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Merry Christmas! Your Gift of Coal: A Pay or Play Penalty Assessment



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As J. Fred Coots sang, “He’s making a list, he’s checking it twice; He’s gonna find out who’s naughty [read *paid*] or nice [read *played*].” On November 2, 2017, the IRS quietly announced that beginning in late 2017, it will send applicable large employers (ALEs) notices of proposed pay or play penalties for the 2015 calendar year. This announcement came via updated FAQs which are available and can be found at <https://www.irs.gov/affordable-care-act/employers/questions-and-answers-on-employer-shared-responsibility-provisions-under-the-affordable-care-act> (see FAQs 55-58).

As a reminder, an ALE is an employer that had an average of at least 50 full-time employees (including full-time equivalent employees) in the previous calendar year. So, for purposes of a pay or play penalty assessment for the 2015 calendar year,

an employer’s ALE status is determined based on its average number of full-time employees in the 2014 calendar year.

Proposed Assessment Notice: Letter 226J

If you were a naughty ALE and receive a proposed pay or play penalty notice, it will come in the form of a Letter 226J. A sample of Letter 226J is available at <https://www.irs.gov/pub/notices/ltr226j.pdf>. The good news is: the IRS only intends to send a Letter 226J to ALEs on behalf of full-time employees who received a premium tax credit, **and for which the ALE did not report either an affordability safe harbor (or other form of relief) in all boxes in row 16 of the employee’s 2015 Form 1095-C.** In other words, if none of an ALE’s 2015 Forms 1095-C contained any blanks in row 16, the ALE should not expect to receive a Letter 226J.

The problem is—unlike Santa Claus—the IRS doesn’t “check its list twice.” So, where Santa’s list may be free from error, we would not be surprised if numerous ALEs receive a Letter 226J in error, or the proposed pay or pay penalty is incorrect.

Responding to Letter 226J

All ALEs that receive a Letter 226J must respond, otherwise the IRS will formally assess the proposed pay or play penalty. Time is of the essence because the ALE only has 30 days from the date of the letter (not the day the letter was received) to respond. When you factor in delays associated with mailing, and routing the Letter 226J to the appropriate person within the ALE (as well as holiday vacations), an ALE may have significantly less than 30 days to formulate a response.

In the likely event that an ALE disagrees with the IRS’s proposed pay or play penalty, the ALE must include in its response: (1) a signed statement of why it disagrees with the IRS; (2) any corrections to the 2015 Forms 1094-C or 1095-C; and (3) any other supporting documentation. (The ALE should **not** file corrected Forms 1094/5-C to fix these errors.)

After the IRS reviews an ALE’s response to Letter 226J, it will respond using Letter 227. If the IRS agrees with the ALE’s response, no further action is necessary except to pay the agreed upon pay or play penalty (if any). (Remember, the penalty is **not** tax deductible.)

On the other hand, if the IRS disagrees with the ALE’s response, the ALE can request a “pre-assessment conference” by filing a formal protest within 30 days with the IRS Office of Appeals. If agreement cannot be reached in Appeals, the ALE may further appeal to the U.S. Tax Court. Alternatively, the ALE can pay the penalty, file a claim for refund and, if that claim for refund is denied (or not approved within six months), the ALE can file a refund lawsuit in Federal District Court or the Federal Court of Claims.

Next Steps

If you are an ALE, we recommend the following steps:

- **Now:** Begin reviewing your 2015 Forms 1095-C to determine if any contain blanks in row 16. Those Forms 1095-C will potentially trigger a Letter 226J. This is especially true if you used a third-party vendor to complete your Form 1094/5-C reporting process, as this may require cooperation from your third-party vendor.
- **Upon Receipt of Letter 226J:** Act quickly to formulate a response. Make sure to include all information required by the IRS and explained in Letter 226J. An ALE may also consider involving legal counsel at this stage. (Please feel free to contact us.)

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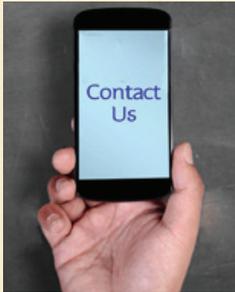
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- **Upon Receipt of Letter 227:** If you didn't contact legal counsel upon the receipt of Letter 226J, you should at this stage. While legal counsel is not required to represent an ALE in a "pre-assessment conference," this conference begins a formal tax controversy with the IRS, where procedure is both complicated and important.
- **Don't:** Pout or cry because "Santa Claus is coming to town!"

Until the Affordable Care Act (ACA) is repealed or replaced, our health care reform team continues to monitor announcements and changes. If you have any questions about this article or any other issues related to the ACA, please contact Tripp VanderWal or Mary Bauman.



Contact us

If you have any questions about the article in this issue, please contact the author. If you have any question on how any proposed health care reform changes will impact your organization, please feel free to contact Mary Bauman, chair of Miller Johnson's Health Care Reform Team, or another member of the team.

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