

Will You Play or Pay in Your Next Deal?

By: Gabriel S. Marinaro, Esq.

With some companies becoming subject to the Affordable Care Act's (ACA) employer mandate and new reporting requirements for the first time in 2015, corporate transactions, such as a merger or acquisition, will now require additional planning (and potential headaches) to reflect these new requirements. As a corporate transaction progresses to closing, it is important for the parties to understand how the employer mandate and reporting requirements apply to the transaction and how such requirements (if any) will be handled post-closing. Due to a scarcity of official IRS guidance, it is especially important for the parties to understand the post-transaction situation so that potential penalties under both the employer mandate and the new reporting requirements are mitigated or avoided altogether. This article highlights the available IRS guidance, areas where additional guidance is needed, and action items that companies should consider in connection with a corporation transaction.

In IRS Notice 2014-49, the IRS has provided some initial guidance on how to address employees moving from a target to acquirer's measurement method, when the target and acquirer use two different measurement methods. Until further guidance is issued, and in any case through the end of the 2016, companies may rely on the guidance in the Notice. The general takeaway from the Notice is that, in a merger or stock acquisition, the acquirer can (a) continue to apply the target's measurement and stability periods for a "transition period" post-closing or (b) transfer target employees on to the acquirer's measurement method, accounting for employees in a stability period with the target and hours worked with the target.

If the acquirer decides to transfer target employees on to acquirer's measurement method, then the following must be observed: (a) if an employee is in a stability period (or administrative period following the end of an initial measurement period) with the target company, the employee will retain his or her status until the end of the applicable stability period of the target and (b) if the employee has not completed a measurement period with the target, the employee's hours will be measured under the acquirer's measurement method, taking into account hours worked with the target.

In an asset purchase, unlike a merger or stock purchase, employees of the target are treated as new hires of the acquirer. Although an asset purchase can be more straightforward with respect to the application of measurement methods and reporting requirements, there could be potential issues where employees hired by the acquirer are granted past service credit (as described more below).

When acquirer moves target employees on to acquirer's measurement method and stability periods

Notice 2014-49 provides examples of how to treat employees that transition to a different measurement period and how these can be applied in a variety of contexts. For our purposes, we will focus on different approaches where the acquirer and the target are both "applicable large employers" (ALEs) (i.e. an employer with 50 or more full-time employees or full-time equivalents) using look-back measurement

methods for their variable hour employees. Assume that Company A (target) merges into Company B (acquirer) and both corporations use the look-back measurement method but with different measurement periods. Notice 2014-49 provides that:

(a) For an employee of Company A that is in a Company A stability period at the effective time of the merger, such employee's status determination as a full-time or non-full-time remains in effect for the remainder of the Company A stability period.

(b) For an employee of Company A that is in an administrative period immediately following the end of an initial measurement period at the effective time of the merger, the employee's status as a full-time or non-full-time employee (based on the hours of service in the initial measurement period) under Company A's measurement method will apply from the start of Company A's stability period and remain in effect for the remainder of Company A's stability period.

(c) At the end of the stability period in (a) or (b) above, an employee of Company A will assume the full-time or non-full-time status that the employee would have under the look-back measurement method applicable under Company B, but including hours of service with Company A when applying the measurement method for Company B.

(d) For an employee of Company A that is not in a Company A stability period or a Company A administrative period following an initial measurement period, the employee's status as a full-time or non-full-time employee is determined solely under the look-back measurement method applicable under Company B as of the effective date of merger, including all hours of service with Company A.

Assume that Company A uses a 12-month initial measurement period that begins on the employee's start date and Company B uses a 6-month initial measurement period beginning on the employee's start date and a 6-month standard measurement period that begins on January 1 and June 1. Employee Y is hired by Company A as a new variable hour employee on January 1, 2015. Employee Y averages 30 hours per week during the period from January 1, 2015 through June 30, 2015. Company A merges into Company B on October 1, 2015, at which time Employee Y is still in his initial measurement period for Company A. At the date of the merger Employee Y is not in a stability period for Company A so Employee Y's status as a full-time employee will be determined under Company B's initial measurement period, taking into account Employee B's hours of service with Company A. Employee Y will be treated as a full-time employee of Company B until December 31, 2015. After December 31, 2015, Employee Y's status is determined using the applicable measurement period for Company B.

Corporate transaction where acquirer adopts target's measurement method for a transition period

Notice 2014-49 also provides that in a merger or stock acquisition, an acquirer is free to adopt the target's measurement method for some or all of the target employees that was in effect for those employees immediately prior to the transaction for a transition period. The "transition period" is the period beginning on the date of the corporate transaction and ending on the last day of the first stability period (following a standard measurement period) that would have applied to the target employees absent the corporate

transaction and that begins after the date of such corporate transaction (or, in the case of an ALE member that uses the monthly measurement method with respect to a category of employees, the last day of the first calendar year that begins after the date of the transaction).

How do companies report corporate transactions for the new ACA reporting requirements under Code Sections 6055 and 6056?

Although we have guidance addressing potential approaches in dealing with different measurement methods, it's unclear how companies are to report certain corporate transactions under Code Sections 6055 and 6056.

In an asset purchase, assuming the target and acquirer are both ALEs, the target will continue to report the type of coverage offered (e.g. COBRA coverage) on a monthly basis, the status of the employee with respect to the coverage offered (e.g. whether employed or not employed), and other required reporting on the 1095-C for the year of the asset purchase. To the extent that the acquirer in an asset purchase hires one or more of the target's employees, the acquirer may also have a 1095-C reporting obligation in the year of the asset purchase. Thus, an individual terminated by the target and hired by the acquirer may receive two 1095-Cs. Both the target and the acquirer will reflect the number of employees, etc. on their respective 1094-Cs for each month. If the seller has terminated all of its employees in connection with the asset purchase, this will be evident in Part III of the 1094-C. The parties to an asset purchase agreement should be aware of these reporting obligations and plan accordingly.

For a merger or stock acquisition where the target company will cease to exist at some point during a calendar year, there does not appear to be an available code or mechanism to report such an event to the IRS on the 1094-C or 1095-C. Assuming the target and acquirer are both ALEs, the acquirer likely will report under the target's EIN the year of the merger or stock acquisition and also separately report under its EIN for purposes of 1094-C and 1095-C. Similar to an asset purchase, an employee entitled to a 1095-C might receive one from the target and one from the acquirer ALE.

One area that might get tricky is where the target terminates its group health plan. The parties will then need to refer to the COBRA regulations and, in some circumstances, the transaction agreement, to determine who is responsible for offering COBRA coverage for those individuals that have rights to continued coverage under either another plan of the target's controlled group or the acquirer's group health plan. The parties will need to plan accordingly for a termination of the seller's group health plans and what impact this will have on their reporting under 6055 and 6056.

Action Items for parties involved in corporate transactions

With uncertainty regarding the new ACA reporting requirements and additional guidance anticipated for complying with the employer mandate in the corporate transaction context, both the target and acquirer should make sure they understand how these new requirements impact their transaction. Depending on the nature of the deal, the target and acquirer should consider the following:

- The acquirer should determine what type of measurement method target is using for some or all of its employees.
- The acquirer should collect detailed records of hours worked and the target's methods for tracking hours to determine the level of the target's compliance with the employer mandate.
- Representations and warranties in the agreement should include specific representations about compliance with various provisions under the ACA, including, to the extent applicable,

- compliance with the employer mandate and the ACA reporting requirements.
- Consideration regarding service credit for the target's employees that are hired by the acquirer and whether this will extend to the acquirer's group health plans.
 - COBRA considerations when it is anticipated that the seller will terminate its group health plan in connection with the closing of the transaction or shortly thereafter.
 - Consider whether indemnities in the agreement should be extended to penalties under the employer mandate and the ACA reporting obligations and for how long.

If you have any questions regarding the ACA, COBRA, Code Sections 6055 and 6056, or anything regarding these regulations, please contact Gabe Marinaro at (231) 486-4540 or gmarinaro@shrr.com.



Gabe Marinaro's practice focuses on all aspects of employee benefits and executive compensation. He can be contacted at gmarinaro@shrr.com or 231-486-4540.