hours of service per week, provided that the employer applies this equivalency rule on a reasonable and consistent basis. This monthly standard takes into account that the average month consists of more than four weeks. Commenters suggested that the 130 hours of service monthly standard is not an appropriate proxy for 30 hours of service per week during certain shorter calendar months. However, the 130 hours of service monthly standard may also be lower than an average of 30 hours of service per week during other longer months of the calendar year (for example, the seven calendar months that consist of 31 days). Under the look-back measurement method in particular, any effect of this approximation will balance out over the calendar year (for example, over a 12-month measurement period, over two successive six-month measurement periods, or over four successive three-month measurement periods).

In developing the final regulations, the Treasury Department and the IRS considered whether the 130 hours of service monthly equivalency standard should apply to the monthly measurement method, described in section VII.B of this preamble, under which the determination of full-time employee status is based on each calendar month. A standard was considered that would prorate any additional days beyond the minimum 28 days in a calendar month, so that, for example, the months of January, March, May, July, August, October, and December would be treated as requiring 133 hours of service for full-time employee status (equal to 4 3/7 weeks multiplied by 30 hours of service per week). However, that standard would result in no less than three different monthly equivalencies (one for February, one for the four calendar months with 30 days, and one for the seven calendar months with 31 days). In addition, a calendar month may start on any day of the week, and there is no standard workweek for all employees so that some employees may, for example, perform services on weekends or for longer or varying shifts rather than set hours Monday through Friday. For these reasons, different standards for each calendar month would not only be an additional burden for employers, but also do little to address the variation in treatment that may occur, for example, between an employee generally performing hours of service on the weekend and an employee performing services on business days, solely due to the day of the week upon which a calendar month begins. Accordingly, the final regulations adopt a standard of 130 hours of service per calendar month for determining whether an employee is a full-time employee under both the look-back measurement method and the monthly measurement method. The 130 hours of service standard is equal to 30 hours of service per week multiplied by 52 weeks and divided by 12 calendar months.

3. Aggregation of Hours of Service Across Applicable Large Employer Members

The proposed regulations provide that, for purposes of identifying a full-time employee, hours of service must be counted across all applicable large employer members. For example, an employee who for a calendar month averaged 25 hours of service per week at one applicable large employer member and 15 hours of service per week at another applicable large employer member of the same applicable large employer would be a full-time employee for that calendar month.

Commenters requested that an employee's status as a full-time employee be determined separately for each applicable large employer member based upon the employee's hours of service at each particular applicable large employer member. The final regulations do not adopt such a rule because it would often produce inequitable results by classifying an employee performing at least 30 hours of service per week for closely related applicable large employer members (for example, two corporations that are wholly-owned by another entity or individual) as not a full-time employee while classifying other employees working the same number of hours of service for one of those entities as full-time employees. For a discussion of how any assessable payment under section 4980H for a calendar month would be allocated among applicable large employer members if a full-time employee performed services for two or more applicable large employer members during the same calendar month, see section X of this preamble. For a discussion of how one applicable large employer member's offer of coverage applies to other applicable large employer members in the same applicable large employer, see section IX of this preamble.

B. *Monthly measurement method*

Commenters requested further information about the identification of full-time employees by employers electing not to use the look-back measurement method. Pursuant to the statute, these full-time employees would be identified based on the hours of service for each calendar month; accordingly, these regulations refer to this method of identifying full-time employees as the monthly measurement method.

Under the look-back measurement method set forth in the proposed regulations, if an employee is reasonably expected at his or her start date to be a full-time employee, an employer that sponsors a group health plan that offers coverage to the employee at or before the conclusion of the employee's initial three full calendar months of employment will not be subject to an assessable payment under section 4980H by reason of its failure to offer coverage to the employee for up to the initial three full calendar months of employment. See section VII.D of this preamble for a discussion of clarifications made to this rule in the final regulations. In developing the final regulations, the Treasury Department and the IRS considered whether a similar rule should be provided under the monthly measurement method.

Under the monthly measurement method in the final regulations, an employer will not be subject to an assessable payment under section 4980H(a) with respect to an employee because of a failure to offer coverage to that employee before the end of the period of three full calendar months beginning with the first full calendar month in which the employee is otherwise eligible for an offer of coverage under a group health plan of the employer if the employee is offered coverage no later than the day after the end of that three-month period. If the coverage for which the employee is otherwise eligible provides MV, the employer also will not be subject to an assessable payment under section 4980H(b) during that three-month period. For this purpose, an employee is otherwise eligible for an offer of coverage in a month if the employee meets all conditions to be offered coverage under the plan other than the completion of a waiting period, within the meaning of § 54.9801–2.[8] This rule applies only once per period of employment of an employee and applies with respect to each of the three full calendar months for which the employee is otherwise eligible for an offer of coverage under a group health plan of the employer. Accordingly, the relief may be available even if the employee terminates before that date (and before coverage is offered).

To avoid inequitable application of the rule that applies to employees who are first otherwise eligible for an offer of coverage by characterizing former employees as rehired employees after a short period of absence, the final regulations clarify that under the monthly measurement method, an employee must be treated as a continuing employee, rather than a new hire, unless the employee has had a period of at least 13 weeks during which no hours of service were credited (26 weeks for an employee of an employer that is an educational organization). At the employer's option, the employee may be treated as a new hire if the employee is not credited with any hours of service during a period that is both at least four consecutive weeks' duration and longer than the employee's immediately preceding period of employment. For a description of the rehire rules, see section VII.E of this preamble.

In determining how an employer should treat periods during which an employee is not credited with hours of service, the final regulations clarify that under the monthly measurement method, the special unpaid leave and employment break period rules do not apply. That is because determinations under the monthly measurement method are based on hours of service during that particular calendar

[8]Section 54.9801–2 provides definitions for terms used in chapter 100 of the Code (sections 9801 through 9834). Currently the definition of the term *waiting period* at § 54.9801–2 contains a cross reference to the definition of the term *waiting period* at § 54.9801–3(a)(3)(iii). Proposed regulations published March 21, 2013, 78 FR 17313, would amend that cross reference to refer to § 54.9815–2708(b) and to remove the definition at § 54.9801–3(a)(3)(iii), and would add § 54.9815–2708 which would include a definition of the term *waiting period* at § 54.9815–2708(b). Thus, § 54.9801–2 provides the relevant definition of the term *waiting period*, and will continue to provide the relevant definition if revised as proposed.

month and are not based on averaging over a prior measurement period. For a description of the special unpaid leave and employment break period rules see section VII.E.2 of this preamble.

Commenters requested that the monthly measurement method be applied in a manner that approximated or otherwise took into account payroll periods. To provide additional flexibility and reduce administrative burden on employers, the final regulations allow an employer to determine an employee's full-time employee status for a calendar month under the monthly measurement method based on the hours of service over successive one-week periods. Under this optional method, referred to as the weekly rule, full-time employee status for certain calendar months is based on hours of service over four-week periods and for certain other calendar months on hours of service over five-week periods. In general, the period measured for the month must contain either the week that includes the first day of the month or the week that includes the last day of the month, but not both. For this purpose, week means any period of seven consecutive calendar days applied consistently by the applicable large employer member for each calendar month of the year. For calendar months calculated using four week periods, an employee with at least 120 hours of service is a full-time employee, and for calendar months calculated using five week periods, an employee with at least 150 hours of service is a full-time employee. However, for purposes of coordination with both the premium tax credit and the section 5000A individual shared responsibility provisions, which are applied on a calendar month basis, an applicable large employer member is only treated as having offered coverage under section 4980H for a calendar month if it offers coverage to a full-time employee for the entire calendar month, regardless of whether the employer uses the weekly rule.

C. *Look-back measurement method*

1. In General

The proposed regulations provide a method, referred to as the look-back measurement method, under which employers may determine the status of an employee as a full-time employee during a future period (referred to as the stability period), based upon the hours of service of the employee in a prior period (referred to as the measurement period). The look-back measurement method for identifying full-time employees is available only for purposes of determining and computing liability under section 4980H and not for purposes of determining status as an applicable large employer.

Under the look-back measurement method for ongoing employees, an applicable large employer member determines each ongoing employee's full-time employee status by looking back at a standard measurement period of at least three months but not more than 12 months, as determined by the employer. The applicable large employer member determines the months in which the standard measurement period starts and ends, provided that the determination must be made on a uniform and consistent basis for all employees in the same category. If the applicable large employer member determines that an employee was employed on average at least 30 hours of service per week during the standard measurement period, then the applicable large employer member treats the employee as a full-time employee during a subsequent stability period, regardless of the employee's number of hours of service during the stability period, so long as the worker remains an employee.

The proposed regulations also provide look-back measurement method rules for new employees, including rules for employees who are reasonably expected to be full-time employees at the start date, and those who are variable hour employees or seasonal employees. A variable hour employee or seasonal employee will have his or her status as a full-time employee determined after an initial measurement period. The proposed regulations then provide transition guidance under which a new employee transitions into having his or her status as a full-time employee determined under the look-back measurement method rules applicable to ongoing employees.

Although some commenters suggested that the look-back measurement method of identifying full-time employees be eliminated, other commenters requested that it be retained. The look-back measurement method is intended as a method of crediting employees with hours of service they earn (during a measurement period) while also providing employers predictability in being able to identify full-time employees before the beginning of a potential coverage period (during a stability period). After reviewing the comments, the Treasury Department and the IRS have concluded that this method provides a practical and fair method for determining average hours of service that will facilitate compliance with section 4980H. Accordingly, the final regulations continue to permit a look-back measurement method as an optional method for identifying full-time employees.

2. Reasonable Expectations with Respect to a New Employee

Under both the proposed regulations and the final regulations, the application of the look-back measurement method to a new employee depends on the employer's reasonable expectations with respect to the status of the new employee at his or her start date. Under the final regulations, if a new employee who is reasonably expected to be a full-time employee at his or her start date is offered coverage by the first day of the month immediately following the conclusion of the employee's initial three full calendar months of employment (and if the employee was otherwise eligible for an offer of coverage during those three months), the employer is not subject to a section 4980H assessable payment for those initial three full calendar months of employment (or for the period prior to the initial three full calendar months of employment), provided that to avoid liability under section 4980H(b) for the initial three full calendar months, the coverage offered after the initial three full calendar months of employment must provide MV. Otherwise, with respect to a new employee who is reasonably expected to be a full-time employee at his or her start date, the employer may be subject to a section 4980H assessable payment beginning with the first full calendar month in which an employee is a full-time employee.

Commenters requested further guidance on the circumstances under which an employer may reasonably expect a new hire to be a full-time employee. In response to these comments, the final regulations provide that whether an employer's determination that a new hire is not a full-time employee (or is a full-time employee) is reasonable is based on the facts and circumstances. Factors to consider include, but are not limited to, whether the employee is replacing an employee who was or was not a full-time employee, the extent to which employees in the same or comparable positions are or are not full-time employees, and whether the job was advertised, or otherwise communicated to the new hire or otherwise documented (for example, through a contract or job description), as requiring hours of service that would average 30 (or more) hours of service per week or less than 30 hours of service per week.

Commenters also requested that employers that are educational organizations be prohibited from taking potential employment break periods into account in determining their expectations of future hours of service. For a description of the employment break period rule, see section VII.E.2 of this preamble. The final regulations clarify that educational organization employers cannot take into account the potential for, or likelihood of, an employment break period in determining their expectations of future hours of service.

3. Administrative Period

Under the proposed and final regulations, an applicable large employer member using the look-back measurement method may, at its option, elect to add an administrative period of no longer than 90 days between the measurement period and the stability period. Under the proposed regulations, the term *administrative period* is defined as an optional period, selected by an applicable large employer member, of no longer than 90 days beginning immediately following the end of a measurement period and ending immediately before the start of the associated stability period. However, the proposed regulations also provide that the period between a variable hour or seasonal employee's start date and the beginning of the initial measurement period must be taken into account in determining the administrative period. The definition of administrative period in the final regulations is revised to reflect that it also includes periods before the initial measurement period. Thus, the combined length of the period before the start of the initial measurement period and the period beginning immediately after the end of the initial measurement period and ending immediately before the beginning of the associated stability period is subject to an overall limit of 90 days.

Commenters requested that the maximum permissible administrative period be extended from 90 days to three full calendar months. The proposed regulations regarding the administrative period in these circumstances were intended to allow employers to structure their plans to coordinate with section 2708 of the PHS Act (relating to the application of the 90-day limitation on waiting periods) in all circumstances. For this reason, the final regulations do not adopt this suggestion.

4. Rules for Full-Time Employee's Stability Periods that are Longer than the Associated Measurement Periods

In general, under the proposed regulations, the minimum length of a measurement period is three months but the minimum length of a stability period for an employee who is a full-time employee based on hours of service in a measurement period is six months. Commenters requested that a three-month stability period be permitted if the employer uses a three-month measurement period and the employee is determined to be a full-time employee during the measurement period. The Treasury Department and the IRS remain concerned that permitting stability periods as short as three months for employees who are full-time employees based on hours of service in the measurement period could lead to employees moving in and out of employer coverage (and potentially Exchange coverage) multiple times during the year, which would be undesirable from both the employee's and employer's perspective, and could also create administrative challenges for the Exchanges. Accordingly, this suggestion is not adopted.

Commenters also asked for clarification of the measurement period that may be used for the subsequent six-month stability period in cases in which a less-than-six month measurement period is used (such as a three-month measurement period) and the employee averages at least 30 hours of service per week during the measurement period, so that a stability period of at least six months must be applied. The final regulations clarify that the stability period refers to the period immediately following the measurement period and any associated administrative period. Therefore, for employees who average at least 30 hours of service per week during a measurement period, who thus must be treated as full-time employees during an associated six-month stability period, the next measurement period begins at a date during the stability period that is the latest date that will not result in any period between the end of that stability period and the beginning of the next stability period associated with the next measurement period. For example, suppose an employer uses a three-month measurement period consisting of January through March of Year 1, followed by a one month administrative period consisting of April of Year 1. In this example, employees who average 30 hours of service per week during the measurement period consisting of January through March of Year 1 must be treated as full-time employees during a six-month stability period consisting of May through October of Year 1. Under the final regulations, the next measurement period would be July through September of Year 1, the associated administrative period would be October of Year 1, and the next associated stability period would begin immediately at the end of the administrative period. Thus, the stability period for employees determined to be full-time employees during the measurement period consisting of July through September of Year 1 would consist of November of Year 1 through April of Year 2 and there would be no period between the end of the first stability period (October 31 of Year 1) and the beginning of the next stability period (November 1 of Year 1). For ongoing employees that do not average at least 30 hours of service per week during a measurement period, the length of the stability period cannot exceed the length of the measurement period.

5. Employee Categories to which Different Measurement and Stability Periods may be Applied

The proposed regulations permit an employer to use measurement periods and stability periods that differ either in length or in their starting and ending dates for different categories of employees specified in the regulations, provided that the employees within each category are treated consistently. The categories specified in the proposed regulations are salaried employees and hourly employees, employees whose primary places of employment are in different states, collectively bargained employees and non-collectively bargained employees, and each group of collectively bargained employees covered by a separate collective bargaining arrangement. Commenters requested that these categories be expanded to, for example, any category established in good faith and consistent with business practices, any category of hourly employees based on payroll classifications, any category of employees of employers in an industry that demonstrates higher turnover than other industries, and any category of employees with turnover that is higher than other categories. The final regulations do not adopt these requests because of the associated administrative difficulties.

Notice 2012–58 had also included employees of different entities as a separate category of employees. The preamble to the proposed regulations provides that because section 4980H generally is applied on an applicable large employer member-by-member basis, including the method of identifying full-time employees, there is no need for a distinct category for employees of different entities, as each such member is a separate entity. However, comments to the proposed regulations requested that the final regulations confirm that different applicable large employer members may use different starting and ending dates and lengths of measurement and stability periods. In response, the final regulations include this confirmation as well as confirmation that different applicable large employer members may use different measurement methods (the look-back measurement method or the monthly measurement method).

6. Variable Hour Employees

As described in the preamble to the proposed regulations, with respect to certain positions of employment, employers have indicated that they could not determine at the start date whether the employee would be a full-time employee because an employee's hours of service in that position may vary significantly. Particularly in the hospitality and retail industries, employers requested that they be permitted to determine full-time employee status for employees whose hours may vary significantly by first considering hours of service for a period of time after the start date. In response to these comments made to the notices published before the proposed regulations, the proposed regulations generally provide that with respect to these employees, referred to as variable hour employees, an employer could use an initial measurement period, in combination with any administrative period, that did not extend beyond the last day of the first calendar month beginning on or after the first anniversary of the employee's start date. The proposed regulations treat an employee as a variable hour employee if, based on the facts and circumstances at the employee's start date, the applicable large employer member cannot determine whether the employee is reasonably expected to be employed on average at least 30 hours of service per week during the initial measurement period because the employee's hours of service are variable or otherwise uncertain. For this purpose, the applicable large employer member may not take into account the likelihood that the employee may terminate employment with the applicable large employer (including any member of the applicable large employer) before the end of the initial measurement period. See proposed § 54.4980H–1(a)(43).

Commenters, generally representing employee organizations, suggested that the treatment provided to variable hour employees be removed. In general, these commenters suggested that employers would categorize an excessive number of employees as variable hour employees in order to take advantage of the ability to avoid section 4980H liability while not offering coverage during the first year of employment. These final regulations retain the treatment of variable hour employees because with respect to certain positions of employment involving variable hours, it is not reasonable to require that an employer assume what those hours will be. In response to the comments, however, the final regulations explicitly set forth certain factors to take into account in determining whether the employer, at the employee's start date, could not determine whether the employee was reasonably expected to be employed on average at least 30 hours of service per week during the initial measurement period. These factors are described in section VII.C.2 of this preamble and are set forth at § 54.4980H–1(a)(49).

7. Temporary Staffing Firms

The preamble to the proposed regulations notes that the application of section 4980H may be particularly challenging for temporary staffing firms and requested comments on certain specific areas relevant to temporary staffing firms, including whether new employees of a temporary staffing firm should be deemed or presumed to be variable hour employees for purposes of the look-back measurement method as well as whether special rules should apply to temporary staffing firms for purposes of determining when an employee has separated from service and the application of the rehire rules when an employee returns after a break in service. See section VII.E of the preamble for a discussion of the rehire rules.

Some commenters requested that new employees of a temporary staffing firm be deemed, or alternatively presumed, to be variable hour employees rather than full-time employees for purposes of the look-back measurement method. Other commenters opposed the use of any presumption that employees of temporary staffing firms are variable hour employees, arguing that some of these employees will work predictable schedules averaging at least 30 hours of service per week. Temporary staffing firms vary widely in the types of assignments they fill for their clients and in the anticipated assignments that a new employee will be offered. Accordingly, the final regulations do not adopt a generally applicable presumption.

To accommodate these variations and provide additional guidance, the final regulations set forth additional factors relevant to the determination of whether a new employee of a temporary staffing firm intended to be placed on temporary assignments at client organizations is a variable hour employee. These factors generally relate to the typical experience of an employee in the position with the temporary staffing firm that hires the new employee (assuming the temporary staffing firm employer has no reason to anticipate that the new employee's experience will differ) and include whether employees in the same position with the temporary staffing firm retain as part of their continuing employment the right to reject temporary placements that the employer temporary staffing firm offers the employee, whether employees in the same position with the temporary staffing firm typically have periods during which no offer of temporary placement is made, whether employees in the same position with the temporary staffing firm typically are offered temporary placements for differing periods of time, and whether employees in the same position with the temporary staffing firm typically are offered temporary placements that do not extend beyond 13 weeks. As demonstrated in the modified and additional examples related to temporary staffing firms, no factor is determinative. In addition, the determination of whether an employee is a variable hour employee is made on the basis of the temporary staffing firm's reasonable expectations at the start date. An employee may accordingly be classified as a variable hour employee if this categorization was appropriate based on the employer's reasonable expectations at the start date, even if the employee in fact averages 30 or more hours of service per week over the initial measurement period.

Commenters suggested that the rehire rules should be adjusted for employees of temporary staffing firms by reducing the length of the break in service required before an employee can be treated as a new hire from 26 weeks to 4 weeks or some other duration. The final regulations do not adopt this suggestion in part because the adoption of such a rule may encourage employers to use temporary staffing firms to provide firm employees to perform certain services in order to attempt to improperly avoid offering coverage or incurring liability for assessable payments under section 4980H. For a discussion of the reduction of the break-in-service period under the rehire rules from 26 weeks to 13 weeks for all employers that are not educational organizations see section VII.E of this preamble.

Commenters requested additional guidance on when a temporary staffing firm may treat an employee who is not working on assignments as having separated from service with the firm. Separation from service is relevant in a number of contexts beyond section 4980H, such as eligibility to receive a distribution from a qualified plan (see, for example, section 401(k)(2)(B)(i)(l)) and the requirement to provide a notice of continuation coverage under COBRA (see section 4980B), and temporary staffing firm employers generally have developed various means of determining when an employee has separated from service with the firm for these purposes. Accordingly, until further guidance is issued, temporary staffing firms, like all employers generally, may determine when an employee has separated from service by considering all available facts and circumstances and by using a reasonable method that is consistent with the employer's general practices for other purposes, such as the qualified plan rules, COBRA, and applicable State law. For a discussion of the rehire rules that apply under section 4980H, see section VII.E of this preamble.

Section II.D.3 of the preamble to the proposed regulations addresses two arrangements under which a client employer may use a temporary staffing firm to attempt to evade application of section 4980H. In one arrangement, the client employer purports to employ an employee for only part of a week, such as 20 hours, and to hire that same individual through a temporary staffing firm for the remaining hours of the week, and then claim that the individual was not a full-time employee of either the client employer or the temporary staffing firm. In the other arrangement, one temporary staffing firm purports to supply a client an individual as a worker for only part of a week, such as 20 hours, while a second temporary staffing firm purports to supply the same client the same individual for the remainder of the week, and then claim that the individual was not a full-time employee of the client or either of the temporary staffing firms. For these reasons and the reasons set forth in section II.D.3 of the preamble to the proposed regulations, the Treasury Department and the IRS continue to be concerned about these arrangements and anticipate that future guidance of general applicability, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b)), will address them.

8. Seasonal Employees

Under the proposed and final regulations, the look-back measurement method, including the use of the initial measurement period for a newly hired employee, may be applied by an employer to its seasonal employees in the same manner in which the rules apply to variable hour employees. The proposed regulations do not provide a definition of the term *seasonal employee* but rather reserve on the issue. Section II.C.2.b of the preamble to the proposed regulations indicates that employers are permitted through 2014 to use a reasonable, good faith interpretation of the term *seasonal employee* for purposes of section 4980H. The preamble further states that the Treasury Department and the IRS contemplated that the final regulations would add to the definition of seasonal employee a specific time limit in the form of a defined period, citing the final sentence of § 1.105–11(c)(2)(iii)(C) as an example that could be adapted for purposes of section 4980H. The Treasury Department and the IRS specifically requested comments on this approach.

Commenters generally supported the proposed treatment of seasonal employees, but had varying notions of the appropriate time limit for a recurring period of service for a seasonal employee, ranging from 45 days to ten months. Consistent with the proposed regulations, the final regulations continue to provide for seasonal employees to be treated under the same rules applicable to variable hour employees. For this purpose, the final regulations provide that a seasonal employee means an employee in a position for which the customary annual employment is six months or less. The reference to customary means that by the nature of the position an employee in this position typically works for a period of six months or less, and that period should begin each calendar year in approximately the same part of the year, such as summer or winter. In certain unusual instances, the employee can still be considered a seasonal employee even if the seasonal employment is extended in a particular year beyond its customary duration (regardless of whether the customary duration is six months or is less than six months). For example, if ski instructors at a resort have a customary period of annual employment of six months, but are asked in a particular year to work an additional month because of an unusually long or heavy snow season, they would still be considered seasonal employees.

An employee in a seasonal position might be promoted or transferred to a permanent position. For example, a ski instructor might be moved to the position of grounds manager, which is anticipated to work year round. Under the final regulations, in general, if a seasonal employee experiences a change in employment status before the end of the initial measurement period in such a way that, if the employee had begun employment in the new position or status, the employee would not have been a seasonal employee (and would have reasonably been expected to be employed on average at least 30 hours of service per week), the employer has until the first day of the fourth month following the change in employment status, or, if earlier, the first day of the first month following the end of the initial measurement period (plus any applicable administrative period) if the employee averaged 30 hours of service per week or more during the initial measurement period, to treat the employee as a full-time employee.

9. Modification of Measurement Periods or Stability Periods to Consolidate Coverage Entry Dates

Commenters requested that the initial measurement period be modified to account for plan designs that consolidate employees into particular entry dates, such as the first day of a pay period, the first day of the month, etc. Specifically these commenters requested that the initial measurement period be permitted to begin on the employee's start date in a period, such as a calendar quarter, but end on a common date, such as 12 months after the beginning of the calendar quarter, and employers be allowed to couple this approach with a uniform stability period. This proposed structure would often result in a stability period significantly longer than the associated measurement period. In this example, all employees starting during the calendar quarter would have a 12 month stability period, whether they started in the first month of the quarter or the last month of the quarter. With respect to an employee who does not have sufficient hours of service to be classified as a full-time employee, the Treasury Department and the IRS have consistently stated that it is not appropriate to apply that status for a longer period than the measurement period. In addition, the proposed approach would add considerable complexity to the rules governing the look-back measurement method. However, consistent with the proposed regulations, the final regulations provide that the initial measurement period for a new variable hour employee or new seasonal employee may begin on the employee's start date or any date after that up to and including the first day of the first calendar month following the employee's start date (or, if later, as of the first day of the first payroll period beginning on or after the employee's start date). Effectively, this allows employers to group new hires into 12 groups throughout the year for purposes of determining the initial measurement period. For these reasons, the final regulations retain the rule in the proposed regulations and do not adopt the commenters' suggestion.

10. Change in Employment Status

The proposed regulations for the look-back measurement method contain a change in employment status rule for a variable hour or seasonal employee who experiences a change in employment status during the initial measurement period such that, if the employee had begun employment in the new position or status, the employee would have reasonably been expected to be employed on average at least 30 hours of service per week. With respect to such an employee, in general, the employer will not be subject to an assessable payment for such an employee until the first day of the fourth full calendar month following the change in employment status if the employer provides coverage at the end of that period (and to avoid liability under section 4980H(b) the coverage provides MV) or, if earlier and the employee is a full-time employee based on the initial measurement period, the first day of the first month following the end of the initial measurement period (including any optional administrative period associated with the initial measurement period). Under the final regulations, this rule is revised to also apply to an employee who has a change in employment status from part-time employee to full-time employee during the initial measurement period. For a description of the requirement that the employee be otherwise eligible for an offer of coverage during the period described in this paragraph, see section VII.D of this preamble.

Commenters to the proposed regulations requested additional rules for how the look-back measurement method applies when an employee experiences various changes in employment status. As described in this section VII.C.10 of the preamble, the final regulations revise the change in employment status rule that applies during the initial measurement period for new employees who experience a change in employment status resulting in full-time employee status. The final regulations also provide a special rule, discussed in section VII.G of this preamble, that applies when an employee experiences a change in employment status from full-time employee status to part-time employee status; the employer is allowed to apply the monthly measurement method to such an employee within three months of the change if the employee actually averages less than 30 hours of service per week for each of the three months following the change in employment status and if the employer has offered the employee continuous coverage that provides MV from at least the fourth month of the employee's employment. Otherwise, under the look-back measurement method, full-time employee status in a stability period is based on hours of service in the prior applicable measurement period, regardless of whether the employee experiences a change in employment status either during the measurement period or during the stability period. Under the look-back measurement method, each employee's hours of service are measured (not just variable hour employees and seasonal employees) during the measurement period. In general, under the look-back measurement method, if the change in employment status results in a change in hours of service, that change is captured in a subsequent stability period. For a description of the rules regarding the use of the look-back measurement method for only some of an employer's employees, see section VII.G of this preamble.

11. New Employees who are Neither Variable Hour Employees nor Seasonal Employees

Under the proposed and final regulations, an ongoing employee is an employee who has been employed by an applicable large employer member for at least one complete standard measurement period. The proposed regulations provide rules for application of the look-back measurement method to new employees who are variable hour employees and seasonal employees but the proposed rules do not fully explain how full-time employee status is determined for other new employees. The final regulations clarify how an applicable large employer member determines full-time employee status of its new employees who are not variable hour employees or seasonal employees, for the period before the rules for ongoing employees apply (that is, for the period before the employee has been employed for a complete standard measurement period).

In general, before becoming an ongoing employee, full-time employee status for a new employee who is reasonably expected at the employee's start date to be a full-time employee (and who is not a seasonal employee) is based on that employee's hours of service each calendar month (but note that an employer will not be subject to a section 4980H(a) assessable payment for the initial three full months of employment if the employee is otherwise eligible for an offer of coverage during those three months and is offered coverage by the first day following those three months (and the employer will not be subject to a section 4980H(b) assessable payment for those months if the coverage offered provides MV).

A definition of part-time employee is added to the final regulations for a new employee who is reasonably expected at the employee's start date not to be a full-time employee (and who is not a variable hour employee or a seasonal employee). The same rules that apply to new variable hour employees and new seasonal employees apply to new part-time employees. In the normal case, an employer's categorization of a new employee as a part-time employee or variable hour employee does not affect the way the look-back measurement method applies (because the initial measurement period is available to both types of employees).

12. Clarifications Regarding the Initial Measurement Period

The final regulations clarify that an applicable large employer member may apply the payroll period rule set forth in § 54.4980H–3(d)(1)(ii) for purposes of determining an initial measurement period, provided that an initial measurement period must begin on the start date or any date between the start date and the later of the first day of the first calendar month following the employee's start date and the first day of the first payroll period that starts after the employee's start date.

The proposed regulations define the initial measurement period, in part, as a period of at least three consecutive calendar months but not more than 12 consecutive calendar months. The final regulations clarify that the initial measurement period need not be based on calendar months but instead may be based on months, defined as either a calendar month or as the period that begins on any date following the first day of the calendar month and that ends on the immediately preceding date in the immediately following calendar month (for example, from March 15 to April 14). In contrast, a stability period must be based on calendar months. The final regulations, consistent with the proposed regulations, also allow an employer to base measurement periods on one week, two week, or semi-monthly payroll periods.

13. Periods of Time Between Stability Periods

Commenters noted that, in certain circumstances, there may be a period of time between the stability period associated with the initial measurement period and the stability period associated with the first full standard measurement period during which a variable hour employee or seasonal employee has been employed. This generally may occur in cases in which a new employee begins providing services a short period after the beginning of the standard measurement period that would apply to the employee if the employee were an ongoing employee.

For example, suppose an employer uses 12-month measurement and stability periods for both its new variable hour employees and its ongoing employees, with the standard measurement period for ongoing employees running from October 15 of one year to the following October 14, the administrative period for ongoing employees running from October 15 through December 31 and with the calendar year as the stability period for ongoing employees. If a new variable hour employee, Employee A, is hired on October 25, 2015, and the employer chooses to begin the initial measurement period for new variable hour employees on the first day of the first calendar month beginning after the start date, the initial measurement period for Employee A will run from November 1, 2015, through October 31, 2016. If Employee A averages at least 30 hours of service per week during the initial measurement period, the employer must treat Employee A as a full-time employee for a period of at least 12 months beginning no later than December 1, 2016 (the first day of the 14th calendar month after hire). If that period begins on December 1, 2016, the period for which Employee A must be treated as a full-time employee will end no earlier than November 30, 2017.

The first standard measurement period applicable to Employee A is the period from October 15, 2016, through October

14, 2017. If Employee A averages 30 hours of service per week during this standard measurement period, the employer must treat Employee A as a full-time employee for the stability period that is coextensive with the 2018 calendar year. However, this would leave a period of time between the end of the stability period associated with Employee A's initial measurement period (November 30, 2017) and the beginning of the stability period associated with the first standard measurement period applicable to Employee A (January 1, 2018).

The final regulations clarify that in circumstances in which there is a period of time between the stability period associated with the initial measurement period and the stability period associated with the first full standard measurement period during which a new employee is employed, the treatment as a full-time employee or not full-time employee that applies during the stability period associated with the initial measurement period continues to apply until the beginning of the stability period associated with the first full standard measurement period during which the employee is employed. If the employee is being treated as a full-time employee during the initial stability period, that treatment must be extended until the first day of the stability period associated with the first full standard measurement period during which the employee is employed, and if the employee is being treated as not a full-time employee during the initial stability period, that treatment may be extended until the first day of the stability period associated with the first full standard measurement period during which the employee is employed. Thus, in the example in the preceding paragraphs, Employee A is a full-time employee for the month of December 2017.

Further, the final regulations also clarify that for a variable hour employee or seasonal employee who does not average at least 30 hours of service per week during the initial measurement period, the maximum length for a stability period associated with the initial measurement period is the end of the first full standard measurement period (plus any associated administrative period) during which the new employee was employed (rather than at the end of the standard measurement period (plus any associated administrative period) in which the initial measurement period ends), which was the rule contained in the proposed regulations.

D. *Clarification of periods during which section 4980H liability does not apply*

In various circumstances, the final regulations provide that an employer will not be subject to an assessable payment under section 4980H for a certain period of time and the term *limited non-assessment period for certain employees* is added to the final regulations to describe these periods. In particular, the final regulations provide, consistent with the proposed regulations, that section 4980H liability does not apply with respect to an employee who is in the initial measurement period (or the associated administrative period), for a period of time after an employee experiences a change to full-time employee status during the initial measurement period, or with respect to a new employee who is reasonably expected to be a full-time employee and to whom coverage is offered on the first of the month following the employee's initial three full calendar months of employment. The final regulations add a rule under the monthly measurement method under which an employer will not be subject to a section 4980H assessable payment with respect to an employee for the first full calendar month in which an employee is first otherwise eligible for an offer of coverage and the immediately subsequent two calendar months. Further, the final regulations provide that with respect to an employee who was not offered coverage by the employer at any point during the prior calendar year, if an employee is offered coverage by an applicable large employer, for the first time, on or before April 1 of the first calendar year for which the employer is an applicable large employer, the employer will not be subject to an assessable payment under section 4980H by reason of its failure to offer coverage to the employee for January through March of that year.

The final regulations clarify that each of these rules is only available if the employee is offered coverage by the first day of the month following the end of the applicable period, and for an employer to not be subject to an assessable payment under section 4980H(b) the employer must offer coverage that provides MV at the end of the period.

In addition, the final regulations clarify that these rules only apply with respect to a calendar month if during the calendar month during the relevant period the employee is otherwise eligible for an offer of coverage (except that this rule does not apply with respect to the rule regarding an employer that is an applicable large employer for the first time, as described in section V.F of this preamble). For purposes of these rules, an employee is otherwise eligible to be offered coverage under a group health plan for a calendar month if, pursuant to the terms of the plan as in effect for that calendar month, the employee meets all conditions to be offered coverage under the plan for that calendar month, other than the completion of a waiting period, within the meaning of § 54.9801–2.

The final regulations also clarify that an employer will not be subject to an assessable payment with respect to an employee for the first month of an employee's employment with the employer, if the employee's first day of employment is a day other than the first day of the calendar month.

Note that the relief from the section 4980H assessable payment provided by the rules described in this section does not affect an employee's eligibility for a premium tax credit. For example, an employee or related individual is not eligible for coverage under the employer's plan (and therefore may be eligible for a premium tax credit or cost-sharing reduction through an Exchange) during any period when coverage is not actually offered to the employee by the employer, including any measurement period or administrative period, even if the employer is not subject to an assessable payment under section 4980H for this period.

E. *Rehire rules and break-in-service rules for continuing employees*

1. Rehire Rules

The proposed regulations provide that, solely for purposes of section 4980H, an employee who resumes providing service to an applicable large employer after a period during which the employee was not credited with any hours of service may be treated as having terminated employment and having been rehired, and therefore may be treated as a new employee upon the resumption of services, only if the employee did not have an hour of service for the applicable large employer for a period of at least 26 consecutive weeks immediately preceding the resumption of services.

In addition, the proposed regulations permit an employer to apply a parity rule, under which an employee may be treated as rehired after a shorter period of at least four consecutive weeks during which no hours of service were credited if that period exceeded the number of weeks of that employee's period of employment with the applicable large employer immediately preceding the period during which the employee was not credited with any hours of service. For example, if an employee started employment and worked for six weeks, then had a period of eight weeks during which no hours of service were credited, the employer could treat the employee as a rehired employee, subject to the rules for new employees under these regulations, if the employee resumed providing services after the eight-week break.

Comments were received on these rehire rules. Several employers and employer groups commented that the rehire rules in general, and the rule of parity in particular, are difficult to implement because they require the employer to maintain records of service of former employees across the employer's controlled group (the group of applicable large employer members that together are treated as an applicable large employer). Commenters requested that employers be permitted to determine, using any reasonable good-faith method, whether an employee resuming services after a break in service constitutes a new employee or a continuing employee. Other commenters requested that the length of the break in service required before a returning employee may be treated as a new employee be reduced from 26 weeks to some shorter length, such as four or ten weeks.

The Treasury Department and the IRS believe that it would be inequitable to employees who had become eligible for coverage prior to the break in service to be subjected to a new period of exclusion from the plan (which can be over a year for variable hour employees) based upon a brief break in service. The Treasury Department and the IRS also remain concerned that without an objective standard for determining when an employee who returns after a break in service may be treated as a new employee, there is a potential for an employer to attempt to evade the requirements of section 4980H through a pattern of terminating and rehiring employees and then treating the returning employees as new employees. However, the Treasury Department and the IRS agree with the commenters suggesting that a break-in-service period shorter than 26 weeks would be sufficient to curtail the potential for abuse. Accordingly, the final regulations retain the rehire rules contained in the proposed regulations but reduce the length of the break in service required before a returning employee may be treated as a new employee from 26 weeks to 13 weeks (except for educational organization employers as described in this section of the preamble). This break-in-service period applies for both the look-back measurement method and the monthly measurement method.

To avoid the treatment of employees of educational organizations as new employees resuming services after a scheduled academic break, however, the final regulations provide that for employees of educational organizations, the 26-week break-in-service period under the rehire rules provided in the proposed regulations continues to apply.

The final regulations also retain the rule of parity, which, as under the proposed regulations, is optional on the part of the employer and need not be used if the employer does not maintain sufficient records of the periods of service of former employees or prefers not to use it for other reasons.

2. Break-In-Service Rules for Continuing Employees (Special Unpaid Leave Rule and Employment Break Period Rule)

For purposes of applying the look-back measurement method to a returning employee not treated as a new employee, the proposed regulations provide an averaging method for special unpaid leave that is applicable to all employers choosing to use the look-back measurement method. For this purpose special unpaid leave is unpaid leave subject to the Family and Medical Leave Act of 1993 (FMLA), Public Law 103–3, 29 U.S.C. 2601 et seq., or to the Uniformed Services Employment and Reemployment Rights Act of 1994 (USERRA), Public Law 103–353, 38 U.S.C. 4301 et seq., or on account of jury duty. Comments were received on the averaging rules for special unpaid leave, and those comments generally favored the approach provided in the proposed regulations.

The proposed regulations also provide an averaging method for employment break periods that is applicable to educational organizations that use the look-back measurement method. For this purpose, an employment break period is a period of at least four consecutive weeks (disregarding special unpaid leave), measured in weeks, during which an employee is not credited with hours of service.

Under the proposed averaging method, in the case of an employee returning from absence who would be treated as a continuing employee (that is, an employee whose break in service was shorter than one resulting in treatment as a rehired employee), the employer would determine the employee's average hours of service for a measurement period by computing the average after excluding any special unpaid leave (and in the case of an educational organization, also excluding any employment break period) during that measurement period and by using that average as the average for the entire measurement period. Alternatively, the employer could treat the employee as credited with hours of service for any periods of special unpaid leave (and, in the case of an educational organization, any employment break period) during that measurement period at a rate equal to the average weekly rate at which the employee was credited with hours of service during the weeks in the measurement period that are not part of a period of special unpaid leave (or, in the case of an educational organization, an employment break period). The two alternative methods were intended to be different expressions of an equivalent calculation, therefore having the same results. In no case, however, would the employer be required to exclude (or credit) more than 501 hours of service during employment break periods in a calendar year (however no such limit applies for special unpaid leave).

In the preamble to the proposed regulations, the Treasury Department and the IRS specifically requested comments on whether the employment break period rules should be applied to all employers, including employers that were not educational organizations. With respect to the averaging rules for employment break periods, commenters differed in their responses to the proposed regulations. Some employers stated that the rules should be eliminated because they were complicated and required administrative recordkeeping that employers do not currently undertake. Some employers and employer groups also requested that the employment break period rules not be extended to employers that are not educational organizations. Other commenters requested clarification on whether the employment break period rules apply to employers that are not educational organizations but that provide services to educational organizations, such as school bus operators. In contrast, some employee organizations supported the employment break period rule, stating that it more accurately reflected positions intended to be full-time employee positions and assisted in curbing potential employer actions to prevent employees from attaining full-time employee status. However, some employers and employees also suggested that the employment break period rule would not result in an expansion of coverage to employees not currently offered coverage, but rather in limiting hours to ensure that those employees were not classified as full-time employees.

The final regulations retain the averaging rules for special unpaid leave and employment break periods as provided in the proposed regulations (that is, for purposes of applying the look-back measurement method to an employee who is not treated as a new employee under the rehire rules described in section VII.E.1 of this preamble). The commenters did not identify a compelling reason to extend the employment break period rule to employers that are not educational organizations. However, the final regulations provide that with respect to the determination of full-time employee status, the Commissioner may prescribe additional guidance of general applicability, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b)), which may include extension of the employment break period to other industries. In addition, the reduction in the break-in-service period under the rehire rule from 26 to 13 weeks in the final regulations (for employers that are not educational organizations) shortens the periods for which an individual may be credited with no hours of service that can be included in a measurement period (thereby lowering the average hours of service per week), addressing in part the issue that the employment break period also is intended to address. The employment break period rule continues to apply only to educational organizations, and the break-in-service period for employees of educational organizations continues to be 26 weeks.

Neither the special unpaid leave rule nor the employment break period rule apply under the monthly measurement method, regardless of whether the employer is an educational organization.

F. *Short-term and high-turnover employees*

1. Short-Term Employees

In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments on the treatment of short-term employees, meaning employees who are reasonably expected to average at least 30 hours of service per week and are hired into positions expected to continue for less than 12 months (but not including seasonal employees, who are employees in positions that also last a certain limited period but are expected to recur on an annual basis). A short-term employee with a tenure of under three months generally should not raise issues under section 4980H as the employer generally would not be subject to liability under section 4980H with respect to those employees provided the employer sponsors a group health plan for which the employee would have been eligible had the employee continued working beyond the three months. The Treasury Department and the IRS continue to be concerned about the potential for abuse of any exception for short-term employees through the use of initial training period positions or other methods intended to artificially divide the tenure of an employee into one or more short-term employment positions in order to avoid application of section 4980H. For these reasons, the final regulations do not adopt any special provisions applicable to short-term employees.

2. Employees in High-Turnover Positions

In the proposed regulations, the Treasury Department and the IRS requested comments on the treatment of employees in high-turnover positions, meaning positions in which a significant percentage of employees can be expected to terminate employment over a reasonably short period of time (for example, over a six-month period). Two categories of potentially high-turnover employees are already addressed in the final regulations. First, failure to offer coverage to full-time employees who do not continue in employment through the first day of the fourth month following the start date generally will not result in a potential payment under section 4980H if coverage would have been offered no later than the first day of the fourth month of employment. See § 54.4980H–3(c)(2) and § 54.4980H–3(d)(2)(iii). Second, failure to offer coverage to employees that are variable hour employees generally will not result in a section 4980H assessable payment under the look-back measurement method until after the last day of the first calendar month beginning on or after the first anniversary of the employee's start date, though the likelihood of the employee failing to continue employment through the initial measurement period may not be taken into account in determining whether the employee is a variable hour employee. See § 54.4980H–3(d)(3)(iii). This leaves at issue positions in which employees are reasonably expected to average 30 hours of service or more per week, and in which a significant portion of new hires are expected to continue in employment beyond three months but not for a significant period beyond three months.

As discussed in the preamble to the proposed regulations, the Treasury Department and the IRS have concerns about the formulation and application of a special rule in this area. Specifically, the discussion in section II.C.6 of the preamble to the proposed regulations noted that "high-turnover" is a category that would require a complex definition that could be subject to manipulation. In addition, any special treatment that is provided for employees hired into a high-turnover position could provide an incentive for employers to terminate employees to ensure that the position remains a high-turnover position under whatever standard was used to make that determination. Because many high-turnover positions may also be filled by variable hour employees for whom the rules governing variable hour employees would address the churning concerns, and because of the concerns regarding the complexity and potential manipulation of any special rules in this area, the final regulations do not adopt any special provisions addressing high-turnover positions.

G. *Employers using different methods of identifying full-time employees for different categories of employees*

Commenters requested clarification as to whether an employer must use the look-back measurement method for all employees if it chooses to use it for some employees or if an employer may use the look-back measurement method for some employees and the monthly measurement method for other employees. Commenters requested that employers have the ability to use the look-back measurement method for employees with variable work schedules and the monthly measurement method for employees with more predictable work schedules. According to these commenters, an employer's use of the look-back measurement method for its employees with fixed-hour schedules will produce the result that the employer is required to treat an employee as a full-time employee for a stability period if the fixed-hour full-time employee changes to a fixed-hour non-full-time schedule. They noted that such an employee may have been hired as a full-time employee and may have been provided coverage upon hire (or within three months), unlike variable hour employees for whom the employer generally has until the end of the first calendar month after the first anniversary of the employee's start date to offer coverage.

The final regulations clarify that with respect to each of the enumerated categories of employees for which an employer may use measurement and stability periods that differ either in length or in their starting and ending dates, the employer may apply either the look-back measurement method or the monthly measurement method. See section VII.C.5 of this preamble regarding the permissible employee category rule. The final regulations neither expand the number of categories of employees nor permit employers to develop their own customized categories. In particular, the final regulations do not permit an employer to adopt the look-back measurement method for variable hour and seasonal employees while using the monthly measurement method for employees with more predictable hours of service. Under the look-back measurement method, the identification of a variable hour employee at the start date is based upon the employer's reasonable expectations. If classified as a variable hour employee, the employer is permitted to wait through the initial measurement period to determine whether the employee is a full-time employee; however, for every subsequent year of that employee's employment the identification of whether the employee is a full-time employee is based upon the employee's hours of service in the prior measurement period, without any application of the employer's reasonable expectations. If employers were permitted to subdivide the permitted categories between variable hour employees and non-variable hour employees (for example, applying the look-back measurement method to variable hour salaried employees and the monthly measurement method to non-variable hour salaried employees), the employer would be required to apply its reasonable expectations at the beginning of every measurement period to determine whether a salaried employee was a variable hour employee. While the treatment of a new hire who does not have previous hours of service is necessary to address how to determine whether a new variable hour employee is a full-time employee, the Treasury Department and the IRS have determined that permitting employees in the same objective category to move between measurement methods based solely on the employer's reasonable expectations brings an excessive level of subjectivity into the determination of an employee's classification as a full-time employee that is not warranted by any lack of information.

The final regulations also provide rules addressing an employee who experiences a change in employment status from a position for which the look-back measurement method is used to a position for which the monthly measurement method is used (or vice versa). In general, these rules are intended to protect an employee's status as a full-time employee during the transition period. Accordingly, these rules require that an employee transferring from a position for which the employer is using the look-back measurement method to a position for which the employer is using the monthly measurement method and who at the date of transfer is in a stability period during which the employee is treated as a full-time employee must continue to be treated as a full-time employee during the remainder of the stability period. If the employee is in a stability period for which the employee is not treated as a full-time employee, the employer may continue to treat the employee as not a full-time employee during the remainder of the stability period. With respect to the stability period that immediately follows the stability period during which the employee transferred, the employee must be treated as a full-time employee for any calendar month during which the employee would be a full-time employee under either the previously applicable look-back measurement method (and thus not lose the hours of service accumulated during the measurement period during which the transfer occurs) or the applicable monthly measurement method. After that immediately following stability period, the employer may determine the employee's status solely through application of the monthly measurement method.

For an employee transferring from a category of employment to which the monthly measurement method applies to a position to which the look-back measurement method applies, the rules generally require that the employer recreate the stability periods that would apply based upon the employee's hours of service before the transfer. However, consistent with the previously described rules, for the stability period immediately subsequent to the transfer, the employee must be treated as a full-time employee for any calendar month that the employee would be a full-time employee under either the previously applicable monthly measurement method or the applicable look-back measurement method. The final regulations provide several examples to illustrate the application of these rules.

In addition, the final regulations allow an employer, in certain limited circumstances, to begin applying the monthly measurement method to an employee to whom the look-back measurement method has been applied sooner than required under the standard rules governing changes in methods. This rule is intended to address the concern raised by commenters that employers that offer coverage to an employee continuously from within three months of an employee's start date should not be required to continue to treat that employee as a full-time employee for many months after that employee experiences a change in employment status to a position in which the employee will average less than 30 hours of service per week. Examples include a circumstance in which an employee who has been a full-time employee for ten years, and who was offered coverage within three months of the start date, changes from a position of employment to another position requiring fewer hours of service either as part of a phased-retirement program or to care for a family member. The final regulations allow an applicable large employer member to begin to apply the monthly measurement method in lieu of the otherwise applicable stability period beginning on the first day of the fourth full calendar month following the change in employment status. This rule applies only with respect to an employee to whom the applicable large employer member offered MV coverage from at least the first day of the month following the employee's initial three full calendar months of employment through the month in which the change in employment status occurs, and this rule applies only if during each of the three full calendar months following the change in employment status the employee has on average less than 30 hours of service per week. Under this rule, an employer may apply the monthly measurement method to an employee even if the employer does not apply the monthly measurement method to employees in the same category (for example, an employer could apply the monthly measurement method to an hourly employee, even if the employer uses the look-back measurement method to determine full-time employee status of all other hourly employees). The employer may continue to apply the monthly measurement method through the end of the first full measurement period (and any associated administrative period) that would have applied had the employee remained under the applicable look-back measurement method.

The Treasury Department and the IRS anticipate that the rules with respect to a transfer from a position to which one look-back measurement method applies to a position to which another look-back measurement method applies will require complex rules because the methods may differ not only in the length of the applicable measurement and stability periods, but also the starting dates of the measurement periods (for example, the use of a calendar year for one measurement period but a non-calendar year period for another measurement period). To provide for these rules in the most comprehensible format, as well as to ensure flexibility to address situations that arise that have not currently been contemplated, the final regulations provide that with respect to the determination of full-time employee status, the Commissioner may prescribe additional guidance of general applicability, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b)).

VIII. *Affordability and Affordability Safe Harbors*

A. *Affordability safe harbors*

Liability under section 4980H only arises if at least one full-time employee of the applicable large employer member receives a premium tax credit. Even if the applicable large employer member offers coverage to 95 percent or more of its full-time employees (and their dependents), thereby avoiding liability under section 4980H(a), the applicable large employer member may be subject to an assessable payment under section 4980H(b) if one or more full-time employees obtain a premium tax credit. See section X of this preamble for a description of rules regarding liability under section 4980H. For an employee who is offered coverage by an employer to be eligible to receive a premium tax credit if the employee enrolls in coverage on an Exchange, the coverage offered to the employee by the employer must either fail to provide MV, or fail to be affordable to that employee, or both. Affordability under section 36B is determined by reference to the taxpayer's household income. Because an employer generally will not know the taxpayer employee's household income, the proposed regulations under section 4980H set forth three separate safe harbors under which an employer could determine affordability based on information that is readily available to the employer. These three safe harbors are (1) the Form W-2 wages safe harbor, (2) the rate of pay safe harbor, and (3) the federal poverty line safe harbor. If an employer meets the requirements of the safe harbor, the offer of coverage is deemed affordable for purposes of section 4980H(b) regardless of whether it is affordable to the employee under section 36B. Subject to the modifications described in this section, the final regulations adopt these affordability safe harbors.

These safe harbors are all optional. An employer may choose to use one or more of these safe harbors for all of its employees or for any reasonable category of employees, provided it does so on a uniform and consistent basis for all employees in a category. In response to a comment, the final regulations clarify that reasonable categories generally include specified job categories, nature of compensation (for example, salaried or hourly), geographic location, and similar bona fide business criteria. However, an enumeration of employees by name would not be considered a reasonable category.

B. *Form W-2 wages safe harbor*

Under the Form W-2 wages safe harbor, the employer may calculate the affordability of the coverage based solely on the wages paid to the employee by that employer (and any other member of the same applicable large employer that also pays wages to that employee), as reported in Box 1 of the Form(s) W-2 ("Wage and Tax Statement"). Consistent with the proposed regulations, the final regulations provide rules for addressing partial years due to the employee beginning or ending employment in the middle of a calendar year. Commenters requested that reductions in Form W-2 wages due to salary reduction elections under a section 401(k) plan or a cafeteria plan under section 125 be disregarded for purposes of the safe harbor. To be consistent with section 36B, under which an employee's household income (and thus the affordability of an offer of coverage) is determined without adding back those reductions, this suggestion is not adopted in the final regulations under section 4980H.

Commenters also requested that employers be permitted to use the wages from the prior year Form W-2 instead of the current year for purposes of determining affordability. The final regulations do not adopt this comment because it would create a greater disconnect between the premium tax credit and the section 4980H assessable payment. Also, use of prior year wages would not be available with respect to new employees who were not employed by the employer in the prior year. Finally, one commenter requested that employers be permitted to impute full Form W-2 wages during periods of unpaid leave for purposes of applying the safe harbor. The final regulations do not adopt this comment; however, instead of the Form W-2 wages safe harbor, employers can use the rate of pay or federal poverty line safe harbor, both of which use a calculation that is based on an assumed wage amount that is not affected by unpaid leave.

C. *Rate of pay safe harbor*

Under the rate of pay safe harbor in the final regulations, an applicable large employer member's offer of coverage to an hourly employee is treated as affordable for a calendar month if the employee's required contribution for the calendar month for the lowest cost self-only coverage that provides MV does not exceed 9.5 percent of an amount equal to 130 hours multiplied by the lower of the employee's hourly 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. Under the same safe harbor, an applicable large employer member's offer of coverage to a non-hourly employee is treated as affordable for a calendar month if the employee's required contribution for the calendar month for the lowest cost self-only coverage that provides MV does not exceed 9.5 percent of the employee's monthly salary, as of the first day of the coverage period (instead of 130 multiplied by the hourly rate of pay); provided that if the monthly salary is reduced, including due to a reduction in work hours, the safe harbor is not available.

The rate of pay safe harbor provides employers with a design-based method for satisfying affordability without having to analyze each employee's wages and hours. Under this safe harbor, for an hourly employee, the employer uses an assumed rate of 130 hours per calendar month multiplied by an hourly employee's rate of pay, regardless of whether the employee actually works more or less than 130 hours during a calendar month. The affordability calculation under the rate of pay safe harbor is not altered by a leave of absence or reduction in hours worked. Thus, for example, under the rate of pay safe harbor, if an hourly employee treated as a full-time employee earns $10 per hour in a calendar month (and earned at least $10 per hour as of the first day of the coverage period) but has one or more calendar months in which the employee has a significant amount of unpaid leave or otherwise reduced hours, the employer may still require an employee contribution of up to 9.5 percent of $10 multiplied by 130 hours ($123.50).

The final regulations, unlike the proposed regulations, permit an employer to use the rate of pay safe harbor even if an hourly employee's hourly rate of pay is reduced during the year. The proposed regulations provide that the rate of pay safe harbor cannot be used if the employer reduces an employee's hourly rate of pay during the year, because otherwise employers could set an artificially high rate of pay at the beginning of the coverage period resulting in an artificially high required employee contribution, and then the employer could reduce the employee's rate of pay for the remainder of the coverage period. One commenter noted that there are instances in which an employer adjusts an employee's rate of pay depending on, for example, whether minimum sales goals are satisfied. Commenters also noted that the rate of pay may be reduced for bona fide reasons, such as a transfer of position, and requested that the rate of pay safe harbor be available in this circumstance as long as the premium was reduced to reflect the reduction in the rate of pay.

In response to these comments, the final regulations permit an employer to apply the rate of pay safe harbor to an hourly employee even if the employee's rate of pay is reduced during the year. In this situation, the rate of pay is applied separately to each calendar month, rather than to the entire year and the employee's required contribution may be treated as affordable if it is affordable based on the lowest rate of pay for the calendar month multiplied by 130 hours. The final regulations adopt these changes because they result in lower employee required contributions in situations in which an employee's hourly rate of pay is reduced during the year.

Commenters noted that the rate of pay safe harbor cannot be used, as a practical matter, for tipped employees or for employees who are compensated solely on the basis of commissions. While this is correct, employers can use the two other affordability safe harbors, Form W-2 wages and federal poverty line, for determining affordability for employees whose compensation is not based on a rate of pay.

D. *Federal poverty line safe harbor*

Under the federal poverty line safe harbor, an applicable large employer member's offer of coverage to an employee is treated as affordable if the employee's required contribution for the calendar month for the lowest cost self-only coverage that provides MV does not exceed 9.5 percent of a monthly amount determined as the federal poverty line for a single individual for the applicable calendar year, divided by 12. This safe harbor is intended to provide employers a predetermined maximum amount of employee contribution that in all cases will result in the coverage being deemed affordable.

The proposed regulations provide that, in the interest of administrative convenience, employers may use the most recently published poverty guidelines as of the first day of the plan year of the applicable large employer member's health plan. One commenter requested that employers be permitted to use the guidelines in effect six months prior to the beginning of the plan year, so as to provide employers with adequate time to establish premium amounts in advance of the plan's open enrollment period. The final regulations adopt this comment.

IX. *Offers of Coverage*

A. *In general*

For an employee to be treated as having been offered coverage for a month (or any day in that month), the coverage offered, if accepted, must be applicable for that month (or that day).

For purposes of section 4980H(a), the proposed and final regulations provide that an applicable large employer member is treated as offering coverage to its full-time employees (and their dependents) for a calendar month if, for that month, it offers coverage to all but five percent or, if greater, five of its full-time employees (provided that an employee is treated as having been offered coverage only if the employer also offered coverage to that employee's dependents as applicable). This relief applies to a failure to offer coverage to the specified number or percentage of employees (and their dependents), regardless of whether the failure to offer was inadvertent. The alternative margin of five full-time employees (and their dependents), if greater than five percent of full-time employees (and their dependents), is designed to accommodate relatively small applicable large employer members because a failure to offer coverage to a few full-time employees (and their dependents) might exceed five percent of the applicable large employer member's full-time employees. Commenters requested that this margin be adjusted based on the size of the employer so that large employers are not allowed to exclude large numbers of employees. This comment is not adopted because use of a uniform percentage reduces complexity and is easier for employers to apply. See section XV.D.7 of this preamble for limited 2015 transition relief under section 4980H(a) for certain employers that offer coverage to at least 70 percent of their full-time employees (and their dependents), and see section XV.D.5 of this preamble for transition relief regarding offers of coverage to dependents.

The final regulations do not apply any specific rules for demonstrating that an offer of coverage was made. The otherwise generally applicable substantiation and recordkeeping requirements in section 6001 apply, including Rev. Proc. 98–25 (1998–1 CB 689). In addition, the offer generally can be made electronically. See § 1.401(a)–21 for a safe harbor method for use of electronic media.

Consistent with the proposed regulations, the final regulations provide that if an employee has not been offered an effective opportunity to accept or decline coverage, the employee will not be treated as having been offered the coverage for purposes of section 4980H. In response to comments, the final regulations provide that an effective opportunity to decline is not required for an offer of coverage that provides MV and is offered either at no cost to the employee or at a cost, for any calendar month, of no more than 9.5 percent of a monthly amount determined as the federal poverty line for a single individual for the applicable calendar year, divided by 12.[9] Thus, an employer may not render an employee ineligible for a premium tax credit by providing an employee with mandatory coverage (that is, coverage which the employee is not offered an effective opportunity to decline) that does not meet MV or that may not be affordable. See the section entitled "Background" of the preamble to the proposed regulations regarding minimum value of eligible employer-sponsored plans and other rules regarding the health insurance premium tax credit for a discussion of concerns raised by an arrangement under which employees are required, as a condition of employment or otherwise, to be enrolled in an employer-sponsored plan that does not provide MV or is unaffordable, at 78 FR 25909, 25910 (May 3, 2013).

The final regulations also provide guidance on an offer of coverage for an employee who is employed by more than one applicable large employer member for a calendar month. The final regulations provide that an offer of coverage by one applicable large employer member to an employee for a calendar month is treated as an offer of coverage by all applicable large employer members for that calendar month. Thus, if one applicable large employer member offers coverage to the employee for a calendar month, every other member of the same applicable large employer is considered to have made the same offer of coverage to that employee for purposes of determining the liability under section 4980H, if any, of each applicable large employer member. For example, in the case of a group of applicable large employer members operating a single plan intended to offer coverage to employees of all the applicable large employer members, any employee offered coverage under the plan would be treated as receiving an offer of that coverage from each applicable large employer member. For a discussion of how any assessable payment under section 4980H for a calendar month would be allocated among applicable large employer members if a full-time employee performs services for two or more applicable large employer members during the same calendar month, see section X of this preamble.

Commenters requested that employers not be subject to an assessable payment for failure to offer coverage to full-time employees who have coverage from other sources, such as Medicare, Medicaid or a spouse's employer. The final regulations do not adopt this comment because it is not consistent with section 4980H and would require that the employer verify alternative coverage in a manner not contemplated by the statute (for example, ob-

[9]For an employee offered coverage for all 12 calendar months of the year, the total cost for the year will be no more than 9.5 percent of the federal poverty line for a single individual. Thus, regardless of the size of the employee's household or the level of other income or loss of any member of the employee's household, either the employer's coverage will be affordable for purposes of the premium tax credit or the employee's household income will be less than 100 percent of the federal poverty line and the employee will not be eligible for a premium tax credit.

ligating an employer to question its employees as to Medicaid eligibility or a spouse's eligibility for and purchase of employer-sponsored coverage). However, an employee who is eligible for Medicare or Medicaid is not eligible for a premium tax credit, and in cases in which no full-time employee receives a premium tax credit (for example, because all of an employer's full-time employees are eligible for Medicare or Medicaid), the employer will not be subject to an assessable payment under section 4980H.[10] In addition, for an employer that satisfies the requirements to avoid a payment under section 4980H(a), the employer will not be subject to a payment under section 4980H(b) with respect to those employees (because they are not eligible for a premium tax credit).

The final regulations clarify that an employee's election of coverage from a prior year that continues for every succeeding plan year unless the employee affirmatively elects to opt out of the plan constitutes an offer of coverage for purposes of section 4980H.

Commenters expressed concern about potential liability under section 4980H in the case of an applicable large employer that cannot obtain or maintain coverage for its employees because the employer cannot satisfy a health insurance issuer's minimum participation requirements. In the large group market, a minimum participation requirement cannot be used to deny guaranteed issue. For small employers, such as relatively small applicable large employers, final regulations issued by HHS provide that an issuer must guarantee issue coverage to a small employer during an annual, month-long open enrollment period regardless of whether the small employer satisfies any minimum participation requirement. See 45 CFR 147.104(b)(1). HHS regulations generally define a small employer as one that has at least one, but not more than 100, employees. For plan years beginning before January 1, 2016, states may set the upper limit at 50 employees.

Commenters requested that the final regulations treat an offer of coverage made by the employer during the collective bargaining process between an employer and a union that is not accepted by the union as an offer of coverage to all employees covered by the collective bargaining agreement. However, even where an offer to the union has been made and rejected, the affected employee has never been provided a chance to accept an offer of coverage in these circumstances. Accordingly, the final regulations do not adopt this suggestion.

B. *Application to multiemployer and single employer Taft-Hartley plans, multiple employer welfare arrangements (MEWAs) and other similar arrangements*

Commenters requested clarification of whether an offer of coverage under a multiemployer or single employer Taft-Hartley plan, if the employer contributed to the plan on behalf of the employee, constitutes an offer of coverage by the employer for purposes of section 4980H. The final regulations clarify that for purposes of section 4980H, an offer of coverage includes an offer of coverage made on behalf of an employer, and that this would include an offer made by a multiemployer or single employer Taft-Hartley plan or a MEWA to an employee on behalf of a contributing employer of that employee. See section XV.E of this preamble for interim guidance on the application of section 4980H to multiemployer plans.

Under this same reasoning, if certain conditions are met, an offer of coverage to an employee performing services for an employer that is a client of a professional employer organization or other staffing firm (in the typical case in which the professional employer organization or staffing firm is not the common law employer of the individual) (referred to in this section IX.B of the preamble as a "staffing firm") made by the staffing firm on behalf of the client employer under a plan established or maintained by the staffing firm, is treated as an offer of coverage made by the client employer for purposes of section 4980H. For this purpose, an offer of coverage is treated as made on behalf of a client employer only if the fee the client employer would pay to the staffing firm for an employee enrolled in health coverage under the plan is higher than the fee the client employer would pay to the staffing firm for the same employee if the employee did not enroll in health coverage under the plan.

X. *Assessment and Payment of Section 4980H Liability*

Under the proposed and final regulations, each applicable large employer member is liable for its section 4980H assessable payment, and is not liable for the section 4980H assessable payment of any other entity in the controlled group comprising the applicable large employer. Any assessable payment under section 4980H is payable upon notice and demand and is assessed and collected in the same manner as an assessable penalty under subchapter B of chapter 68 of the Code. The IRS will adopt procedures that ensure employers receive certification, pursuant to regulations issued by HHS, that one or more employees have received a premium tax credit or cost-sharing reduction. 45 CFR 155.310(i). The IRS will contact employers to inform them of their potential liability and provide them an opportunity to respond before any liability is assessed or notice and demand for payment is made. It is anticipated that additional guidance of general applicability, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b)), will provide that the contact for a given calendar year will not occur until after employees' individual tax returns are due for that year claiming premium tax credits and after the due date for employers that meet the 50 full-time employee (plus FTE) threshold to file the information returns identifying their full-time employees and describing the coverage that was offered (if any).

Commenters requested that employers be permitted to aggregate applicable large employer members within an applicable large employer for purposes of determining section 4980H liability. For example, commenters requested that an applicable large employer member offering coverage to all of its full-time employees be permitted to aggregate with one or more applicable large employer members so that the aggregated group would be treated as hav-

[10] For rules on when an individual is treated as eligible for Medicare or Medicaid, see § 1.36B–2(c).

ing offered coverage to at least 95 percent of its full-time employees (and their dependents) to avoid a payment under section 4980H(a). Due to concerns regarding increased administrative complexity and potential for abuse, the final regulations do not adopt this request.

With respect to a full-time employee who performs services for two or more applicable large employer members during the same calendar month, the final regulations provide that the member for whom the employee has the greatest number of hours of service for that calendar month is the member that treats that employee as a full-time employee for purposes of assessable payment determinations under section 4980H(a) and (b). This rule modifies the rule in the proposed regulations, which provides an allocation rule only for purposes of the section 4980H(b) assessable payment liability and which allocated the payment amount among the different members in accordance with the number of hours of service the employee had from each such member for that calendar month. For any calendar month in which the employee has the same number of hours of service for two or more applicable large employer members, the final regulations provide that the members can treat one of the members for which the employee performs services as the employer of that employee for that calendar month for purposes of the assessable payment determination. The Treasury Department and the IRS anticipate that the member who is treated as the employer of that employee would report that employee as its full-time employee on the member's section 6056 information return, and if the employee is not included in any applicable large employer member's section 6056 information return, the IRS will select a member to be treated as the employer of that employee for purposes of the assessable payment determination.

In complying with section 4980H, applicable large employer members are responsible for ensuring that they comply with the recordkeeping requirements in section 6001, including Rev. Proc. 98–25 (1998–1 CB 689) (see § 601.601(d)(2)(ii)(b)).

Pursuant to section 275(a)(6) regarding the nondeductibility of certain excise taxes, including those under chapter 43, an assessable payment imposed under section 4980H is not deductible.

XI. *Definition of Dependent*

A. *In general*

Section 4980H provides that in order to avoid a potential assessable payment under section 4980H, an applicable large employer must offer coverage to its full-time employees and the full-time employees' dependents. For this purpose, the proposed regulations define the term *dependent* to mean a child (as defined in section 152(f)(1)) of an employee who has not attained age 26. For this purpose, a dependent does not include the spouse of an employee. This definition of dependent applies only for purposes of section 4980H. See section XV.D.5 of this preamble for transition relief regarding offers of coverage to dependents.

Commenters requested that the definition of dependent be expanded to include grandchildren and qualifying relatives (within the meaning of section 152). The final regulations do not expand the definition of dependent to include these categories because such a definition would be inconsistent with the typical coverage provided by employer-sponsored plans.

Some commenters requested that the definition of dependent be expanded to include spouses, and other commenters supported the proposal to exclude spouses from the definition of dependent. The definition of dependent in the final regulations, consistent with the definition in the proposed regulations, excludes spouses.

B. *Foster children and stepchildren*

By incorporating section 152(f)(1), the definition of dependent in the proposed regulations includes biological children, stepchildren, adopted children, and foster children. Commenters requested that foster children and stepchildren be removed from the definition of dependent for purposes of section 4980H. With respect to foster children, commenters noted that the government entities responsible for a foster system typically provide health benefits for the foster child, so that employer-provided coverage would be duplicative and difficult to administer. With respect to stepchildren, commenters noted that in the case of a stepchild, the child in most cases will have two parents who are not stepparents both of whom potentially would be able to provide for the child's coverage and both of whose employers potentially could be subject to section 4980H for failing to offer coverage to that child. These commenters suggested that applying section 4980H to an employee's stepchildren would in many cases be duplicative and that, for this reason, many employers currently do not extend offers of coverage to stepchildren of an employee. In light of these considerations, the final regulations exclude both foster children and stepchildren from the definition of dependent for purposes of section 4980H only.

C. *Treatment during month in which dependent attains age 26*

A commenter requested clarification of the application of section 4980H to an employee's child for the month in which the child attains age 26. In response, the final regulations clarify that for purposes of section 4980H, a child is a dependent for the entire calendar month during which he or she attains age 26.

D. *Citizens or nationals of other countries*

The definition of dependent under the proposed regulations includes children who are not citizens or residents of the United States. Section 152(b)(3), which is not incorporated in the definition of dependent under the proposed regulations, provides that the term *dependent* does not include an individual who is not a citizen or national of the United States unless such individual is a resident of the United States or a country contiguous to the United States (certain adopted children are excepted from this rule). Based on a commenter's concerns about offering coverage to the children of an employee who works for an applicable large employer in the United States but whose children are not U.S. citizens and who do not reside in the United States, the final regulations modify the definition of dependent to incorporate the rules under section 152(b)(3). Accordingly, the final regulations exclude a child who is not a U.S. citizen or national from the definition of dependent, unless that child is a resident of a country contiguous to the United

States or is within the exception for adopted children described in section 152(b)(3)(B).

XII. *Worker Classification and Section 4980H*

Consistent with the proposed regulations, these final regulations define an employee for purposes of section 4980H as an individual who is an employee under the common law standard, and as not including a leased employee (as defined in section 414(n)(2)), a sole proprietor, a partner in a partnership, a 2-percent S corporation shareholder, or a worker described in section 3508 (this last category is added to the list of exclusions in the final regulations). Commenters expressed concerns about the consequences under section 4980H of an IRS examination in which workers providing services to a service recipient entity are reclassified as employees of that entity. Specifically, commenters pointed out that if a worker who was not treated as an employee by the service recipient and was not offered health coverage by the service recipient is reclassified as an employee of the service recipient for past periods, and that worker had sufficient hours of service to be a full-time employee for such past periods, the reclassification may impact whether the service recipient employer had offered coverage to no less than 95 percent of its full-time employees for a particular calendar month (and therefore whether an assessable amount was payable under section 4980H(a)). In addition, one commenter noted that, even if the reclassification did not result in liability for an assessable payment under section 4980H(a), the service recipient could still be liable for an assessable payment under section 4980H(b) if the reclassified full-time employee had received a premium tax credit.

Commenters discussed the applicability of section 530 of the Revenue Act of 1978 (referred to in this preamble as "Section 530") for purposes of section 4980H. Section 530, which is not incorporated into the Code, provides that "if (A) for purposes of employment taxes, the taxpayer did not treat an individual as an employee for any period, and (B) in the case of periods after December 31, 1978, all Federal tax returns (including information returns) required to be filed by the taxpayer with respect to such individual for such period are filed on a basis consistent with the taxpayer's treatment of such individual as not being an employee, then, for purposes of applying such taxes for such period with respect to the taxpayer, the individual shall be deemed not to be an employee unless the taxpayer had no reasonable basis for not treating such individual as an employee." However, the relief under Section 530 applies solely for purposes of the employment tax provisions of the Code, and therefore does not apply to potential liabilities under section 4980H.

In response to the limitation on the relief under Section 530, commenters requested that the Treasury Department and the IRS formulate a similar provision in these final regulations applicable to potential liabilities under section 4980H. The Treasury Department and the IRS are concerned that the relief requested would serve to increase the potential for worker misclassification by significantly increasing the benefit of having an employee treated as an independent contractor. Accordingly, the final regulations do not adopt this suggestion.

XIII. *Particular Positions of Employment*

A. *Home care workers*

Commenters on behalf of the home care industry, as well as other industries, stated that the additional expense of providing coverage or paying the assessable payment under section 4980H could cause an employer financial difficulties. The Treasury Department and the IRS understand that in certain instances the additional expense may be a burden for an employer; however, section 4980H applies to all applicable large employers and does not provide an exception, either for employers in a particular industry such as the home care industry, or for employers with more difficulty adjusting revenue streams. Accordingly, the final regulations do not provide for these types of exceptions.

Section 4980H applies, however, only with respect to an applicable large employer, and in some circumstances the service recipient rather than a home care agency may be the common law employer of the health care provider. For example, if the service recipient has the right to direct and control the home care provider as to how they perform the services, including the ability to choose the home care provider, select the services to be performed, and set the hours of the home care provider, these facts would indicate that the service recipient is the employer under the common law standard. In that case, the agency that placed the home care provider would not be subject to section 4980H with respect to that particular provider, and the service recipient employer generally would not be subject to section 4980H with respect to any employee because the service recipient is unlikely to employ 50 full-time employees (including FTEs).

B. *Section 3508 employees*

Commenters requested clarification on whether the categories of workers identified in section 3508 (that is, real estate agents and direct sellers) are treated as employees for purposes of section 4980H. Because section 3508 provides that the identified categories of workers are not treated as employees for any purpose of the Code, the final regulations clarify that workers identified in section 3508 do not constitute employees for purposes of section 4980H (and, therefore, do not constitute full-time employees for any purpose, and their hours of service are not taken into account in determining the number of an employer's FTEs).

XIV. *International Issues*

A. *Foreign states and international organizations*

One commenter requested that the Treasury Department and the IRS consider the effect of U.S. laws and treaty obligations on the applicability of section 4980H to certain operations of foreign states and certain international organizations in the United States. Due to these applicable U.S. laws and treaty obligations, certain operations of foreign states and certain international organizations would not be subject to assessable payments under section 4980H. Accordingly, the final regulations do not explicitly address this matter. See section 894(a)(1).

B. *Employees holding H-2A and H-2B visas*

Commenters, generally representing employers in the agricultural industry, requested that holders of H-2A and H-2B visas be exempted from the definition of employee for purposes of section 4980H. The commenters suggested that such employees are generally seasonal workers, but that the exemption for certain seasonal workers for purposes of the definition of an applicable large employer, which excludes only those seasonal workers employed for a period of no more than 120 days, does not adequately address these workers because many of these individuals work more than 120 days due to serial growing seasons. However, the statutory provisions related to seasonal workers are explicit that seasonal workers are employees and that seasonal workers may be disregarded for purposes of the determination of whether an employer is an applicable large employer only if the seasonal workers cause the employer to exceed 50 full-time employees for a period of no more than 120 days. Furthermore, no justification was provided for exempting holders of H-2B visas, which cover non-agricultural workers. For these reasons, the final regulations do not adopt the suggestion that holders of H-2A and H-2B visas be generally exempted from the definition of employee for purposes of section 4980H.

The final regulations also do not adopt a special rule with respect to these workers' status as seasonal employees. The definition of seasonal employee is different from the definition of seasonal worker, and is relevant to the determination of a worker's status as a full-time employee for reasons other than the entity's determination of status as an applicable large employer. In applying the definition of seasonal employee, whether the employee holds any particular visa is not relevant. See section VII.C.8 of this preamble for a discussion of the definition of a seasonal employee.

C. *Employees performing services on cruise ships*

Representatives of the cruise ship industry requested that services performed on a cruise ship be treated as services performed outside the United States, meaning that those services would not count as hours of service for purposes of identifying an employer as an applicable large employer, or an employee as a full-time employee. However, that treatment would be inconsistent with the longstanding rules in section 863(c) that apply to transportation income derived from personal services and treat some such income as income from sources within the United States. Under the general rules for determining hours of service under both the proposed and the final regulations, hours of service do not include hours for which an employee receives compensation that is taxed as income from sources outside the United States. The final regulations clarify that this rule applies to transportation employees such as employees of cruise ships by specifically stating that hours of service do not include hours of service to the extent the compensation for such hours of service constitutes income from sources without the United States as determined under section 863.

The commenter also requested that cruise ship employers not be subject to section 4980H if they comply with the requirements of the Maritime Labor Convention of 2006 and provide employees certain coverage while they are on board the vessel. Regardless of whether that coverage constitutes MEC under section 5000A, if an offer of coverage is not extended to an employee's dependent children, it would fail to meet the requirements of an offer under section 4980H (but note that, as described in section XI.D of this preamble, the final regulations exclude a child who is not a U.S. citizen or national from the definition of dependent, unless that child is a resident of a country contiguous to the United States or is within the exception for adopted children described in section 152(b)(3)(B)). The final regulations do not adopt this suggestion.

D. *Modifications to the definition of hours of service*

Consistent with the proposed regulations, the final regulations exclude from the definition of hours of service those hours the compensation for which constitutes income from sources without the United States (within the meaning of sections 861 through 863 and the regulations thereunder). For this purpose, the term *United States* means United States as defined in section 7701(a)(9), which includes only the States and the District of Columbia and does not include the U.S. territories. In response to comments, the heading to this provision (§ 54.4980H–1(a)(24)(ii)(C)) removes the reference to nonresident alien individuals, because the application of the provision does not depend upon the residency or citizenship status of the employee. In addition, the reference to section 862(a)(3) in the proposed regulations has been expanded to reference sections 861 through 863, and the regulations thereunder, to incorporate all of the special rules applicable to the identification of the source of compensation income.

E. *Employees transferring from a domestic applicable large employer member to a foreign applicable large employer member (or vice versa)*

One commenter asked whether an employee transferred from a foreign entity to a U.S. entity in cases in which the two entities are treated as a single employer could be treated as a new hire (and whether an employee transferred from a U.S. entity to a foreign entity in the same organization could be treated as a terminated employee). The commenter pointed out that treatment of the employee as a continuing employee in such circumstances may result in certain anomalies, especially in the case of an employer using the look-back measurement method. For example, if a full-time employee who transferred from a domestic corporation to a foreign corporation were treated as a continuing employee, the commenter asked whether this means that the stability period must continue so that the employee must be offered coverage while employed at the foreign corporation to avoid any potential liability under section 4980H. In contrast, an employee performing services at a foreign corporation generally will have no hours of service if compensation for those services is not treated as U.S. source income, so if transferred to a domestic corporation and treated as a continuing employee such an employee would not have any hours of service before the U.S. transfer as part of the measurement period utilized by the domestic corporation.

To avoid these anomalies, the final regulations provide that, for both the look-back measurement method and the monthly measurement method, an employee who transfers employment from a domestic applicable large employer member to a foreign applicable large employer member may be treated as having terminated employment, but only if the position is anticipated to continue indefinitely or for at least 12 months and if substantially all of the compensation received following the transfer is treated as foreign-source income.

With respect to an employee who transfers from a foreign applicable large employer member at which the employee's services had not resulted in hours of service to a domestic applicable large employer member, if the employee had no prior hours of service with the applicable large employer (because, for example, the employee had only received non-U.S. source income in connection with services performed for the foreign applicable large employer member), the employee is treated as a newly hired employee by the domestic applicable large employer member. If the same transfer occurs with respect to an employee who had prior hours of service with the applicable large employer, the period at the foreign applicable large employer member may be treated as a period for which no hours of service are earned under the rehire rules (if the employee did not receive U.S. source income with respect to that period), so that if that period is at least 13 weeks in length, the employee is treated as a newly hired employee of the domestic applicable large employer member. See section VII.E of this preamble for a description of the rehire rules.

XV. *Transition Relief and Interim Guidance*

A. *Transition guidance in the preamble to the proposed regulations*

The preamble to the proposed regulations includes transition guidance addressing (1) the application of section 4980H to applicable large employers with non-calendar year plans[11], (2) salary reduction elections for accident and health plans provided through cafeteria plans with non-calendar year plan years beginning in 2013, (3) for purposes of determining full-time employee status, measurement periods for stability periods starting in 2014, (4) the application of section 4980H to applicable large employer members participating in multiemployer plans, (5) the determination of applicable large employer status for 2014, (6) the application of section 4980H to an offer of coverage to a full-time employee's dependents, and (7) for purposes of determining full-time employee status, the variable hour employee definition. See 78 FR 218, 236–239. The transition guidance for applicable large employer members participating in multiemployer plans was clarified in the correction to the proposed regulations. See 78 FR 16445, 16445–16446. The transition guidance in the preamble to the proposed regulations, as corrected, generally applies for 2014 or for the plan year beginning in 2014 (but additional broader transition relief was provided after the issuance of the proposed regulations; see discussion in section XV.B of this preamble.)

B. *Transition guidance for 2014—Notice 2013–45*

Section 1513(d) of the Affordable Care Act provides that section 4980H applies to months after December 31, 2013; however, Notice 2013–45, issued on July 9, 2013, provides as transition relief that no assessable payments under section 4980H will apply for 2014. (Transition relief was also provided for the section 6056 information reporting requirements for applicable large employers and the section 6055 information reporting requirements for issuers of MEC.) Notice 2013–45 provides that the employer shared responsibility provisions under section 4980H (and the information reporting provisions) will become effective for 2015.[12]

C. *Section 125 non-calendar year guidance*

The preamble to the proposed regulations provides transition relief that allows flexibility for individuals to make changes in salary reduction elections for accident and health plans provided through section 125 cafeteria plans for non-calendar cafeteria plan years beginning in 2013. The scope of this transition relief was clarified in section VI of Notice 2013–71, issued on October 31, 2013. Generally, the rules allowing employees to change their employer health plan elections under a section 125 cafeteria plan do not allow mid-year changes, see § 1.125–4. Temporary relief was needed because generally the section 5000A requirement to maintain coverage is first effective on January 1, 2014, and enrollment in qualified health plans on an Exchange is first available for 2014. The relief allowed employers to amend their plans to permit employees who had not enrolled in an employer's plan with a non-calendar plan year that began in 2013 to enroll in the middle of the plan year in order for the employees to maintain coverage for 2014 or if the employees wished to enroll in an Exchange plan, to drop enrollment in the employer's plan with a non-calendar plan year that began in 2013 in the middle of the plan year. Both the implementation of section 5000A and the initial availability of the qualified health plans on an Exchange were one-time events at the beginning of 2014 only affecting employee decisions during 2013 non-calendar plan years. Consequently, these rules are not extended for non-calendar cafeteria plan years beginning in 2014.

D. *Transition guidance for 2015*

1. Non-Calendar Year Plans

Section IX.A of the preamble to the proposed regulations provides transition guidance for the period prior to the first day of the plan year beginning in 2014 for employers sponsoring non-calendar year plans. 78 FR 218, 236.

[11] The preamble to the proposed regulations refers to plans with plan years other than the calendar year as fiscal year plans. To avoid confusion, this preamble refers to these plans as non-calendar year plans.

[12] Also, the preamble to the proposed regulations on MV of eligible employer-sponsored plans and other rules regarding the health insurance premium tax credit provide transition guidance under section 4980H for determining affordability and MV as related to wellness programs for plan years of an employer's group health plan beginning before January 1, 2015. See 78 FR 25909, 25911–25912 (May 3, 2013).

The following three pieces of transition guidance apply for the period before the first day of the first non-calendar year plan year beginning in 2015 (the 2015 plan year) for employers that maintained non-calendar year plans as of December 27, 2012, if the plan year was not modified after December 27, 2012, to begin at a later calendar date. The first two pieces (pre-2015 eligibility transition guidance and significant percentage transition guidance (all employees)) are extensions of the rules provided in section IX.A of the preamble to the proposed regulations. A new option (significant percentage transition guidance (full-time employees)) is added in this preamble.

In essence, this guidance provides transition relief for the period before the first day of the 2015 plan year with respect to all employees who, under the eligibility terms of the plan as in effect on February 9, 2014, are eligible as of the first day of the 2015 plan year for coverage under a non-calendar year plan, and who are offered, no later than the first day of the 2015 plan year, affordable coverage that provides MV. Also, in general, unless the employees described in the preceding sentence comprise an insufficient percentage of all the employer's employees, this guidance also provides relief with respect to all other employees of the employer who are offered affordable coverage that provides MV as of the first day of the 2015 plan year. This exception reflects that the need for transition relief enabling employers to begin offering coverage to employees who are not currently offered coverage at the beginning of a non-calendar year plan year, in order to coincide with the program for employees currently offered coverage, is not as compelling if the number of existing employees eligible for coverage under a non-calendar year plan is a relatively small portion of the employer's total work force.

a. Pre-2015 eligibility transition guidance

If an applicable large employer member maintained a non-calendar year plan as of December 27, 2012, and the plan year was not modified after December 27, 2012 to begin at a later calendar date, this rule applies with respect to employees of the applicable large employer member (whenever hired) who would be eligible for coverage effective beginning on the first day of the 2015 plan year under the eligibility terms of the plan as in effect on February 9, 2014. If an employee described in the preceding sentence is offered affordable coverage that provides MV no later than the first day of the 2015 plan year, no section 4980H assessable payment will be due with respect to that employee for the period prior to the first day of the 2015 plan year. To provide relief with respect to employees who are not offered coverage during one or more calendar months in 2015 solely because they terminate employment before the beginning of the 2015 plan year, this relief also applies with respect to an employee who would be eligible for coverage effective beginning on the first day of the 2015 plan year under the eligibility terms of the plan as in effect on February 9, 2014, but for the fact that the employee terminated employment (and was not rehired) prior to the first day of the 2015 plan year. This relief only applies with respect to employees who would not have been eligible for coverage under any group health plan maintained by an applicable large employer member as of February 9, 2014, that has a calendar year plan year.

Notwithstanding the foregoing, an applicable large employer member may be subject to an assessable payment under section 4980H(a) if it does not offer coverage to all but five percent (or, if greater, five) of its full-time employees (and their dependents) (or, if the transition relief set forth in section XV.D.7 of this preamble applies, if it does not offer coverage to all but 30 percent of its full-time employees (and their dependents)) as of the first day of the 2015 plan year. If an applicable large employer member does not do so, an assessable payment under section 4980H(a) may be due for any calendar month in 2015 under the section 4980H(a) rules as applied without regard to the relief set forth in this section XV.D.1.a of the preamble. See section XV.D.5 of this preamble for transition relief regarding offers of coverage to dependents.

As an illustration of the application of this rule, assume Employer Z has 600 employees, all of whom are full-time employees within the meaning of the final regulations, and Employer Z maintained a plan with an April 1 plan year as of December 27, 2012 (Plan P). Plan P's plan year was not modified after December 27, 2012, and all of Employer Z's employees are eligible for coverage under Plan P under the eligibility terms as in effect on February 9, 2014, however coverage offered prior to the 2015 plan year is not affordable. All of Employer Z's employees are offered affordable coverage that provides MV effective no later than April 1, 2015. In this case, no section 4980H assessable payment will be due with respect to any employee of Employer Z for the period before April 1, 2015. The same transition relief would apply to those 600 employees even if Employer Z also had a calendar year plan (Plan Q) and had a total of 1,000 full-time employees, 600 of whom were described above (and were not eligible for coverage under Plan Q) and 400 of whom were eligible for coverage under Plan Q as of January 1, 2015. However, the same transition relief would not apply to those 600 employees if as of April 1, 2015, the 400 other employees were not offered coverage (because as of that date Employer Z would not have offered coverage to all but five percent (or, if greater, five) of its full-time employees (and their dependents)) (and if the transition relief set forth in section XV.D.7 of this preamble applied, as of that date Employer Z would not have offered coverage to all but 30 percent of its full-time employees (and their dependents)).

b. Significant percentage transition guidance (all employees)

Additional transition guidance is also provided for employers that maintained a non-calendar year plan as of December 27, 2012 (or that maintained two or more non-calendar year plans that have the same plan year as of December 27, 2012), if the plan year of the non-calendar year plan was not modified to begin after December 27, 2012, at a later calendar date after December 27, 2012, and that either—(1) had, as of any date in the 12 months ending on February 9, 2014, at least one quarter of its employees covered under those non-calendar year plans, or (2) offered coverage under those plans to one third or more of its employees during the open enrollment period that ended most recently before February 9, 2014.

Under the additional transition guidance in this section, no assessable payment under section 4980H will be due for any month prior to the first day of the 2015 plan year with respect to employees who (1) are offered affordable coverage that provides MV no later than the first day of the 2015 plan year, and (2) would not have been eligible for coverage under any group health plan maintained by the applicable large employer member as of February 9, 2014, that has a calendar year plan year. Notwithstanding the foregoing, if an applicable large employer member does not offer coverage to all but five percent (or, if greater, five) of its full-time employees (and their dependents) (or, if the transition relief set forth in section XV.D.7 of this preamble applies, if it does not offer coverage to all but 30 percent of its full-time employees (and their dependents)) as of the first day of the 2015 plan year, an assessable payment under section 4980H(a) may be due for any calendar month in 2015 under the section 4980H(a) rules as applied without regard to the relief set forth in this section XV.D.1.b of the preamble. See section XV.D.5 of this preamble for transition relief regarding offers of coverage to dependents.

For example, assume Employer Y has 1,100 employees. One thousand of Employer Y's employees are full-time employees and 100 of Employer Y's employees are not full-time employees. Employer Y maintained a plan with a July 1 plan year (Plan M) as of December 27, 2012. Plan M's plan year was not modified after December 27, 2012, to begin at a later calendar date. Employer Y does not offer any coverage other than Plan M.

For purposes of applying the significant percentage transition guidance (all employees), Employer Y chooses December 1, 2013, as the date in the 12 months ending on February 9, 2014, to measure the number of employees it covered under Plan M. On December 1, 2013, Plan M covered 23 percent of Employer Y's employees (253 out of 1,100). During the open enrollment period that ended most recently before February 9, 2014, Employer Y offered coverage under Plan M to 45 percent of its employees (495 out of 1,100). As of the first day of the 2015 plan year (July 1, 2015), Employer Y offers affordable coverage that provides MV under Plan M to all full-time employees. Employer Y does not offer coverage to employees who are not full-time employees.

Under the significant percentage transition guidance (all employees), no section 4980H assessable payment will be due with respect to any of the full-time employees of Employer Y for the period before July 1, 2015, because Employer Y offered coverage to 45 percent (which exceeds one third) of its employees during the open enrollment period that ended most recently before February 9, 2014, and the full-time employees of Employer Y are offered affordable coverage that provides MV no later than the first day of the 2015 plan year (July 1, 2015).

Relief is not provided under the significant percentage transition guidance (all employees) with respect to the 100 employees who are not full-time employees and to whom coverage is not offered as of July 1, 2015, but no relief is necessary for these employees because an employer is not liable for an assessable payment under section 4980H for failure to offer coverage to an employee who is not a full-time employee; however, nothing in section 4980H precludes an employer from providing coverage to employees who are not full-time employees.

c. Significant percentage transition guidance (full-time employees)

Commenters noted that because the significant percentage transition guidance (all employees), as set forth in section IX.A of the preamble to the proposed regulations and generally extended in section XV.D.1.b of this preamble, applies based on the total number of employees, including seasonal and part-time employees, employers with large numbers of seasonal or part-time employees might not be able to meet the requirements of the significant percentage transition guidance (all employees), regardless of the percentage of full-time employees eligible for or enrolled in health care coverage. Commenters requested that the significant percentage transition guidance (all employees) take into account only full-time employees (within the meaning of section 4980H).

Additional transition guidance is provided for employers that, as of December 27, 2012, maintained a non-calendar year plan (or two or more such plans that, as of that date, have the same plan year) if the plan year was not modified to begin after that date to begin at a later calendar date, and if the employer either—(1) had, as of any date in the 12 months ending on February 9, 2014, at least one third of its full-time employees covered under those non-calendar year plans, or (2) offered coverage under those plans to one half or more of its full-time employees during the open enrollment period that ended most recently before February 9, 2014. Under the additional transition guidance in this section XV.D.1.c of the preamble, no payment under section 4980H will be due for any month prior to the first day of the 2015 plan year with respect to full-time employees who (1) are offered affordable coverage that provides MV no later than the first day of the 2015 plan year, and (2) would not have been eligible for coverage under any group health plan maintained by the applicable large employer member as of February 9, 2014, that has a calendar year plan year. Notwithstanding the foregoing, if an applicable large employer member does not offer coverage to all but five percent (or, if greater, five) of its full-time employees (and their dependents) (or, if the transition relief set forth in section XV.D.7 of this preamble applies, if it does not offer coverage to all but 30 percent of its full-time employees (and their dependents)) as of the first day of the 2015 plan year, an assessable payment under section 4980H(a) may be due for any calendar month in 2015 under the section 4980H(a) rules as applied without regard to the relief set forth in this section XV.D.1.c of the preamble. See section XV.D.5 of this preamble for transition relief regarding offers of coverage to dependents.

For example, assume Employer W has 2,000 employees, of whom 500 are full-time employees and 1,500 are not full-time employees. Employer W maintained a plan with a July 1 plan year (Plan N) as of December 27, 2012. Plan N's plan year was not modified after December 27, 2012. Employer W does not offer any coverage other than Plan N.

For purposes of applying the significant percentage transition guidance (full-time employees), Employer W chooses

December 1, 2013, as the date in the 12 months ending on February 9, 2014, to count the number of full-time employees it covered under Plan N. On December 1, 2013, Plan N covered 20 percent of Employer W's full-time employees (100 of 500).

During the open enrollment period that ended most recently before February 9, 2014, Employer W offered coverage under Plan N to 60 percent of its full-time employees (that is, 300 of 500). As of the first day of the 2015 plan year (July 1, 2015), Employer W offers affordable coverage that provides MV under Plan N to all full-time employees. Employer W does not offer coverage to employees who are not full-time employees.

Under the significant percentage transition guidance (full-time employees), no section 4980H assessable payment will be due with respect to Employer W's full-time employees for the period before July 1, 2015, because Employer W offered coverage to at least one half of its full-time employees during the open enrollment period that ended most recently before February 9, 2014, and the full-time employees of Employer W are offered affordable coverage that provides MV no later than the first day of the 2015 plan year (July 1, 2015).

Relief is not provided under the significant percentage transition guidance (full-time employees) with respect to Employer W's employees that are not full-time employees, but no relief is necessary for these employees because an employer is not liable for an assessable payment under section 4980H for failure to offer coverage to an employee who is not a full-time employee; however, nothing in section 4980H precludes an employer from providing coverage to employees who are not full-time employees.

d. Requirement of no change to plan year

The transition guidance for applicable large employer members sponsoring non-calendar year plans set forth in section XV.D.1 of this preamble are available for a non-calendar year plan only if that plan's plan year was not modified after December 27, 2012, to begin at a later calendar date. For example, if, as of December 27, 2012, an applicable large employer member sponsored a non-calendar year plan with a plan year starting on July 1 and later changed the start of the plan year to December 1, the transition guidance for applicable large employer members sponsoring non-calendar year plans set forth in section XV.D.1 of this preamble would not apply.

e. Section 6056 reporting for 2015 transition period for non-calendar year plans

Employers eligible for the transition guidance for plans with non-calendar year plan years remain subject to the reporting requirements under section 6056 for the entire 2015 calendar year. Because no section 4980H liability applies whether or not a full-time employee is offered coverage during the portion of the 2014 plan year falling in 2015, the applicable large employer may determine the full-time employees for that period for purposes of the section 6056 reporting requirements after the period has ended, using actual service data or using the look-back measurement method, and use those determinations for the reporting required for the period during 2015 that precedes the start of the 2015 plan year. In addition, the employer should be able to determine whether the coverage offered provides MV and the employee portion of the applicable premium in time to complete the required reporting for 2015 (that is, for section 6056 returns furnished to employees and filed with the IRS in 2016). Because this reporting is needed by the employee and the IRS for the administration of the premium tax credit, applicable large employers are required to report this information for the entire 2015 calendar year, even if during some calendar months in 2015 section 4980H liability will not apply by reason of the transition guidance for non-calendar year plan years. The section 6056 return instructions will provide additional information on how to report for 2015.

2. Shorter Measurement Periods Permitted for Stability Period Starting During 2015

For purposes of section 4980H, the term *full-time employee* means, with respect to any month, an employee who is employed on average at least 30 hours of service per week with an employer. Section 4980H(c)(4)(A). Like the proposed regulations, the final regulations include an optional alternative method to determine full-time employee status (for purposes other than determining applicable large employer status) referred to as the look-back measurement method. See section VII.C of this preamble for a description of the look-back measurement method.

As an extension of guidance provided in section IX.C of the preamble to the proposed regulations, for purposes of stability periods beginning in 2015[13], employers may adopt a transition measurement period that is shorter than 12 consecutive months but that is no less than 6 consecutive months and that begins no later than July 1, 2014, and ends no earlier than 90 days before the first day of the plan year beginning on or after January 1, 2015 (90 days being the maximum permissible administrative period). For example, an employer with a calendar year plan may use a measurement period from April 15, 2014, through October 14, 2014 (six months), followed by an administrative period ending on December 31, 2014.

As a further example, an employer with a plan year beginning April 1 that also elected to implement a 90-day administrative period may use a measurement period from July 1, 2014, through December 31, 2014 (six months), followed by an administrative period ending on March 31, 2015. However, an employer with a plan year beginning on July 1 must use a measurement period that is longer than 6 months to comply with the requirement that the measurement period begin no later than July 1, 2014, and end no earlier than 90 days before the stability period. For example, the employer may have a 10-month measurement period from June 15, 2014, through April 14, 2015, fol-

[13]An employer may continue to rely on the transition relief in section IX.C of the preamble to the proposed regulations if the employer applies that transition relief to a stability period that begins in 2014 and ends in 2015.

lowed by an administrative period from April 15, 2015, through June 30, 2015.

This transition guidance applies to a stability period beginning in 2015 through the end of that stability period (including any portion of the stability period falling in 2016), and applies to individuals who are employees as of the first day of the transition measurement period. For employees hired during or after the transition measurement period described in this section XV.D.2 of the preamble, the general rules for new employees under the look-back measurement method set forth in § 54.4980H–3(d) apply.

3. Shorter Period Permitted for Determining Applicable Large Employer Status for 2015

An applicable large employer is, with respect to a calendar year, an employer that employed an average of at least 50 full-time employees (including FTEs) on business days during the preceding calendar year. See section 4980H(c)(2); § 54.4980H–2.

Similar to the transition guidance provided in section IX.E of the preamble to the proposed regulations, for the 2015 calendar year, an employer may determine its status as an applicable large employer by reference to a period of at least six consecutive calendar months, as chosen by the employer, during the 2014 calendar year (rather than the entire 2014 calendar year). Thus, an employer may determine whether it is an applicable large employer for 2015 by determining whether it employed an average of at least 50 full-time employees (including FTEs) on business days during any consecutive six-month period in 2014. Whether an employer meets the requirements of the seasonal worker exception, as described in section V.C of this preamble, for purposes of determining applicable large employer status for 2015 is based on the calendar year, rather than on the calendar months chosen by the employer under the 2015 applicable large employer transition guidance, if applicable. See section V of this preamble for a discussion of the determination of status as an applicable large employer.

This guidance allows employers to choose to use either a period to prepare to count their employees or a period afterward to ascertain and implement the results of the determination, or both. For example, an employer could use at least six months through August 2014 to determine its applicable large employer status and, if it is an applicable large employer, the period from September through December 2014 to make any needed adjustments to its plan (or to establish a plan).

Commenters noted that, under the transition guidance for applicable large employer status in 2014, the hours of service (or lack of hours of service) during the summer season could be taken into account by schools in determining applicable large employer status even though, during the summer, employees may provide no formal, in-school service. These commenters expressed concern that this would affect the educational employer's total number of full-time employees and status as an applicable large employer by overweighting the summer period in relation to the non-summer academic year. The Treasury Department and the IRS understand this concern and have considered various options for addressing these comments in developing this transition guidance, but have concluded that the options for addressing this concern (such as basing the rule on non-consecutive months or applying an employee-by-employee rule such as the employment break period rule set forth in § 54.4980H–3(d)(6)(ii)(B)) would add more complexity and administrative burden than is justified for a rule that applies only for 2015.

Also note that in addition to this transition rule, as described in section V.F of this preamble, the final regulations provide with respect to an employee who was not offered coverage at any point in the prior calendar year, if an employer that is an applicable large employer for the first time offers the employee coverage at or before April 1 of the first year in which the employer is an applicable large employer, the employer will not be subject to an assessable payment under section 4980H by reason of its failure to offer coverage to the employee for January through March of that year, provided that in order to avoid an assessable payment under section 4980H(b), the coverage offered on or before April 1 provides MV.

In addition, section XV.D.6 of this preamble provides 2015 transition relief for certain applicable large employers with fewer than 100 full-time employees (including FTEs). The rule described in this section XV.D.3 of the preamble may be used by an applicable large employer to determine its number of full-time employees (including FTEs) for purposes of the transition rule set forth in section XV.D.6 of this preamble.

4. Offer of Coverage for January 2015

The final regulations provide, in general, that if an applicable large employer member fails to offer coverage to a full-time employee for any day of a calendar month, that employee is treated as not offered coverage during that entire month. See § 54.4980H–4(c).

The Treasury Department and the IRS understand that many employers offer coverage for a new year effective as of the first day of the first pay period beginning on or after the first day of the year, and that questions have arisen as to whether a full-time employee will be treated as having been offered coverage for the first month to which section 4980H applies if the offer of coverage applies no later than the first day of the first payroll period that begins in that month.

Solely for purposes of January 2015, if an applicable large employer member offers coverage to a full-time employee no later than the first day of the first payroll period that begins in January 2015, the employee will be treated as having been offered coverage for January 2015. This transition guidance, which was not contained in the preamble to the proposed regulations, applies only for January 2015.

5. Coverage for Dependents

In order to avoid a potential assessable payment under section 4980H, an applicable large employer member must offer coverage to its full-time employees and the full-time employees' dependents. To provide employers sufficient time to expand their health plans to add dependent coverage, section IX.F of the preamble to the proposed regulations provides that any employer that takes steps during its plan year that begins in 2014 (2014 plan year) toward satisfying the section 4980H provisions relating to offering coverage to full-time employees' dependents will not be liable for any assessable payment under section 4980H solely on account of a failure to offer coverage to the dependents for that plan year.

This relief is extended to plan years that begin in 2015 (2015 plan years). It applies to employers for the 2015 plan year with respect to plans under which (1) dependent coverage is not offered, (2) dependent coverage that does not constitute MEC is offered, or (3) dependent coverage is offered for some, but not all, dependents.

The relief is not available to the extent the employer offered dependent coverage during either the plan year that begins in 2013 (2013 plan year) or the 2014 plan year (meaning the relief is not available to the extent the employer had offered dependent coverage during either of those plan years and subsequently dropped that offer of coverage). If coverage was offered to some, but not all, dependents during the 2013 or 2014 plan year, the relief as extended applies only with respect to dependents who were not offered coverage at any time during the 2013 or 2014 plan year (in other words, the relief as extended applies only with respect to dependents who were without an offer of coverage from the employer in both the 2013 and 2014 plan years). In addition, the relief is available only if the employer takes steps during the 2014 or 2015 plan year (or both) to extend coverage under the plan to dependents not offered coverage during the 2013 or 2014 plan year (or both). References in this section XV.D.5 of the preamble to dependents refer to dependents of the employer's full-time employees, and references to coverage (other than specific references to coverage that does not constitute MEC) refer to MEC. For a discussion of the definition of dependent under the final regulations, including the treatment of stepchildren and foster children, see section XI of this preamble.

6. 2015 Transition Relief for Applicable Large Employers with Fewer than 100 Full-Time Employees (Including FTEs)

The Treasury Department and the IRS understand that application of section 4980H will involve changes for applicable large employers that did not previously offer coverage, or that did not offer affordable, minimum value coverage. A large percentage of those employers are in the smaller size range, such as those with fewer than 100 full-time employees (including FTEs). To assist these employers in transitioning into compliance with section 4980H, the transition relief described below is provided for all of 2015 plus, in the case of any non-calendar plan year that begins in 2015 (2015 plan year), the portion of that 2015 plan year that falls in 2016. For employers eligible for the transition relief described in this section XV.D.6, no assessable payment under section 4980H(a) or (b) will apply for any calendar month during 2015 or any calendar month during the portion of the 2015 plan year that falls in 2016.

a. Eligibility conditions for transition relief

An employer is eligible for the transition relief described in this section XV.D.6 if it satisfies the following conditions:

(1) *Limited Workforce Size*. The employer employs on average at least 50 full-time employees (including FTEs) but fewer than 100 full-time employees (including FTEs) on business days during 2014. For this purpose, the determination of the number of full-time employees (including FTEs) is made in accordance with the otherwise applicable rules for determining status as an applicable large employer.[14]

(2) *Maintenance of Workforce and Aggregate Hours of Service*. During the period beginning on February 9, 2014, and ending on December 31, 2014, the employer does not reduce the size of its workforce or the overall hours of service of its employees in order to satisfy the workforce size condition set forth in paragraph (1) of this section XV.D.6. A reduction in workforce size or overall hours of service for bona fide business reasons will not be considered to have been made in order to satisfy the workforce size condition. For example, reductions of workforce size or overall hours of service because of business activity such as the sale of a division, changes in the economic marketplace in which the employer operates, terminations of employment for poor performance, or other similar changes unrelated to eligibility for the transition relief provided in this section XV.D.6 are for bona fide business reasons and will not affect eligibility for that transition relief.

(3) *Maintenance of Previously Offered Health Coverage*. Except as otherwise provided in this paragraph (3), during the coverage maintenance period the employer does not eliminate or materially reduce the health coverage, if any, it offered as of February 9, 2014. For purposes of this paragraph (3), in no event will an employer be treated as eliminating or materially reducing health coverage if (i) it continues to offer each employee who is eligible for coverage during the coverage maintenance period an employer contribution toward the cost of employee-only coverage that either (A) is at least 95 percent of the dollar amount of the contribution toward such coverage that the employer was offering on February 9, 2014, or (B) is the same (or a higher) percentage of the cost of coverage that the employer was offering to contribute toward coverage on February 9, 2014; (ii) in the event there is a change in benefits under the employee-only coverage offered, that coverage provides minimum value after the change; and (iii) the employer does not alter the terms of its group health plans to narrow or reduce the class or classes of employees (or the employees' dependents) to whom coverage under those plans was offered on February 9, 2014. For purposes of this paragraph, the term *coverage maintenance period* means (1) for an employer with a calendar year plan, the period beginning on February 9, 2014, and ending on December 31, 2015, and (2) for an employer with a non-calendar year plan, the period beginning on February 9, 2014, and ending on the last day of the plan year that begins in 2015.

[14]The rules for determining status as an applicable large employer include application of the aggregation rules under section 414 (see § 54.4980H–1(a)(16)), the rule regarding employers whose workforce exceeds the applicable threshold (which for this purpose is 99) for 120 days or fewer during the calendar year due to the employment of seasonal workers (see § 54.4980H–2(b)(2)), and the transition relief permitting the use of any consecutive month period during 2014 of at least six months in lieu of the entire calendar year as provided in section XV.D.3 of this preamble.

For example, if on February 9, 2014, an employer was contributing $300 per month for coverage that costs $400 per month for employee-only coverage, and the employer continues to offer to contribute $300 per month after the cost of employee-only coverage increases to $425 per month for the plan year beginning on July 1, 2014, the increase in cost to the employee will not be treated for this purpose as an elimination or material reduction of health coverage offered.

(4) *Certification of Eligibility for Transition Relief*. The applicable large employer certifies on a prescribed form that it meets the eligibility requirements set forth in paragraphs (1) through (3). The forthcoming final regulations under section 6056 are expected to provide that an applicable large employer, or an applicable large employer member, that otherwise qualifies for the transition relief described in this section XV.D.6 will provide this certification as part of the transmittal form it is required to file with the IRS under the section 6056 regulations, in accordance with the instructions to that transmittal form. See section III of the preamble regarding section 6056.

b. Application of transition relief to non-calendar year plans

The transition relief described in this section XV.D.6 applies to all calendar months of 2015 plus any calendar months of 2016 that fall within the 2015 plan year. It is not available for an employer that modifies the plan year of its plan after February 9, 2014, to begin on a later calendar date (for example, changing the start date of the plan year from January 1 to December 1). Notwithstanding paragraph (a)(3) of this section XV.D.6, an employer with a non-calendar year plan meeting the coverage maintenance period requirements for 2015 may be eligible for the relief for 2015 even if the employer does not meet the coverage maintenance period requirements later (during the portion of the 2015 plan year falling in 2016).

c. Application of transition relief to new employers

As described in section V.B of this preamble, an employer that was not in existence on any day of the previous calendar year may be an applicable large employer for the current calendar year if the employer is reasonably expected to employ an average of at least 50 full-time employees (including FTEs) on business days during the current calendar year and it actually employs an average of at least 50 full-time employees (including FTEs) on business days during the calendar year. For employers first coming into existence in 2015 that are applicable large employers under the standard in the preceding sentence, the relief described in this section XV.D.6 applies if (1) the employer reasonably expects to employ and actually employs fewer than 100 full-time employees (including FTEs) on business days during 2015, (2) the employer reasonably expects to meet and actually meets the maintenance standards described in paragraphs (2) and (3) above, as measured from the date the employer is first in existence, and (3) the employer certifies in the manner described in paragraph (4) above.

d. Coordination with other transition relief

For periods on or after January 1, 2016 (or, if applicable, for any period after the last day of the 2015 plan year), the transition relief set forth in section XV.D.1 (non-calendar plan years), section XV.D.2 (shorter measurement periods permitted for stability period starting during 2015), section XV.D.4 (offer of coverage for January 2015), section XV.D.5 (coverage for dependents), and section XV.D.7 (limited 2015 section 4980H(a) transition relief) of the preamble will not be available. The transition relief listed in the prior sentence is available only with respect to 2015 or, if applicable, the 2015 plan year and does not apply to an applicable large employer that is eligible for the relief described in this section XV.D.6 because that eligible employer will first become subject to a potential assessable payment under section 4980H after 2015 or, if applicable, after the 2015 plan year and, accordingly, already will have had the benefit of an extra year to plan for and implement changes. However, an employer may use the rule set forth in section XV.D.3 of the preamble (shorter period in 2014 permitted for determining applicable large employer status for 2015) in determining applicable large employer status and full-time employee count for 2015 (but not for any subsequent year).[15]

e. Example

The following example illustrates the transition relief described in this section XV.D.6 of the preamble:

(i) *Facts*. As of February 9, 2014, Employer A sponsors a group health plan with a calendar year plan year under which 40 of its full-time employees are offered coverage with an employer contribution of $300 per month for employee-only coverage. The offer of coverage is affordable with respect to some, but not all, of Employer A's full-time employees. During the period from February 9, 2014, through December 31, 2014, two of Employer A's employees voluntarily terminate employment and Employer A terminates three employees because of the nonrenewal of a customer contract but does not otherwise reduce the size of its workforce or reduce any employee's hours of service. Had those five employees continued in employment throughout 2014, the employer would have had an average of 100 full-time employees (including FTEs) on business days in 2014. However, as a result of the terminations, it had an average of only 97 full-time employees (including FTEs) for business days in 2014. During the coverage maintenance period, Employer A does not change the eligibility requirements for the group health plan (including not amending it to eliminate its existing health coverage for dependents) and continues to make an employer contribution of $300 per month toward the cost of employee-only coverage that provides minimum valve. Employer A certifies in a timely manner as to its eligibility for the transition relief.

(ii) *Conclusion*. Employer A will not be subject to an assessable payment under section 4980H(a) or (b) for 2015.

7. Limited 2015 Section 4980H(a) Transition Relief

a. Offers of coverage to at least 70 percent (rather than 95 percent) of full-time employees (and their dependents)

For purposes of section 4980H(a), the final regulations provide that an applica-

[15] Section 54.4980H–2(b)(5) of the final regulations provides a transition rule for an employer's first year as an applicable large employer, subject to certain conditions. Because an employer qualifies for the relief set forth in § 54.4980H–2(b)(5) only for the first year that the employer is an applicable large employer, the relief set forth in § 54.4980H–2(b)(5) will not be available to an applicable large employer that is eligible for the relief described in this section XV.D.6 for the first year for which the employer may be subject to an assessable payment under section 4980H (generally 2016).

ble large employer member is treated as offering coverage to its full-time employees (and their dependents) for a month if, for that month, it offers coverage to all but five percent or, if greater, five, of its full-time employees. As provided in § 54.4980H–4(a), an employee is treated as having been offered coverage only if the employer also offered coverage to that employee's dependents. But see section XV.D.5 of this preamble for transition relief for a failure to offer coverage to dependents for the 2015 plan year.

As further transition relief, for each calendar month during 2015 and any calendar months during the 2015 plan year that fall in 2016, an applicable large employer member that offers coverage to at least 70 percent (or that fails to offer to no more than 30 percent) of its full-time employees (and, to the extent required under § 54.4980H–4(a) and the transition relief in section XV.D.5 of this preamble, their dependents) will not be subject to an assessable payment under section 4980H(a). Applicable large employer members qualifying for the transition relief set forth in this section XV.D.7.a continue to be subject to a potential assessable payment under section 4980H(b).

b. Calculation of assessable payments under section 4980H(a) for applicable large employers with 100 or more full-time employees (including FTEs) for 2015

In general, an assessable payment under section 4980H(a) is equal to the number of all full-time employees (excluding 30 full-time employees) multiplied by one-twelfth of $2,000 for each calendar month. For purposes of the liability calculation under section 4980H(a), with respect to each calendar month, an applicable large employer member's number of full-time employees is reduced by that member's allocable share of 30. Accordingly, an applicable large employer with 50 full-time employees that is subject to an assessable payment under section 4980H(a) may be subject to an assessable payment based on 20 employees (that is, 50 minus 30) times one-twelfth of $2,000 for each calendar month. An applicable large employer member's allocation is equal to 30 allocated ratably among all members of the applicable large employer on the basis of the number of full-time employees employed by each applicable large employer member during the calendar month. See § 54.4980H–4(e).

For 2015 plus any calendar months of 2016 that fall within the employer's 2015 plan year, if an applicable large employer with 100 or more full-time employees (including FTEs) on business days during 2014 (or an applicable large employer member that is part of such an applicable large employer) is subject to an assessable payment under section 4980H(a), the assessable payment under section 4980H(a) with respect to the transition relief period will be calculated by reducing an applicable large employer member's number of full-time employees by that member's allocable share of 80 rather than 30. The rules set forth in § 54.4980H–4(e) apply with respect to allocation of the reduction by 80 full-time employees for the applicable large employer. For this transition relief period, the aggregate amount of assessable payment determined under section 4980H(b) for an applicable large employer member also may not exceed the potential assessable payment under section 4980H(a), including the reduction by the ratable portion of 80 as set forth in this paragraph, for that applicable large employer member.[16]

c. Application to non-calendar year plans

The transition relief described in this section XV.D.7 applies to all calendar months of 2015 plus any calendar months of 2016 that fall within the employer's 2015 plan year, and is available for an employer only if it did not modify the plan year of its plan after February 9, 2014, to begin on a later calendar date (for example, changing the start date of the plan year from January 1 to December 1).

d. Coordination with other transition relief

The relief described in this section XV.D.7 of the preamble applies in addition to the forms of transition relief described in section XV.D.1 (non-calendar plan years), section XV.D.2 (shorter measurement periods permitted for stability period starting during 2015), section XV.D.3 (shorter period permitted in 2014 for determining applicable large employer status for 2015), section XV.D.4 (offer of coverage for January 2015), and section XV.D.5 (coverage for dependents) of this preamble.

E. *Interim guidance with respect to multiemployer arrangements*

In response to commenters' requests for special rules for employers participating in multiemployer plans in view of such plans' unique operating structures, section IX.D of the preamble to the proposed regulations, as corrected, contains transition guidance that is intended to provide an administratively feasible means for employers that contribute to multiemployer plans to comply with section 4980H.

Pursuant to this preamble, employers may rely on the interim guidance described in this section XV.E. This interim guidance is intended to continue the transition guidance originally set forth in section IX.D of the preamble to the proposed regulations, as corrected, and as clarified in this preamble. Any future guidance that limits the scope of the interim guidance will be applied prospectively and will apply no earlier than January 1 of the calendar year beginning at least six months after the date of issuance of the guidance.

This interim guidance applies to an applicable large employer member that is required by a collective bargaining agreement or an appropriate related participation agreement to make contributions, with respect to some or all of its employees, to a multiemployer plan that offers, to individuals who satisfy the plan's eligibility conditions, coverage that is affordable and provides MV, and that offers cover-

[16]The number 80 applies for purposes of the 2015 transition rule in lieu of the number 30 that applies under the general rule because this maintains the same 20-full-time-employee difference between the applicable threshold number (50 under the general rule; 100 under the 2015 transition rule) and the number of full-time employees (30 under the general rule; 80 under the 2015 transition rule) by which the applicable large employer's number of full-time employees is reduced.

age to those individuals' dependents. Under this interim guidance, the applicable large employer member will not be treated, with respect to employees for whom the employer is required by the collective bargaining agreement or appropriate related participation agreement to make contributions to the multiemployer plan, as failing to offer the opportunity to enroll in MEC to full-time employees (and their dependents) for purposes of section 4980H(a), and will not be subject to an assessable payment under section 4980H(b). For purposes of this section XV.E of the preamble, whether the employee is a full-time employee is determined under section 4980H(c)(4), whether coverage is affordable is determined under section 36B(c)(2)(C)(i), and whether coverage provides MV is determined under section 36B(c)(2)(C)(ii).

For purposes of determining whether coverage under the multiemployer plan is affordable, employers participating in the plan may use any of the affordability safe harbors set forth in the final regulations. Coverage under a multiemployer plan will also be considered affordable with respect to a full-time employee if the employee's required contribution, if any, toward self-only health coverage under the plan does not exceed 9.5 percent of the wages reported to the qualified multiemployer plan, which may be determined based on actual wages or an hourly wage rate under the applicable collective bargaining agreement or participation agreement.

If any assessable payment were due under section 4980H, it would be payable by a participating applicable large employer member and that member would be responsible for identifying its full-time employees for this purpose (which would be based on hours of service for that employer). If the applicable large employer member contributes to one or more multiemployer plans and also maintains a single employer plan, the interim guidance applies to each multiemployer plan but not to the single employer plan.

One commenter asked whether the rule set out in section IX.D of the preamble to the proposed regulations, as corrected, applies to non-federal governmental multiemployer plans. The commenter noted that the proposed regulations do not define multiemployer plan but that section 414(f)(1) defines a multiemployer plan as a plan (A) to which more than one employer is required to contribute, (B) which is maintained pursuant to one or more collective bargaining agreements between one or more employee organizations and more than one employer, and (C) which satisfies such other requirements as the Secretary of Labor may prescribe by regulation. The commenter asked whether the rule set out in section IX.D of the preamble to the proposed regulations, as corrected, applies to public sector multiemployer plans which are not subject to the jurisdiction of DOL. The rule set out in section IX.D of the preamble to the proposed regulations and in this section of the preamble applies to a multiemployer plan that is not subject to the jurisdiction of DOL if the plan meets the requirements of section 414(f)(1)(A) and (B).

XVI. *Effective Dates and Reliance*

Section 1513(d) of the Affordable Care Act provides that section 4980H applies to months beginning after December 31, 2013; however, Notice 2013–45 provides transition relief from section 4980H for 2014.

These final regulations are effective February 12, 2014. These final regulations are applicable for periods after December 31, 2014. Employers may rely on these final regulations for periods before January 1, 2015. If and to the extent an employer has relied on Notice 2012–58, the employer may continue to rely on Notice 2012–58 to the extent reliance is provided in section IV of that notice.

Availability of IRS Documents

The IRS notices and other IRS guidance cited in this preamble are available in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b)).

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866, as supplemented by Executive Order 13563. Therefore, a regulatory assessment is not required. It has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulations do not impose a collection of information requirement on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) (RFA) does not apply.

Pursuant to section 7805(f) of the Code, the proposed regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration (SBA Chief Counsel for Advocacy) for comment on their impact on small business, and the SBA Chief Counsel for Advocacy submitted comments on the regulations. The SBA Chief Counsel for Advocacy disagreed with the statement that the RFA does not apply to the proposed regulations because the regulations do not impose a collection of information on small entities. Specifically, the SBA Chief Counsel for Advocacy stated that the proposed regulations impose a collection because they require employers to maintain records for a number of calculations and the determination of whether employers are subject to section 4980H, including calculating full-time employees and FTEs and calculating affordability. However, the regulations do not contain any recordkeeping requirement. For purposes of the RFA, a recordkeeping requirement is a mandate to maintain *specified* records. 5 U.S.C. 601(8). Therefore, to constitute a recordkeeping requirement, the mandate to maintain specified records must be a requirement in addition to the general requirement in section 6001 that taxpayers must keep adequate books and records to support what they reported on their return. Thus, because a recordkeeping requirement is one that requires *specified* records, a regulation that does not require that particular records be maintained, but nonetheless prompts some taxpayers to maintain records consistent with the provisions of section 6001, does not impose a recordkeeping requirement. Neither the proposed nor final regulations require employers to maintain any *specified* records. Rather, the preambles to both the final and the proposed regulations provide that the otherwise generally applicable substantiation and recordkeeping requirements in section 6001 apply.

Drafting Information

The principal authors of these final regulations are Kathryn Johnson and Shad Fagerland of the Office of the Division

Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). Other personnel from the Treasury Department and the IRS participated in the development of the regulations.

List of Subjects

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Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1, 54, and 301 are amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 1.1361–4 is amended as follows:

1. In paragraph (a)(8)(i)(C), the language "and 4412; and" is removed and "and 4412;" is added in its place.

2. In paragraph (a)(8)(i)(D), the language "or 6427." is removed and "or 6427; and" is added in its place.

3. Paragraph (a)(8)(i)(E) is added.

4. In paragraph (a)(8)(ii), the language "January 1, 2008." is removed and "January 1, 2008, except that paragraph (a)(8)(i)(E) of this section applies for periods after December 31, 2014." is added in its place.

The addition reads as follows:

§ 1.1361–4 Effect of QSub election.

(a) * * *

(8) * * *

(i) * * *

(E) Assessment and collection of an assessable payment imposed by section 4980H and reporting required by section 6056.

* * * * *

PART 54—PENSION EXCISE TAXES

Par. 3. The authority citation for part 54 is amended by adding entries in numerical order to read as follows:

Authority: 26 U.S.C. 7805 * * *

Section 54.4980H–3 is also issued under 26 U.S.C. 4980H(c)(4)(B); * * *

Par. 4. Sections 54.4980H–0, 54.4980H–1, 54.4980H–2, 54.4980H–3, 54.4980H–4, 54.4980H–5, and 54.4980H–6 are added to read as follows:

Sec.

* * * * *

54.4980H–0 Table of contents.

54.4980H–1 Definitions.

54.4980H–2 Applicable large employer and applicable large employer member.

54.4980H–3 Determining full-time employees.

54.4980H–4 Assessable payments under section 4980H(a).

54.4980H–5 Assessable payments under section 4980H(b).

54.4980H–6 Administration and procedure.

* * * * *

§ 54.4980H–0 Table of contents.

This section lists the table of contents for §§ 54.4980H–1 through 54.4980H-6.

§ 54.4980H–1 Definitions.

§ 54.4980H–2 Applicable large employer and applicable large employer member.

§ 54.4980H–3 Determining full-time employees.

(2) Hourly employees calculation.

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(c) Monthly measurement method.

(1) In general.

(2) Employee first otherwise eligible for an offer of coverage.

(3) Use of weekly periods.

(4) Employees rehired after termination of employment or resuming service after other absence.

(5) Examples.

(d) Look-back measurement method.

(1) Ongoing employees.

(2) New non-variable hour, new non-seasonal and new non-part-time employees.

(3) New variable hour employees, new seasonal employees, and new part-time employees.

(4) Transition from new variable hour employee, new seasonal employee, or new part-time employee to ongoing employee.

(5) Examples.

(6) Employees rehired after termination of employment or resuming service after other absence.

(e) Use of the look-back measurement method and the monthly measurement method for different categories of employees.

(f) Changes in employment status resulting in a change in full-time employee determination method.

(1) Change in employment status from a position to which a look-back measurement method applies to a position to which the monthly measurement method applies, or vice versa.

(2) Special rule for certain employees to whom minimum value coverage has been continuously offered.

(g) Nonpayment or late payment of premiums.

(h) Additional guidance.

(i) Effective/applicability date.

§ 54.4980H–4 Assessable payments under section 4980H(a).

(a) In general.

(b) Offer of coverage.

(1) In general.

(2) Offer of coverage on behalf of another entity.

(c) Partial calendar month.

(d) Application to applicable large employer member.

(e) Allocated reduction of 30 full-time employees.

(f) Example.

(g) Additional guidance.

(h) Effective/applicability date.

§ 54.4980H–5 Assessable payments under section 4980H(b).

(a) In general.

(b) Offer of coverage.

(c) Partial calendar month.

(d) Applicability to applicable large employer member.

(e) Affordability.

(1) In general.

(2) Affordability safe harbors for section 4980H(b) purposes.

(f) Additional guidance.

(g) Effective/applicability date.

§ 54.4980H–6 Administration and procedure.

(a) In general.

(b) Effective/applicability date.

§ 54.4980H–1 Definitions.

(a) *Definitions*. The definitions in this section apply only for purposes of this section and §§ 54.4980H–2 through 54.4980H-6.

(1) *Administrative period*. The term *administrative period* means an optional period, selected by an applicable large employer member, of no longer than 90 days beginning immediately following the end of a measurement period and ending immediately before the start of the associated stability period. The administrative period also includes the period between a new employee's start date and the beginning of the initial measurement period, if the initial measurement period does not begin on the employee's start date.

(2) *Advance credit payment*. The term *advance credit payment* means an advance payment of the premium tax credit as provided in Affordable Care Act section 1412 (42 U.S.C. 18082).

(3) *Affordable Care Act*. The term *Affordable Care Act* means the Patient Protection and Affordable Care Act, Public Law 111–148 (124 Stat. 119 (2010)), and the Health Care and Education Reconciliation Act of 2010, Public Law 111–152 (124 Stat. 1029 (2010)), as amended by the Medicare and Medicaid Extenders Act of 2010, Public Law 111–309 (124 Stat. 3285 (2010)), the Comprehensive 1099 Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011, Public Law 112–9 (125 Stat. 36 (2011)), the Department of Defense and Full-Year Continuing Appropriations Act, 2011, Public Law 112–10 (125 Stat. 38 (2011)), and the 3% Withholding Repeal and Job Creation Act, Public Law 112–56 (125 Stat. 711 (2011)).

(4) *Applicable large employer*. The term *applicable large employer* means, with respect to a calendar year, an employer that employed an average of at least 50 full-time employees (including full-time equivalent employees) on business days during the preceding calendar year. For rules relating to the determination of applicable large employer status, see § 54.4980H–2.

(5) *Applicable large employer member*. The term *applicable large employer member* means a person that, together with one or more other persons, is treated as a single employer that is an applicable large employer. For this purpose, if a person, together with one or more other persons, is treated as a single employer that is an applicable large employer on any day of a calendar month, that person is an applicable large employer member for that calendar month. If the applicable large employer comprises one person, that one person is the applicable large employer member. An applicable large employer member does not include a person that is not an employer or only an employer of employees with no hours of service for the calendar year. For rules for government entities, and churches, or conventions or associations of churches, see § 54.4980H–2(b)(4).

(6) *Applicable premium tax credit*. The term *applicable premium tax credit* means any premium tax credit that is allowed or paid under section 36B and any advance payment of such credit.

(7) *Bona fide volunteer*. The term *bona fide volunteer* means an employee of a government entity or an organization described in section 501(c) that is exempt from taxation under section 501(a) whose only compensation from that entity or organization is in the form of—

(i) Reimbursement for (or reasonable allowance for) reasonable expenses incurred in the performance of services by volunteers, or

(ii) Reasonable benefits (including length of service awards), and nominal fees, customarily paid by similar entities in connection with the performance of services by volunteers.

(8) *Calendar month*. The term *calendar month* means one of the 12 full months named in the calendar, such as January, February, or March.

(9) *Church or a convention or association of churches*. The term *church or a convention or association of churches* has the same meaning as provided in § 1.170A–9(b).

(10) *Collective bargaining agreement*. The term *collective bargaining agreement* means an agreement that the Secretary of Labor determines to be a collective bargaining agreement, provided that the health benefits provided under the collective bargaining agreement are the subject of good faith bargaining between employee representatives and one or more employers, and the agreement between employee representatives and one or more employers satisfies section 7701(a)(46).

(11) *Cost-sharing reduction*. The term *cost-sharing reduction* means a cost-sharing reduction and any advance payment of the reduction as defined under section 1402 of the Affordable Care Act and 45 CFR 155.20.

(12) *Dependent*. The term *dependent* means a child (as defined in section 152(f)(1) but excluding a stepson, stepdaughter or an eligible foster child (and excluding any individual who is excluded from the definition of dependent under section 152 by operation of section 152(b)(3))) of an employee who has not attained age 26. A child attains age 26 on the 26th anniversary of the date the child was born. A child is a dependent for purposes of section 4980H for the entire calendar month during which he or she attains age 26. Absent knowledge to the contrary, applicable large employer members may rely on an employee's representation about that employee's children and the ages of those children. The term *dependent* does not include the spouse of an employee.

(13) *Educational organization*. The term *educational organization* means an entity described in § 1.170A–9(c)(1), whether or not described in section 501(c)(3) and tax-exempt under section 501(a). Thus, the term *educational organization* includes taxable entities, tax-exempt entities and government entities.

(14) *Eligible employer-sponsored plan*. The term *eligible employer-sponsored plan* has the same meaning as provided under section 5000A(f)(2) and the regulations thereunder and any other applicable guidance.

(15) *Employee*. The term *employee* means an individual who is an employee under the common-law standard. See § 31.3401(c)–1(b). For purposes of this paragraph (a)(15), a leased employee (as defined in section 414(n)(2)), a sole proprietor, a partner in a partnership, a 2-percent S corporation shareholder, or a worker described in section 3508 is not an employee.

(16) *Employer*. The term *employer* means the person that is the employer of an employee under the common-law standard. See § 31.3121(d)–1(c). For purposes of determining whether an employer is an applicable large employer, all persons treated as a single employer under section 414(b), (c), (m), or (o) are treated as a single employer. Thus, all employees of a controlled group of entities under section 414(b) or (c), an affiliated service group under section 414(m), or an entity in an arrangement described under section 414(o), are taken into account in determining whether the members of the controlled group or affiliated service group together are an applicable large employer. For purposes of determining applicable large employer status, the term *employer* also includes a predecessor employer (see paragraph (a)(36) of this section) and a successor employer.

(17) *Employment break period*. The term *employment break period* means a period of at least four consecutive weeks (disregarding special unpaid leave), measured in weeks, during which an employee of an educational organization is not credited with hours of service for an applicable large employer.

(18) *Exchange*. The term *Exchange* means an Exchange as defined in 45 CFR 155.20.

(19) *Federal poverty line*. The term *federal poverty line* means for a plan year any of the poverty guidelines (updated periodically in the **Federal Register** by the Secretary of Health and Human Services under the authority of 42 U.S.C. 9902(2)) in effect within six months before the first day of the plan year of the applicable large employer member's health plan, as selected by the applicable large employer member.

(20) *Form W-2 wages*. The term *Form W-2 wages* with respect to an employee refers to the amount of wages as defined under section 3401(a) for the applicable calendar year (required to be reported in Box 1 of the Form W-2 (Wage and Tax Statement)) received from an applicable large employer.

(21) *Full-time employee*—(i) *In general*. The term *full-time employee* means, with respect to a calendar month, an employee who is employed an average of at least 30 hours of service per week with an employer. For rules on the determination of whether an employee is a full-time employee, including a description of the look-back measurement method and the monthly measurement method, see § 54.4980H–3. The look-back measurement method for identifying full-time employees is available only for purposes of determining and computing liability under section 4980H and not for the purpose of determining status as an applicable large employer under § 54.4980H–2.

(ii) *Monthly equivalency*. Except as otherwise provided in paragraph (a)(21)(iii) of this section, 130 hours of service in a calendar month is treated as the monthly equivalent of at least 30 hours of service per week, and this 130 hours of service monthly equivalency applies for both the look-back measurement method and the monthly measurement method for determining full-time employee status.

(iii) *Determination of full-time employee status using weekly rule under the monthly measurement method*. Under the optional weekly rule set forth in § 54.4980H–3(c)(3), full-time employee status for certain calendar months is based on hours of service over four weekly periods and for certain other calendar months is based on hours of service over five weekly periods. With respect to a month with four weekly periods, an employee with at least 120 hours of service is a full-time employee, and with respect to a month with five weekly periods, an employee with at least 150 hours of service is a full-time employee. For purposes of this rule, the seven continuous calendar days that constitute a week (for example Sunday through Saturday) must be consistently applied for all calendar months of the calendar year.

(22) *Full-time equivalent employee (FTE)*. The term *full-time equivalent employee*, or *FTE*, means a combination of employees, each of whom individually is not treated as a full-time employee because he or she is not employed on average at least 30 hours of service per week with an employer, who, in combination, are counted as the equivalent of a full-time employee solely for purposes of determining whether the employer is an applicable large employer. For rules on the method for determining the number of an employer's full-time equivalent employees, or FTEs, see § 54.4980H–2(c).

(23) *Government entity*. The term *government entity* means the government of the United States, any State or political subdivision thereof, any Indian tribal government (as defined in section 7701(a)(40)) or subdivision of an Indian tribal government (determined in accordance with section 7871(d)), or any agency or instrumentality of any of the foregoing.

(24) *Hour of service*—(i) *In general*. The term *hour of service* means each hour for which an employee is paid, or entitled to payment, for the performance of duties for the employer; and each hour for which an employee is paid, or entitled to payment by the employer for a period of time during which no duties are performed due to vacation, holiday, illness, incapacity (including disability), layoff, jury duty, military duty or leave of absence (as defined in 29 CFR 2530.200b–2(a)). For the rules for determining an employee's hours of service, see § 54.4980H–3.

(ii) *Excluded hours*—(A) *Bona fide volunteers*. The term *hour of service* does not include any hour for services performed as a bona fide volunteer.

(B) *Work-study program*. The term *hour of service* does not include any hour for services to the extent those services are performed as part of a Federal Work-Study Program as defined under 34 CFR 675 or a substantially similar program of a State or political subdivision thereof.

(C) *Services outside the United States*. The term *hour of service* does not include any hour for services to the extent the compensation for those services constitutes income from sources without the United States (within the meaning of sections 861 through 863 and the regulations thereunder).

(iii) *Service for other applicable large employer members*. In determining hours of service and status as a full-time employee for all purposes under section 4980H, an hour of service for one applicable large employer member is treated as an hour of service for all other applicable large employer members for all periods during which the applicable large employer members are part of the same group of employers forming an applicable large employer.

(25) *Initial measurement period*. The term *initial measurement period* means a period selected by an applicable large employer member of at least three consecutive months but not more than 12 consecutive months used by the applicable large employer as part of the look-back measurement method in § 54.4980H–3(d).

(26) *Limited non-assessment period for certain employees*. References to the *limited non-assessment period for certain employees* refers to the limited period during which an employer will not be subject to an assessable payment under section 4980H(a), and in certain cases section 4980H(b), with respect to an employee as set forth in—

(i) Section 54.4980H–2(b)(5) (regarding the transition rule for an employer's first year as an applicable large employer),

(ii) Section 54.4980H–3(c)(2) (regarding the application of section 4980H for the three full calendar month period beginning with the first full calendar month in which an employee is first otherwise eligible for an offer of coverage under the monthly measurement method),

(iii) Section 54.4980H–3(d)(2)(iii) (regarding the application of section 4980H during the initial three full calendar months of employment for an employee reasonably expected to be a full-time employee at the start date, under the look-back measurement method),

(iv) Section 54.4980H–3(d)(3)(iii) (regarding the application of section 4980H during the initial measurement period to a new variable hour employee, seasonal employee or part-time employee determined to be employed on average at least 30 hours of service per week, under the look-back measurement method),

(v) Section 54.4980H–3(d)(3)(vii) (regarding the application of section 4980H following an employee's change in employment status to a full-time employee during the initial measurement period, under the look-back measurement method), and

(vi) Section 54.4980H–4(c) and § 54.4980H–5(c) (regarding the application of section 4980H to the calendar month in which an employee's start date occurs on a day other than the first day of the calendar month).

(27) *Minimum essential coverage*. The term *minimum essential coverage*, or *MEC*, has the same meaning as provided in section 5000A(f) and any regulations or other guidance thereunder.

(28) *Minimum value*. The term *minimum value* has the same meaning as provided in section 36B(c)(2)(C)(ii) and any regulations or other guidance thereunder.

(29) *Month*. The term *month* means—

(i) A *calendar month* as defined in paragraph (a)(8) of this section, or

(ii) The period that begins on any date following the first day of a calendar month and that ends on the immediately preceding date in the immediately following calendar month (for example, from February 2 to March 1 or from December 15 to January 14).

(30) *New employee*. Under the look-back measurement method, the term *new employee* means an employee who has been employed by an applicable large employer for less than one complete standard measurement period; for treatment of the employee as a new employee or continuing employee under the look-back measurement method following a period for which no hours of service are earned, see the rehire and continuing employee rules at § 54.4980H–3(d)(6). Under the monthly measurement method, the term *new employee* means an employee who either has not previously been employed by the applicable large employer or has previously been employed by the applica-

ble large employer but is treated as a new employee under the rehire and continuing employee rules at § 54.4980H–3(c)(4).

(31) *Ongoing employee*. The term *ongoing employee* means an employee who has been employed by an applicable large employer member for at least one complete standard measurement period. For the treatment of an ongoing employee as a new employee or continuing employee following a period for which no hours of service are earned, see the rehire and continuing employee rules at § 54.4980H–3(d)(6).

(32) *Part-time employee*. The term *part-time employee* means a new employee who the applicable large employer member reasonably expects to be employed on average less than 30 hours of service per week during the initial measurement period, based on the facts and circumstances at the employee's start date. Whether an employer's determination that a new employee is a part-time employee is reasonable is based on the facts and circumstances at the employee's start date. Factors to consider in determining a new employee's full-time employee status are set forth in § 54.4980H–3(d)(2)(ii).

(33) *Period of employment*. The term *period of employment* means the period of time beginning on the first date for which an employee is credited with an hour of service for an applicable large employer (including any member of that applicable large employer) and ending on the last date on which the employee is credited with an hour of service for that applicable large employer, both dates inclusive. An employee may have one or more periods of employment with the same applicable large employer.

(34) *Person*. The term *person* has the same meaning as provided in section 7701(a)(1) and the regulations thereunder.

(35) *Plan year*. A *plan year* must be twelve consecutive months, unless a short plan year of less than twelve consecutive months is permitted for a valid business purpose. A *plan year* is permitted to begin on any day of a year and must end on the preceding day in the immediately following year (for example, a plan year that begins on October 15, 2015, must end on October 14, 2016). A calendar year *plan year* is a period of twelve consecutive months beginning on January 1 and ending on December 31 of the same calendar year. Once established, a plan year is effective for the first plan year and for all subsequent plan years, unless changed, provided that such change will only be recognized if made for a valid business purpose. A change in the plan year is not permitted if a principal purpose of the change in plan year is to circumvent the rules of section 4980H or these regulations.

(36) *Predecessor employer*. [Reserved]

(37) *Qualified health plan*. The term *qualified health plan* means a qualified health plan as defined in Affordable Care Act section 1301(a) (42 U.S.C. 18021(a)), but does not include a catastrophic plan described in Affordable Care Act section 1302(e) (42 U.S.C. 18022(e)).

(38) *Seasonal employee*. The term *seasonal employee* means an employee who is hired into a position for which the customary annual employment is six months or less.

(39) *Seasonal worker*. The term *seasonal worker* means a worker who performs labor or services on a seasonal basis as defined by the Secretary of Labor, including (but not limited to) workers covered by 29 CFR 500.20(s)(1), and retail workers employed exclusively during holiday seasons. Employers may apply a reasonable, good faith interpretation of the term *seasonal worker* and a reasonable good faith interpretation of 29 CFR 500.20(s)(1) (including as applied by analogy to workers and employment positions not otherwise covered under 29 CFR 500.20(s)(1)).

(40) *Section 1411 Certification*. The term *Section 1411 Certification* means the certification received as part of the process established by the Secretary of Health and Human Services under which an employee is certified to the employer under section 1411 of the Affordable Care Act as having enrolled for a calendar month in a qualified health plan with respect to which an applicable premium tax credit or cost-sharing reduction is allowed or paid with respect to the employee.

(41) *Section 4980H(a) applicable payment amount*. The term *section 4980H(a) applicable payment amount* means, with respect to any calendar month, 1/12 of $2,000, adjusted for inflation in accordance with section 4980H(c)(5) and any applicable guidance thereunder.

(42) *Section 4980H(b) applicable payment amount*. The term section *4980H(b) applicable payment amount* means, with respect to any calendar month, 1/12 of $3,000, adjusted for inflation in accordance with section 4980H(c)(5) and any applicable guidance thereunder.

(43) *Self-only coverage*. The term *self-only coverage* means health insurance coverage provided to only one individual, generally the employee.

(44) *Special unpaid leave*. The term *special unpaid leave* means—

(i) Unpaid leave that is subject to the Family and Medical Leave Act of 1993 (FMLA), Public Law 103–3, 29 U.S.C. 2601 et seq.;

(ii) Unpaid leave that is subject to the Uniformed Services Employment and Reemployment Rights Act of 1994 (USERRA), Public Law 103–353, 38 U.S.C. 4301 et seq.; or

(iii) Unpaid leave on account of jury duty.

(45) *Stability period*. The term *stability period* means a period selected by an applicable large employer member that immediately follows, and is associated with, a standard measurement period or an initial measurement period (and, if elected by the employer, the administrative period associated with that standard measurement period or initial measurement period), and is used by the applicable large employer member as part of the look-back measurement method in § 54.4980H–3(d).

(46) *Standard measurement period*. The term *standard measurement period* means a period of at least three but not more than 12 consecutive months that is used by an applicable large employer member as part of the look-back measurement method in § 54.4980H–3(d). See § 54.4980H–3(d)(1)(ii) for rules on the use of payroll periods that include the beginning and end dates of the measurement period.

(47) *Start date*. The term *start date* means the first date on which an employee is required to be credited with an hour of service with an employer. For rules relating to when, following a period for which an employee does not earn an hour of service, that employee may be treated as a new employee with a new start date rather

than a continuing employee, see the rehire and continuing employee rules at § 54.4980H–3(c)(4) and § 54.4980H–3(d)(6).

(48) *United States*. The term *United States* means United States as defined in section 7701(a)(9).

(49) *Variable hour employee*–(i) *In general*. The term *variable hour employee* means an employee if, based on the facts and circumstances at the employee's start date, the applicable large employer member cannot determine whether the employee is reasonably expected to be employed on average at least 30 hours of service per week during the initial measurement period because the employee's hours are variable or otherwise uncertain.

(ii) *Factors*—(A) *In general*. Factors to consider in determining whether it can be determined that the employee is reasonably expected to be (or reasonably expected not to be) employed on average at least 30 hours of service per week during the initial measurement period include, but are not limited to, whether the employee is replacing an employee who was a full-time employee or a variable hour employee, the extent to which the hours of service of employees in the same or comparable positions have actually varied above and below an average of 30 hours of service per week during recent measurement periods, and whether the job was advertised, or otherwise communicated to the new employee or otherwise documented (for example, through a contract or job description) as requiring hours of service that would average at least 30 hours of service per week, less than 30 hours of service per week, or may vary above and below an average of 30 hours of service per week. These factors are only relevant for a particular new employee if the employer has no reason to anticipate that the facts and circumstances related to that new employee will be different. In all cases, no single factor is determinative. For purposes of determining whether an employee is a variable hour employee, the applicable large employer member may not take into account the likelihood that the employee may terminate employment with the applicable large employer (including any member of the applicable large employer) before the end of the initial measurement period.

(B) *Additional factors for an employee hired by an employer for temporary placement at an unrelated entity*. In the case of an individual who, under all the facts and circumstances, is the employee of an entity (referred to solely for purposes of this paragraph (a)(49) as a "temporary staffing firm") that hired such individual for temporary placement at an unrelated entity that is not the common law employer, additional factors to consider to determine whether the employee is reasonably expected to be (or reasonably expected not to be) employed by the temporary staffing firm on average at least 30 hours of service per week during the initial measurement period include, but are not limited to, whether other employees in the same position of employment with the temporary staffing firm, as part of their continuing employment, retain the right to reject temporary placements that the temporary staffing firm offers the employee; typically have periods during which no offer of temporary placement is made; typically are offered temporary placements for differing periods of time; and typically are offered temporary placements that do not extend beyond 13 weeks.

(C) *Educational organizations*. An employer that is an educational organization cannot take into account the potential for, or likelihood of, an employment break period in determining its expectation of future hours of service.

(iii) *Application only for look-back measurement method*. The term *variable hour employee* is used as a category of employees under the look-back measurement method and is not relevant to the monthly measurement method.

(50) *Week*. The term *week* means any period of seven consecutive calendar days applied consistently by the applicable large employer member.

(b) *Effective/applicability date*. This section is applicable for periods after December 31, 2014.

§ 54.4980H–2 Applicable large employer and applicable large employer member.

(a) *In general*. Section 4980H applies to an applicable large employer and to all of the applicable large employer members that comprise that applicable large employer.

(b) *Determining applicable large employer status*—(1) *In general*. An employer's status as an applicable large employer for a calendar year is determined by taking the sum of the total number of full-time employees (including any seasonal workers) for each calendar month in the preceding calendar year and the total number of FTEs (including any seasonal workers) for each calendar month in the preceding calendar year, and dividing by 12. The result, if not a whole number, is then rounded to the next lowest whole number. If the result of this calculation is less than 50, the employer is not an applicable large employer for the current calendar year. If the result of this calculation is 50 or more, the employer is an applicable large employer for the current calendar year, unless the seasonal worker exception in paragraph (b)(2) of this section applies.

(2) *Seasonal worker exception*. If the sum of an employer's full-time employees and FTEs exceeds 50 for 120 days or less during the preceding calendar year, and the employees in excess of 50 who were employed during that period of no more than 120 days are seasonal workers, the employer is not considered to employ more than 50 full-time employees (including FTEs) and the employer is not an applicable large employer for the current calendar year. In the case of an employer that was not in existence on any business day during the preceding calendar year, if the employer reasonably expects that the sum of its full-time employees and FTEs for the current calendar year will exceed 50 for 120 days or less during the calendar year, and that the employees in excess of 50 who will be employed during that period of no more than 120 days will be seasonal workers, the employer is not an applicable large employer for the current calendar year. For purposes of this paragraph (b)(2) only, four calendar months may be treated as the equivalent of 120 days. The four calendar months and the 120 days are not required to be consecutive.

(3) *Employers not in existence in preceding calendar year*. An employer not in existence throughout the preceding calendar year is an applicable large employer

for the current calendar year if the employer is reasonably expected to employ an average of at least 50 full-time employees (taking into account FTEs) on business days during the current calendar year and it actually employs an average of at least 50 full-time employees (taking into account FTEs) on business days during the calendar year. An employer is treated as not having been in existence throughout the prior calendar year only if the employer was not in existence on any business day in the prior calendar year. See paragraph (b)(2) of this section for the application of the seasonal worker exception to employers not in existence in the preceding calendar year.

(4) *Special rules for government entities, churches, and conventions and associations of churches*. [Reserved]

(5) *Transition rule for an employer's first year as an applicable large employer*. With respect to an employee who was not offered coverage by the employer at any point during the prior calendar year, if the applicable large employer offers coverage to the employee on or before April 1 of the first calendar year for which the employer is an applicable large employer, the employer will not be subject to an assessable payment under section 4980H by reason of its failure to offer coverage to the employee for January through March of that year, provided that this relief applies only with respect to potential liability under section 4980H(b) (for January through March of the first calendar year for which the employer is an applicable large employer) if the coverage offered by April 1 provides minimum value. If the employer does not offer coverage to the employee by April 1, the employer may be subject to a section 4980H(a) assessable payment with respect January through March of the first calendar year for which the employer is an applicable large employer in addition to any later calendar months for which coverage was not offered. If the employer offers coverage to the employee by April 1 that does not provided minimum value, the employer may be subject to a section 4980H(b) assessable payment with respect to the employee for January through March of the first calendar year for which the employer is an applicable large employer in addition to any later calendar months for which coverage does not provide minimum value or is not affordable. This rule applies only during the first year that an employer is an applicable large employer (and would not apply if, for example, the employer falls below the 50 full-time employee (plus FTE) threshold for a subsequent calendar year and then increases employment and becomes an applicable large employer again).

(c) *Full-time equivalent employees (FTEs)*—(1) *In general*. In determining whether an employer is an applicable large employer, the number of FTEs it employed during the preceding calendar year is taken into account. All employees (including seasonal workers) who were not employed on average at least 30 hours of service per week for a calendar month in the preceding calendar year are included in calculating the employer's FTEs for that calendar month.

(2) *Calculating the number of FTEs*. The number of FTEs for each calendar month in the preceding calendar year is determined by calculating the aggregate number of hours of service for that calendar month for employees who were not full-time employees (but not more than 120 hours of service for any employee) and dividing that number by 120. In determining the number of FTEs for each calendar month, fractions are taken into account; an employer may round the number of FTEs for each calendar month to the nearest one hundredth.

(d) *Examples*. The following examples illustrate the rules of paragraphs (a) through (c) of this section. In these examples, hours of service are computed following the rules set forth in § 54.4980H–3, and references to years refer to calendar years unless otherwise specified. The employers in *Example 2* through *Example 6* are each the sole applicable large employer member of the applicable large employer, as determined under section 414(b), (c), (m), and (o).

Example 1 (Applicable large employer/controlled group). (i) *Facts*. For all of 2015 and 2016, Corporation Z owns 100 percent of all classes of stock of Corporation Y and Corporation X. Corporation Z has no employees at any time in 2015. For every calendar month in 2015, Corporation Y has 40 full-time employees and Corporation X has 60 full-time employees. Corporations Z, Y, and X are a controlled group of corporations under section 414(b).

(ii) *Conclusion*. Because Corporations Z, Y and X have a combined total of 100 full-time employees during 2015, Corporations Z, Y, and X together are an applicable large employer for 2016. Each of Corporations Z, Y and X is an applicable large employer member for 2016.

Example 2 (Applicable large employer with FTEs). (i) *Facts*. During each calendar month of 2015, Employer W has 20 full-time employees each of whom averages 35 hours of service per week, 40 employees each of whom averages 90 hours of service per calendar month, and no seasonal workers.

(ii) *Conclusion*. Each of the 20 employees who average 35 hours of service per week count as one full-time employee for each calendar month. To determine the number of FTEs for each calendar month, the total hours of service of the employees who are not full-time employees (but not more than 120 hours of service per employee) are aggregated and divided by 120. The result is that the employer has 30 FTEs for each calendar month ($40 \times 90 = 3{,}600$, and $3{,}600 \div 120 = 30$). Because Employer W has 50 full-time employees (the sum of 20 full-time employees and 30 FTEs) during each calendar month in 2015, and because the seasonal worker exception is not applicable, Employer W is an applicable large employer for 2016.

Example 3 (Seasonal worker exception). (i) *Facts*. During 2015, Employer V has 40 full-time employees for the entire calendar year, none of whom are seasonal workers. In addition, Employer V also has 80 seasonal workers who are full-time employees and who work for Employer V from September through December 2015. Employer V has no FTEs during 2015.

(ii) *Conclusion*. Before applying the seasonal worker exception, Employer V has 40 full-time employees during each of eight calendar months of 2015, and 120 full-time employees during each of four calendar months of 2015, resulting in an average of 66.67 full-time employees for the year. However, Employer V's workforce exceeded 50 full-time employees (counting seasonal workers) for no more than four calendar months (treated as the equivalent of 120 days) in calendar year 2015, and the number of full-time employees would be less than 50 during those months if seasonal workers were disregarded. Accordingly, because after application of the seasonal worker exception described in paragraph (b)(2) of this section Employer V is not considered to employ more than 50 full-time employees, Employer V is not an applicable large employer for 2016.

Example 4 (Seasonal workers and other FTEs). (i) *Facts*. Same facts as *Example 3*, except that Employer V has 20 FTEs in August, some of whom are seasonal workers.

(ii) *Conclusion*. The seasonal worker exception described in paragraph (b)(2) of this section does not apply if the number of an employer's full-time employees (including seasonal workers) and FTEs exceeds 50 for more than 120 days during the calendar year. Because Employer V has at least 50 full-time employees for a period greater than four calendar months (treated as the equivalent of 120 days) during 2015, the exception described in paragraph (b)(2) of this section does not apply. Employer V averaged 68 full-time employees in 2015: $[(40 \times 7) + (60 \times 1) + (120 \times 4)] \div 12 = 68.33$, and accordingly, Employer V is an applicable large employer for calendar year 2016.

Example 5 (New employer). (i) *Facts*. Corporation S is incorporated on January 1, 2016. On January 1, 2016, Corporation S has three employees. However, prior to incorporation, Corporation S's owners purchased a factory intended to open within two calendar months of incorporation and to employ approximately 100 full-time employees. By March 15, 2016, Corporation S has more than 75 full-time employees.

(ii) *Conclusion*. Because Corporation S can reasonably be expected to employ on average at least 50 full-time employees on business days during 2016, and actually employs an average of at least 50 full-time employees on business days during 2016, Corporation S is an applicable large employer (and an applicable large employer member) for calendar year 2016.

Example 6 (First year as applicable large employer). (i) *Facts*. As of January 1, 2015, Employer R has been in existence for several years and did not average 50 or more full-time employees (including FTEs) on business days during 2014. Employer R averages 50 or more full-time employees on business days during 2015, so that for 2016 Employer R is an applicable large employer, for the first time. For all the calendar months of 2016, Employer R has the same 60 full-time employees. Employer R offered 20 of those full-time employees healthcare coverage during 2015, and offered those same employees coverage providing minimum value for 2016. With respect to the 40 full-time employees who were not offered coverage during 2015, Employer R offers coverage providing minimum value for calendar months April 2016 through December 2016.

(ii) *Conclusion*. For the 40 full-time employees not offered coverage during 2015 and offered coverage providing minimum value for the calendar months April 2016 through December 2016, the failure to offer coverage during the calendar months January 2016 through March 2016 will not result in an assessable payment under section 4980H with respect to those employees for those three calendar months. For those same 40 full-time employees, the offer of coverage during the calendar months April 2016 through December 2016 may result in an assessable payment under section 4980H(b) with respect to any employee for any calendar month for which the offer is not affordable and for which Employer R has received a Section 1411 Certification. For the other 20 full-time employees, the offer of coverage during 2016 may result in an assessable payment under section 4980H(b) for any calendar month if the offer is not affordable and Employer R has received a Section 1411 Certification with respect to the employee who received the offer of coverage. For all calendar months of 2016, Employer R will not be subject to an assessable payment under section 4980H(a).

(e) *Additional guidance*. With respect to an employer's status as an applicable large employer, the Commissioner may prescribe additional guidance of general applicability, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter).

(f) *Effective/applicability date*. This section is applicable for periods after December 31, 2014.

§ 54.4980H–3 Determining full-time employees.

(a) *In general*. This section sets forth the rules for determining hours of service and status as a full-time employee for purposes of section 4980H. These regulations provide two methods for determining full-time employee status—the monthly measurement method, set forth in paragraph (c) of this section, and the look-back measurement method, set forth in paragraph (d) of this section. The monthly measurement method applies for purposes of determining and calculating liability under section 4980H(a) and (b), as well as, with respect to paragraph (c)(1) of this section, determination of applicable large employer status (except with respect to the weekly rule under the monthly measurement method). The look-back measurement method applies solely for purposes of determining and calculating liability under section 4980H(a) and (b) (and not for purposes of determining status as an applicable large employer). See § 54.4980H–1(a)(21) for the definition of full-time employee. The rules set forth in this section prescribe the minimum standards for determining status as a full-time employee for purposes of section 4980H; treatment of additional employees as full-time employees for other purposes does not affect section 4980H liability if those employees are not full-time employees under the look-back measurement method or the monthly measurement method.

(b) *Hours of service*—(1) *In general*. The following rules on the calculation of hours of service apply for purposes of applying both the look-back measurement method and the monthly measurement method.

(2) *Hourly employees calculation*. Under the look-back measurement method and the monthly measurement method, for employees paid on an hourly basis, an employer must calculate actual hours of service from records of hours worked and hours for which payment is made or due.

(3) *Non-hourly employees calculation*—(i) *In general*. Except as otherwise provided, under the look-back measurement method and the monthly measurement method, for employees paid on a non-hourly basis, an employer must calculate hours of service by using one of the following methods:

(A) Using actual hours of service from records of hours worked and hours for which payment is made or due;

(B) Using a days-worked equivalency whereby the employee is credited with eight hours of service for each day for which the employee would be required to be credited with at least one hour of service in accordance with paragraph (b)(2) of this section; or

(C) Using a weeks-worked equivalency whereby the employee is credited with 40 hours of service for each week for which the employee would be required to be credited with at least one hour of service in accordance with paragraph (b)(2) of this section.

(ii) *Change in method*. An employer must use one of the three methods in paragraph (b)(3)(i) of this section for calculating the hours of service for non-hourly employees. An employer is not required to use the same method for all non-hourly employees, and may apply different methods for different categories of non-hourly employees, provided the categories are reasonable and consistently applied. Similarly, an applicable large employer member is not required to apply the same methods as other applicable large employer members of the same applicable large employer for the same or different categories of non-hourly employees, provided that in each case the categories are reasonable and consistently applied by the applicable large employer member. An employer may change the method of calculating the hours of service of non-hourly employees (or of one or more categories of non-hourly employees) for each calendar year.

(iii) *Prohibited use of equivalencies*. The number of hours of service calculated using the days-worked or weeks-worked equivalency must reflect generally the hours actually worked and the hours for which payment is made or due. An employer is not permitted to use the days-worked equivalency or the weeks-worked equivalency if the result is to substantially understate an employee's hours of service in a manner that would cause that employee not to be treated as a full-time employee, or if the result is to understate the hours of service of a substantial number of employees (even if no particular employee's hours of service are understated substantially and even if the understatement would not cause the employee to not be treated as a full-time employee). For example, as to the former, an employer may not use a days-worked equivalency in the case of an employee who generally works three 10-hour days per week, because the equivalency would substantially understate the employee's hours of service as 24 hours of service per week, which would result in the employee being treated as not a full-time employee.

(c) *Monthly measurement method*—(1) *In general*. Under the monthly measurement method, an applicable large employer member determines each employee's status as a full-time employee by counting the employee's hours of service for each calendar month. See § 54.4980H–1(a)(21) for the definition of full-time employee. This paragraph (c)(1) (except with respect to the weekly rule) applies for purposes of the determination of status as an applicable large employer; paragraphs (c)(2) through (4) of this section do not apply for purposes of the determination of status as an applicable large employer. For rules regarding the use of the look-back measurement method and the monthly measurement method for different categories of employees, see paragraph (e) of this section.

(2) *Employee first otherwise eligible for an offer of coverage*. The rule in this paragraph (c)(2) applies with respect to an employee who, in a calendar month, first becomes otherwise eligible to be offered coverage under a group health plan of an employer using the monthly measurement method with respect to that employee. For purposes of this paragraph (c)(2), an employee is otherwise eligible to be offered coverage under a group health plan for a calendar month if, pursuant to the terms of the plan as in effect for that calendar month, the employee meets all conditions to be offered coverage under the plan for that calendar month, other than the completion of a waiting period, within the meaning of § 54.9801–2, and an employee is first otherwise eligible if the employee has not previously been eligible or otherwise eligible for an offer of coverage under a group health plan of the employer during the employee's period of employment. An employer is not subject to an assessable payment under section 4980H(a) with respect to an employee for each calendar month during the period of three full calendar months beginning with the first full calendar month in which the employee is otherwise eligible for an offer of coverage under a group health plan of the employer, provided that the employee is offered coverage no later than the first day of the first calendar month immediately following the three-month period if the employee is still employed on that day. If the coverage for which the employee is otherwise eligible during the three-month period, and which the employee actually is offered on the day following that three-month period if still employed, provides minimum value, the employer also will not be subject to an assessable payment under section 4980H(b) with respect to that employee for the three-month period. This rule cannot apply more than once per period of employment of an employee. If an employee terminates employment and returns under circumstances that would constitute a rehire as set forth in paragraph (c)(4) of this section, the rule in this paragraph (c)(2) may apply again.

(3) *Use of weekly periods.* With respect to a category of employees for whom an employer uses the monthly measurement method, an employer may determine full-time employee status for a calendar month based on hours of service over a period that:

(i) begins on the first day of the week that includes the first day of the calendar month, provided that the period over which hours of service are measured does not include the week in which falls the last day of the calendar month (unless that week ends with the last day of the calendar month, in which case it is included); or

(ii) begins on the first day of the week immediately subsequent to the week that includes the first day of the calendar month (unless the week begins on the first day of the calendar month, in which case it is included), provided the period over which hours of service are measured includes the week in which falls the last day of the calendar month.

(4) *Employees rehired after termination of employment or resuming service after other absence*—(i) *Treatment as a new employee after a period of absence for employees of employers other than educational organizations*. Except as provided in paragraph (c)(4)(ii) of this section (related to rules for employers that are educational organizations), an employee who resumes providing services to (or is otherwise credited with an hour of service for) an applicable large employer after a period during which the individual was not credited with any hours of service may be treated as having terminated employment and having been rehired, and therefore may be treated as a new employee upon the resumption of services only if the employee did not have an hour of service for the applicable large employer for a period of at least 13 consecutive weeks immediately preceding the resumption of services. The rule set forth in this paragraph (c)(4)(i) applies solely for the purpose of determining whether the employee, upon the resumption of services, is treated as a new employee or as a continuing employee, and does not determine whether the employee is treated as a continuing full-time employee (for example, an employee on leave) or a terminated employee for some or all of the period during which no hours of service are credited.

(ii) *Treatment as a new employee after a period of absence for employees of educational organizations*. With respect to an employer that is an educational organization, an employee who resumes providing services to (or is otherwise credited with an hour of service for) an applicable large employer after a period during which the individual was not credited with any hours of service may be treated as having terminated employment and having been rehired, and therefore may be treated as a new employee upon the resumption of services, only if the employee did not have an hour of service for the applicable large employer for a period of at least 26 consecutive weeks immediately preceding the resumption of services. The rule set forth in this paragraph (c)(4)(ii) applies solely for the purpose of determining whether the employee, upon the resumption of services, is treated as a new employee or as a continuing employee, and does not determine whether the employee is treated as a continuing full-time employee (for example, an employee on leave) or a terminated employee for some or all of the period during which no hours of service are credited.

(iii) *Averaging method for special unpaid leave and employment break periods*. The averaging method for periods of special unpaid leave and employment break periods does not apply under the monthly measurement method, regardless of whether the employer is (or is not) an educational organization.

(iv) *Treatment of continuing employee*. The rule set forth in paragraph (c)(2) of this section applies to an employee treated as a continuing employee in the same way that it applies to an employee who has not experienced a period with no hours of service. A continuing employee treated as a full-time employee is treated as offered coverage upon resumption of services if the employee is offered coverage as of the first day that employee is credited with an hour of service, or, if later, as soon as administratively practicable. For this purpose, offering coverage by no later than the first day of the calendar month following resumption of services is deemed to be as soon as administratively practicable.

(v) *Rule of parity*. For purposes of determining the period after which an employee may be treated as having terminated employment and having been rehired, an applicable large employer may choose a period, measured in weeks, of at least four consecutive weeks during which the employee was not credited with any hours of service that exceeds the number of weeks of that employee's period of employment with the applicable large employer immediately preceding the period that is shorter than 13 weeks (for an employee of an educational organization employer, a period that is shorter than 26 weeks).

(vi) *International transfers*. An employer may treat an employee as having terminated employment if the employee transfers to a position at the same applicable large employer (including a different applicable large employer member that is part of the same applicable large employer) if the position is anticipated to continue indefinitely or for at least 12 months and if substantially all of the compensation will constitute income from sources without the United States (within the meaning of sections 861 through 863 and the regulations thereunder). With respect to an employee transferring from a position that was anticipated to continue indefinitely or for at least 12 months and in which substantially all of the compensation for the hours of service constitutes income from sources without the United States (within the meaning of sections 861 through 863 and the regulations thereunder) to a position at the same applicable large employer (including a different applicable large employer member that is part of the same applicable large employer) with respect to which substantially all of the compensation will constitute U.S. source income, the employer may treat that employee as a new hire to the extent consistent with the rules related to rehired employees as set forth in paragraph (c)(4) of this section.

(5) *Examples*. The following examples illustrate the rules of paragraphs (c)(1) through (4) of this section. In each example, the employer is an applicable large employer with 200 full-time employees (including FTEs) that uses the monthly measurement method to identify full-time employees and offers coverage only to employees who are full-time employees (and their dependents).

Example 1 (Monthly measurement method – employee first otherwise eligible for an offer of coverage). (i) *Facts*. Employer Z uses the monthly measurement method. Employer Z hires Employee A on January 1, 2016. For each calendar month in 2016, Employee A averages 20 hours of service per week and is not eligible (or otherwise eligible) for an offer of coverage under the group health plan of Employer Z. Effective January 1, 2017, Employee A is promoted to a position that is eligible for an offer of coverage under a group health plan of Employer Z, following completion of a 90-day waiting period. For January 2017 through March 2017, Employee A meets all of the conditions for eligibility under the group health plan, other than completion of the waiting period. The coverage that would have been offered to Employee A under the terms of the plan, but for the waiting period, during those three months would have provided minimum value. Effective April 1, 2017, Employer Z offers Employee A coverage that provides minimum value. Employee A averages 40 hours of service per week for each calendar month in 2017.

(ii) *Conclusion*. Because Employer Z offers minimum value coverage to Employee A no later than the first day following the period of three full calendar months beginning with the first full calendar month in which Employee A is otherwise eligible for an offer of coverage under a group health plan of Employer Z, Employer Z is not subject to an assessable payment for January 2017 through March 2017 under section 4980H by reason of its failure to offer coverage to Employee A during those months. For calendar months after March 2017, an offer of minimum value coverage may result in an assessable payment under section 4980H(b) with respect to Employee A for any month for which the offer is not affordable and for which Employer Z has received a Section 1411 Certification. Employer Z is not subject to an assessable payment under section 4980H by reason of its failure to offer coverage to Employee A during each month of 2016 because for each month of 2016, Employee A was not a full-time employee.

Example 2 (Rehire rules under monthly measurement method for employers that are not educational organizations). (i) *Facts*. Same as *Example 1*, except that Employee A has zero hours of service during a nine week period of unpaid leave (that constitutes special unpaid leave) beginning on June 25, 2017, and ending on August 26, 2017. As a result of the nine week period during which Employee A has zero hours of service, Employee A averages less than 30 hours of service per week for July 2017 and August 2017. Employee A averages more than 30 hours of service per week for each month between and including September 2017 through December 2017. Employer Z does not use the rule of parity, set forth in paragraph (c)(4)(v) of this section, and Employer Z is not an educational organization.

(ii) *Conclusion*. Because Employee A resumes providing services for Employer Z after a period during which the employee was not credited with any hours of service of less than 13 consecutive weeks, Employer Z may not treat Employee A as having terminated employment and having been rehired. Therefore, Employer Z may not treat Employee A as a new employee upon the resumption of services, and, accordingly, Employer Z may not again apply the rule set forth in paragraph (c)(2) of this section. Although the nine consecutive weeks of zero hours of service constitute special unpaid leave, the averaging method for periods of special unpaid leave does not apply under the monthly measurement method. Therefore, Employer Z may treat Employee A as a non-full-time employee for July 2017 and August 2017.

Example 3 (Use of weekly rule). (i) *Facts*. Employer Y uses the monthly measurement method in combination with the weekly rule for purposes of determining whether an employee is a full-time employee for a particular calendar month. For purposes of applying the weekly rule, Employer Y uses the period of Sunday through Saturday as a week and includes the week that includes the first day of a calendar month and excludes the week that includes the last day of a calendar month (except in any case in which the last day of the calendar month occurs on a Saturday). Employer Y measures hours of service for the five weeks from Sunday, December 27, 2015, through Saturday, January 30, 2016, to determine an employee's full-time employee status for January 2016, for the four weeks from Sunday, January 31, 2016, through Saturday, February 27, 2016, to determine an employee's status for February 2016, and the four weeks from Sunday, February 28, 2016, through Saturday, March 26, 2016, to determine an employee's status for March 2016. For January 2016, Employer Y treats an employee as a full-time employee if the employee has at least 150 hours of service (30 hours per week x 5 weeks). For February 2016 and March 2016, Employer Y treats an employee as a full-time employee if the employee has at least 120 hours of service (30 hours per week x 4 weeks).

(ii) *Conclusion*. Employer Y has correctly applied the weekly rule as part of the monthly measurement method for determining each employee's status as a full-time employee for the months January, February, and March 2016.

(d) *Look-back measurement method*—(1) *Ongoing employees*—(i) *In general*. Under the look-back measurement method for ongoing employees, an applicable large employer determines each ongoing employee's full-time employee status by looking back at the standard measurement period. The applicable large employer member determines the months in which the standard measurement period starts and ends, provided that the determination must be made on a uniform and consistent basis for all employees in the same category (see paragraph (d)(1)(v) of this section for a list of permissible categories). For example, if an applicable large employer member chooses a standard measurement period of 12 months, the applicable large employer member could choose to make it the calendar year, a non-calendar plan year, or a different 12-month period, such as one that ends shortly before the start of the plan's annual open enrollment period. If the applicable large employer member determines that an employee was employed on average at least 30 hours of service per week during the standard measurement period, then the applicable large employer member must treat the employee as a full-time employee during a subsequent stability period, regardless of the employee's number of hours of service during the stability period, so long as he or she remains an employee.

(ii) *Use of payroll periods*. For payroll periods that are one week, two weeks, or semi-monthly in duration, an employer is permitted to treat as a measurement period a period that ends on the last day of the payroll period preceding the payroll period that includes the date that would otherwise be the last day of the measurement period, provided that the measurement period begins on the first day of the payroll period that includes the date that would otherwise be the first day of the measurement period. An employer may also treat as a measurement period a period that begins on the first day of the payroll period that follows the payroll period that includes the date that would otherwise be the first day of the measurement period, provided that the measurement period ends on the last day of the payroll period that includes the date that would otherwise be the last day of the measurement period. For example, an employer using the calendar year as a measurement period could exclude the entire payroll period that included January 1 (the beginning of the year) if it included the entire payroll period that included December 31 (the end of that same year), or, alternatively, could exclude the entire payroll period that included December 31 of a calendar year if it included the entire payroll period that included January 1 of that calendar year.

(iii) *Employee determined to be employed an average of at least 30 hours of service per week*. An employee who was employed on average at least 30 hours of service per week during the standard measurement period must be treated as a full-time employee for a stability period that begins immediately after the standard measurement period and any applicable administrative period. The stability period must be at least six consecutive calendar months but no shorter in duration than the standard measurement period.

(iv) *Employee determined not to be employed on average at least 30 hours of service per week*. If an employee was not employed an average of at least 30 hours of service per week during the standard measurement period, the applicable large employer member may treat the employee as not a full-time employee during the stability period that follows, but is not longer than, the standard measurement period. The stability period must begin immediately after the end of the measurement period and any applicable administrative period.

(v) *Permissible employee categories*. Different applicable large employer members of the same applicable large employer may use measurement periods and stability periods that differ either in length or in their starting or ending dates. In addition, subject to the rules governing the relationship between the length of the measurement period and the stability period, applicable large employer members may use measurement periods and stability periods that differ either in length or in their starting and ending dates for—

(A) Collectively bargained employees and non-collectively bargained employees,

(B) Each group of collectively bargained employees covered by a separate collective bargaining agreement,

(C) Salaried employees and hourly employees, and

(D) Employees whose primary places of employment are in different States. (vi) *Optional administrative period*. An applicable large employer member may provide for an administrative period that begins immediately after the end of a standard measurement period and that ends immediately before the associated stability period; however, any administrative period between the standard measurement period and the stability period for ongoing employees may neither reduce nor lengthen the measurement period or the stability period. The administrative period following the standard measurement period may last up to 90 days. To prevent this administrative period from creating a period during which coverage is not available, the administrative period must overlap with the prior stability period, so that, during any such administrative period applicable to ongoing employees following a standard measurement period, ongoing employees who are enrolled in coverage because of their status as full-time employees based on a prior measurement period must continue to be covered through the administrative period. Applicable large employer members may use administrative periods that differ in length for the categories of employees identified in paragraph (d)(1)(v) of this section.

(vii) *Change in employment status*. Except as provided in paragraph (f)(2) of this section, if an ongoing employee experiences a change in employment status before the end of a stability period, the change will not affect the application of the classification of the employee as a full-time employee (or not a full-time employee) for the remaining portion of the stability period. For example, if an ongoing employee in a certain position of employment is not treated as a full-time employee during a stability period because the employee's hours of service during the prior measurement period were insufficient for full-time-employee treatment, and the employee experiences a change in employment status that involves an increased level of hours of service, the treatment of the employee as a non-full-time employee during the remainder of the stability period is unaffected. Similarly, if an ongoing employee in a certain position of employment is treated as a full-time employee during a stability period because the employee's hours of service during the prior measurement period were sufficient for full-time-employee treatment, and the employee experiences a change in employment status that involves a lower level of hours of service, the treatment of the employee as a full-time employee during the remainder of the stability period is unaffected.

(viii) *Example*. The following example illustrates the application of paragraph (d)(1) of this section:

(A) *Facts*. Employer Z is an applicable large employer member and computes hours of service following the rules in this paragraph (d)(1). Employer Z chooses to use a 12-month stability period that begins January 1 and a 12-month standard measurement period that begins October 15. Consistent with the terms of Employer Z's group health plan, only employees classified as full-time employees using the look-back measurement method are eligible for coverage. Employer Z chooses to use an administrative period between the end of the standard measurement period (October 14) and the beginning of the stability period (January 1) to determine which employees were employed on average 30 hours of service per week during the measurement period, notify them of their eligibility for the plan for the calendar year beginning on January 1 and of the coverage available under the plan, answer questions and collect materials from employees, and enroll those employees who elect coverage in the plan. Previously-determined full-time employees already enrolled in coverage continue to be offered coverage through the administrative period. Employee A and Employee B have been employed by Employer Z for several years, continuously from their start date. Employee A was employed on average 30 hours of service per week during the standard measurement period that begins October 15, 2015, and ends October 14, 2016, and for all prior standard measurement periods. Employee B also was employed on average 30 hours of service per week for all prior standard measurement periods, but averaged less than 30 hours of service per week during the standard measurement period that begins October 15, 2015, and ends October 14, 2016.

(B) *Conclusions*. Because Employee A was employed for the entire standard measurement period that begins October 15, 2015, and ends October 14, 2016, Employee A is an ongoing employee with respect to the stability period running from January 1, 2017, through December 31, 2017. Because Employee A was employed on average 30 hours of service per week during that standard measurement period, Employee A is offered coverage for the entire 2017 stability period (including the administrative period from October 15, 2017, through December 31, 2017). Because Employee A was employed on average 30 hours of service per week during the prior standard measurement period, Employee A is offered coverage for the entire 2016 stability period and, if enrolled, would continue such coverage during the administrative period from October 15, 2016, through December 31, 2016. Because Employee B was employed for the entire standard measurement period that begins October 15, 2015, and ends October 14, 2016, Employee B is also an ongoing employee with respect to the stability period in 2017. Because Employee B was not a full-time employee based on hours of service during this standard measurement period, Employee B is not offered coverage for the stability period in 2017 (including the administrative period from October 15, 2017, through December 31, 2017). However, because Employee B was employed on average 30 hours of service per week during the prior standard measurement period, Employee B is offered coverage through the end of the 2016 stability period and, if enrolled, would continue such coverage during the administrative period from October 15, 2016, through December 31, 2016. Employer Z complies with the standards of paragraph (d)(1) of this section because the standard measurement period is no longer than 12 months, the stability period for ongoing employees who are full-time employees based on hours of service during the standard measurement period is not shorter than the standard measurement period, the stability period for ongoing employees who are not full-time employees based on hours of service during the standard measurement period is no longer than the standard measurement period, and the administrative period is no longer than 90 days.

(2) *New non-variable hour, new non-seasonal and new non-part-time employees*—(i) *In general*. For a new employee who is reasonably expected at the employee's start date to be a full-time employee (and is not a seasonal employee), an applicable large employer member determines such employee's status as a full-time employee based on the employee's hours of service for each calendar month. If the employee's hours of service for the calendar month equal or exceed an average of 30 hours of service per week, the employee is a full-time employee for that calendar month. Once a new employee who is reasonably expected at the employee's start date to be a full-time employee (and is not a seasonal employee) becomes an ongoing employee, the rules set forth in paragraph (d)(1) of this section apply for determining full-time employee status.

(ii) *Factors for determining full-time employee status*. Whether an employer's determination that a new employee (who is not a seasonal employee) is a full-time employee or is not a full-time employee is reasonable is based on the facts and circumstances at the employee's start date. Factors to consider in determining whether a new employee who is not a seasonal employee is reasonably expected at the employee's start date to be a full-time employee include, but are not limited to, whether the employee is replacing an employee who was (or was not) a full-time employee, the extent to which hours of service of ongoing employees in the same or comparable positions have varied above and below an average of 30 hours of service per week during recent measurement periods, and whether the job was advertised, or otherwise communicated to the new hire or otherwise documented (for example, through a contract or job description), as requiring hours of service that would average 30 (or more) hours of service per week or less than 30 hours of service per week. In all cases, no single factor is determinative. An educational organization employer cannot take into account the potential for, or likelihood of, an employment break period in determining its expectation of future hours of service.

(iii) *Application of section 4980H to initial full three calendar months of employment*. Notwithstanding paragraph (d)(2)(i) of this section, with respect to an employee who is reasonably expected at his or her start date to be a full-time employee (and is not a seasonal employee), the employer will not be subject to an assessable payment under section 4980H(a) for any calendar month of the three-month period beginning with the first day of the first full calendar month of employment if, for the calendar month, the employee is otherwise eligible for an offer of coverage under a group health plan of the employer, provided that the employee is offered coverage by the employer no later than the first day of the fourth full calendar month of employment if the employee is still employed on that day. If the offer of coverage for which the employee is otherwise eligible during the first three full calendar months of employment, and which the employee actually is offered by the first day of the fourth month if still employed, provides minimum value, the employer also will not be subject to an assessable payment under section 4980H(b) with respect to that employee for the first three full calendar months of employment. For purposes of this paragraph (d)(2)(iii), an employee is otherwise eligible to be offered coverage under a group health plan for a calendar month if, pursuant to the terms of the plan as in effect for that calendar month, the employee meets all conditions to be offered coverage under the plan for that calendar month, other than the completion of a waiting period, within the meaning of § 54.9801–2.

(3) *New variable hour employees, new seasonal employees, and new part-time employees*—(i) *In general*. For new variable hour employees, new seasonal employees, and new part-time employees, applicable large employer members are permitted to determine whether the new employee is a full-time employee using an initial measurement period of no less than three consecutive months and no more than 12 consecutive months (as selected by the applicable large employer member) that begins on the employee's start date or on any date up to and including the first day of the first calendar month following the employee's start date (or on the first day of the first payroll period starting on or after the employee's start date, if later, as set forth in paragraph (d)(3)(ii) of this section). The applicable large employer member measures the new employee's hours of service during the initial measurement period and determines whether the employee was employed on average at least 30 hours of service per week during this period. The stability period for such employees must be the same length as the stability period for ongoing employees.

(ii) *Use of payroll periods*. An applicable large employer member may apply the payroll period rule set forth in paragraph (d)(1)(ii) of this section for purposes of determining an initial measurement period, provided that the initial measurement period must begin on the start date or any date during the period beginning with the employee's start date and ending with the later of the first day of the first calendar month following the employee's start date and the first day of the first payroll period that starts after the employee's start date. As set forth in paragraph (d)(1)(ii) of this section, the use of payroll periods for purposes of determining the initial measurement period applies for payroll periods that are one week, two weeks, or semi-monthly in duration.

(iii) *Employees determined to be employed on average at least 30 hours of service per week*. If a new variable hour employee, new seasonal employee, or new part-time employee has on average at least 30 hours of service per week during the initial measurement period, the applicable large employer member must treat the employee as a full-time employee during the stability period that begins after the initial measurement period (and any associated administrative period). The stability period must be a period of at least six consecutive calendar months that is no shorter in duration than the initial measurement period. The stability period must begin immediately after the end of the measurement period and any applicable administrative period. With respect to an employee who has on average at least 30 hours of service per week during the initial measurement period, the employer will not be subject to an assessable payment under section 4980H(a) for any calendar month during the initial measurement period and any associated administrative period if, for the calendar month, the employee is otherwise eligible for an offer of coverage under a group health plan of the employer, provided that the employee is offered coverage by the employer no later than the first day of the associated stability period if the employee is still employed on that day. If the offer of coverage for which the employee is otherwise eligible during the initial measurement period, and which the employee actually is offered by the first day of the stability period if still employed, provides minimum value, the employer also will not be subject to an assessable payment under section 4980H(b) with respect to that employee during the initial measurement period and any associated administrative period. For purposes of this paragraph (d)(3)(iii), an employee is otherwise eligible to be offered coverage under a group health plan for a month if, pursuant to the terms of the plan as in effect for that calendar month, the employee meets all conditions to be offered coverage under the plan for that month, other than the completion of a waiting period, within the meaning of § 54.9801–2.

(iv) *Employees determined not to be employed on average at least 30 hours of service per week*. If a new variable hour employee, new seasonal employee, or new part-time employee does not have on average at least 30 hours of service per week during the initial measurement period, the applicable large employer member may treat the employee as not a full-time employee during the stability period that follows the initial measurement period. Except as provided in paragraph (d)(4)(iv) of this section, the stability period for such employees must not be more than one month longer than the initial measurement period and must not exceed the remainder of the first entire standard measurement period (plus any associated administrative period) for which a variable hour employee, seasonal employee, or part-time employee has been employed. The stability period must begin immediately after the end of the measurement period and any applicable administrative period.

(v) *Permissible differences in measurement or stability periods for different categories of employees*. Subject to the rules governing the relationship between the length of the measurement period and the stability period, with respect to a new variable hour employee, new seasonal employee, or new part-time employee, applicable large employer members may use measurement periods and stability periods that differ either in length or in their starting and ending dates for the categories of employees identified in paragraph (d)(1)(v) of this section.

(vi) *Optional administrative period*—(A) *In general*. Subject to the limits in paragraph (d)(3)(vi)(B) of this section, an applicable large employer member may apply an administrative period in connection with an initial measurement period and before the start of the stability period. This administrative period must not exceed 90 days in total. For this purpose, the administrative period includes all periods between the start date of a new variable hour employee, new seasonal employee, or new part-time employee and the date the employee is first offered coverage under the applicable large employer member's group health plan, other than the initial measurement period. Thus, for example, if the applicable large employer member begins the initial measurement period on the first day of the first month following a new employee's start date, the period between the employee's start date and the first day of the next month must be taken into account in applying the 90-day limit on the administrative period. Similarly, if there is a period between the end of the initial measurement period and the date the employee is first offered coverage under the plan, that period must be taken into account in applying the 90-day limit on the administrative period. Applicable large employer members may use administrative periods that differ in length for the categories of employees identified in paragraph (d)(1)(v) of this section.

(B) *Limit on combined length of initial measurement period and administrative period*. In addition to the specific limits on the initial measurement period (which must not exceed 12 months) and the administrative period (which must not exceed 90 days), there is a limit on the combined length of the initial measurement period and the administrative period applicable to a new variable hour employee, new seasonal employee, or new part-time employee. Specifically, the initial measurement period and administrative period together cannot extend beyond the last day of the first calendar month beginning on or after the first anniversary of the employee's start date. For example, if an applicable large employer member uses a 12-month initial measurement period for a new variable hour employee, and begins that initial measurement period on the first day of the first calendar month following the employee's start date, the period between the end of the initial measurement period and the offer of coverage to a new variable hour employee who is a full-time employee based on hours of service during the initial measurement period must not exceed one month.

(vii) *Change in employment status during the initial measurement period*—(A) *In general*. If a new variable hour employee, new seasonal employee, or new part-time employee experiences a change in employment status before the end of the initial measurement period such that, if the employee had begun employment in the new position or status, the employee would have reasonably been expected to be employed on average at least 30 hours of service per week (or, if applicable, would not have been a seasonal employee and would have been expected to be employed on average at least 30 hours of service per week), the rules set forth in the remainder of this paragraph (d)(3)(vii) apply. With respect to an employee described in this paragraph (d)(3)(vii) and subject to the rules in the next sentence, the employer will not be subject to an assessable payment under section 4980H for the period before the first day of the fourth full calendar month following the change in employment status (or, if earlier and the employee averages 30 or more hours of service per week during the initial measurement period, the first day of the first month following the end of the initial measurement period (including any optional administrative period associated with the initial measurement period)). An employer will not be subject to an assessable payment under section 4980H(a) with respect to an employee described in this paragraph (d)(3)(vii) for any calendar month during the period described in the prior sentence if, for the calendar month, the employee is otherwise eligible for an offer of coverage under a group health plan of the employer, provided that the employee is offered coverage by the employer no later than the end of the period described in the prior sentence if the employee is still employed on that date; if the offer of coverage for which the employee is otherwise eligible during the period described in the prior sentence, and which the employee is actually offered by the first day after the end of that period if still employed, provides minimum value, the employer also will not be subject to an assessable payment under section 4980H(b) with respect to that employee during that period. For purposes of this paragraph (d)(3)(vii), an employee is otherwise eligible to be offered coverage under a group health plan for a calendar month if, pursuant to the terms of the plan as in effect for that calendar month, the employee meets all conditions to be offered coverage under the plan for that calendar month, other than the completion of a waiting period, within the meaning of § 54.9801–2.

(B) *Example*. The following example illustrates the provisions of paragraph (d)(3)(vii) of this section. In the following example, the applicable large employer member has 200 full-time employees and offers all of its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan. The coverage is affordable within the meaning of section 36B(c)(2)(C)(i) (or is treated as affordable under one of the affordability safe harbors described in § 54.4980H–5) and provides minimum value.

Example (Change in employment status from variable hour employee to full-time employee). (i) *Facts*. For new variable hour employees, Employer Z uses a 12-month initial measurement period that begins on the start date and applies an administrative period from the end of the initial measurement period through the end of the first calendar month beginning on or after the end of the initial measurement period. For new variable hour employees, Employer Z offers coverage no later than the first day of the fourteenth month after the start date if an employee averages 30 or more hours of service per week during the initial measurement period. Employer Z hires Employee A on May 10, 2015. Employee A's initial measurement period runs from May 10, 2015, through May 9, 2016, with the optional administrative period ending June 30, 2016. At Employee A's May 10, 2015, start date, Employee A is a variable hour employee. On September 15, 2015, Employer Z promotes Employee A to a position that can reasonably be expected to average at least 30 hours of service per week. For October 2015 through December 2015, Employee A is otherwise eligible for an offer of coverage that provides minimum value, and, on January 1, 2016, Employee A is offered coverage by the employer that provides minimum value.

(ii) *Conclusion*. Employer Z will not be subject to an assessable payment under section 4980H(a) with respect to Employee A for October 2015, November 2015, or December 2015, because for each of those months Employee A is otherwise eligible for an offer of coverage and because Employee A is offered coverage by January 1, 2016 (the date that is the earlier of the first day of the fourth calendar month following the change in employment status (January 1, 2016) or the first day of the calendar month after the end of the initial measurement period plus the optional administrative period (July 1, 2016)). Because the coverage offered on January 1, 2016, provides minimum value, Employer Z also will not be subject to an assessable payment under section 4980H(b) with respect to Employee A for October 2015, November 2015, or December 2015.

(4) *Transition from new variable hour employee, new seasonal employee, or new part-time employee to ongoing employee*—(i) *In general*. Once a new variable hour employee, new seasonal employee, or new part-time employee has been employed for an entire standard measurement period, the applicable large employer member must test the employee for

full-time employee status, beginning with that standard measurement period, at the same time and under the same conditions as apply to other ongoing employees. Accordingly, for example, an applicable large employer member with a calendar year standard measurement period that also uses a one-year initial measurement period beginning on the employee's start date would test a new employee whose start date is April 12 for full-time employee status first based on the initial measurement period (April 12 of the year including the start date through April 11 of the following year) and again based on the calendar year standard measurement period (if the employee continues in employment for that entire standard measurement period) beginning on January 1 of the year after the start date.

(ii) *Employee determined to be employed an average of at least 30 hours of service per week*. An employee who was employed an average of at least 30 hours of service per week during an initial measurement period or standard measurement period must be treated as a full-time employee for the entire associated stability period. This is the case even if the employee was employed an average of at least 30 hours of service per week during the initial measurement period but was not employed an average of at least 30 hours of service per week during the overlapping or immediately following standard measurement period. In that case, the applicable large employer member may treat the employee as not a full-time employee only after the end of the stability period associated with the initial measurement period. Thereafter, the applicable large employer member must determine the employee's status as a full-time employee in the same manner as it determines such status in the case of its other ongoing employees as described in paragraph (d)(1) of this section.

(iii) *Employee determined not to be employed an average of at least 30 hours of service per week*. If the employee was not employed an average of at least 30 hours of service per week during the initial measurement period, but was employed at least 30 hours of service per week during the overlapping or immediately following standard measurement period, the employee must be treated as a full-time employee for the entire stability period that corresponds to that standard measurement period (even if that stability period begins before the end of the stability period associated with the initial measurement period). Thereafter, the applicable large employer member must determine the employee's status as a full-time employee in the same manner as it determines such status in the case of its other ongoing employees as described in paragraph (d)(1) of this section.

(iv) *Treatment during periods between stability periods*. If there is a period between the end of the stability period associated with the initial measurement period and the beginning of the stability period associated with the first full standard measurement period during which an employee is employed, the treatment as a full-time employee or not a full-time employee that applies during the stability period associated with the initial measurement period continues to apply until the beginning of the stability period associated with the first full standard measurement period during which the employee is employed.

(5) *Examples*. The following examples illustrate the look-back measurement methods described in paragraphs (d)(1), (d)(3) and (d)(4) of this section. In all of the following examples, the applicable large employer member has 200 full-time employees and offers all of its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan. The coverage is affordable within the meaning of section 36B(c)(2)(C)(i) (or is treated as affordable coverage under one of the affordability safe harbors described in § 54.4980H–5) and provides minimum value. In *Example 1* through *Example 8*, the new employee is a new variable hour employee, and the employer has chosen to use a 12-month standard measurement period for ongoing employees starting October 15 and a 12-month stability period associated with that standard measurement period starting January 1. (Thus, during the administrative period from October 15 through December 31 of each calendar year, the employer continues to offer coverage to employees who qualified for coverage for that entire calendar year based upon having an average of at least 30 hours of service per week during the prior standard measurement period.) In *Example 9* and *Example 10*, the new employee is a new variable hour employee, and the employer uses a six-month standard measurement period, starting each May 1 and November 1, with six-month stability periods associated with those standard measurement periods starting January 1 and July 1. In *Example 12*, *Example 13*, and *Example 14*, the employer is in the trade or business of providing temporary workers to numerous clients that are unrelated to the employer and to one another; the employer is the common law employer of the temporary workers based on all of the facts and circumstances; the employer offers health plan coverage only to full-time employees (including temporary workers who are full-time employees) and their dependents; and the employer uses a 12-month initial measurement period for new variable hour employees that begins on the start date and applies an administrative period from the end of the initial measurement period through the end of the first calendar month beginning after the end of the initial measurement period.

Example 1 (12-Month initial measurement period followed by 1+ partial month administrative period). (i) *Facts*. For new variable hour employees, Employer Z uses a 12-month initial measurement period that begins on the start date and applies an administrative period from the end of the initial measurement period through the end of the first calendar month beginning on or after the end of the initial measurement period. Employer Z hires Employee A on May 10, 2015. Employee A's initial measurement period runs from May 10, 2015, through May 9, 2016. Employee A has an average of 30 hours of service per week during this initial measurement period. Employer Z offers coverage that provides minimum value to Employee A for a stability period that runs from July 1, 2016, through June 30, 2017. For each calendar month during the period beginning with June 2015 and ending with June 2016, Employee A is otherwise eligible for an offer of coverage with respect to the coverage that is offered to Employee A on July 1, 2016.

(ii) *Conclusion*. Employer Z uses an initial measurement period that does not exceed 12 months; an administrative period totaling not more than 90 days; and a combined initial measurement period and administrative period that does not last beyond the final day of the first calendar month beginning on or after the one-year anniversary of Employee A's start date. Accordingly, Employer Z complies with the standards for the initial measurement period and stability periods for a new variable hour employee. Employer Z will not be subject to an assessable payment under section 4980H(a) with respect to Employee A for any calendar month from June 2015 through June

2016 because, for each month during that period, Employee A is otherwise eligible for an offer of coverage and because coverage is offered no later than the end of the initial measurement period plus the associated administrative period (July 1, 2016). Employer Z will not be subject to an assessable payment under section 4980H(b) with respect to Employee A for any calendar month from June 2015 through June 2016 because the coverage Employer Z offers to Employee A provides minimum value. Employer Z will not be subject to an assessable payment under section 4980H(a) or (b) with respect to Employee A for May 2015 because an applicable large employer member is not subject to an assessable payment under section 4980H with respect to an employee for the calendar month in which falls the employee's start date if the start date is on a date other than the first day of the calendar month. Employer Z must test Employee A again based on the period from October 15, 2015, through October 14, 2016 (Employer Z's first standard measurement period that begins after Employee A's start date).

Example 2 (11-Month initial measurement period followed by 2+ partial month administrative period). (i) *Facts*. Same as *Example 1*, except that Employer Z uses an 11-month initial measurement period that begins on the start date and applies an administrative period from the end of the initial measurement period until the end of the second calendar month beginning after the end of the initial measurement period. Employee A's initial measurement period runs from May 10, 2015, through April 9, 2016. The administrative period associated with Employee A's initial measurement period ends on June 30, 2016. Employee A has an average of 30 hours of service per week during this initial measurement period.

(ii) *Conclusion*. Same as *Example 1*.

Example 3 (11-Month initial measurement period preceded by partial month administrative period and followed by 2-month administrative period). (i) *Facts*. Same as *Example 1*, except that Employer Z uses an 11-month initial measurement period that begins on the first day of the first calendar month beginning after the start date and applies an administrative period that runs from the end of the initial measurement period through the end of the second calendar month beginning on or after the end of the initial measurement period. Employee A's initial measurement period runs from June 1, 2015, through April 30, 2016. The administrative period associated with Employee A's initial measurement period ends on June 30, 2016. Employee A has an average of 30 hours of service per week during this initial measurement period.

(ii) *Conclusion*. Same as *Example 1*.

Example 4 (12-Month initial measurement period preceded by partial month administrative period and followed by 2-month administrative period). (i) *Facts*. For new variable hour employees, Employer Z uses a 12-month initial measurement period that begins on the first day of the first month following the start date and applies an administrative period that runs from the end of the initial measurement period through the end of the second calendar month beginning on or after the end of the initial measurement period. Employer Z hires Employee A on May 10, 2015. Employee A's initial measurement period runs from June 1, 2015, through May 31, 2016. Employee A has an average of 30 hours of service per week during this initial measurement period. Employer Z offers coverage to Employee A for a stability period that runs from August 1, 2016, through July 31, 2017.

(ii) *Conclusion*. Employer Z does not satisfy the standards for the look-back measurement method in paragraph (d)(3)(vi)(B) of this section because the combination of the initial partial month delay, the 12-month initial measurement period, and the two month administrative period means that the coverage offered to Employee A does not become effective until after the first day of the second calendar month following the first anniversary of Employee A's start date. Accordingly, Employer Z is potentially subject to an assessable payment under section 4980H for each full calendar month during the initial measurement period and associated administrative period.

Example 5 (Continuous full-time employee). (i) *Facts*. Same as *Example 1*; in addition, Employer Z tests Employee A again based on Employee A's hours of service from October 15, 2015, through October 14, 2016 (Employer Z's first standard measurement period that begins after Employee A's start date), determines that Employee A has an average of 30 hours of service per week during that period, and offers Employee A coverage for July 1, 2017, through December 31, 2017. (Employee A already has an offer of coverage for the period of January 1, 2017, through June 30, 2017, because that period is covered by the initial stability period following the initial measurement period, during which Employee A was determined to be a full-time employee.)

(ii) *Conclusion*. Employer Z is not subject to any payment under section 4980H for any calendar month during 2017 with respect to Employee A.

Example 6 (Initially full-time employee, becomes non-full-time employee). (i) *Facts*. Same as *Example 1*; in addition, Employer Z tests Employee A again based on Employee A's hours of service from October 15, 2015, through October 14, 2016 (Employer Z's first standard measurement period that begins after Employee A's start date), and determines that Employee A has an average of 28 hours of service per week during that period. Employer Z continues to offer coverage to Employee A through June 30, 2017 (the end of the stability period based on the initial measurement period during which Employee A was determined to be a full-time employee), but does not offer coverage to Employee A for the period of July 1, 2017, through December 31, 2017.

(ii) *Conclusion*. Employer Z is not subject to any payment under section 4980H for any calendar month during 2017 with respect to Employee A.

Example 7 (Initially non-full-time employee). (i) *Facts*. Same as *Example 1*, except that Employee A has an average of 28 hours of service per week during the initial measurement period (May 10, 2015, through May 9, 2016), and Employer Z does not offer coverage to Employee A for any calendar month in 2016.

(ii) *Conclusion*. From Employee A's start date through the end of 2016, Employer Z is not subject to any payment under section 4980H with respect to Employee A, because Employer Z complies with the standards for the measurement and stability periods for a new variable hour employee with respect to Employee A and because under those standards, Employee A is not a full-time employee for any month during 2016.

Example 8 (Initially non-full-time employee, becomes full-time employee). (i) *Facts*. Same as *Example 7*; in addition, Employer Z tests Employee A again based on Employee A's hours of service from October 15, 2015, through October 14, 2016 (Employer Z's first standard measurement period that begins after Employee A's start date), determines that Employee A has an average of 30 hours of service per week during this standard measurement period, and offers coverage to Employee A for 2017.

(ii) *Conclusion*. Employer Z is not subject to any payment under section 4980H for any calendar month during 2017 with respect to Employee A.

Example 9 (Initially full-time employee). (i) *Facts*. For new variable hour employees, Employer Y uses a six-month initial measurement period that begins on the start date and applies an administrative period that runs from the end of the initial measurement period through the end of the first full calendar month beginning after the end of the initial measurement period. Employer Y hires Employee B on May 10, 2015. Employee B's initial measurement period runs from May 10, 2015, through November 9, 2015, during which Employee B has an average of 30 hours of service per week. Employer Y offers coverage that provides minimum value to Employee B for a stability period that runs from January 1, 2016, through June 30, 2016. For each calendar month during the period from June 2015 through December 2015, Employee B is otherwise eligible for an offer of coverage with respect to the coverage that is offered to Employee B on January 1, 2016.

(ii) *Conclusion*. Employer Y uses an initial measurement period that does not exceed 12 months; an administrative period totaling not more than 90 days; and a combined initial measurement period and administrative period that does not extend beyond the final day of the first calendar month beginning on or after the one-year anniversary of Employee B's start date. Employer Y complies with the standards for the measurement and stability periods for a new variable hour employee with respect to Employee B. Employer Y is not subject to an assessable payment under section 4980H(a) with respect to Employee B for any calendar month from June 2015 through December 2015 because, for each month during that period, Employee B is otherwise eligible for an offer of coverage and because Employee B is offered coverage no later than the end of the initial measurement period plus the associated administrative period (January 1, 2016). Employer Y is not subject to an assessable payment under section 4980H(b) with respect to Employee B for any calendar month from June 2015 through December 2015 because the coverage Employer Y offers to Employee B no later than January 1, 2016, provides minimum value. Employer Y is not subject to an assessable payment under section 4980H(a) or (b) with respect to Employee B for May 2015 because an applicable large employer member is not subject to an assessable payment under section 4980H with respect to an employee for the calendar month in which falls the employee's start date if the start date is on a date other than the first day of the calendar month. Employer Y must test Employee B again based on

Employee B's hours of service during the period from November 1, 2015, through April 30, 2016 (Employer Y's first standard measurement period that begins after Employee B's start date).

Example 10 (Initially full-time employee, becomes non-full-time employee). (i) *Facts*. Same as *Example 9*; in addition, Employer Y tests Employee B again based on Employee B's hours of service during the period from November 1, 2015, through April 30, 2016 (Employer Y's first standard measurement period that begins after Employee B's start date), during which period Employee B has an average of 28 hours of service per week. Employer Y continues to offer coverage to Employee B through June 30, 2016 (the end of the initial stability period based on the initial measurement period during which Employee B has an average of 30 hours of service per week), but does not offer coverage to Employee B from July 1, 2016, through December 31, 2016.

(ii) *Conclusion*. Employer Y is not subject to any payment under section 4980H with respect to Employee B for any calendar month during 2016.

Example 11 (Seasonal employee, 12-month initial measurement period; 1+ partial month administrative period). (i) *Facts*. Employer X offers health plan coverage only to full-time employees (and their dependents). Employer X uses a 12-month initial measurement period for new seasonal employees that begins on the start date and applies an administrative period from the end of the initial measurement period through the end of the first calendar month beginning after the end of the initial measurement period. Employer X hires Employee C, a ski instructor, on November 15, 2015, with an anticipated season during which Employee C will work running through March 15, 2016. Employee C's initial measurement period runs from November 15, 2015, through November 14, 2016.

(ii) *Conclusion*. Employer X determines that Employee C is a seasonal employee because Employee C is hired into a position for which the customary annual employment is six months or less. Accordingly, Employer X may treat Employee C as a seasonal employee during the initial measurement period.

Example 12 (Variable hour employee; temporary staffing firm). (i) *Facts*. Employer W hires Employee D on January 1, 2015, in a position under which Employer W will offer assignments to Employee D to provide services in temporary placements at clients of Employer W, and employees of Employer W in the same position as Employee D, as part of their continuing employment, retain the right to reject an offer of placement. Employees of Employer W in the same position of employment as Employee D typically perform services for a particular client for 40 hours of service per week for a period of less than 13 weeks, and for each employee there are typically periods in a calendar year during which Employer W does not have an assignment to offer the employee. At the time Employee D is hired by Employer W, Employer W has no reason to anticipate that Employee D's position of employment will differ from the typical employee in the same position.

(ii) *Conclusion*. Employer W cannot determine whether Employee D is reasonably expected to average at least 30 hours of service per week for the 12-month initial measurement period. Accordingly, Employer W may treat Employee D as a variable hour employee during the initial measurement period.

Example 13 (Variable hour employee; temporary staffing firm). (i) *Facts*. Employer V hires Employee E on January 1, 2015, in a position under which Employer V will offer assignments to Employee E to provide services in temporary placements at clients of Employer V. Employees of Employer V in the same position of employment as Employee E typically are offered assignments of varying hours of service per week (so that some weeks of the assignment typically result in more than 30 hours of service per week and other weeks of the assignment typically result in less than 30 hours of service per week). Although a typical employee in the same position of employment as Employee E rarely fails to have an offer of an assignment for any period during the calendar year, employees of Employer V in the same position of employment, as part of their continuing employment, retain the right to reject an offer of placement, and typically refuse one or more offers of placement and do not perform services for periods ranging from four to twelve weeks during a calendar year. At the time Employee E is hired by Employer V, Employer V has no reason to anticipate that Employee E's position of employment will differ from the typical employee in the same position.

(ii) *Conclusion*. Employer V cannot determine whether Employee E is reasonably expected to average at least 30 hours of service per week for the 12-month initial measurement period. Accordingly, Employer V may treat Employee E as a variable hour employee during the initial measurement period.

Example 14 (Variable hour employee; temporary staffing firm). (i) *Facts*. Employer T hires Employee F on January 1, 2015, in a position under which Employer T will offer assignments to Employee F to provide services in temporary placements at clients of Employer T. Employees of Employer T in the same position typically are offered assignments of 40 or more hours of service per week for periods expected to last for periods of three months to 12 months, subject to a request for renewal by the client. Employees of Employer T in similar positions to Employee F are typically offered and take new positions immediately upon cessation of a placement. At the time Employee F is hired by Employer T, Employer T has no reason to anticipate that Employee F's position of employment will differ from the typical employee in the same position.

(ii) *Conclusion*. Employer T must assume that Employee F will be employed by Employer T and available for an offer of temporary placement for the entire initial measurement period. Under that assumption, Employer T would reasonably determine that Employee F is reasonably expected to average at least 30 hours of service per week for the 12-month initial measurement period. Accordingly, Employer T may not treat Employee F as a variable hour employee during the initial measurement period.

Example 15 (Variable hour employee). (i) *Facts*. Employee G is hired on an hourly basis by Employer S to fill in for employees who are absent and to provide additional staffing at peak times. Employer S expects that Employee G will average 30 hours of service per week or more for Employee G's first few months of employment, while assigned to a specific project, but also reasonably expects that the assignments will be of unpredictable duration, that there will be periods of unpredictable duration between assignments, that the hours per week required by subsequent assignments will vary, and that Employee G will not necessarily be available for all assignments.

(ii) *Conclusion*. Employer S cannot determine whether Employee G is reasonably expected to average at least 30 hours of service per week for the initial measurement period. Accordingly, Employer S may treat Employee G as a variable hour employee during the initial measurement period.

Example 16 (Period between initial stability period and standard stability period). (i) *Facts*. Employer R uses an 11-month initial measurement period for new variable hour, new seasonal, and new part-time employees with an administrative period that lasts from the end of the initial measurement period through the last day of the first calendar month beginning on or after the first anniversary of the employee's start date. Employer R uses a standard measurement period of October 15 through October 14, and an administrative period of October 15 through December 31. Employee H is hired as a variable hour employee on October 20, 2015, with an initial measurement period of October 20, 2015, through September 19, 2016, and an administrative period lasting through November 30, 2016. Employee H is a full-time employee based on the hours of service in the initial measurement period, and Employee H's stability period for the initial measurement period is December 1, 2016, through November 30, 2017. Employee H's first full standard measurement period begins on October 15, 2016, with an associated stability period beginning on January 1, 2018. The standard measurement period beginning on October 15, 2015, does not apply to Employee H because Employee H is not hired until October 20, 2015.

(ii) *Conclusion*. For the period after the stability period associated with the initial measurement period and before the stability period associated with Employee H's first full standard measurement period (that is December 1, 2017, through December 31, 2017), Employer R must treat Employee H as a full-time employee because the treatment as a full-time employee (or not a full-time employee) that applies during the stability period associated with the initial measurement period continues to apply until the beginning of the stability period associated with the first full standard measurement period during which the employee is employed.

(6) *Employees rehired after termination of employment or resuming service after other absence*—(i) *Treatment as a new employee after a period of absence for employees of employers other than educational organizations*—(A) *In general*. The rules in this paragraph (d)(6)(i) apply to employers that are not educational organizations. For rules relating to employers that are educational organizations, see paragraph (d)(6)(ii) of this sec-

tion. An employee who resumes providing services to (or is otherwise credited with an hour of service for) an applicable large employer that is not an educational organization after a period during which the employee was not credited with any hours of service may be treated as having terminated employment and having been rehired, and therefore may be treated as a new employee upon the resumption of services, only if the employee did not have an hour of service for the applicable large employer for a period of at least 13 consecutive weeks immediately preceding the resumption of services. The rule set forth in this paragraph (d)(6)(i) applies solely for the purpose of determining whether the employee, upon the resumption of services, is treated as a new employee or as a continuing employee, and does not determine whether the employee is treated as a continuing full-time employee or a terminated employee during the period during which no hours of service are credited.

(B) *Averaging method for special unpaid leave*. For purposes of applying the look-back measurement method described in paragraph (d) of this section to an employee who is not treated as a new employee under paragraph (d)(6)(i) of this section, the employer determines the employee's average hours of service for a measurement period by computing the average after excluding any special unpaid leave during that measurement period and by using that average as the average for the entire measurement period. Alternatively, for purposes of determining the employee's average hours of service for the measurement period, the employer may choose to treat the employee as credited with hours of service for any periods of special unpaid leave during that measurement period at a rate equal to the average weekly rate at which the employee was credited with hours of service during the weeks in the measurement period that are not part of a period of special unpaid leave. There is no limit on the number of hours of service required to be excluded or credited (as the case may be) with respect to special unpaid leave. For purposes of this paragraph (d)(6)(i)(B), in computing the average weekly rate, employers are permitted to use any reasonable method if applied on a consistent basis. In addition, if an employee's average weekly rate under this paragraph (d)(6)(i)(B) is computed for a measurement period and that measurement period is shorter than six months, the six-month period ending with the close of the measurement period is used to compute the average hours of service.

(C) *Averaging rules for employment break periods for employers other than educational organizations*. The averaging rule for employment break periods described in paragraph (d)(6)(ii)(B) of this section applies only to educational organizations and does not apply to other employers.

(ii) *Treatment as a new employee after a period of absence for employees of employers that are educational organizations*—(A) *In general*. The rules of this paragraph (d)(6)(ii) apply only to employers that are educational institutions. An employee who resumes providing services to (or is otherwise credited with an hour of service for) an applicable large employer that is an educational organization after a period during which the employee was not credited with any hours of service may be treated as having terminated employment and having been rehired, and therefore may be treated as a new employee upon the resumption of services, only if the employee did not have an hour of service for the applicable large employer for a period of at least 26 consecutive weeks immediately preceding the resumption of services. The rule set forth in this paragraph (d)(6)(ii)(A) applies solely for the purpose of determining whether the employee, upon the resumption of services, is treated as a new employee or as a continuing employee, and does not determine whether the employee is treated as a continuing full-time employee or a terminated employee during the period during which no hours of service are credited.

(B) *Averaging method for special unpaid leave and employment break periods*. For purposes of applying the look-back measurement method described in paragraph (d) of this section to an employee who is not treated as a new employee under paragraph (d)(6)(ii)(A) of this section, an educational organization employer determines the employee's average hours of service for a measurement period by computing the average after excluding any special unpaid leave and any employment break period during that measurement period and by using that average as the average for the entire measurement period. Alternatively, for purposes of determining the employee's average hours of service for the measurement period, the employer may choose to treat the employee as credited with hours of service for any periods of special unpaid leave and any employment break period during that measurement period at a rate equal to the average weekly rate at which the employee was credited with hours of service during the weeks in the measurement period that are not part of a period of special unpaid leave or an employment break period. Notwithstanding the preceding two sentences, no more than 501 hours of service during employment break periods in a calendar year are required to be excluded (under the first sentence) or credited (under the second sentence) by an educational organization, provided that this 501-hour limit does not apply to hours of service required to be excluded or credited in respect of special unpaid leave. In applying the preceding sentence, an employer that uses the method described in the first sentence of this paragraph (d)(6)(ii)(B) determines the number of hours excluded by multiplying the average weekly rate for the measurement period (determined as in the second sentence of this paragraph (d)(6)(ii)(B)) by the number of weeks in the employment break period. For purposes of this paragraph (d)(6)(ii)(B), in computing the average weekly rate, employers are permitted to use any reasonable method if applied on a consistent basis. In addition, if an employee's average weekly rate under this paragraph (d)(6)(ii)(B) is being computed for a measurement period and that measurement period is shorter than six months, the six-month period ending with the close of the measurement period is used to compute the average hours of service.

(iii) *Treatment of continuing employee*. Under the look-back measurement method, an employee treated as a continuing employee retains, upon resumption of services, the status that employee had with respect to the application of any stability period (for example, if the continuing employee returns during a stability period in which the employee is treated as a full-time employee, the employee is treated as a full-time employee upon return and through the end of that stability period). For purposes of the preceding sentence, a continuing employee treated as a full-time employee is treated as offered coverage upon resumption of services if the employee is offered coverage as of the first day that employee is credited with an hour of service, or, if later, as soon as administratively practicable. For this purpose, offering coverage by no later than the first day of the calendar month following resumption of services is deemed to be as soon as administratively practicable. If a continuing employee returns during a stability period in which the employee is treated as a full-time employee and the employer previously made the employee an offer of coverage with respect to the entire stability period and the employee declined the offer, the employer will continue to be treated as having offered coverage for that stability period and the employer need not make a new offer of coverage for the remainder of the ongoing stability period due to the employee's resumption of services.

(iv) *Rule of parity*. For purposes of determining the period after which an employee may be treated as having terminated employment and having been rehired, an applicable large employer may choose a period, measured in weeks, of at least four consecutive weeks during which the employee was not credited with any hours of service that exceeds the number of weeks of that employee's period of employment with the applicable large employer immediately preceding the period and that is shorter than 13 weeks (for an employee of an educational organization employer, a period that is shorter than 26 weeks). For purposes of the preceding sentence, the duration of the immediately preceding period of employment is determined after application to that period of employment of the averaging methods described in paragraphs (d)(6)(i)(B) and (d)(6)(ii)(B) of this section (relating to employment break periods and special unpaid leave), if applicable.

(v) *International transfers*. An employer may treat an employee as having terminated employment if the employee transfers to a position at the same applicable large employer (including a different applicable large employer member that is part of the same applicable large employer) if the position is anticipated to continue indefinitely or for at least 12 months and if substantially all of the compensation will constitute income from sources without the United States (within the meaning of sections 861 through 863 and the regulations thereunder). With respect to an employee transferring from a position that was anticipated to continue indefinitely or for at least 12 months and in which substantially all of the compensation for the hours of service constitutes income from sources without the United States (within the meaning of sections 861 through 863 and the regulations thereunder) to a position at the same applicable large employer (including a different applicable large employer member that is part of the same applicable large employer) with respect to which substantially all of the compensation will constitute U.S. source income, the employer may treat that employee as a new hire to the extent consistent with the rules related to rehired employees in paragraph (d)(6) of this section.

(vi) *Anti-abuse rule*. For purposes of this paragraph (d)(6), any hour of service is disregarded if the hour of service is credited, or the services giving rise to the crediting of the hour of service are requested or required of the employee, for a purpose of avoiding or undermining the application of the employee rehire rules under paragraph (d)(6) of this section, or the application of the averaging method for employment break periods under paragraph (d)(6)(ii)(B) of this section. For example, if an employee of an educational organization would otherwise have a period with no hours of service to which the rules under paragraph (d)(6)(ii)(B) of this section would apply, but for the employer's request or requirement that the employee perform one or more hours of service for a purpose of avoiding the application of those rules, any such hours of service for the week are disregarded, and the rules under paragraph (d)(6)(ii)(B) of this section will apply.

(vii) *Examples*. The following examples illustrate the provisions of paragraph (d)(6) of this section. All employers in these examples are applicable large employer members with 200 full-time employees (including full-time equivalent employees), each is in a different applicable large employer group, and each determines full-time employee status under the look-back measurement method. None of the periods during which an employee is not credited with an hour of service for an employer involve special unpaid leave or the employee being credited with hours of service for any applicable large employer member in the same applicable large employer as the employer.

Example 1. (i) *Facts*. As of April 1, 2015, Employee A has been an employee of Employer Z (which is not an educational organization) for 10 years. On April 1, 2015, Employee A terminates employment and is not credited with an hour of service until June 1, 2015, when Employer Z rehires Employee A and Employee A continues as an employee through December 31, 2015, which is the close of the measurement period as applied by Employer Z.

(ii) *Conclusion*. Because the period for which Employee A is not credited with any hours of service is not longer than Employee A's prior period of employment and is less than 13 weeks, Employee A is not treated as having terminated employment and been rehired for purposes of determining whether Employee A is treated as a new employee upon resumption of services. Therefore, Employee A's hours of service prior to termination are required to be taken into account for purposes of the measurement period, and Employee A's period with no hours of service is taken into account as a period of zero hours of service during the measurement period.

Example 2. (i) *Facts*. Same facts as *Example 1*, except that Employee A is rehired on December 1, 2015.

(ii) *Conclusion*. Because the period during which Employee A is not credited with an hour of service for Employer Z exceeds 13 weeks, Employee A is treated as having terminated employment on April 1, 2015, and having been rehired as a new employee on December 1, 2015, for purposes of determining Employee A's full-time employee status. Because Employee A is treated as a new employee, Employee A's hours of service prior to termination are not taken into account for purposes of the measurement period, and the period between termination and rehire with no hours of service is not taken into account in the new measurement period that begins after the employee is rehired.

Example 3. (i) *Facts*. Employee B is employed by Employer Y, an educational organization. Employee B is employed for 38 hours of service per week on average from September 7, 2014, through May 23, 2015, and then does not provide services (and is not otherwise credited with an hour of service) during the summer break when the school is generally not in session. Employee B resumes providing services for Employer Y on September 7, 2015, when the new school year begins.

(ii) *Conclusion*. Because the period from May 24, 2015 through September 5, 2015 (a total of 15 weeks), during which Employee B is not credited with an hour of service does not exceed 26 weeks, and also does not exceed the number of weeks of Employee B's immediately preceding period of employment, Employee B is not treated as having terminated employment on May 24, 2015, and having been rehired on September 6, 2015. Also, for purposes of determining Employee B's average hours of service per week for the measurement period, Employee B is credited, under the averaging method for employment break periods applicable to educational organizations, as having an average of 38 hours of service per week for the 15 weeks between May 24, 2015 and September 5, 2015, during which Employee B otherwise was credited with no hours of service. However, Employer Y is not required to credit more than 501 hours of service for the employment break period (15 weeks x 38 hours = 570 hours).

Example 4. (i) *Facts*. Same facts as *Example 3*, except that Employee B does not resume providing services for Employer Y until December 5, 2015.

(ii) *Conclusion*. Because the period from May 24, 2015 through December 5, 2015, exceeds 26 weeks, Employee B may be treated as having terminated employment on May 24, 2015, and having been rehired on December 5, 2015. Because Employee B is treated as a new employee on December 5, 2015, Employee B's hours of service prior to termination are not taken into account for purposes of the measurement period, and the period between termination and rehire with no hours of service is not taken into account in the new measurement period that begins after Employee B is rehired. The averaging method for employment break periods applicable to educational organizations does not apply because Employee B is treated as a new employee rather than a continuing employee as of the date of resumption of services.

(e) *Use of the look-back measurement method and the monthly measurement method for different categories of employees*. Different applicable large employer members of the same applicable large employer may use different methods of determining full-time employee status (that is, either the monthly measurement method or the look-back measurement method). In addition, an applicable large employer member may use either the monthly measurement method or the look-back measurement method for each of the categories of employees set forth in paragraphs (d)(1)(v) and (d)(3)(v) of this section, and is not required to use the same method for all categories.

(f) *Changes in employment status resulting in a change in full-time employee determination method*—(1) *Change in employment status from a position to which a look-back measurement method applies to a position to which the monthly measurement method applies, or vice versa*—(i) *Change from look-back measurement method to monthly measurement method*. For an employee transferring from a position under which the look-back measurement method is used to determine the employee's status as a full-time employee, to a position under which the monthly measurement method is used to determine the employee's status as a full-time employee, the following rules apply:

(A) For an employee who at the time of the change of position is in a stability period under which the employee is treated as a full-time employee, the employer must continue to treat the employee as a full-time employee through the end of the stability period;

(B) For an employee who at the time of the change of position is in a stability period under which the employee is not treated as a full-time employee, the employer may continue to treat the employee as not a full-time employee through the end of the stability period, or may apply the monthly measurement method set forth in paragraph (c) of this section through the end of the stability period beginning with any calendar month including the calendar month in which the change in employment status occurs or any subsequent calendar month;

(C) For the stability period associated with the measurement period during which the change in employment status occurs, the employer must treat the employee as a full-time employee for any calendar month during which the employee either would be treated as a full-time employee under the stability period that would have applied based on the measurement period in which the change in employment status occurred or would be treated as a full-time employee under the monthly measurement method; and

(D) For any calendar month subsequent to the stability period identified in paragraph (f)(1)(i)(C) of this section, the monthly measurement method applies for determination of the employee's status as a full-time employee.

(ii) *Change from monthly measurement method to look-back measurement method*. For an employee who is transferring from a position under which the monthly measurement method is used to determine the employee's status as a full-time employee, to a position under which a look-back measurement method is used to determine the employee's status as a full-time employee, the following rules apply:

(A) For the remainder of the applicable stability period during which the change in employment status occurs, the employer must continue to use the monthly measurement method to determine the employee's status as a full-time employee unless the employee's hours of service prior to the change in employment status would have resulted in the employee being treated as a full-time employee during the stability period in which the change in employment status occurs, in which case the employer must treat the employee as a full-time employee for that stability period;

(B) For the applicable stability period following the measurement period during which the change in employment status occurs, the employer must treat the employee as a full-time employee for any calendar month during which the employee either would be treated as a full-time employee based on the measurement period during which the change in employment status occurs or would be treated as a full-time employee under the monthly measurement method; and

(C) For any calendar month subsequent to the stability period identified in paragraph (f)(1)(ii)(B) of this section, the look-back measurement method applies for determination of the employee's status as a full-time employee.

(iii) *Examples*. The following examples illustrate the rules of this paragraph (f). In each example, the employer is an applicable large employer with 200 full-time employees (including FTEs). For each example, the employer uses the monthly measurement method for determining whether a salaried employee is a full-time employee, and the look-back measurement method for determining whether an hourly employee is a full-time employee with a measurement period from October 15 through October 14 of the following calendar year, and a stability period from January 1 through December 31. In each case, the relevant employee has been employed continuously for several years.

Example 1 (Look-back measurement method to monthly measurement method). Employee A is an hourly employee. Based on Employee A's hours of service from October 15, 2015, through October 14, 2016, Employee A is treated as a full-time employee from January 1, 2017, through December 31, 2017. On July 1, 2017, Employee A transfers from a position as an hourly employee to a position as a salaried employee. For the months July 2017 through December 2017, Employee A must be treated as a full-time employee. Employee A is employed for hours of service from October 15, 2016, through October 14, 2017, such that under the applicable look-back measurement method Employee A would be treated as a full-time employee for the period of January 1, 2018, through December 31, 2018. Accordingly, Employee A must be treated as a full-time employee for the calendar year 2018. For calendar year 2019, the determination of whether Employee A is a full-time employee is made under the monthly measurement method.

Example 2 (Look-back measurement method to monthly measurement method). Same facts as *Example 1*, except that based on Employee A's hours of service from October 15, 2015, through October 14, 2016, Employee A is not treated as a full-time employee from January 1, 2017, through December 31, 2017. For the months July 2017 through December 2017, Employer Z may either treat Employee A as not a full-time employee or apply the monthly measurement method to determine Employee A's status as a full-time employee. Employee A is employed for hours of service from October 15, 2016, through October 14, 2017, such that under the applicable look-back measurement method Employee A would be treated as a full-time employee for the period of January 1, 2018, through December 31, 2018. Employee A must be treated as a full-time employee for the calendar year 2018. For calendar year 2019, the determination of whether Employee A is a full-time employee is made under the monthly measurement method.

Example 3 (Look-back measurement method to monthly measurement method). Same facts as *Example 1*, except that Employee A is employed for hours of service from October 15, 2016, through October 14, 2017, such that under the applicable look-back measurement method Employee A would not be treated as a full-time employee for the period of January 1, 2018, through December 31, 2018. For the calendar year 2018, Employer Z must treat Employee A as a full-time employee only for calendar months during which Employee A would be a full-time employee under the monthly measurement method. For calendar year 2019, the determination of whether Employee A is a full-time employee is made under the monthly measurement method.

Example 4 (Monthly measurement method to look-back measurement method). Employee B is a salaried employee of Employer Y. On July 1, 2017, Employee B transfers to an hourly employee position. Based on Employee B's hours of service from October 15, 2015, through October 14, 2016, Employee B would have been treated as a full-time employee for the stability period from January 1, 2017, through December 31, 2017, had the look-back measurement method applicable to hourly employees applied to Employee B for the entire stability period. For the calendar months January 2017 through June 2017 (prior to Employee B's change to hourly employee status), Employee B's status as a full-time employee is determined using the monthly measurement method. For the calendar months July 2017 through December 2017, Employer Y must treat Employee B as a full-time employee because Employee B would have been treated as a full-time employee during that portion of the stability period had the look-back measurement method applied to Employee B for that entire stability period. Employee B is employed for hours of service from October 15, 2016, through October 14, 2017, such that under the applicable look-back measurement method Employee B would be treated as a full-time employee for the period January 1, 2018, through December 31, 2018. Accordingly, Employee B must be treated as a full-time employee for the calendar year 2018. For calendar year 2019, the determination of whether Employee B is a full-time employee is made under the applicable look-back measurement method.

Example 5 (Monthly measurement method to look-back measurement method). Same facts as *Example 4*, except that based on Employee B's hours of service from October 15, 2015, through October 14, 2016, Employee B would not have been treated as a full-time employee from January 1, 2017, through December 31, 2017. For the calendar months of 2017, Employer Y applies the monthly measurement method to determine Employee B's status as a full-time employee. Employee B is employed for hours of service from October 15, 2016, through October 14, 2017, such that under the applicable look-back measurement method Employee B would be treated as a full-time employee for the period January 1, 2018, through December 31, 2018. Accordingly, Employee B must be treated as a full-time employee for the calendar year 2018. For calendar year 2019, the determination of whether Employee B is a full-time employee is made under the applicable look-back measurement method.

Example 6 (Monthly measurement method to look-back measurement method). Same facts as *Example 4*, except that Employee B is employed for hours of service from October 15, 2016, through October 14, 2017, such that under the applicable look-back measurement method Employee B would not be treated as a full-time employee for the period of January 1, 2018, through December 31, 2018. For the calendar year 2018, Employer Y must treat Employee B as a full-time employee only for calendar months during which Employee B would be a full-time employee under the monthly measurement method.

(2) *Special rule for certain employees to whom minimum value coverage has been continuously offered*—(i) *In general*. Notwithstanding the rules in paragraphs (e) and (f) of this section, an employer using the look-back measurement method to determine the full-time employee status of an employee may apply the monthly measurement method to that employee beginning on the first day of the fourth full calendar month following the calendar month in which the employee experiences a change in employment status such that, if the employee had begun employment in the new position or status, the employee would have reasonably been expected not to be employed on average at least 30 hours of service per week (for example, the employee has changed to a part-time position of only 20 hours of service per week). This rule only applies with respect to an employee to whom the applicable large employer member offered minimum value coverage by the first day of the calendar month following the employee's initial three full calendar months of employment through the calendar month in which the change in employment status described in this paragraph (f)(2) occurs, and only if the employee actually averages less than 30 hours of service per week for each of the three full calendar months following the change in employment status. For the three full calendar months between the employee's change in employment status and the application of the monthly measurement method, the employee's full-time employee status is determined based on the employee's status during the applicable stability period(s). Under this rule, an employer may apply the monthly measurement method to an employee even if the employer does not apply the monthly measurement method to the other employees in the same category of employees under paragraph (d)(1)(v) or (d)(3)(v) of this section (for example, under this method an employer could apply the monthly measurement method to an hourly employee, even if the employer uses the look-back measurement method to determine full-time employee status of all other hourly employees). The employer may continue to apply the monthly measurement method through the end of the first full measurement period (and any associated administrative period) that would have applied had the employee remained under the applicable look-back measurement method.

(ii) *Examples*. The following examples illustrate the rule of paragraphs (f)(2) of this section. In each example, the employer is an applicable large employer with 200 full-time employees (including FTEs).

Example 1 (New variable hour employee, no delay in coverage, becomes non-full-time employee). (i) *Facts*. Employer Z, an applicable large employer, uses the look-back measurement method to determine the full-time employee status for all of its employees. On May 10, 2015, Employer Z hired Employee A who is a variable hour employee. Although Employee A is a new variable hour employee, so that Employer Z could wait until the end of an initial measurement period to offer coverage to Employee A without an assessable payment under section 4980H with respect to Employee A, Employer Z offers coverage that provides minimum value to Employee A on September 1, 2015. For its ongoing employees, Employer Z has chosen to use a 12-month standard measurement period starting October 15 and a 12-month stability period associated with that standard measurement period starting January 1. Employee A continues in employment with Employer Z for over five years and averages more than 30 hours of service per week for all measurement periods through the measurement period ending October 14, 2020. On February 12, 2021, Employee A experiences a change in position of employment with Employer Z to a position under which Employer Z reasonably expects Employee A to average less than 30 hours of service per week. For the calendar months after February 2021, Employee A averages less than 30 hours of service per week. Employer Z offered Employee A coverage that provided minimum value continuously from September 1, 2015, through May 31, 2021. Effective June 1, 2021, Employer Z elects to apply the monthly measurement method to determine Employee A's status as a full-time employee for the remainder of the stability period ending December 31, 2021, and the calendar year 2022 (which is through the end of the first full measurement period following the change in employment status plus the associated administrative period). Applying the stability period beginning January 1, 2021, Employer Z treats Employee A as a full-time employee for each calendar month from January 2021 through May 2021. Applying the monthly measurement method, for each calendar month from June 2021 through December 2022, Employer Z treats Employee A as not a full-time employee.

(ii) *Conclusion*. Because Employer Z offered coverage that provided minimum value to Employee A from no later than the first day of the fourth full calendar month following Employee A's start date through the calendar month in which the change in employment status occurred, and because Employee A did not average 30 hours of service per week for any of the three calendar months immediately following Employee A's change in employment status to an employee not reasonably expected to average 30 hours of service per week, Employer Z may use the monthly measurement method to determine the full-time employee status of Employee A beginning on the first day of the fourth month following the change in employment status (June 1, 2021) through the end of the first full measurement period (plus any associated administrative period) immediately following the change in employment status (December 31, 2022). Because Employee A did not average at least 30 hours of service per week for any calendar month from June 2021 through December 2022, Employer Z has properly treated Employee A as not a full-time employee for those calendar months.

Example 2 (New full-time employee, no delay in coverage, becomes non-full-time employee). (i) *Facts*. Same facts as *Example 1*, except that at Employee A's start date, Employer Z reasonably expects that Employee A will average at least 30 hours of service per week. Accordingly, Employer Z offers coverage to Employee A beginning on September 1, 2015, and offers coverage continuously to Employee A for all calendar months through May 2021.

(ii) *Conclusion*. Same as *Example 1*.

(g) *Nonpayment or late payment of premiums*. An applicable large employer member will not be treated as failing to offer to a full-time employee (and his or her dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan for an employee whose coverage under the plan is terminated during the coverage period solely due to the employee failing to make a timely payment of the employee portion of the premium. This treatment continues only through the end of the coverage period (typically the plan year). For this purpose, the rules in § 54.4980B–8, Q&A–5(a), (c), (d) and (e) apply under this section to the payment for coverage with respect to a full-time employee in the same manner that they apply to payment for COBRA continuation coverage under § 54.4980B–8.

(h) *Additional guidance*. With respect to the determination of full-time employee status, including determination of hours of service, the Commissioner may prescribe additional guidance of general applicability, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter).

(i) *Effective/applicability date*. This section is applicable for periods after

December 31, 2014.

§ 54.4980H–4 Assessable payments under section 4980H(a).

(a) *In general*. If an applicable large employer member fails to offer to its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan for any calendar month, and the applicable large employer member has received a Section 1411 Certification with respect to at least one full-time employee, an assessable payment is imposed. For the calendar month, the applicable large employer member will owe an assessable payment equal to the product of the section 4980H(a) applicable payment amount and the number of full-time employees of the applicable large employer member (other than employees in a limited non-assessment period for certain employees and as adjusted in accordance with paragraph (e) of this section). For purposes of this paragraph (a), an applicable large employer member is treated as offering such coverage to its full-time employees (and their dependents) for a calendar month if, for that month, it offers such coverage to all but five percent (or, if greater, five) of its full-time employees (provided that an employee is treated as having been offered coverage only if the employer also offers coverage to that employee's dependents). For purposes of the preceding sentence, an employee in a limited non-assessment period for certain employees is not included in the calculation.

(b) *Offer of coverage*—(1) *In general*. An applicable large employer member will not be treated as having made an offer of coverage to a full-time employee for a plan year if the employee does not have an effective opportunity to elect to enroll in the coverage at least once with respect to the plan year, or does not have an effective opportunity to decline to enroll if the coverage offered does not provide minimum value or requires an employee contribution for any calendar month of more than 9.5 percent of a monthly amount determined as the federal poverty line for a single individual for the applicable calendar year, divided by 12. For this purpose, the applicable federal poverty line is the federal poverty line for the 48 contiguous states and the District of Columbia. Whether an employee has an effective opportunity to enroll or to decline to enroll is determined based on all the relevant facts and circumstances, including adequacy of notice of the availability of the offer of coverage, the period of time during which acceptance of the offer of coverage may be made, and any other conditions on the offer. An employee's election of coverage from a prior year that continues for the next plan year unless the employee affirmatively elects to opt out of the plan constitutes an offer of coverage for purposes of section 4980H.

(2) *Offer of coverage on behalf of another entity*. For purposes of section 4980H, an offer of coverage by one applicable large employer member to an employee for a calendar month is treated as an offer of coverage by all applicable large employer members for that calendar

month. In addition, an offer of coverage made to an employee on behalf of a contributing employer under a multiemployer or single employer Taft-Hartley plan or multiple employer welfare arrangement (MEWA) is treated as made by the employer. For an offer of coverage to an employee performing services for an employer that is a client of a staffing firm, in cases in which the staffing firm is not the common law employer of the individual and the staffing firm makes an offer of coverage to the employee on behalf of the client employer under a plan established or maintained by the staffing firm, the offer is treated as made by the client employer for purposes of section 4980H only if the fee the client employer would pay to the staffing firm for an employee enrolled in health coverage under the plan is higher than the fee the client employer would pay the staffing firm for the same employee if that employee did not enroll in health coverage under the plan.

(c) *Partial calendar month*. If an applicable large employer member fails to offer coverage to a full-time employee for any day of a calendar month, that employee is treated as not offered coverage during that entire month, regardless of whether the employer uses the payroll period rule set forth in § 54.4980H–3(d)(1)(ii) or the weekly rule set forth in § 54.4980H–3(c)(3) to determine full-time employee status for the calendar month. However, in a calendar month in which the employment of a full-time employee terminates, if the employee would have been offered coverage for the entire calendar month had the employee been employed for the entire calendar month, the employee is treated as having been offered coverage for that entire calendar month. In addition, an applicable large employer member is not subject to an assessable payment under section 4980H with respect to an employee for the calendar month in which the employee's start date occurs if the start date is on a date other than the first day of the calendar month, and, in addition, with respect to the calendar month in which the start date occurs, such an employee is not included for purposes of the calculation of any potential liability under section 4980H(a).

(d) *Application to applicable large employer member*. The liability for an assessable payment under section 4980H(a) for a calendar month with respect to a full-time employee applies solely to the applicable large employer member that was the employer of that employee for that calendar month. For an employee who was an employee of more than one applicable large employer member of the same applicable large employer during a calendar month, the liability for the assessable payment under section 4980H(a) for a calendar month applies to the applicable large employer member for whom the employee has the greatest number of hours of service for that calendar month (if the employee has an equal number of hours of service for two or more applicable large employer members of the same applicable large employer for the calendar month, those applicable large employer members can treat one of those members as the employer of that employee for that calendar month for purposes of this section, and if the members do not select one member, or select in an inconsistent manner, the IRS will select a member to be treated as the employer of that employee for purposes of the assessable payment determination). For a calendar month, an applicable large employer member may be liable for an assessable payment under section 4980H(a) or under section 4980H(b), but will not be liable for an assessable payment under both section 4980H(a) and section 4980H(b).

(e) *Allocated reduction of 30 full-time employees*. For purposes of the liability calculation under paragraph (a) of this section, with respect to each calendar month, an applicable large employer member's number of full-time employees is reduced by that member's allocable share of 30. The applicable large employer member's allocation is equal to 30 allocated ratably among all members of the applicable large employer on the basis of the number of full-time employees employed by each applicable large employer member during the calendar month (after application of the rules of paragraph (d) of this section addressing employees who work for more than one applicable large employer member during a calendar month). If an applicable large employer member's total allocation is not a whole number, the allocation is rounded to the next highest whole number. This rounding rule may result in the aggregate reduction for the entire group of applicable large employer members exceeding 30.

(f) *Example*. The following example illustrates the provisions of paragraphs (a) and (e) of this section.

Example. (i) *Facts*. Applicable large employer member Z and applicable large employer member Y are the two members of an applicable large employer. Applicable large employer member Z employs 40 full-time employees in each calendar month of 2017. Applicable large employer member Y employs 35 full-time employees in each calendar month of 2017. Assume that for 2017, the applicable payment amount for a calendar month is $2,000 divided by 12. Applicable large employer member Z does not sponsor an eligible employer-sponsored plan for any calendar month of 2017, and receives a Section 1411 Certification for 2017 with respect to at least one of its full-time employees. Applicable large employer member Y sponsors an eligible employer-sponsored plan under which all of its full-time employees are eligible for minimum essential coverage.

(ii) *Conclusion*. Pursuant to section 4980H(a) and this section, applicable large employer member Z is subject to an assessable payment under section 4980H(a) for 2017 of $48,000, which is equal to 24 x $2,000 (40 full-time employees reduced by 16 (its allocable share of the 30-employee offset ((40/75) x 30 = 16)) and then multiplied by $2,000). Applicable large employer member Y is not subject to an assessable payment under section 4980H(a) for 2017.

(g) *Additional guidance*. With respect to assessable payments under section 4980H(a), the Commissioner may prescribe additional guidance of general applicability, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter).

(h) *Effective/applicability date*. This section is applicable for periods after December 31, 2014.

§ 54.4980H–5 Assessable payments under section 4980H(b).

(a) *In general*. If an applicable large employer member offers to its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan for any calendar month (including an offer of coverage to all but five percent or less (or, if greater, five or less) of its full-time employees (provided that an employee is treated as having been offered coverage only if the employer also offers coverage to that employee's dependents)) and the applicable large employer member has received a Section 1411 Certification with respect to one or more full-time employees of the applicable large employer member, then there is imposed on the applicable large employer member an assessable payment equal to the product of the number of full-time employees of the applicable large employer member for which it has received a Section 1411 Certification (minus the number of those employees in a limited non-assessment period for certain employees and the number of other employees who were offered the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan that satisfied minimum value and met one or more of the affordability safe harbors described in paragraph (e) of this section) and the section 4980H(b) applicable payment amount. Notwithstanding the foregoing, the aggregate amount of assessable payment determined under this paragraph (a) with respect to all employees of an applicable large employer member for any calendar month may not exceed the product of the section 4980H(a) applicable payment amount and the number of full-time employees of the applicable large employer member during that calendar month (reduced by the applicable large employer member's ratable allocation of the 30 employee reduction under § 54.4980H–4(e)).

(b) *Offer of coverage*. For purposes of this section, the same rules with respect to an offer of coverage for purposes of section 4980H(a) apply. See § 54.4980H–4.

(c) *Partial calendar month*. If an applicable large employer member fails to offer coverage to a full-time employee for any day of a calendar month, that employee is treated as not offered coverage during that entire month, regardless of whether the employer uses the payroll period rule set forth in § 54.4980H–3(d)(1)(ii) or the weekly rule set forth in § 54.4980H–3(c)(3) to determine full-time employee status for the calendar month. However, in a calendar month in which a full-time employee's employment terminates, if the employee would have been offered coverage if the employee had been employed for the entire month, the employee is treated as having been offered coverage during that month. Also, an applicable large employer member is not subject to an assessable payment under section 4980H with respect to an employee for the calendar month in which the employee's start date occurs if the start date is on a date other than the first day of the calendar month.

(d) *Applicability to applicable large employer member*. The liability for an assessable payment under section 4980H(b) for a calendar month with respect to a full-time employee applies solely to the applicable large employer member that was the employer of that employee for that calendar month. For an employee who was a full-time employee of more than one applicable large employer member during that calendar month, the liability for the assessable payment under section 4980H(b) for a calendar month applies to the applicable large employer member for whom the employee has the greatest number of hours of service for that calendar month (if the employee has an equal number of hours of service for two or more applicable large employer members for the calendar month, those applicable large employer members can treat one of those members as the employer of that employee for that calendar month for purposes of this paragraph (d), and if the members do not select one member, or select in an inconsistent manner, the IRS will select a member to be treated as the employer of that employee for purposes of the assessable payment determination). For a calendar month, an applicable large employer member may be liable for an assessable payment under section 4980H(a) or under section 4980H(b), but will not be liable for an assessable payment under both section 4980H(a) and section 4980H(b).

(e) *Affordability*—(1) *In general*. An employee who is offered coverage by an applicable large employer member may be eligible for an applicable premium tax credit or cost-sharing reduction if that offer of coverage is not affordable within the meaning of section 36B(c)(2)(C)(i) and the regulations thereunder.

(2) *Affordability safe harbors for section 4980H(b) purposes*. The affordability safe harbors set forth in paragraph (e)(2)(ii) through (iv) of this section apply solely for purposes of section 4980H(b), so that an applicable large employer member that offers minimum essential coverage providing minimum value will not be subject to an assessable payment under section 4980H(b) with respect to any employee receiving the applicable premium tax credit or cost-sharing reduction for a period for which the coverage is determined to be affordable under the requirements of an affordability safe harbor. This rule applies even if the applicable large employer member's offer of coverage that meets the requirements of an affordability safe harbor is not affordable for a particular employee under section 36B(c)(2)(C)(i) and an applicable premium tax credit or cost-sharing reduction is allowed or paid with respect to that employee.

(i) *Conditions of using an affordability safe harbor*. An applicable large employer member may use one or more of the affordability safe harbors described in this paragraph (e)(2) only if the employer offers its full-time employees and their dependents the opportunity to enroll in minimum essential coverage under an eligible employer-sponsored plan that provides minimum value with respect to the self-only coverage offered to the employee. Use of any of the safe harbors is optional for an applicable large employer member, and an applicable large employer member may choose to apply the safe harbors for any reasonable category of employees, provided it does so on a uniform and consistent basis for all employees in a category. Reasonable categories generally include specified job categories, nature of compensation (hourly or salary), geographic location, and similar bona fide business criteria. An enumeration of employees by name or other specific criteria having substantially the same effect as an enumeration by name is not considered a reasonable category.

(ii) *Form W-2 safe harbor*–(A) *Full-year offer of coverage*. An employer will not be subject to an assessable payment under section 4980H(b) with respect to a full-time employee if that employee's required contribution for the calendar year for the employer'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 9.5 percent of that employee's Form W-2 wages from the employer (and any other member of the same applicable large employer that also pays wages to that employee) for the calendar year. Application of this safe harbor is determined after the end of the calendar year and on an employee-by-employee basis, taking into account the Form W-2 wages and the required employee contribution for that year. In addition, to qualify for this 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) so that an applicable large employer member is not permitted to 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.

(B) *Adjustment for partial-year offer of coverage*. For an employee not offered coverage for an entire calendar year, the Form W-2 safe harbor is applied by adjusting the Form W-2 wages to reflect the period for which coverage was offered, then determining whether the employee's required contribution for the employer's lowest cost self-only coverage that provides minimum value, totaled for the periods during which coverage was offered, does not exceed 9.5 percent of the adjusted amount of Form W-2 wages. To adjust Form W-2 wages for this purpose, the Form W-2 wages are multiplied 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 employer 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.

(iii) *Rate of pay safe harbor*. An applicable large employer member satisfies the rate of pay safe harbor with respect to an hourly employee for a calendar month if the employee's required contribution for the calendar month for the applicable large employer member's lowest cost self-only coverage that provides minimum value does not exceed 9.5 percent of an amount equal to 130 hours multiplied by the lower of the employee's hourly 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. An applicable large employer member satisfies the rate of pay safe harbor with respect to a non-hourly employee for a calendar month if the employee's required contribution for the calendar month for the applicable large employer member's lowest cost self-only coverage that provides minimum value does not exceed 9.5 percent of the employee's monthly salary, as of the first day of the coverage period (instead of 130 multiplied by the hourly rate of pay); provided that if the monthly salary is reduced, including due to a reduction in work hours, the safe harbor is not available, and, solely for purposes of this paragraph (e)(2)(iii), an applicable large employer member may use any reasonable method for converting payroll periods to monthly salary. For this purpose, if coverage is offered during at least one day during the calendar month, the entire calendar month is counted both for purposes of determining the assumed income for the calendar month and for determining the employee's share of the premium for the calendar month.

(iv) *Federal poverty line safe harbor*. An applicable large employer member satisfies the federal poverty line safe harbor with respect to an employee for a calendar month if the employee's required contribution for the calendar month for the applicable large employer member's lowest cost self-only coverage that provides minimum value does not exceed 9.5 percent of a monthly amount determined as the federal poverty line for a single individual for the applicable calendar year, divided by 12. For this purpose, if coverage is offered during at least one day during the calendar month, the entire calendar month is counted both for purposes of determining the monthly amount for the calendar month and for determining the employee's share of the premium for the calendar month. For this purpose, the applicable federal poverty line is the federal poverty line for the State in which the employee is employed.

(v) *Examples*. The following examples illustrate the application of the affordability safe harbors described in this paragraph (e)(2). In each example, each employer is an applicable large employer member with 200 full-time employees (including full-time equivalent employees).

Example 1 (Form W-2 wages safe harbor). (i) *Facts*. Employee A is employed by Employer Z consistently from January 1, 2015, through December 31, 2015. In addition, Employer Z offers Employee A and his dependents minimum essential coverage during that period that provides minimum value. The employee contribution for self-only coverage is $100 per calendar month, or $1,200 for the calendar year. For 2015, Employee A's Form W-2 wages with respect to employment with Employer Z are $24,000.

(ii) *Conclusion*. Because the employee contribution for 2015 is less than 9.5 percent of Employee A's Form W-2 wages for 2015, the coverage offered is treated as affordable with respect to Employee A for 2015 ($1,200 is 5 percent of $24,000).

Example 2 (Form W-2 wages safe harbor). (i) *Facts*. Employee B is employed by Employer Y from January 1, 2015, through September 30, 2015. In addition, Employer Y offers Employee B and his dependents minimum essential coverage during that period that provides minimum value. The employee contribution for self-only coverage is $100 per calendar month, or $900 for Employee B's period of employment. For 2015, Employee B's Form W-2 wages with respect to employment with Employer Y are $18,000. For purposes of applying the affordability safe harbor, the Form W-2 wages are multiplied by 9/9 (9 calendar months of coverage offered over 9 months of employment during the calendar year) or 1. Accordingly, affordability is determined by comparing the adjusted Form W-2 wages ($18,000) to the employee contribution for the period for which coverage was offered ($900).

(ii) *Conclusion*. Because the employee contribution for 2015 is less than 9.5 percent of Employee B's adjusted Form W-2 wages for 2015, the coverage offered is treated as affordable with respect to Employee B for 2015 ($900 is 5 percent of $18,000).

Example 3 (Form W-2 wages safe harbor). (i) *Facts*. Employee C is employed by Employer X from May 15, 2015, through December 31, 2015. In addition, Employer X offers Employee C and her dependents minimum essential coverage during the period from August 1, 2015, through December 31, 2015, that provides minimum value. The employee contribution for self-only coverage is $100 per calendar month, or $500 for Employee C's period of employment. For 2015, Employee C's Form W-2 wages with respect to employment with Employer X are $15,000. For purposes of applying the affordability safe harbor, the Form W-2 wages are multiplied by 5/8 (5 calendar months of coverage offered over 8 months of employment during the calendar year). Accordingly, affordability is determined by comparing the adjusted Form W-2 wages ($9,375 or $15,000 x 5/8) to the employee contribution for the period for which coverage was offered ($500).

(ii) *Conclusion*. Because the employee contribution of $500 is less than 9.5 percent of $9,375 (Employee C's adjusted Form W-2 wages for 2015), the coverage offered is treated as affordable with respect to Employee C for 2015 ($500 is 5.33 percent of $9,375).

Example 4 (Rate of pay safe harbor). (i) *Facts*. Employer W offers its full-time employees and their dependents minimum essential coverage that provides minimum value. For the 2016 calendar year, Employer W is using the rate of pay safe harbor to establish premium contribution amounts for full-time employees paid at a rate of $7.25 per hour (the minimum wage in Employer W's jurisdiction) for each calendar month of the entire 2016 calendar year. Employer W can apply the affordability safe harbor by using an assumed monthly income amount that is based on an assumed 130 hours of service multiplied by $7.25 per hour ($942.50 per calendar month). To satisfy the safe harbor, Employer W would set the employee monthly contribution amount at a rate that does not exceed 9.5 percent of the assumed monthly income of $942.50. Employer W sets the employee contribution for self-only coverage at $85 per calendar month for 2016.

(ii) *Conclusion*. Because $85 is less than 9.5 percent of the employee's assumed monthly income at a $7.25 rate of pay, the coverage offered is treated as affordable under the rate of pay safe harbor for each calendar month of 2016 ($85 is 9.01 percent of $942.50).

Example 5 (Rate of pay safe harbor). (i) *Facts*. Employee E is employed by Employer V from May 1, 2015, through December 31, 2015. Employer V offers Employee E and her dependents minimum essential coverage from May 1, 2015, through December 31, 2015, that provides minimum value. The employee contribution for self-only coverage is $100 per calendar month. From May 1, 2015, through October 31, 2015, Employee E is paid at a rate of $10 per hour. From November 1, 2015, through December 31, 2015, Employee E is paid at a rate of $12 per hour. For purposes of applying the affordability safe harbor for the calendar months May 2015 through October 2015, Employer V may assume that Employee E earned $1,300 per calendar month (130 hours of service multiplied by $10 (which is the lower of the employee's hourly rate of pay at the beginning of the coverage period ($10) and the lowest hourly rate of pay for the calendar month ($10)). Accordingly, affordability is determined by comparing the assumed income ($1,300 per month) to the employee contribution ($100 per calendar month). For the calendar months November 2015 through December 2015, Employer V may assume that Employee E earned $1,300 per calendar month (130 hours of service multiplied by $10 (which is the lower of the employee's hourly rate of pay at the beginning of the coverage period ($10) and the lowest hourly rate of pay for the calendar month ($12)). Accordingly, affordability is determined by comparing the assumed income ($1,300 per month) to the employee contribution ($100 per calendar month).

(ii) *Conclusion*. Because $100 is less than 9.5 percent of Employee E's assumed monthly income for each calendar month from May 2015 through December 2015, the coverage offered is treated as affordable with respect to Employee E for May 2015 through December 2015 ($100 is 7.69 percent of $1,300).

Example 6 (Federal poverty line safe harbor). (i) *Facts*. Employee F is employed by Employer T from January 1, 2015, through December 31, 2015. In addition, Employer T offers Employee F and his dependents minimum essential coverage during that period that provides minimum value. Employer T uses the look-back measurement method. Under that measurement method as applied by Employer T, Employee F is treated as a full-time employee for the entire calendar year 2015. Employee F is regularly credited with 35 hours of service per week but is credited with only 20 hours of service during the month of March 2015 and only 15 hours of service during the month of August 2015. Assume for this purpose that the federal poverty line for 2015 for an individual is $11,670. With respect to Employee F, Employer T sets the monthly employee contribution for employee single-only coverage for each calendar month of 2015 at $92.39 (9.5 percent of $11,670, divided by 12).

(ii) *Conclusion*. Regardless of Employee F's actual wages for any calendar month in 2015, including the months of March 2015 and August 2015, when Employee F has lower wages because of significantly lower hours of service, the coverage under the plan is treated as affordable with respect to Employee F, because the employee contribution does not exceed 9.5 percent of the federal poverty line.

(f) *Additional guidance*. With respect to assessable payments under section 4980H(b), including the determination of whether an offer of coverage is affordable for purposes of section 4980H, the Commissioner may prescribe additional guidance of general applicability, published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter).

(g) *Effective/applicability date*. This section is applicable for periods after December 31, 2014.

§ 54.4980H–6 Administration and procedure.

(a) *In general*. [Reserved]

(b) *Effective/applicability date*. This section is applicable for periods after December 31, 2014.

PART 301—PROCEDURE AND ADMINISTRATION

Par. 5. The authority citation for part 301 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 6. Section 301.7701–2 is amended as follows:

1. In paragraph (c)(2)(v)(A)(*3*), the language "and 4412; and" is removed and "and 4412;" is added in its place.

2. In paragraph (c)(2)(v)(A)(*4*), the language "or 6427." is removed and "or 6427; and" is added in its place.

3. Paragraphs (c)(2)(v)(A)(*5*) and (e)(6)(iii) are added.

The additions read as follows:

§ 301.7701–2 Business entities; definitions.

* * * * *

(c) * * *

(2) * * *

(v) * * *

(A) * * *

(*5*) Assessment and collection of an assessable payment imposed by section 4980H and reporting required by section 6056.

* * * * *

(e) * * *

(6) * * *

(iii) Paragraph (c)(2)(v)(A)(*5*) of this section applies for periods after December 31, 2014.

* * * * *

John Dalrymple
Deputy Commissioner for Services and Enforcement.

Approved February 7, 2014.

Mark J. Mazur
Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on February 10, 2014, at 4:15 p.m., and published in the issue of Federal Register for February 12, 2014, F.R. 8544)

Part III. Administrative, Procedural, and Miscellaneous

Section 5000A Transition Relief for Individuals with Certain Government-Sponsored Limited-Benefit Health Coverage

Notice 2014–10

This notice provides relief from the individual shared responsibility payment required under § 5000A of the Internal Revenue Code for months in 2014 in which individuals have, under Medicaid and chapter 55 of Title 10, U.S.C., limited-benefit health coverage that is not minimum essential coverage.

BACKGROUND

For each month beginning after December 31, 2013, § 5000A requires individuals to either maintain minimum essential coverage for themselves and any nonexempt family members, qualify for an exemption, or include an individual shared responsibility payment with their Federal income tax return. A taxpayer is liable under § 5000A for any nonexempt individual whom the taxpayer may claim as a dependent.

Under § 5000A(f)(1)(A), minimum essential coverage includes coverage under certain specified government-sponsored programs ("government-sponsored minimum essential coverage"). On August 30, 2013, the Treasury Department and the Internal Revenue Service (IRS) published final regulations under § 5000A. The final regulations provide that government-sponsored minimum essential coverage includes coverage under the Medicaid program under Title XIX of the Social Security Act (42 U.S.C. 1396 and following sections), other than the following limited coverage under Medicaid:

optional coverage of family planning services under section 1902(a)(10)(A)(ii)(XXI) of the Social Security Act (42 U.S.C. 1396a(a)(10)(A)(ii)(XXI)) ("family planning services Medicaid"), optional coverage of tuberculosis-related services under section 1902(a)(10)(A)(ii)(XII) of the Social Security Act (42 U.S.C. 1396a(a)(10)(A)(ii)(XII) ("tuberculosis-related services Medicaid"), coverage of pregnancy-related services under section 1902(a)(10)(A)(i)(IV) and (a)(10)(A)(ii)(IX) of the Social Security Act (42 U.S.C. 1396a(a)(10)(A)(i)(IV), (a)(10)(A)(ii)(IX)) ("pregnancy-related Medicaid"), and coverage limited to treatment of emergency medical conditions in accordance with 8 U.S.C. 1611(b)(1)(A), as authorized by section 1903(v) of the Social Security Act (42 U.S.C. 1396b(v)) ("emergency medical conditions Medicaid"). The final § 5000A regulations also provide that government-sponsored minimum essential coverage includes medical coverage under chapter 55 of Title 10, U.S.C., including coverage under the TRICARE program.

The final § 5000A regulations reserve on whether certain government-sponsored programs that provide limited benefits are minimum essential coverage, including (i) coverage authorized under section 1115 of the Social Security Act ("Section 1115 demonstration projects"); (ii) coverage for medically needy individuals, see section 1902(a)(10)(C) of the Social Security Act (42 U.S.C. 1396a(a)(10)(C)) and 42 CFR 435.300 and following sections; (iii) coverage under section 1079(a), 1086(c)(1), or 1086(d)(1) of Title 10, U.S.C., for certain individuals who are excluded from TRICARE coverage for health care services from private sector providers and only eligible for space available care in a facility for the uniformed services ("space available care"); and (iv) coverage under sections 1074a and 1074b of Title 10, U.S.C., for individuals not on active duty who are entitled to episodic care for an injury, illness, or disease incurred or aggravated in the line of duty ("line-of-duty care"). See § 1.5000A–2(b)(2) (78 FR 53646, 53658).

The preamble to the final § 5000A regulations indicates that future guidance will provide that the government-sponsored limited-benefit coverage reserved on in the final § 5000A regulations is not minimum essential coverage. However, the preamble to the final § 5000A regulations also indicates that, if future rulemaking clarifies that such limited-benefit coverage is not minimum essential coverage, individuals with that coverage for a month in 2014 will not be subject to the § 5000A individual shared responsibility payment for that month. See T.D. 9632 (78 FR 53646, 53648–53650).

Proposed regulations (REG–141036–13) published concurrently with this notice provide that coverage under certain Section 1115 demonstration projects authorized under section 1115(a)(2) of the Social Security Act (42 U.S.C. 1315(a)(2)), coverage for medically needy individuals, space available care, and line-of-duty care is not government-sponsored minimum essential coverage.

DISCUSSION

Individuals enrolled in family planning services Medicaid, tuberculosis-related services Medicaid, pregnancy-related Medicaid, emergency medical conditions Medicaid, certain Section 1115 demonstration projects, coverage for medically needy individuals, space available care, or line-of-duty care may not know when enrolling for the 2014 coverage year that such coverage is not minimum essential coverage. Accordingly, to provide relief to individuals in this situation (or to taxpayers who are liable under § 5000A for other individuals in this situation), and consistent with the preamble to the final regulations, the § 5000A shared responsibility payment is not imposed with respect to an individual for months in 2014 when the individual has coverage under family planning services Medicaid, tuberculosis-related services Medicaid, pregnancy-related Medicaid, emergency medical conditions Medicaid, a Section 1115 demonstration project authorized under section 1115(a)(2) of the Social Security Act (42 U.S.C. 1315(a)(2)), coverage for medically needy individuals, space available care, or line-of-duty care.

The relief provided by this notice applies only for determining a taxpayer's § 5000A individual shared responsibility payment for not maintaining minimum essential coverage in 2014. Solely for the purpose of determining whether a period without coverage qualifies as a short coverage gap described in § 5000A(e)(4), an individual will be treated as having minimum essential coverage for any month in 2014 when that individual is eligible for the transition relief provided by this notice.

DRAFTING INFORMATION

The principal author of this notice is John B. Lovelace of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this notice contact Mr. Lovelace at (202) 317-7006 (not a toll-free number).

2014 Calendar Year Resident Population Figures

Notice 2014–12

This notice advises State and local housing credit agencies that allocate low-income housing tax credits under § 42 of the Internal Revenue Code, and States and other issuers of tax-exempt private activity bonds under § 141, of the population figures to use in calculating: (1) the 2014 calendar year population-based component of the State housing credit ceiling (Credit Ceiling) under § 42(h)(3)(C)(ii); (2) the 2014 calendar year volume cap (Volume Cap) under § 146; and (3) the 2014 volume limit (Volume Limit) under § 142(k)(5).

Generally, § 146(j) requires determining the population figures for the population-based component of both the Credit Ceiling and the Volume Cap for any calendar year on the basis of the most recent census estimate of the resident population of a State (or issuing authority) released by the U.S. Census Bureau before the beginning of the calendar year. Similarly, § 142(k)(5) bases the Volume Limit on the State population.

Sections 42(h)(3)(H) and 146(d)(2) require adjusting for inflation the population-based component of the Credit Ceiling and the Volume Cap. The adjustments for the 2014 calendar year are in Rev. Proc. 2013–35, 2013–47 I.R.B. 537. Section 3.08 of Rev. Proc. 2013–35 provides that, for calendar year 2014, the amount for calculating the Credit Ceiling under § 42(h)(3)(C)(ii) is the greater of $2.30 multiplied by the State population, or $2,635,000. Further, section 3.19 of Rev. Proc. 2013–35 provides that the amount for calculating the Volume Cap under § 146(d)(1) for calendar year 2014 is the greater of $100 multiplied by the State population, or $296,825,000.

For the 50 states, the District of Columbia, and Puerto Rico, the population figures for calculating the Credit Ceiling, the Volume Cap, and the Volume Limit for the 2014 calendar year are the resident population estimates released electronically by the U.S. Census Bureau on December 30, 2013, in Press Release CB13-tps111. For American Samoa, Guam, the Northern Mariana Islands, and the U.S. Virgin Islands, the population figures for the 2014 calendar year are the 2013 mid-year population figures in the U.S. Census Bureau's International Data Base (IDB). The U.S. Census Bureau electronically announced an update of the IDB on June 27, 2012, in Press Release CB12-118.

For convenience, these figures are reprinted below.

Resident Population Figures

Alabama	4,833,722
Alaska	735,132
American Samoa	54,719
Arizona	6,626,624
Arkansas	2,959,373
California	38,332,521
Colorado	5,268,367
Connecticut	3,596,080
Delaware	925,749
District of Columbia	646,449
Florida	19,552,860
Georgia	9,992,167
Guam	160,378
Hawaii	1,404,054
Idaho	1,612,136
Illinois	12,882,135
Indiana	6,570,902
Iowa	3,090,416
Kansas	2,893,957
Kentucky	4,395,295
Louisiana	4,625,470
Maine	1,328,302
Maryland	5,928,814
Massachusetts	6,692,824
Michigan	9,895,622
Minnesota	5,420,380
Mississippi	2,991,207
Missouri	6,044,171
Montana	1,015,165
Nebraska	1,868,516
Nevada	2,790,136
New Hampshire	1,323,459
New Jersey	8,899,339
New Mexico	2,085,287
New York	19,651,127
North Carolina	9,848,060
North Dakota	723,393
Northern Mariana Islands	51,170
Ohio	11,570,808
Oklahoma	3,850,568
Oregon	3,930,065
Pennsylvania	12,773,801
Puerto Rico	3,615,086
Rhode Island	1,051,511
South Carolina	4,774,839
South Dakota	844,877
Tennessee	6,495,978
Texas	26,448,193
Utah	2,900,872
Vermont	626,630
Virginia	8,260,405
Virgin Islands, U.S.	104,737
Washington	6,971,406
West Virginia	1,854,304
Wisconsin	5,742,713
Wyoming	582,658

The principal authors of this notice are Jian H. Grant, Office of the Associate Chief Counsel (Passthroughs and Special Industries), and Timothy L. Jones, Office of the Associate Chief Counsel (Financial Institutions and Products). For further information regarding this notice, please contact Ms. Grant at (202) 317-4137 (not a toll-free number).

26 CFR 601.204: Changes in accounting periods and in methods of accounting. (Also Part I, §§ 162, 263(a), 263A, 446, 481; 1.446–1.)

Rev. Proc. 2014–16

SECTION 1. PURPOSE

This revenue procedure modifies the procedures in Rev. Proc. 2012–19, 2012–14 I.R.B. 689, and Rev. Proc. 2011–14, 2011–4 I.R.B. 330, regarding certain changes in method of accounting for amounts paid to acquire, produce, or improve tangible property. This revenue procedure supersedes Rev. Proc. 2012–19 and provides the procedures by which a taxpayer may obtain the automatic consent of the Commissioner of Internal Revenue to change to the methods of accounting provided in §§ 1.162–3, 1.162–4, 1.263(a)–1, 1.263(a)–2, and 1.263(a)–3 of the Income Tax Regulations and §§ 1.162–3T, 1.162–4T, 1.263(a)–1T, 1.263(a)–2T, and 1.263(a)–3T of the temporary regulations. This revenue procedure also modifies Rev. Proc. 2011–14 and provides the procedures by which a taxpayer may obtain the automatic consent of the Commissioner of Internal Revenue to change to a reasonable method described in § 1.263A–1(f)(4) for self-constructed assets and to change to a permissible method of accounting under section 263A(b)(2) of the Internal Revenue Code and § 1.263A–3(a)(1) for certain costs related to real property acquired through foreclosure, by deed in lieu of foreclosure, or in another similar transaction. Finally, this revenue procedure also modifies section 3.09 of the APPENDIX of Rev. Proc. 2011–14 regarding a change to the method of accounting described in Rev. Proc. 2011–43, 2011–37 I.R.B. 326, for taxpayers in the business of transporting, delivering, or selling electricity.

SECTION 2. BACKGROUND

.01 The Internal Revenue Service (IRS) and the Treasury Department recently issued final regulations under §§ 1.162–3, 1.162–4, 1.263(a)–1, 1.263(a)–2, and 1.263(a)–3 (T.D. 9636, 2013-43 I.R.B. 331, 78 Fed. Reg. 57686) (the final tangible property regulations). Section 1.162–3 provides rules for amounts paid or incurred for materials and supplies. Section 1.162–4 provides rules for amounts paid or incurred for repairs and maintenance. Section 1.263(a)–1 provides general rules for capital expenditures. Section 1.263(a)–2 provides rules for amounts paid or incurred for the acquisition and production of tangible property. Section 1.263(a)–3 provides rules for amounts paid or incurred for the improvement of tangible property. The final tangible property regulations generally apply to taxable years beginning on or after January 1, 2014, but also permit a taxpayer to choose to apply these sections to taxable years beginning on or after January 1, 2012. Alternatively, the final tangible property regulations permit a taxpayer to apply the temporary regulations under §§ 1.162–3T, 1.162–4T, 1.263(a)–1T, 1.263(a)–2T, and 1.263(a)–3T (T.D. 9564, 2012-14 I.R.B. 614, 76 Fed. Reg. 81060) (the temporary tangible property regulations) to taxable years (or where applicable, to amounts paid or incurred) beginning on or after January 1, 2012, and before January 1, 2014.

.02 Except as otherwise expressly provided by the Internal Revenue Code or the regulations thereunder, section 446(e) and § 1.446–1(e)(2) require a taxpayer to secure the consent of the Commissioner before changing a method of accounting for federal income tax purposes.

.03 Sections 1.162–3(i), 1.162–4(b), 1.263(a)–1(g), 1.263(a)–2(i), and 1.263(a)–3(q) of the final tangible property regulations provide that a taxpayer seeking to change to a method of accounting provided in the final tangible property regulations must secure the consent of the Commissioner in accordance with the requirements of § 1.446–1(e).

.04 Sections 1.162–3T(i), 1.162–4T(b), 1.263(a)–1T(f), 1.263(a)–2T(j), and 1.263(a)–3T(o) of the temporary tangible property regulations provide that a taxpayer seeking to change to a method of accounting provided in the temporary tangible property regulations must secure the consent of the Commissioner in accordance with the requirements of § 1.446–1(e).

.05 Section 1.446–1(e)(3)(ii) authorizes the Commissioner to prescribe administrative procedures setting forth the terms and conditions necessary for a taxpayer to obtain consent to change a method of accounting. Rev. Proc. 2011–14 provides procedures by which a taxpayer may obtain automatic consent from the Commissioner to change to a method of accounting described in the APPENDIX of Rev. Proc. 2011–14. A taxpayer complying with all the applicable provisions of Rev. Proc. 2011–14 obtains the consent of the Commissioner to change its method of accounting under section 446(e).

.06 Section 3.01 of this revenue procedure modifies the APPENDIX of Rev. Proc. 2011–14 to amend existing method change procedures to be consistent with both the temporary and final tangible property regulations.

.07 Section 3.02 of this revenue procedure modifies the APPENDIX of Rev. Proc. 2011–14 to provide new method change procedures consistent with both the temporary and final tangible property regulations.

.08 Section 11.01 and 11.02 of the APPENDIX of Rev. Proc. 2011–14 provide procedures by which a taxpayer may obtain the automatic consent of the Commissioner to change to certain uniform capitalization (UNICAP) methods of accounting. These procedures do not apply to a change to a reasonable method, within the meaning of § 1.263A–1(f)(4), to properly allocate direct and indirect costs among units of property produced during the taxable year unless the methods are specifically described in § 1.263A–1(f)(2) or (3).

.09 The IRS is aware that, as a result of applying the final tangible property regulations, taxpayers may want to change to a reasonable method, within the meaning of § 1.263A–1(f)(4), other than the methods specifically described in § 1.263A–1(f)(2) or (3) to properly allocate direct and indirect costs among units of property produced during the taxable year. To align the filing requirements for certain changes in method of accounting for amounts paid to acquire, produce, or improve tangible property with a change to a reasonable method described in § 1.263A–1(f)(4), section 3.02 of this revenue procedure adds section 11.09 to the APPENDIX of Rev. Proc. 2011–14 to provide automatic consent for changes to a reasonable method of accounting under section 263A, provided certain limited conditions are met.

.10 The IRS is aware that questions have arisen regarding whether the capitalization rules of section 263A(b)(2)(A) apply to real property acquired by certain taxpayers through a foreclosure proceeding, or a deed-in-lieu of foreclosure transaction. Currently there is no automatic consent procedure for a change in method of accounting to stop capitalizing under section 263A(b)(2) costs of acquiring and holding property obtained through foreclosure (or similar transaction). To facilitate a change in method of accounting in this situation, section 3.02 of this revenue procedure adds section 11.10 to the APPENDIX to provide automatic consent for a change in method of accounting to an otherwise permissible method of accounting that does not capitalize under section 263A(b)(2) amounts for acquiring or holding real property obtained through a foreclosure proceeding, a deed-in-lieu of foreclosure transaction, or another similar transaction.

.11 Section 3.09 of the APPENDIX to Rev. Proc. 2011–14 allows taxpayers in the business of transporting, delivering, or selling electricity to change their method of accounting to the safe harbor method of accounting described in Rev. Proc. 2011–43. Under Rev. Proc. 2011–43, the scope limitations of section 4.02 of Rev. Proc. 2011–14 do not apply to an electric transmission or distribution company that changes to the method of accounting provided in Rev. Proc. 2011–43 for its first or second taxable year ending after December 30, 2010. Under Rev. Proc. 2012–39, 2012–41 I.R.B. 470, the scope waiver limitation was modified to include the first, second, or third taxable year ending after December 30, 2010.

.12 The IRS is aware that a number of electric transmission and distribution companies still have not had time to change their method of accounting to the safe harbor method of accounting described in Rev. Proc. 2011–43. Accordingly, this revenue procedure modifies section 3.09 of the APPENDIX of Rev. Proc. 2011–14 to extend the waiver of scope limitations to the fourth taxable year ending after December 30, 2010.

SECTION 3. CHANGES IN METHODS OF ACCOUNTING

.01 *Modifications to existing automatic changes*.

(1) Section 3.05 and section 3.06 of the APPENDIX to Rev. Proc. 2011–14 are modified to read as follows:

3.05 *Materials and supplies*. See section 10.11 of the APPENDIX.

3.06 *Repair and maintenance costs*. See section 10.11 of the APPENDIX.

(2) Section 3.09(2) of the APPENDIX to Rev. Proc. 2011–14 is modified to read as follows:

The scope limitations in section 4.02 of this revenue procedure do not apply to an electric transmission or distribution company that changes to the method of accounting provided in Rev. Proc. 2011–43 for its first, second, third, or fourth taxable year ending after December 30, 2010.

(3) Sections 3.10 through 3.19, and sections 10.08 through 10.10 of the APPENDIX to Rev. Proc. 2011–14 are modified to read "*Reserved*."

(4) Section 10.03(1) of the APPENDIX to Rev. Proc. 2011–14 is modified to read as follows:

(1) *Description of Change*

(a) *Applicability*. This change applies to a taxpayer that wants to change its method of accounting for certain costs in the retirement and removal of a depreciable asset to conform with Rev. Rul. 2000–7, 2000–1 C.B. 712, or for removal costs in disposal of a depreciable asset, including a partial disposition, as described under § 1.263(a)–3(g)(2)(i).

(b) *Inapplicability*. This change does not apply to a taxpayer that wants to change its method of accounting for removal costs in the disposal of a component of a unit of property where the disposal of the component is not a disposition for federal tax purposes. To make this change, see section 10.11 of the APPENDIX of this revenue procedure.

(c) *Manner of Making Change*.

(i) A qualifying taxpayer, as defined in paragraph (ii) below, is required to complete only the following information on Form 3115:

(A) The identification section of page 1 (above Part I);

(B) The signature section at the bottom of page 1;

(C) Part I, line 1(a);

(D) Part II, all lines except lines 11, 13, 14, 15, and 17;

(E) Part II, line 13, if the change is to depreciating property;

(F) Part IV, lines 25 and 26; and

(G) Schedule E, if applicable.

(ii) The term qualifying taxpayer means a taxpayer whose average annual gross receipts, as determined under § 1.263(a)–3(h)(3), for the three preceding taxable years is less than or equal to $10,000,000.

.02 *New automatic changes*.

(1) Rev. Proc. 2011–14 is modified to add new section 10.11 of the APPENDIX, to read as follows:

.11 *Tangible property*.

(1) *Description of change*.

(a) *Applicability*. This change applies to a taxpayer that wants to make a change to a method of accounting specified in section 10.11(3) of this APPENDIX and permitted under:

(i) Section 1.162–3, § 1.162–4, § 1.263(a)–1, § 1.263(a)–2, or § 1.263(a)–3 of the Income Tax Regulations (the final tangible property regulations) for taxable years beginning on or after January 1, 2012;

(ii) Section 1.162–3T, § 1.162–4T, § 1.263(a)–2T, or § 1.263(a)–3T of the temporary Income Tax Regulations (T.D. 9564, 76 Fed. Reg. 81060, as contained in 26 CFR part 1 edition revised as of Apr. 1, 2013) (the temporary tangible property regulations) for a taxable year beginning on or after January 1, 2012, and before January 1, 2014; or

(iii) Section 1.446–1(e)(2)(ii)(*d*)(2) if the property for which the taxpayer is otherwise changing its method of accounting under this section of the APPENDIX is depreciable under either the present or the proposed method of accounting.

(b) *Inapplicability*. This change does not apply to:

(i) A taxpayer that wants to change its method of accounting for dispositions of depreciable property, including a change in the asset disposed of (but see sections 6.29, 6.30, 6.31, 6.33, 6.34, and 6.35 of this APPENDIX);

(ii) Amounts paid or incurred for certain materials and supplies that the taxpayer has elected to capitalize and depreciate under § 1.162–3(d);

(iii) Amounts paid or incurred to which the taxpayer has elected to apply the de minimis safe harbor under § 1.263(a)–1(f);

(iv) Amounts paid or incurred for employee compensation or overhead that the taxpayer has elected to capitalize under § 1.263(a)–2(f)(2)(iv)(B);

(v) Amounts paid or incurred to which the taxpayer has elected to apply the safe harbor for small taxpayers under § 1.263(a)–3(h);

(vi) Amounts paid or incurred for repair and maintenance costs that the taxpayer has elected to capitalize under § 1.263(a)–3(n); or

(vii) Amounts paid or incurred to facilitate the acquisition or disposition of assets that constitute a trade or business (but see section 10.05 of this APPENDIX).

(2) *Certain scope limitations inapplicable*.

(a) *In general*. The scope limitations in section 4.02 of this revenue procedure do not apply to a taxpayer that makes one or more changes in method of accounting under this section of this APPENDIX for any taxable year beginning before January 1, 2015.

(b) *Concurrent automatic change*. If the taxpayer makes both a change under this section of this APPENDIX and a change to a UNICAP method under section 11.01, 11.02, or 11.09 of this APPENDIX (as applicable) for any taxable year beginning before January 1, 2015, on a single Form 3115 for the same year of change in accordance with section 10.11(5) of this APPENDIX, the scope limitations in section 4.02 of this revenue procedure do not apply to the taxpayer for either change.

(3) *Covered Changes*. Section 10.11 of this APPENDIX only applies to the following changes in methods of accounting:

(a) *Changes under the final tangible property regulations*.

(i) A change to deducting amounts paid or incurred to acquire or produce non-incidental materials and supplies in the taxable year in which they are first used in the taxpayer's operations or consumed in the taxpayer's operations in accordance with §§ 1.162–3(a)(1) and 1.162–3(c)(1);

(ii) A change to deducting amounts to acquire or produce incidental materials and supplies in the taxable year in which paid or incurred in accordance with §§ 1.162–3(a)(2) and 1.162–3(c)(1);

(iii) A change to deducting amounts paid or incurred to acquire or produce non-incidental rotable and temporary spare parts in the taxable year which the taxpayer disposes of the parts in accordance with §§ 1.162–3(a)(3) and 1.162–3(c)(2);

(iv) A change to the optional method of accounting for rotable and temporary spare parts in accordance with § 1.162–3(e);

(v) A change to deducting amounts paid or incurred for repair and maintenance in accordance with § 1.162–4, including a change, if any, in identifying the unit of property under § 1.263(a)–3(e) or, in the case of a building, identifying the building structure or building systems under § 1.263(a)–3(e)(2) for purposes of making the change to deducting the amounts;

(vi) A change to capitalizing amounts paid or incurred for improvements to tangible property in accordance with § 1.263(a)–3 and, if depreciable, to depreciating such property under section 167 or section 168, including a change, if any, in identifying the unit of property under § 1.263(a)–3(e) or, in the case of a building, identifying the building structure or building systems under § 1.263(a)–3(e)(2) for purposes of making the change to capitalizing the amounts;

(vii) A change by a dealer in property to deduct amounts paid or incurred for commissions and other transaction costs that facilitate the sale of property in accordance with § 1.263(a)–1(e)(2);

(viii) A change by a non-dealer in property to capitalizing amounts paid or incurred for commissions and other costs that facilitate the sale of property in accordance with § 1.263(a)–1(e);

(ix) A change to capitalizing amounts paid or incurred to acquire or produce property in accordance with § 1.263(a)–2, and if depreciable, to depreciating such property under section 167 or section 168;

(x) A change to deducting amounts paid or incurred in the process of investigating or otherwise pursuing the acquisition of real property if the amounts meet the requirements of § 1.263(a)–2(f)(2)(iii); and

(xi) A change to the optional regulatory accounting method in accordance with § 1.263(a)–3(m) to determine whether amounts paid or incurred to repair, maintain, or improve tangible property are treated as deductible expenses or capital expenditures.

(b) *Changes under the temporary tangible property regulations.*

(i) A change to deducting amounts paid or incurred to acquire or produce non-incidental materials and supplies in the taxable year in which they are used or consumed in the taxpayer's operations in accordance with §§ 1.162–3T(a)(1) and 1.162–3T(c)(1);

(ii) A change to deducting amounts to acquire or produce incidental materials and supplies in the taxable year in which they are paid or incurred in accordance with §§ 1.162–3T(a)(2) and 1.162–3T(c)(1);

(iii) A change to deducting the amounts paid or incurred to acquire or produce non-incidental rotable and temporary spare parts in the taxable year which the taxpayer disposes of the parts in accordance with §§ 1.162–3T(a)(3) and 1.162–3T(c)(2);

(iv) A change to the optional method of accounting for rotable and temporary spare parts in accordance with § 1.162–3T(e);

(v) A change to deducting amounts paid or incurred for repair and maintenance in accordance with § 1.162–4T, including a change, if any, in identifying the unit of property under § 1.263(a)–3T(e) or, in the case of a building, identifying the building structure or building systems under § 1.263(a)–3T(e)(2) for purposes of making the change to deducting the amounts;

(vi) A change to capitalizing amounts paid or incurred for improvements to tangible property in accordance with § 1.263(a)–3T and, if depreciable, to depreciating such property under section 167 or section 168, including a change, if any, in identifying the unit of property under § 1.263(a)–3T(e) or, in the case of a building, identifying the building structure or building systems under § 1.263(a)–3T(e)(2) for purposes of making the change to capitalizing the amounts;

(vii) A change by a dealer in property to deduct amounts paid or incurred for commissions and other transaction costs that facilitate the sale of property in accordance with § 1.263(a)–1T(d);

(viii) A change by a non-dealer in property to capitalizing amounts paid or incurred for commissions and other costs that facilitate the sale of property in accordance with § 1.263(a)–1T(e);

(ix) A change to capitalizing amounts paid or incurred to acquire or produce property in accordance with § 1.263(a)–2T, and if depreciable, to depreciating such property under section 167 or section 168;

(x) A change to deducting amounts paid or incurred in the process of investigating or otherwise pursuing the acquisition of real property if the amounts meet the requirements of § 1.263(a)–2T(f)(2)(iii);

(xi) A change to apply the de minimis rule under § 1.263(a)–2T(g) to amounts paid or incurred to acquire or produce a unit of property; and

(xii) A change to the optional regulatory accounting method in accordance with § 1.263(a)–3T(k) to determine whether amounts paid or incurred to repair, maintain, or improve tangible property are treated as deductible expenses or capital expenditures.

(4) *Manner of making change*.

(a) *Form 3115*. In addition to the other information required on line 12 of Form 3115, the taxpayer must include the following:

(i) The citation to the paragraph of the final tangible property regulations or temporary tangible property regulations that provides for the proposed method, or methods, of accounting to which the taxpayer is changing (e.g., § 1.162–3(a), § 1.263(a)–3(i), § 1.263(a)–3(k)); and

(ii) If the taxpayer is changing any unit(s) of property under § 1.263(a)–3(e) (or § 1.263(a)–3T(e)) or, in the case of a building, is changing the identification of any building structure(s) or building system(s) under § 1.263–3(e)(2) (or § 1.263–3T(e)(2)) for purposes of determining whether amounts are deducted as repair and maintenance costs under section § 1.162–4 (or § 1.162–4T) or capitalized as improvement costs under § 1.263(a)–3 (or § 1.263(a)–3T), the taxpayer must include a detailed description of the unit(s) of property, building structure(s), or buildings system(s) used under its present method of accounting and a detailed description of the unit(s) of property, building structure(s), and building system(s) under its proposed method of accounting, together with a citation to the paragraph of the final regulation or temporary regulation under which the unit of property is permitted.

(iii) A taxpayer changing its method of accounting under this section of the APPENDIX to capitalizing amounts paid or incurred and to depreciating such property under section 167 or section 168, as applicable, must complete Schedule E of Form 3115.

(b) *Reduced Filing Requirement for Small Taxpayers*.

(i) A qualifying taxpayer, as defined in paragraph (ii) below, is required to complete only the following information on Form 3115:

(A) The identification section of page 1 (above Part I);

(B) The signature section at the bottom of page 1;

(C) Part I, line 1(a);

(D) Part II, all lines except lines 11, 13, 14, 15, and 17;

(E) Part II, line 13, if the change is to depreciating property;

(F) Part IV, lines 25 and 26; and

(G) Schedule E, if applicable.

(ii) The term qualifying taxpayer means a taxpayer whose average annual gross receipts, as determined under § 1.263(a)–3(h)(3), for the three preceding taxable years is less than or equal to $10,000,000.

(5) *Concurrent automatic change*.

(a) A taxpayer that wants to make two or more changes in method of accounting pursuant to this section 10.11 of the APPENDIX should file a single Form 3115 for all of these changes and must enter the designated automatic accounting method change numbers for all of these changes on the appropriate line on the Form 3115. For additional guidance on filing a single application for two or more changes, see section 6.02(1)(b)(ii) of this revenue procedure.

(b) A taxpayer that wants to make both one or more changes in method of accounting pursuant to this section 10.11 of the APPENDIX and a change to a UNICAP method pursuant to the APPENDIX for the same year of change should file a single Form 3115 that includes all of these changes and must enter the designated automatic accounting method change numbers for all of these changes on the appropriate line on the Form 3115. For additional guidance on filing a single application for two or more changes, see section 6.02(1)(b)(ii) of this revenue procedure.

(6) *Section 481(a) adjustment*.

(a) *In general*. Except as provided in paragraph 10.11(6)(b) of this APPENDIX, a taxpayer changing to a method of accounting provided in Section 10.11 of this APPENDIX must apply section 481(a) and take into account any applicable section 481(a) adjustment in the manner provided in sections 5.03 and 5.04 of this revenue procedure.

(b) *Modified section 481(a) adjustment*.

(i) *Final tangible property regulations*. A taxpayer changing to a method of accounting under § 1.162–3 (except § 1.162–3(e)), § 1.263(a)–2(f)(2)(iii), § 1.263(a)–2(f)(3)(ii), § 1.263(a)–3(m), § 1.263A–1(e)(2)(i)(A), and § 1.263A–1(e)(3)(ii)(E) is required to calculate a section 481(a) adjustment as of the first day of the taxpayer's taxable year of change that takes into account only amounts paid or incurred in taxable years beginning on or after January 1, 2014 ("modified section 481(a) adjustment"). Optionally, a taxpayer may take into account amounts paid or incurred in taxable years beginning on or after January 1, 2012. For guidance on computing a section 481(a) adjustment see sections 5.03 and 5.04 of this revenue procedure.

(ii) *Temporary tangible property regulations*. A taxpayer changing to a method of accounting under § 1.162–3T (except § 1.162–1T(e)), § 1.263(a)–2T(f)(2)(iii), § 1.263(a)–2T(f)(3)(ii), § 1.263(a)–2T(g), § 1.263(a)–3T(k), § 1.263A–1T(e)(2)(i)(A), and § 1.263A–1T(e)(3)(ii)(E) is required to calculate a section 481(a) adjustment as of the first day of the taxpayer's taxable year of change that takes into account only amounts paid or incurred in taxable years beginning on or after January 1, 2012, for a year of change beginning on or after January 1, 2012, and ending before January 1, 2014 . For guidance on computing a section 481(a) adjustment see sections 5.03 and 5.04 of this revenue procedure.

(c) *Itemized listing on Form 3115*. A taxpayer changing to a method of accounting provided in section 10.11 of this APPENDIX must include on Form 3115, Part IV, line 25, the total section 481(a) adjustment for each change in method of accounting being made. If the taxpayer is making more than one change in method of accounting under the final tangible property regulations, the taxpayer must include on an attachment to Form 3115 —

(i) The information required by Part IV, line 25 for each change in method of accounting (including the amount of the section 481(a) adjustment for each change in method of accounting, which includes the portion of the section 481(a) adjustment attributable to UNICAP);

(ii) The information required by Part II, line 12 of Form 3115 that is associated with each change; and

(iii) The citation to the paragraph of the final tangible property regulations or temporary tangible property regulations that provides for each proposed method of accounting.

(d) *Repair allowance property*. A taxpayer changing to a method of accounting provided by § 1.263(a)–3 of the final tangible property regulations or § 1.263(a)–3T of the temporary tangible property regulations under this section of the APPENDIX must not include in the section 481(a) adjustment any amount attributable to property for which the taxpayer elected to apply the repair allowance under § 1.167(a)–11(d)(2) for any taxable year in which the repair allowance election was made.

(e) *Statistical Sampling*. Except for a change in accounting method under this section 10.11 of the APPENDIX that requires a modified section 481(a) adjustment, a taxpayer changing its method of accounting under section 10.11 of the APPENDIX may use statistical sampling in determining the section 481(a) adjustment by following the guidance provided in Rev. Proc. 2011–42, 2011–37 I.R.B. 318.

(7) *Ogden copy of Form 3115 required in lieu of national office copy*. A taxpayer changing its method of accounting under this section of the APPENDIX must file a signed copy of its completed Form 3115 with the IRS in Ogden, UT (Ogden copy), in lieu of filing the national office copy, no earlier than the first day of the year of change and no later than the date the taxpayer files the original Form 3115 with its federal income tax return for the year of change. If a taxpayer makes both this change and a change to a UNICAP method under section 11.01, 11.02, or 11.09 of this APPENDIX (as applicable) on a single Form 3115 for the same year of change in accordance with section 10.11 of this APPENDIX, the taxpayer must file a signed copy of that completed Form 3115 with the IRS in Ogden, UT (Ogden copy), in lieu of filing the national office copy, no earlier than the first day of the year of change and no later than the date the taxpayer files the original Form 3115 with its federal income tax return for the year of change. *See* sections 6.02(3)(a)(ii)(B) (providing the general rules) and 6.02(7)(b) (providing the mailing address) of this revenue procedure.

(8) *Designated automatic accounting method change number*. See the following tables for the designated automatic accounting method change numbers for the changes in method of accounting under section 10.11 of this APPENDIX. *See* section 6.02(4) of this revenue procedure.

(a) *Changes under the final tangible property regulations.*

Description of Change	*DCN*	*Citation*
A change to deducting amounts paid or incurred for repair and maintenance or a change to capitalizing amounts paid or incurred for improvements to tangible property and, if depreciable, to depreciating such property under section 167 or section 168. Includes a change, if any, in the method of identifying the unit of property, or in the case of a building, identifying the building structure or building systems for the purpose of making this change.	184	§§ 1.162–4, 1.263(a)–3
Change to the regulatory accounting method.	185	§ 1.263(a)–3(m)
Change to deducting non-incidental materials and supplies when used or consumed.	186	§§ 1.162–3(a)(1), (c)(1)
Change to deducting incidental materials and supplies when paid or incurred.	187	§§ 1.162–3(a)(2), (c)(1)
Change to deducting non-incidental rotable and temporary spare parts when disposed of.	188	§ 1.162–3(a)(3), (c)(2)
Change to the optional method for rotable and temporary spare parts.	189	§ 1.162–3(e)
Change by a dealer in property to deduct commissions and other transaction costs that facilitate the sale of property.	190	§ 1.263(a)–1(e)(2)
Change by a non-dealer in property to capitalizing commissions and other costs that facilitate the sale of property.	191	§ 1.263(a)–1(e)(1)
Change to capitalizing acquisition or production costs and, if depreciable, to depreciating such property under section 167 or section 168.	192	§ 1.263(a)–2
Change to deducting certain costs for investigating or pursuing the acquisition of real property (whether and which).	193	§ 1.263(a)–2(f)(2)(iii)

(b) *Changes under the temporary tangible property regulations*.

Description of Change	*DCN*	*Citation*
A change to deducting amounts paid or incurred for repair and maintenance or a change to capitalizing amounts paid or incurred for improvements to tangible property and, if depreciable, to depreciating such property under section 167 or section 168. Includes a change, if any, in the method of identifying the unit of property, or in the case of a building, identifying the building structure or building systems for the purpose of making this change.	162	§§ 1.162–4T, 1.263(a)–3T
Change to the regulatory accounting method.	163	§ 1.263(a)–3T(k)(2)
Change to deducting non-incidental materials and supplies when used or consumed.	164	§§ 1.162–3T(a)(1), (c)(1)
Change to deducting incidental materials and supplies when paid or incurred.	165	§§ 1.162–3T(a)(2), (c)(1)
Change to deducting non-incidental rotable and temporary spare parts when disposed of.	166	§ 1.162–3T(a)(3), (c)(2)
Change to the optional method for rotable and temporary spare parts.	167	§ 1.162–3T(e)
Change by a dealer in property to deduct commissions and other costs that facilitate sales.	168	§ 1.263(a)–1T(d)(1)
Change to applying the de minimis rule	169	§§ 1.263(a)–2T(g), 1.263A–1T(b)(14)
Change to deducting certain costs for investigating or pursuing the acquisition of real property.	170	§ 1.263(a)–2T(f)(2)(iii)
Change by non-dealer in property to capitalizing commissions and other costs that facilitate sales.	172	§ 1.263(a)–1T(d)(1)
Change to capitalizing acquisition or production costs and, if depreciable, to depreciating such property under section 167 or section 168.	173	§ 1.263(a)–2T

(9) *Contact information*. For further information regarding a change under this section, contact Alan S. Williams at 202-317-5100 (not a toll-free number).

(2) Rev. Proc. 2011–14 is modified to add new section 11.09 of the APPENDIX, to read as follows:

.09 *Change to a reasonable allocation method described in § 1.263A–1(f)(4) for self-constructed assets*.

(1) *Description of change*.

(a) *Applicability*. This change applies to a producer (as defined in section 11.01(2)(d) of this APPENDIX) that wants to change to a UNICAP method that uses a reasonable method, within the meaning of § 1.263A–1(f)(4), other than the methods specifically described in § 1.263A–1(f)(2) or (3) to properly allocate direct and indirect costs among self-constructed assets produced during the taxable year, including any necessary changes in the identification of costs subject to § 263A that will be accounted for using the new method.

(b) *Inapplicability*. This change does not apply to an allocation method based on the number of units produced or an allocation method that does not allocate costs to the units of property produced. This change does not apply to a change described in another section of this APPENDIX or in other guidance published in the Internal Revenue Bulletin. For example, this change does not apply to a change described in section 11.01 or 11.02 of this APPENDIX.

(2) *No ruling on reasonableness of method*. The consent granted under this revenue procedure for this change is not a determination by the Commissioner that the taxpayer is using a reasonable allocation method for costs subject to section 263A and does not create any presumption that the proposed allocation method is permissible. The director will ascertain whether the taxpayer's allocation method is reasonable within the meaning of § 1.263A–1(f)(4).

(3) *Multiple changes*. A taxpayer making both this change and another change in method of accounting under section 10.11 of the APPENDIX for the same year of change must comply with the ordering rules of § 1.263A–7(b)(2).

(4) *Ogden copy of Form 3115 required in lieu of national office copy*. A taxpayer changing its method of accounting under this section 11.09 of the APPENDIX must file a signed copy of its completed Form 3115 with the IRS in Ogden, UT (Ogden copy), in lieu of filing the national office copy, no earlier than the first day of the year of change and no later than the date the taxpayer files the original Form 3115 with its federal income tax return for the year of change. If a taxpayer makes both this change and a change under section 10.11 of this APPENDIX on a single Form 3115 for the same year of change, then the taxpayer must file a signed copy of that completed Form 3115 with the IRS in Ogden, UT (Ogden copy), in lieu of filing the national office copy, no earlier than the first day of the year of change and no later than the date the taxpayer files the original Form 3115 with its federal income tax return for the year of change and in accordance with section 10.11 of this APPENDIX. *See* sections 6.02(3)(a)(ii)(B) (providing the general rules) and 6.02(7)(b) (providing the mailing address) of this revenue procedure.

(5) *Designated automatic accounting method change number*. The designated automatic accounting method change number for a change under section 11.09 of this APPENDIX is "194." *See* section 6.02(4) of this revenue procedure.

(6) *Contact information*. For further information regarding a change under this section, contact Christopher W. Call at 202-317-7007 (not a toll-free number).

(3) Rev. Proc. 2011–14 is modified to add new section 11.10 of the APPENDIX, to read as follows:

.10 *Real property acquired through foreclosure*.

(1) *Applicability*. This change applies to a taxpayer that capitalizes costs under section 263A(b)(2) and § 1.263A–3(a)(1) to real property acquired through foreclosure, or similar transaction, where the taxpayer wants to change its method of accounting to an otherwise permissible method of accounting under which the acquisition and holding costs for real property acquired through foreclosure, or similar transaction, are not capitalized under section 263A(b)(2) and § 1.263A–3(a)(1). To qualify for this change in method of accounting, a taxpayer must:

(a) originate, or acquire and hold for investment, loans that are secured by real property; and

(b) acquire the real property that secures the loans at a foreclosure sale, by deed in lieu of foreclosure, or in another similar transaction.

(2) *Inapplicability*. This change does not apply to costs capitalized under § 263A(b)(1) and § 1.263A–2(a)(1) by the taxpayer to the acquired real property as a result of production activities.

(3) *Certain scope limitations temporarily inapplicable*. The scope limitations in sections 4.02(1) through (4) and (7) of this revenue procedure do not apply to a taxpayer making this accounting method change for its first or second taxable year ending after December 31, 2012.

(4) *Ogden copy of Form 3115 required in lieu of national office copy*. A taxpayer changing its method of accounting under this section 11.10 of the APPENDIX must file a signed copy of its completed Form 3115 with the IRS in Ogden, UT (Ogden copy), in lieu of filing the national office copy, no earlier than the first day of the year of change and no later than the date the taxpayer files the original Form 3115 with its federal income tax return for the year of change. *See* sections 6.02(3)(a)(ii)(B) (providing the general rules) and 6.02(7)(b) (providing the mailing address) of this revenue procedure.

(5) *Designated automatic accounting method change numbers*. The designated automatic accounting method change number for a change under section 11.10 of this APPENDIX is "195."

(6) *Contact information*. For further information regarding a change under this section, contact Roy Hirschhorn at (202) 317-7007 (not a toll-free number).

SECTION 4. EFFECTIVE DATE

.01 *In general*. Except as provided in section 4.02 of this revenue procedure, this revenue procedure is effective January 24, 2014.

.02 *Transition rules*. The following transition rules apply:

(1) *Form 3115 filed under Rev. Proc. 97–27*. If before January 24, 2014, a taxpayer properly filed an application under Rev. Proc. 97–27 requesting consent for a change in method of accounting described in section 3 of this revenue procedure, and the Form 3115 is pending with the national office on January 24, 2014, the taxpayer may choose to make the change under this revenue procedure if the taxpayer is otherwise eligible under this revenue procedure. The taxpayer must notify the national office of its intent to make the change under this revenue procedure prior to the issuance of a letter ruling granting or denying consent for the change. If the taxpayer timely notifies the national office that it will make the change under this revenue procedure, the national office ordinarily will return the Form 3115 to the taxpayer to make the necessary modifications to comply with the applicable provisions of this revenue procedure and will refund the user fee submitted with the Form 3115.

A Form 3115 that is returned to the taxpayer for necessary modifications will be converted to an application under this revenue procedure if the taxpayer resubmits the Form 3115 with the necessary modifications, along with a copy of the national office letter sent with the returned Form 3115, to the national office within 30 calendar days after the date of the IRS's letter returning the Form 3115 to the taxpayer.

(2) *Form 3115 filed under Rev. Proc. 2012–19*.

(a) *General rule*. If a taxpayer properly files an application with the IRS in Ogden, UT (Ogden Copy) under Rev. Proc. 2012–19 to make a change in method of accounting described in Rev. Proc. 2012–19 and the application was either post-marked or received by the IRS on or before January 24, 2014, the taxpayer makes the change under Rev. Proc. 2012–19.

(b) *Option to file an amended application*. If on or before January 24, 2014, a taxpayer properly filed an application under Rev. Proc. 2012–19, the taxpayer may choose to file an amended application for that year of change under this revenue procedure if, by the due date of the federal income tax return for the year of change (excluding extensions), the taxpayer (i) files an original or amended return using the new method of accounting pursuant to this revenue procedure, (ii) attaches the original amended application filed under this revenue procedure to its original or amended return for the year of change, (iii) writes on the top of page 1 of the Ogden Copy of the amended application "FILED UNDER SECTION 4.02(2) OF REV. PROC. 2014–16"; and (iv) sends the Ogden Copy of the amended application to the following address no later than the date the original amended application is filed with the original or amended return: Internal Revenue Service, 1973 North Rulon White Blvd., Mail Stop 4917, Ogden, UT 84404.

SECTION 5. EFFECT ON OTHER DOCUMENTS

.01 Rev. Proc. 2011–14 is modified and clarified.

.02 Rev. Proc. 2012–19 is modified and superseded.

SECTION 6. PAPERWORK REDUCTION ACT

The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1551. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

The collections of information in this revenue procedure are in section 3. This information is necessary and will be used to determine whether the taxpayer properly changed to a permitted method of accounting. The collections of information are required for the taxpayer to obtain consent to change its method of accounting. The likely respondents are the following: individuals, farms, business or other for-profit institutions, nonprofit institutions, and small businesses or organizations.

The estimated total annual reporting and/or recordkeeping burden is 9,162.5 hours.

The estimated annual burden per respondent/recordkeeper varies from ¼ hour to 8½ hours, depending on individual circumstances, with an estimated average of 1¼ hours. The estimated number of respondents is 7,330. The estimated annual frequency of responses is on occasion.

SECTION 7. DRAFTING INFORMATION

The principal author of this revenue procedure is Alan S. Williams of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this revenue procedure contact Alan S. Williams at 202-317-5100 (not a toll free number).

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26 CFR 601.105: Examination of returns and claims for refund, credit or abatement; determination of correct tax liability.

Rev. Proc. 2014–20

SECTION 1. PURPOSE

This revenue procedure provides a safe harbor under which the Internal Revenue Service (the "Service") will treat indebtedness that is secured by 100 percent of the ownership interest in a disregarded entity holding real property as indebtedness that is secured by real property for purposes of § 108(c)(3)(A) of the Internal Revenue Code.

SECTION 2. BACKGROUND

.01 Often borrowers incur debt in connection with real property used in a trade or business. If the debt is later discharged, the income from the discharge of indebtedness may be excluded from gross income if certain requirements are met. In some cases, the real property is held by the borrower in an entity that is wholly owned by the borrower, and is, for federal tax purposes, disregarded as an entity separate from its owner. In these cases, the debt may be secured by the borrower's ownership interest in the disregarded entity holding the real property.

.02 Section 61(a)(12) provides that gross income includes income from the discharge of indebtedness.

.03 Section 108(a)(1)(D) excludes income from the discharge of indebtedness from gross income if, in the case of a taxpayer other than a C corporation, the indebtedness discharged is qualified real property business indebtedness ("QRPBI").

.04 To qualify as QRPBI, § 108(c)(3) requires that the indebtedness must be incurred or assumed by the taxpayer in connection with real property used in a trade or business and be secured by such real property. The taxpayer must make an election to treat the indebtedness as QRPBI. QRPBI does not include qualified farm indebtedness. Section 108(c)(3)(B) provides that QRPBI must be indebtedness that was incurred or assumed before January 1, 1993, or if the indebtedness was incurred or assumed on or after January 1, 1993, it must be qualified acquisition indebtedness. Section 108(c)(3) also provides that indebtedness under § 108(c)(3)(B) includes indebtedness resulting from the refinancing of indebtedness under § 108(c)(3)(B), but only to the extent it does not exceed the amount of indebtedness being refinanced.

.05 Section 108(c)(4) defines qualified acquisition indebtedness as indebtedness incurred or assumed to acquire, construct, reconstruct, or substantially improve real property used in a trade or business.

.06 Section 108(c)(2)(A) limits the amount that may be excluded from gross income with respect to a discharge of QRPBI to the excess of (i) the outstanding principal amount of the QRPBI immediately before the discharge, over (ii) the fair market value of the real property reduced by the outstanding principal amount of any other QRPBI secured by the property at the time of discharge.

.07 Section 108(c)(1) provides that the basis of depreciable real property of a taxpayer shall be reduced by the amount excluded from gross income under § 108(a)(1)(D).

.08 Neither the statute nor the legislative history contains any explanation of or definition for the term "secured by such real property" used in § 108(c)(3)(A). Mortgages are commonly used by lenders to secure an interest in real estate. The legislative history does not suggest, however, that mortgages are the exclusive form of security for § 108(c)(3)(A). *See* H.R. Rep. No. 103–111 (1993), 1993–3 C.B. 167, 622–625. The fact that the statutory language does not limit the § 108 security interest to a mortgage indicates an intent to include a broader range of security interests.

.09 Section 301.7701–3(b)(1)(ii) of the Procedure and Administration Regulations provides that certain entities (including limited liability companies) with a single member that do not elect to be treated as corporations are disregarded as entities separate from their owners for federal tax purposes ("disregarded entity").

.10 In other contexts, the Service has, where certain conditions are satisfied, treated debt as secured by real property when the debt is secured by the sole membership interest in a disregarded entity that holds the real property. *See* Rev. Proc. 2003–65, 2003–2 C.B. 336.

SECTION 3. SCOPE

.01 This revenue procedure applies to the discharge of indebtedness of any taxpayer, other than a C corporation, provided the requirements of section 3.03 of this revenue procedure are satisfied.

.02 This revenue procedure provides a safe harbor under which the Service will treat debt as "secured by" real property for purposes of § 108(c)(3)(A).

.03 The requirements of this section 3.03 of this revenue procedure are satisfied if:

(1) The taxpayer or a wholly owned disregarded entity of the taxpayer ("Borrower") incurs indebtedness.

(2) Borrower directly or indirectly owns 100% of the ownership interest in a separate disregarded entity owning real property ("Property Owner"). Borrower is not the same entity as Property Owner.

(3) Borrower pledges to the lender a first priority security interest in Borrower's ownership interest in Property Owner. Any further encumbrance on the pledged ownership interest must be subordinate to the lender's security interest in Property Owner.

(4) At least 90 percent of the fair market value of the total assets (immediately before the discharge) directly owned by Property Owner must be real property used in a trade or business and any other assets held by Property Owner must be incidental to Property Owner's acquisition, ownership, and operation of the real property.

(5) Upon default and foreclosure on the indebtedness, the lender will replace Borrower as the sole member of Property Owner.

.04 If a taxpayer does not meet the requirements of this safe harbor, it is not precluded from arguing, based on facts and circumstances, that its debt satisfies the "secured by" requirement of § 108(c)(3)(A).

SECTION 4. PROCEDURE

Indebtedness that satisfies the requirements of section 3.03 of this revenue procedure will be treated as indebtedness secured by real property for purposes of § 108(c)(3)(A). Provided the indebtedness meets the other requirements of § 108(c)(3), such indebtedness will be QRPBI and, accordingly, any income from the discharge of such indebtedness will be excluded from the taxpayer's gross income pursuant to § 108(a)(1)(D) subject to the limitations provided in § 108(c). Further, as provided in § 108(c)(1), the basis of depreciable real property of the taxpayer will be reduced by the amount excluded from gross income.

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective for taxpayers who make an election under § 108(c)(3) regarding discharged indebtedness on or after February 5, 2014.

DRAFTING INFORMATION

The principal author of this revenue procedure is Seoyeon Sharon Park of the Office of Associate Chief Counsel (Income Tax and Accounting). For further information regarding this revenue procedure, contact Ms. Park at (202) 317-7006 (not a toll-free number).

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with modified, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

*Modified*is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with amplified and *clarified*, above).

*Obsoleted*describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in laws or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

*Revoked*describes situations where the position in the previously published ruling is not correct and the correct position is being stated in a new ruling.

*Superseded*describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, modified and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statement of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1]A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2013–27 through 2013–52 is in Internal Revenue Bulletin 2013–52, dated December 23, 2013.

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[1]A cumulative list of current actions on previously published items in Internal Revenue Bulletins 2013–27 through 2013–52 is in Internal Revenue Bulletin 2013–52, dated December 23, 2013.

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Key to Abbreviations:

Ann	Announcement
CD	Court Decision
DO	Delegation Order
EO	Executive Order
PL	Public Law
PTE	Prohibited Transaction Exemption
RP	Revenue Procedure
RR	Revenue Ruling
SPR	Statement of Procedural Rules
TC	Tax Convention
TD	Treasury Decision
TDO	Treasury Department Order

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INTERNAL REVENUE BULLETIN

The Introduction at the beginning of this issue describes the purpose and content of this publication. The weekly Internal Revenue Bulletins are available at *www.irs.gov/irb/*.

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The contents of the weekly Bulletins were consolidated semiannually into permanent, indexed, Cumulative Bulletins through the 2008–2 edition.

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