Balancing SCA with Employer Mandates Under Healthcare Reform

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With 2013 at our doorstep, I am increasingly asked one question by PSC member companies and others: “How will healthcare reform affect my business?” The answer is not an easy one and is different for each contractor. At more than 350,000 words, healthcare reform, also known as the Affordable Care Act (ACA), PPACA or ObamaCare, is complicated, complex, and confusing. This is especially true in evaluating how government contractors performing work covered by the Service Contract Act (SCA) will be affected by the ACA’s new employer mandates. Yet with the right education and preparation, the transition to ACA compliance can be a smooth one.

Contractors typically choose one of two avenues in anticipation of healthcare reform. The first is the “wait-and-see” approach taken by contractors that believe the healthcare reform requirements will change significantly before the implementation of its final regulations in the contractor’s first plan year following January 1, 2014. These contractors plan to hold off until late 2013 to make the necessary changes to their company’s benefits, waiting to see exactly what will be required at that point. Alternatively, contractors that believe the law is here to stay as is will choose to work toward becoming compliant with the ACA sooner rather than later. These contractors are typically larger employers who want to be certain they are both compliant with health care reform and competitive under the Service Contract Act.

To know how healthcare reform affects businesses, we must first understand how contractors satisfy their fringe benefits obligations under the Service Contract Act (SCA) will be affected by the ACA’s new employer mandates. Yet with the right education and preparation, the transition to ACA compliance can be a smooth one.

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To know how healthcare reform affects businesses, we must first understand how contractors satisfy their fringe benefits obligations under the Service Contract Act (SCA). Contractors who offer benefit plans provide full benefits, hourly based plans, or limited-medical plans. Some contractors exclude their

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SCA employees from benefits altogether or choose to pay the health and welfare fringe to the SCA employees in cash in lieu of benefits. Regardless of how they are currently fulfilling the requirement, companies must decide what they need to do to become compliant with the ACA. This may prove challenging due to the manner in which the Service Contract Act interacts with the ACA. A closer look at both laws is required to properly structure a compliant program.

Of course, each contractor’s situation is unique and the following is simply a general overview of the ACA’s employer mandate applicable to service contractors.

As of publication, the ACA will require most employers (including contractors) with more than 50 full-time employees to offer essential health benefits to employees and their dependents, and subsequently pay a specific portion of employee health benefit premiums. If the employer does not do both, the employer will pay a penalty in the form of an excise tax if even one full-time employee receives federal assistance, in the form of a subsidy, to purchase health coverage on an exchange established by the states to provide affordable coverage. Each employer/contractor must also provide their employees an affordable healthcare plan. An affordable plan is one in which the required contribution for self-only coverage does not exceed 9.5 percent of the taxpayer’s household income. Thus, employers who choose to pay less than 100 percent of the cost of an employee’s insurance will be required to prove that the employer’s share of the health insurance premium meets these government guidelines. Failure to meet these guidelines could result in penalties of up to $3,000 per employee per year.

There is no requirement under the ACA to provide ancillary benefits coverage such as life or disability insurance. The employer is required only to provide health coverage.

The silver lining for SCA contractors (as opposed to other employers) is that providing employees fringe dollars is already built into these contracts and therefore at their disposal for use in providing a compliant health care plan. Although some employers will strip back their ancillary benefits coverage to provide essential health benefits with fringe dollars, others will find that action to be unnecessary. The goal of every SCA-covered contractor should be to use the fringe benefit dollars already required to first cover the cost of their affordable healthcare coverage as required under the ACA, and then work to fit in ancillary benefits after that.

A good rule for assessing the amount available for an affordable plan is to assume 30 hours per week, or 120 hours per month, per employee. For example, at $3.71 in fringe benefits under SCA, a company would have $445.20 per month to cover health benefits for one employee and his dependents. But keep in mind that medical inflation seems to outpace the annual health and welfare rate increase, so it may be wise to be conservative in your estimates.

The ACA mainly pertains to existing employees who work an average of at least 30 hours per week, or for new employees who are expected to work an average of at least 30 hours per week. Seasonal or temporary employees could be subject to the ACA depending on a contractor’s specific eligibility calculation period. Calculations must be done to determine whether benefits are owed to an employee based on the hours worked. Because of this, contractors with both full- and part-time employees should start classifying these populations separately, if they are not doing so already. Many contractors simply label these employees as “non-exempt” or “SCA-covered” but don’t track their full-time/part-time status. Tracking their work-hour status now will make the transition to the ACA easier in 2014, as well as help with projecting costs.

There are many other components of ACA, none of which have been finalized, that are of interest to contractors. One key anticipated regulation will address discrimination between management and non-management health plans. Depending on the specifics of the rule, this could be an issue for many government contractors. In addition, contractors with two health plans or who offer an inferior health benefit package to their SCA employees, could be subject to penalties should they continue these practices unchanged. For most SCA contractors, the smart play is to design either a single health plan for all employees or separate plans that favor their hourly

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SCA employees. Structuring a plan that either provides richer benefits and/or employer cost shares for SCA (typically your rank-and-file) employees should position a contractor well for the implementation of and compliance with the ACA.

Service contractors paying health and welfare dollars will also need to take a closer look at their policies. Many contractors satisfy their SCA fringe obligations by giving employees the choice between receiving cash or benefits. They typically use traditional major medical style programs and allow their employees to also elect coverage. These contractors are certainly compliant with the current SCA requirements because they provide and account for fringe dollars, but with the ACA employer mandate on the horizon, consideration must be made as to how health and welfare fringe dollars will be treated for ACA compliance.

This is where things could get even trickier with healthcare reform. Are the fringe benefits provided under the SCA “employee” dollars or “employer” dollars in the eyes of the IRS? It depends on whether employees have a choice between cash and benefits. The general rule is that if an employee is given a choice between cash and benefits, then the fringe is viewed as additional wages and the benefit elections are treated as payroll deductions and thus generally would be considered employee dollars because the employee was given constructive receipt of those dollars and chose either cash or benefits. In this case, the company could face significant penalties for not providing the appropriate cost shares and minimum essential coverage. Conversely, in cases where employers spend the fringe on a bona fide benefit program in which the employee has no option to receive cash, those benefits are typically viewed as employer-provided dollars. This is a key distinction, and is especially important under the ACA as the contractor has a responsibility to either provide affordable coverage or face the penalties.

As we progress through 2013, there is little doubt that health care reform will continue to move forward and ultimately be implemented in some capacity and that there will be further regulations issued to implement the ACA. Service contractors who are prepared and taking action now will be ahead of the curve come the end of 2013. Those who choose to forgo early planning may be left with difficulty finding and implementing a compliant program in time. Late 2013 will be a challenging and busy time for benefit providers, carriers, and brokers. I recommend that every contractor who anticipates having an SCA-covered contract take a good look at their situation now rather than later and start working with the appropriate parties to develop their own plan to stay competitive and in compliance.

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