

# ACA Compliance When Employees Move from Full-Time to Part-Time Mid-Year

by Karen K. Hartford on February 9, 2024

We are well into the Affordable Care Act (“ACA”) information reporting season. Forms 1095-B/1095-C must be provided to employees by March 1, 2024, and the deadline for electronic transmittal of Forms 1094-B/1094-C to the IRS is April 1, 2024. A common fact pattern that frequently results in ACA reporting errors is the employee who moves from a full-time position to a part-time position mid-year. Must plan sponsors continue to offer this part-time employee health coverage? Doesn’t the ACA only require employers to offer health coverage to their full-time employees? The answers to these questions depend on which measurement methodology the employer uses to calculate full-time employee/full-time equivalent (“FTE”) status.

## Background

As a reminder, the ACA requires employers with fifty or more FTEs (an FTE is an employee who works at least 30 hours per week or 130 hours per month) to offer minimum essential health coverage to at least 95% of those FTEs and their dependents. The ACA provides two methods for determining who is an FTE: the monthly measurement method (“MMM”) and the look-back measurement method (“LBMM”).

## Monthly Measurement Method

The MMM requires tracking actual hours worked. Under the MMM, employees who average at least 30 hours per week or at least 130 hours per month are FTEs. The determination cannot be made with certainty until the end of the month. The MMM is often used by employers with stable workforces that work mostly full-time hours.

## Look-Back Measurement Method

At a high level, the LBMM requires tracking employee hours for a certain period, called the “measurement period,” which determines the employee’s FTE status for a subsequent period, called the “stability period.” The LBMM requires the plan sponsor to establish three things: (1) a “measurement period” of 3 to 12 months, during which employee hours are tracked to determine whether they average at least 30 hours per week or at least 130 hours per month; (2) a “stability period” that must be at least 6 months or, if longer, the length of the measurement period, during which those employees who were determined to be full-time during the measurement period continue to be treated as full-time – regardless of the number of hours worked during

the stability period; and (3) an “administrative period” of up to 90 days that falls between the measurement period and the stability period and allows time for enrollment and other administrative tasks. The LBMM is often used by employers with less predictable workforces and a significant number of part-time and/or variable hour employees because the stability period eliminates the need to make a change each time an employee’s hours drop below the FTE hours thresholds, thereby providing administrative simplicity.

## The Fact Pattern

Often, plan sponsors tell us that the terms of their plan document exclude part-time or per diem employees and therefore, when an employee moves into a part-time position mid-year, the employer terminates their coverage and offers COBRA.<sup>1</sup> While this approach can work for employers who use the MMM to determine FTE status, it generally does not work for employers using the LBMM because ongoing FTEs must remain in their measurement period status for the entire stability period.<sup>2</sup> An ongoing FTE is one who has completed one full standard measurement period. There are, however, two exceptions to this rule:

1. **The FTE was a new hire.** When using the LBMM, a newly hired FTE must be offered coverage by no later than the first day of the fourth full calendar month of employment (known as the “limited non-assessment period”), but will not become an “ongoing employee” under the LBMM until completing one full standard measurement period that is applicable to ongoing employees. During this “gap period” at the start of employment—which may be over two years depending on the length of the measurement period and administrative period—the FTE’s status is determined monthly. A change to a part-time position could result in a loss of coverage if the employee fails to work 30 hours per week or 130 hours per month, and the employer is not required to continue to offer coverage to avoid potential ACA employer shared responsibility penalties because the employee is treated as part-time for such month. Once the new FTE completes one full standard measurement period, however, the employee’s FTE status is determined by the results of the measurement period for the associated stability period, the same as for all other ongoing employees.

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<sup>1</sup> As an aside, any plan sponsor using the LBMM should ensure that their plan document’s eligibility provisions are ACA-compliant by at least cross-referencing the employer’s policy for determining FTE status.

<sup>2</sup> At the end of the stability period, the individual may be treated as losing coverage due to a reduction in hours and offered COBRA at that time.

2. **Special Rule for Certain Employees to whom Minimum Value Coverage Has Been Continuously Offered.** Treasury Regulation § 54.4980H-3(f)(2) provides a special rule for ongoing employees who move mid-year into an employment status that would have been considered part-time if the employee had originally been hired into that position. If the rule's conditions are satisfied, the employer may switch such an ongoing employee to the MMM. The change to the MMM must begin no earlier than the first day of the fourth full calendar month following the calendar month of transfer and may only occur if:
  - a. The employer continuously offered coverage to the employee after the employee completed the limited non-assessment period following the start of employment through the date of the move; and
  - b. The employee actually averages less than 30 hours per week for each of the three full calendar months after the move.

For the three full calendar months following the employee's change in employment status, the employee's right to an offer of coverage is determined based on the employee's status during the applicable stability period. That is, an employee who was full-time during the stability period must continue to be considered full-time for at least three months following transfer to a part-time position. Note that moving an employee to the MMM does not necessarily mean that the employee's right to an offer of coverage is eliminated. An employee credited with 30 hours of service per week or 130 hours in a month remains entitled to an offer of coverage for that month under the MMM.

### **Correctly Applying the LBMM is Key to Avoiding Penalties**

It's important to note that an employer using the LBMM is not required to utilize either of the above exceptions; an employer may always follow the general rule of continuing to offer coverage each month for the remainder of the stability period. What an employer using the LBMM may *not* do, however, is immediately stop offering coverage to an ongoing employee whose hours are reduced below the FTE threshold mid-year. An employer's misunderstanding of the LBMM rules will become apparent when it comes time to complete and file the ACA Form 1095-B/1095-C information returns for these employees, as the Forms will be flagged by automated return software as ACA-non-compliant, creating a risk of reporting penalties. The error can be compounded if the employer manually adjusts the Forms to incorrectly code the employee as part-time or COBRA-eligible and, in the meantime, the employee picks up health coverage on the government exchange and qualifies for a premium subsidy. In this scenario, the employer is at high risk of receiving an IRS Letter 226-J with a proposed penalty assessment either because the employee was incorrectly coded or because the COBRA coverage is unaffordable. Under Internal Revenue Code Section 4980H(b), penalties may be assessed when at least one FTE is allowed the premium tax credit because the coverage was unaffordable or did not provide minimum value, or the FTE



did not receive an offer of coverage. As explained in our past blog posts [here](#) and [here](#), the penalties for incorrect ACA reporting can be troublesome and steep.

Employers should be sure they understand what ACA measurement method they use and that it is being correctly applied. Employers that use the LBMM and do not wish to continue coverage for ongoing employees who move to part-time positions mid-year should consider the two exceptions described in this post.

If you have any questions about ACA compliance, please contact a member of [Verrill's Employee Benefits & Executive Compensation Group](#).



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