

**THE HEALTH CARE LAW: THE EFFECT OF THE  
BUSINESS AGGREGATION RULES ON SMALL  
EMPLOYERS**

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**HEARING**  
BEFORE THE  
**COMMITTEE ON SMALL BUSINESS**  
**UNITED STATES**  
**HOUSE OF REPRESENTATIVES**  
**ONE HUNDRED THIRTEENTH CONGRESS**

FIRST SESSION

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# **THE HEALTH CARE LAW: THE EFFECT OF THE BUSINESS AGGREGATION RULES ON SMALL EMPLOYERS**

**WEDNESDAY, DECEMBER 4, 2013**

HOUSE OF REPRESENTATIVES,  
COMMITTEE ON SMALL BUSINESS,  
*Washington, DC.*

The Committee met, pursuant to call, at 1:00 p.m., in Room 2360, Rayburn House Office Building. Hon. Chris Collins presiding.  
Present: Representatives Collins, Luetkemeyer, Tipton, Huelskamp, Schweikert, Bntivolio, Velázquez, Hahn, Payne, Meng, and Barber.

Mr. COLLINS. [Presiding] Good afternoon. I call this meeting to order.

As we are all well aware, the health care law requires businesses that employ 50 or more full-time or full-time equivalent employees to offer health insurance or pay an employer mandate penalty or tax. A critical issue is the definition of employee, but equally important is the issue of which and how many employees are attributed to the business. The answer may be simple for one business with a single owner. However, when an individual shares ownership of multiple entities or when a business has multiple owners, the answer is less clear.

Today, we will examine the process of determining whether businesses are considered single or multiple entities under the healthcare law, which requires business owners to aggregate employees and could subject the business to the Obamacare employee mandate. According to the National Federation of Independent Business, 39 percent of small businesses with 20 or more employees own at least 10 percent of one or more other businesses. To determine if the threshold of 50 or more employees has been met in these situations, the health care law utilizes the Internal Revenue Service code controlled group business aggregation rules, which are complex and confusing even for experts. Some experts have suggested that most small business owners could not interpret these rules without the guidance and related cost of a tax specialist. Despite the administration's promises that the health care law would help small businesses, each week seems to bring entrepreneurs more bad news, more costly regulations, more uncertainty, and less incentive to grow their business and create jobs.

A recent U.S. Chamber of Commerce International Franchise Association survey found that 53 percent of small business owners believe the law will have a negative impact on their business. In our

challenging economy, many small business owners are simply not hiring or are reducing worker hours to avoid the employer mandate.

Thank you to this outstanding panel of witnesses who have taken time from their busy schedules to be here today. We do look forward to your testimony.

I now yield to Ranking Member Velázquez for her opening statement.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman.

Small businesses are the backbone of our economy, but in the past high health care costs and declining coverage have hindered small business owners under employees. These factors have hampered our nation's entrepreneurial progress and held back small businesses. In fact, the chairman mentioned NFIB and the U.S. Chamber of Commerce. They have conducted surveys about small businesses, asking them what is the main issue that they are concerned about. They talk about the cost of health insurance and being able to provide it. In fact, 62 percent of small businesses in this country provide no health insurance to their employees, their families, or themselves. So if anything, this law will enable small businesses to participate in the exchanges so that we have a larger pool, and in the process we will bring premium costs down because that will provide the kind of leverage that will enable them to negotiate good premiums.

But the Affordable Care Act has changed the health care landscape for small firms. It has expanded coverage options, increased purchasing power, and gave consumers control over their own health care. Yet, as with any law of this magnitude, some fixes will need to be made along the way. It happens every day. That is what the legislative process is all about. We pass laws, we implement them, and we will fix what needs to be fixed, that is what the mechanism of legislation is all about. That means listening to the feedback of those most affected and working together to ensure small firms secure quality, affordable health care.

Today we will do just that by hearing from witnesses about a complicated issue. The health care law includes an employer mandate that requires businesses with more than 50 full-time employees to provide health insurance. Its goal is to discourage employers from dropping coverage and leaving employees on their own to find insurance. While the enforcement of this rule has been delayed until 2015, many small employers must begin adopting now.

This hearing will focus on a particular area of the law that many small firms may not be familiar with, the business aggregation rules. Traditionally, this rule has been used to treat a separate business as a single employer for purposes of retirement plans. This is not new. It is on the books when it comes to benefit plans. This tax rule will incorporate it into proposed regulations to deter entities from splitting into smaller companies with the purpose of avoiding the employer mandate. The intent behind this regulation is admirable, but I remain concerned about how these very complex rules will impact small firms. What kind of outreach, what kind of resources will be in place to assist small businesses so they understand the rule and how to abide by the rule.

I am sure it came as little surprise to many tax experts that these rules are being employed to determine business sizes. Unfortunately, for many small, family-owned businesses and franchise owners, these rules are not commonplace. For that reason, we must consider how the business aggregation rules impact many entrepreneur business models. Though some small employers have already been applying this rule to comply with ERISA, other firms have a steep learning curve ahead of them.

I hope our hearing today provides more information on just how many small employers currently navigate this rule and how many more will be newly affected. Our witnesses today will help walk us through these complicated standards on how best to educate owners of their nuances. With careful planning and proper outreach, small employers may avoid many pitfalls when complying with new obligations under the Affordable Care Act.

I thank all the witnesses for being here, and I look forward to our insightful comments. Thank you very much, Mr. Chairman. I yield back.

Mr. COLLINS. Our first witness today is Deborah Walker. Ms. Walker is a certified public account and the National Director of Compensation and Benefits for Cherry Bekaert, LLP, in Tysons Corner, Virginia. She advises small and large businesses on compensation, benefits, and employment tax matters. Welcome, and you have five minutes.

**STATEMENTS OF DEBORAH WALKER, CPA, NATIONAL DIRECTOR, COMPENSATION AND BENEFITS, CHERRY BEKAERT, LLP; SIBYL BOGARDUS, CHIEF COMPLIANCE OFFICER, WESTERN REGION EMPLOYEE BENEFITS, HUB INTERNATIONAL INSURANCE SERVICES, INC.; ELLIS WINSTANLEY, CHIEF EXECUTIVE OFFICER, TRADELOGIC CORPORATION, ON BEHALF OF THE NATIONAL RESTAURANT ASSOCIATION; DONNA BAKER, CPA, DONNA BAKER & ASSOCIATES.**

**STATEMENT OF DEBORAH WALKER**

Ms. WALKER. Good afternoon, Chairman Collins, Ranking Member Velázquez, and members of the Committee. Thank you for hosting this important hearing on the effect of the business aggregation rules on small business in applying the healthcare provisions. I am Deborah Walker, a CPA with over 35 years of experience in the employee benefits area.

To determine if the employer is subject to the shared responsibility rules of the Affordable Care Act, the business needs to determine who the employer is, and that determination is made by looking at related entities, related by common ownership, related by attribution, and also by services that the entities provide to each other. To make the determination, one needs to understand detailed ownership and the services that are provided to each other. My written submission describes these rules in excruciating detail, and I can assure you that no one would apply the rules in a complex situation without looking at the regulations.

The rules, as mentioned, used by the Affordable Care Act are the same rules used for determining whether qualified retirement plan benefits are provided on a nondiscriminatory basis to a fair cross-

section of employees. Those rules for retirement plans are voluntary, not mandatory. In addition, because we are looking at bright-line tests, bright-line tests offer the opportunity as evidenced by the qualified plan rules of ways to plan around them. In other words, for people to avoid the rules. In addition, because they are bright-line tests, it often happens that the application does not make as much sense as it otherwise may.

In the healthcare context, whether we looking at whether we have 50 employees or not, it is a complicated test for the few taxpayers that are nearing the 50-employee limit. One can expect that those employers nearing the 50-employee limit would, in fact, consider the increased healthcare cost in deciding whether to hire additional workers. It will lead to inefficient and unwarranted economic behavior.

Many small employers, as mentioned, offer a retirement plan, a 401(K) Safe Harbor Plan. They do not even need to apply these rules because they are not subject to the discrimination tests due to the safe harbor. The small businesses could not do this without advice, and many of the advisors for small business are not familiar with the rules. So therefore, I offer an alternative suggestion, and it is a suggestion that would be a facts and circumstances test. It would look to who is the individual who hires, that fires, and makes purchasing decisions, that sets prices, who operates that business on a day-to-day basis. And in that case, we do not have to worry about who is merely a passive investor and aggregate those entities. By focusing on control of day-to-day operations, the employer would be defined by the industry in which that employer individual operates, and it would not affect the competitive position of the business. The opportunity to avoid the bright-line test through planning would not be available, and the unwanted effects of a bright-line test would not exist.

Now, this facts and circumstance idea is not new. We use it and have in the tax law for years—30, 40 years in determining whether somebody is an employee or independent contractor. And people tried in the 1980s to have certainty with determining whether somebody was an employee or independent contractor, and it was determined that there were too many varied situations between service providers and recipients, and it was too hard to draw a hard and fast bright-line rule, and bright-line rules would be circumvented.

So what we have is a 20-factor test. The 20-factor test, there is not specific weight to any factor. In fact, the weight of the factors changes depending on the industry. And any advisor and the IRS reviews the 20 factors, reviews the particular situation, and makes a judgment call. It is a facts and circumstances test subject to everybody's judgment, of course, subject to audit.

There is another place where we talk about separate lines of business. This is also in the qualified retirement plan area, a separate line of business. It is a portion of an employer identified by property and services that are provided to a customer. So the regulations define what is a separate line of business and it has to be organized individually. There has to be a distinct profit center, and there can be no more than moderate overlap between employees

and management. A rule such as that, more of a facts and circumstances test, may be more appropriate.

Of course, as I mentioned, the determination is always subject to audit by the IRS. The rules could require a notice requirement. The rules could also have a procedure, such as they do for separate line of business and employee independent contractors where, in fact, the two businesses could apply to the IRS for the IRS to make a determination.

To summarize, the mechanical test used for qualified plan rules are overly complex and understood by only a limited number of tax professionals. A small business cannot apply them without professional help. It is a small subset of professionals that deal with these rules, and these rules are only going to apply for businesses for a few years of their lifecycle when they are close to the 50-employee test. For that reason, facts and circumstances to me, based on who controls day-to-day businesses, is a much more logical rule. The statute or communiqué reports could list characteristics of management and control and taxpayers would be able to make a judgment as to what constitutes the employer for purposes of these rules.

Thank you for your time and attention.

Mr. COLLINS. Thank you, Ms. Walker.

I would like to yield to Ranking Member Velázquez to introduce our next witness.

Ms. VELAZQUEZ. Thank you, Mr. Chairman.

It is my pleasure to introduce Ms. Sibyl Bogardus. Ms. Bogardus is an attorney serving as the chief compliance officer for Hub International Insurance Services. In this position, she provides compliance and consulting services regarding health plans and other employee benefits. Ms. Bogardus was previously chosen as one of the 100 leading women in insurance by Business Insurance and was selected as one of the 25 Most Influential Business Women by the St. Louis Business Journal. Welcome, and thank you for being here.

#### **STATEMENT OF SIBYL BOGARDUS**

Ms. BOGARDUS. Thank you. Thank you, Mr. COLLINS. Thank you Ranking Member Velázquez. I am honored and very happy to be here to be able to give some comments and testimony on this very important issue. I want to have an echo for what Ms. Walker said regarding some possible compromises or concessions towards small businesses. I think a controlled test would be a great first step as opposed to a bright-line standard.

I want everyone to keep in mind as we go through these types of discussions that the importance of the 50-employee rule and the control group rules which can cause small businesses to be treated as one employer has impacts not just on the basic issue of whether the employer will be subject to the law as a whole; it has huge implications also for the practical compliance under the rules.

I want to address specifically today the issues of complexity. Also, the issues of awareness. And then finally, confusion. And I think the issue of complexity, as you read through the rules, very quickly you begin to learn, as you have seen from the written testimony and comments, that these are very complex rules. It defi-

nately requires a tax advisor or a corporate planner to assist an employer in determining whether they have a control group. As to the awareness, the level of awareness is low. If an employer has voluntarily decided to create a retirement plan, yes, they have generally addressed these issues. But for employers that are made up of various small groups, they have likely not done this if they have not put in place a retirement plan. And while it is true that insurance carriers ask questions about the employer's size, they do so not so much to do an analysis. It is not an analysis. They are asking questions about size so that they can put into their programs how COBRA should be administered if it does apply, whether Medicare secondary payer rules apply, and other technical issues like that, but it is not an analysis of the control group. They are also asking that question so they can determine whether they will issue a small group or large group policy.

We are already seeing confusion around that issue. For example, just this week I received an e-mail regarding a small employer in California, and they were unable to get a small employer policy because they were considered to be part of a larger control group by the insurance carrier. The insurance carrier in California said they would not issue that policy because it would be discriminatory. However, that same control group had a small employer in Arizona. That small employer in Arizona was able to get the policy. For the employees in California, very low paid employees. They are now put into a very expensive PPO and they cannot afford it. It is \$1,300 a month. So we have seen quite a bit of low awareness around this issue, even among not just small employers but large employers. They say many times I was not aware of this and we do get comments that are very incredulous that this would even be the case.

In terms of some of the additional confusion, there are myths around association plans. Unless you have stickiness within a group, it is difficult to put unrelated or even fairly closely-related employers together. Some insurance carriers will not write them even though they technically would be a control group for U.S. tax purposes. So keep that in mind. Part of the problem is the practical access to the insurance coverage, which the law unfortunately does not guarantee for the small employers.

Are there planning opportunities? Yes. Do we see smaller employers trying to use those to avoid compliance with the law? Not yet. And I think part of the lack of awareness is also a little bit of a reaction to the delays that have occurred. The employers believe that there have been delays and that those delays will continue. For smaller businesses, there is a sentiment that the rules for the large employers were delayed, which they were until 2015. However, for the smaller businesses, they have already felt, many of them, the brunt of the very expensive renewals this year. Of our clients that were offered an early renewal option to renew their policy this December and to delay the cost impacts of health reform, invariably they have taken that offer if the carrier has extended it. So they have basically kicked the issue down the road for another year, so to speak. And also the cost impacts. We will hear more about that next fall. Additional policy cancellations and increases. We are seeing some premium increases of 100 percent

for smaller employers. So it is a matter of the law providing access to coverage with no preexisting conditions, but it is not by any means affordable, even for the small businesses.

The small businesses are also different. If they are part of a control group, that does not mean there is actual control or authority or even cooperation among the various owners. There is generally no central payroll system, no central HR person. They may handle that function at various locations but not centrally. Commonly, there are situations where the employers simply do not have a common point person. Now, of course, they could appoint someone but creating common systems to determine whether the employer is 50 employees or more and then also consistency across the group for payroll purposes is very difficult.

I want to also touch quickly on participation requirements that insurance carriers have in the small group marketplace. The rules under the Federal law do allow participation requirement of 70 percent. The insurance carrier can require that percentage of the employees to elect the coverage. Alternatively, many carriers require the employer to pay a significant percentage of the premium for employee only, sometimes 100 percent of the cost. So the concept that the employer is only going to pay for the coverage based on the 9-½ percent rule is not the case. Not for small employers and not for large employers. The employers are paying significantly more, especially because of the fact that they cannot know household income. The discrimination rules, which have yet to be issued, are a continuing concern. Just for information, the senior counsel for the Treasury Department indicated to me that they cannot enforce those rules. That is what we have experienced in actual practice. Even when there is an audit, they ask to see the testing, check it off their list, and they are done with the issue. They cannot enforce the current rules for self-funded plans. It would be extremely difficult for them to do so for small insured plans and very difficult for the employers to be able to coordinate a nondiscriminatory program across various companies in different industries in different states quite commonly. Automatic enrollment, if the group should happen to be above 200, will be another serious issue whenever that rule does eventually take effect.

And then finally, MIWA issues. Commonly held, commonly controlled groups for federal tax purposes may not be sufficiently related for either carrier purposes. They may not issue the policy. Or the states may consider those groups to be an illegal MIWA under state law, even though it is not being formed as a self-funded plan to do anything to avoid state rules. And it would require licensing as an insurance carrier for those groups if they would try to self-fund, and then also capitalization as a carrier and regulation as a carrier. So very onerous.

Just in summary, I think there are many issues that are affecting the smaller employer's awareness, complexity of the rules certainly, but I think the issue is around confusion and the fear of the smaller employers as to what impacts they will feel from the law and what they should do now with the uncertainty without regulations. Thank you.

Mr. COLLINS. Thank you, Ms. Bogardus.

Our next witness is Ellis Winstanley. He is the chief executive officer of Trade Logic Corporation in Austin, Texas. With several of his family members, Mr. Winstanley owns a number of businesses, including restaurants, a catering company, a software company, and a promotional products company. Welcome.

#### **STATEMENT OF ELLIS WINSTANLEY**

Mr. WINSTANLEY. Chairman Collins, Ranking Member Velázquez, and members of the House Committee on Small Business. Thank you for the opportunity to testify today on the effects of the business aggregation rules included in the healthcare law on small businesses like ours.

My name is Ellis Winstanley. I am the CEO of Tradelogic Corporation. I own a variety of small businesses in Austin, Texas, with my twin brother, parents, and other partners. I am honored to share the perspective of our companies, especially our restaurants, on behalf of the National Restaurant Association, the leading trade organization for the restaurant and food service industry.

I am a business executive with a successful track record of starting up, turning around, and growing businesses in the hospitality, construction, software, printing and promotional products, and apparel industries. My brother and I are entrepreneurs who got started in business while we were students at the University of Texas. We are known for rescuing local historic restaurant brands and turning them around to maintain their place in the community as contributors and job creators.

Currently, we own eight restaurants with our partners, which I oversee on a day-to-day basis. We also partner with our parents in two construction and three printing and promotional products small businesses. In addition, we own software development companies, one of which is Trade Logic Corporation, which also serves as our management company.

The healthcare law presents compliance challenges for all of our small businesses, but particularly for the restaurant and foodservice operations due to the unique characteristics of our workforce. It is difficult for many restaurants, especially small businesses, to determine how the law impacts us and what we must do to comply. The employer aggregation rules present a significant complication to our business. It may seem like a simple thing to do, but due to the aggregation rules and the structure of many restaurant companies, determining the employer is more complicated than many may expect. Austin, Texas, like many other cities around the country, has a rapidly developing restaurant community, and we, like most of the operators we know, participate in multiple restaurant entities with various partners, often with family members. Though we consider each operation to be a small business, many of us are discovering that for the purpose of the healthcare law, all of the businesses must be considered one employer due to the aggregation rule. This threatens to stunt the development of restaurants in our community.

The application of these aggregation rules is already having an impact on small businesses, consuming valuable time and resources as businesses attempt to decipher the law's effect on them. Most of our small businesses each have less than 50 full-time

equivalent employees and independently would not be considered applicable large employers. Two are highly seasonable businesses and may not be considered large depending on the calendar month and uncontrollable factors, such as whether or not our legislature is in session, the performance of UT sports and the academic calendars related to the surrounding universities.

Based on my understanding of the aggregation rules, I believe we will be considered as one employer under the law, thus an applicable large employer. The effect of this is that the cost of doing business for each of our companies will go up. Restaurants operate on thin margins already forcing operators to manage labor costs very closely to remain viable. Austin, Texas remains one of the strongest economies in the country, but since the recession we have regularly tightened our belts to manage rising costs, and we are very much still feeling the impact, including double-digit health insurance premium increases even since the law was passed. This puts pressure on our team, our vendors, our pricing, and in the end, our customers. I see the cost associated with the way the healthcare law has been implemented as adding significantly to that pressure. In addition to the aggregation rules, there are several other sections of the law that impact restaurant operations and similar small businesses.

While the increasing cost of offering coverage remains a major concern, I am also very concerned about the administrative demands that compliance with this law will impose on our businesses. The restaurant and food service industry attracts people seeking a flexible work environment, whether they are students, between careers, or just looking for a second job to make ends meet. There is significant movement in and out of the industry and between employers.

Given the short-term nature of individual employment, the administrative burden of educating and processing enrollments and declinations could prove almost as expensive as the coverage itself. Restaurants cannot absorb this cost and ultimately the cost will be borne by the public as a whole. The implementation also threatens the safe haven of the flexible work environment for those who depend on it.

Thank you again for the opportunity to testify before you today regarding the healthcare law and its effects of the business aggregation rules on small businesses like ours. I am both proud and grateful for the responsibility of serving my community in Austin, Texas, creating jobs, boosting the economy, and serving our customers. We are committed to working with Congress to find solutions that foster growth and truly benefit the communities we serve.

Mr. COLLINS. Thank you, Mr. Winstanley.

Our final witness is Donna Baker. Ms. Baker is a certified public accountant in Adrian, Michigan. She holds an MBA from Michigan State University and a B.A. in accounting from Siena Heights University. Welcome.

**STATEMENT OF DONNA BAKER**

Ms. BAKER. Thank you, Chairman Collins, and Ranking Member Velázquez, and members of the Committee. It is really an honor to be here to testify on this subject.

I am Donna Baker, CPA. I have been a CPA for 25 years and I have owned my own accounting firm for the last 13 years. I live and practice in Lenawee County, Michigan, which is a very small, rural area. On top of owning my own CPA firm, I also own a small payroll company. I have invested in a retail store, and my husband Kim, who is also with me here today, is a partner in a family dairy farm.

As you have already heard, the business aggregation rules require any group of companies under common control to be treated as a single employer. The primary key in determining which companies should be combined is either direct or attributed ownership or affiliated service but not operational control. These rules may cause unrelated businesses held by family members or trusts to be aggregated. Companies within a control group do not need to have the same management or even be in the same industry. Also, the business aggregation rules are very complicated, as you have heard, and are rarely applicable to small businesses. Therefore, they are unfamiliar to both small businesses and small business advisors. I have had many webinars and training on the ACA rules, and most of the materials will mention that the controlled group rules apply but do not cover the specifics of these rules. And unfortunately, I think many business advisors that deal with just primarily small businesses assume that controlled groups means hands-on control instead of the actual emphasis of director-attributed ownership.

I have two examples of applying these control groups to two businesses. One is my own personal business. Like I said, I own 100 percent of a very small CPA firm that I also manage, along with a payroll company that I manage. And I have invested in the retail store. However, that is an investment. I do not manage that or operate that on a day-to-day basis. And then, of course, my husband's farm. He is a partner with his brother in the dairy farm. I have no management responsibilities. I do not make decisions for that company, but my name is on some of the land and I do provide some bookkeeping services. So based on the business aggregation rules, we would have to combine all four of those entities. We are not quite close to 50 employees yet but close, and the payroll company is new and very quickly growing.

My second example is one of my clients. I have an elderly woman that owns 100 percent of two local restaurants, and her son manages and controls all of the business decisions in those two restaurants. She recently provided the capital for a nephew to open a restaurant in Florida in which the restaurant in Florida, the nephew manages and makes all the business decisions for that restaurant. Under the current business aggregation rules, those three entities would be combined and they would exceed the 50 full-time equivalents and require them to provide the minimum essential health insurance benefits.

So those two examples illustrate how the control group rules will aggregate businesses that are not directly owned by the same per-

son, they do not have the same management, are not in the same industry, and may not even be in the same state.

Therefore, the implications of requiring small businesses to use these aggregation rules could create several negative effects. It could hinder growth and discourage owners from hiring new employees. It can create that environment where the owners try to manipulate their ownership percentages or minimize their employees and keep them within the 30 hours. It could discourage small business owners from investing in other businesses, and it could require them to provide health insurance benefits in industries where it is not typically the norm, and the additional cost could create it difficult for them to compete in those industries.

Lastly, I would like to mention the increased cost of my own plan. I do provide basic health insurance for the people in my accounting firm and my payroll company. This policy has been canceled, and the closest policy, I have been quoted a 40 to 44 percent increase that would have reduced benefits. It would have higher copays and higher maximum out-of-pocket expenses. So these increased costs would be very difficult to absorb. Thank you.

Mr. COLLINS. Thank you very much, Ms. Baker.

We will now enter a questioning period, and I guess I would like to start by just stating the obvious. Hearings like the one that we are having today give us all an opportunity to obtain testimony on the record that will highlight the consequences, intended and unintended, of various laws and regulations. And it is very helpful then, as Ms. Velázquez said, as we move down the road and we look at potential changes that we need. And again, to state the obvious, we all need and want more jobs in the economy. The economy is kind of languishing today and more jobs is what everything is about, getting the unemployment down and increasing payroll across the country to drive the economy.

Ms. VELAZQUEZ. Will you yield?

Mr. COLLINS. Certainly.

Ms. VELAZQUEZ. So I will join you in supporting legislation that—passing the jobs bill. What we need is to pass legislation to create jobs and we are just waiting for the leadership to do so.

Mr. COLLINS. I can appreciate that. It is jobs. We may disagree though on what stimulates jobs. I know, myself, I believe in lower taxes, less regulation, less government interference, and certainly, we will have some other questions today to indicate the impact of the ACA.

What I heard today though, and again, I am a small business guy. We have the mantra “grow or die.” And if you are not growing, you are not doing what you should do as an entrepreneur. But growth requires capital. Accounts receivable, inventory, et cetera, et cetera. And any and all dollars wasted on regulatory burdens, such as the business aggregation rule and hiring a tax expert is, in fact, a dollar that is not available to invest in growth.

So I guess briefly, we have a lot of members to ask questions, but just to reconfirm, I think I heard it in your testimony, but I would like to go down the line starting with Ms. Walker and just ask you if you think this business aggregation rule is, as it is currently written, would have a negative impact on jobs and the econ-

omy hindering job creation and economic growth and therefore should be altered.

Ms. WALKER. I think anytime that you have a bright-line test it is going to hinder people that do not want to cross the bright-line test. And that, in this case, is going to hinder hiring, hinder expansion, and the “grow or die,” they are just going to choose to stop growth and perhaps move over to other forms of business, other ownership. So yes.

Mr. COLLINS. Thank you.

Ms. Bogardus.

Ms. BOGARDUS. Yes, Mr. Chairman, the provisions definitely do hinder job growth, and they hinder strong job growth. And by that I mean that the jobs that could be created in the future would instead be part-time jobs. That is, of course, advisers on this topic have their own bag of tricks and it is definitely possible to stay outside of compliance with respect to each individual employee if you can keep that individual in a part-time position. Full-time jobs are absolutely necessary. You cannot serve two masters. It is hard to have coordination just on the part of the employee, much less between two separate employers. So strong job growth is necessary. And of course, there are other issues involved as well but I agree that the funds that are spent to analyze the issue and then also to comply are extremely high, and it is not just the initial cost. It is the participation every single year in the premium payment.

Mr. COLLINS. Thank you.

Mr. Winstanley.

Mr. WINSTANLEY. Yes. I think what we are seeing now is less people have insurance than have had insurance. We are seeing the reverse effect of what we were hoping to achieve here. And I think we have also, in the restaurant industry specifically, you hear a lot of talk about people getting pushed below 30 hours a week, and that being the reaction, you see that being tried around the country, and I think that is extremely negative for the industry. I think that is negative for the employees. I think long term, while some groups I think feel that that is their only option, but I think in the long run that is not healthy for our economy.

Mr. COLLINS. Thank you.

Ms. Baker.

Ms. BAKER. Yes, I do. As in the testimony, I think there is a lot of concern with that. But I am also concerned with those that have the true entrepreneurial spirit to be discouraged from investing in more small businesses and expanding in other areas. That would definitely hinder.

Mr. COLLINS. One more quick question and then I will yield to Ms. Velázquez.

Kind of a yes/no. You know, we are focused today on the complex business aggregation rules but we are talking about other issues, and certainly, Mr. Winstanley has talked about the impact and the employees getting their hours cut and the like to get them under the 30-hour rule. So, as we look and try to message some changes that could be made, I would first like to ask each of you if you think in your opinion the 30-hour definition of full-time should be increased back to 40 hours.

Ms. Walker.

Ms. WALKER. Yes. It will prevent the people from ratcheting down workers to 30 hours and leave them at 40.

Mr. COLLINS. Yeah.

Ms. Bogardus.

Ms. BOGARDUS. Yes.

Mr. COLLINS. Okay.

Mr. Winstanley.

Mr. WINSTANLEY. Yes, I do.

Mr. COLLINS. Ms. Baker.

Ms. BAKER. Yes. Absolutely.

Mr. COLLINS. Very succinct.

Now, the other question, we talk a lot about the 50 employee threshold, and there are a lot of companies in that 40-plus, going to 50, wanting to go to 75, and under Obamacare, this arbitrary selection of 50 now defining a large corporation, does not fit with the entrepreneurial spirit. So in the same, what do you think, yes or no, do you think we should increase beyond 50 the number of FTEs that would trigger the Affordable Care Act? I do not know if it is 100 or 150, but do you believe that 50 is too low and stifles job creation and therefore, we as Congress should increase it to a number higher than 50?

Ms. WALKER. I think the bright-line test of a certain number of people is the wrong test. You need a facts and circumstances test on who has day-to-day control. If you increase it to 50, then the same thing that happens at 50 will happen beyond 50, whether it is 75, 150, 200, or 500.

Mr. COLLINS. Yeah.

Ms. Bogardus.

Ms. BOGARDUS. As with the 30-hour rule, I would agree that increasing the number above 50 would alleviate a number of the issues. But as with the 30-hour rule, it is a legislative fix. There would have to be the change to the statute itself.

Mr. COLLINS. Right.

Mr. Winstanley.

Mr. WINSTANLEY. I think that the challenge comes in that every industry cannot be put in the same box. I think in the evaluation of really any organization that tries to encapsulate multiple industries, there is always different criteria for different industries, and I think looking at an industry with a somewhat mobile workforce or by general definition, a short-term workforce, I think the costs are going to be significantly higher for the same number of employees, the same number of FTEs than it would be with a longer term workforce. So yes, I think it should be higher, but I do not think it can be the same number for every industry.

Mr. COLLINS. Okay. Thank you.

Ms. Baker.

Ms. BAKER. Yes. I think that would definitely help, but then I, you know, support what has previously been said. A facts and circumstance would make a whole lot more sense when it comes to defining control. And then when you do have something that crosses different industries, it is adding additional complications.

Mr. COLLINS. Thank you all. I will yield to Ranking Member Velázquez.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman.

I would like to call the attention of committee members to the hearing that we conducted on October 9th, "The Effect of the Law and Definition of Full-Time Employee on Small Businesses." And one of the expert witnesses was Dean Baker, the executive director for the Center for Economic and Policy Research, who analyzed data right after we passed the Affordable Care Act and where small businesses were expecting the employer mandate to go into effect. Since then, he did not find any data that showed small businesses were not hiring employees or increasing the 30 hours because the Affordable Care Act going into effect and when people were expecting the employer mandate to go into effect. The Federal Reserve from San Francisco conducted research demonstrating that it has not had any effect. But like any law, we will continue to monitor it and make the fixes that are necessary.

My question to the panel of witnesses, the business aggregation rules are meant to prevent skirting the law. In your opinion, what is the correct balance between preventing abuses and protecting closely-held businesses from potential penalties?

Ms. Walker.

Ms. WALKER. I think anytime that you have a bright-line test, you are going to end up with abuses because people will walk right up to that bright line and not cross it. So what you have to do is come back and put it into a facts and circumstances test where you apply judgment, I apply judgment, the IRS applies judgment, and each person decides based on the facts and circumstances in that situation whether there should be an aggregation, whether it truly operates as an employer.

Ms. VELAZQUEZ. So do you consider that a final regulation should incorporate a fact and circumstances test?

Ms. WALKER. Yes. That would be a statutory change, however.

Ms. VELAZQUEZ. Ms. Bogardus.

Ms. BOGARDUS. I agree with Ms. Walker that the facts and circumstances test is a much better standard, again, requiring a legislative change.

Ms. VELAZQUEZ. And that will create more jobs?

Ms. BOGARDUS. I think it would, and I think also serious consideration should be given to changing the threshold from 50 to perhaps 250 and look at it on an industry basis instead, or perhaps blend the two. There are some precedents for using 250, such as the W-2 payroll reporting rule.

Ms. VELAZQUEZ. Mr. Winstanley.

Mr. WINSTANLEY. Sure. I think when you look at the original context that the control group provision was put together per the IRS, it was put out there to stimulate the use of corporations and companies growing, and I think the way it is being implemented now is having the alternate effect. I think what businesses need is clarity around what the rules are they need some rules that they can reasonably work with based on the industry they are in. And then I think that job growth will loosen up.

Ms. VELAZQUEZ. Thank you.

Ms. Baker, I would like to ask you another question.

When it comes to contracting programs in the federal government, or maybe Ms. Bogardus, you may be willing to answer this question, a business must meet not only ownership by holding a

majority of shares, but also demonstrate active control over business operation and you described that in your testimony. Yet, for purposes of the ACA and business aggregation rules, only common ownership is considered. Which standard, in your opinion, is a better indicator of ownership?

Ms. Baker.

Ms. BAKER. I am not sure if I really got that but to me it would be control over the entity, the day-to-day operations, the decision-making, not just investment. So the day-to-day operations, which supports the facts and circumstance that they have been discussing here.

Ms. VELÁZQUEZ. Ms. Bogardus.

Ms. BOGARDUS. I would agree. Actual control and the facts and circumstances of the day-to-day operations, which is also necessary, absolutely necessary for compliance. And as I said before, the small businesses do not have centralized systems, payroll, HR.

Ms. VELAZQUEZ. Thank you. I would like to ask other questions but I know that all the members would like to ask their questions as well.

Mr. COLLINS. Thank you.

At this point I would like to yield five minutes to Representative Tipton.

Mr. TIPTON. Thank you, Mr. Chairman. I think I would like to start out with Mr. Winstanley. When you are talking about the variety of businesses you have, do you file separate tax returns?

Mr. WINSTANLEY. Yes. They all file separate tax returns.

Mr. TIPTON. Are you allowed, if you have a loss on your small software business versus your restaurant, can you write that loss off against your restaurant?

Mr. WINSTANLEY. No, they are separate.

Mr. TIPTON. What happened to business aggregation?

Mr. WINSTANLEY. Right. There is a significant administrative burden that goes into running the multiple entities separately and there is value to doing so.

Mr. TIPTON. So effectively what we are seeing through this administration is a policy to be able to force you to be able to provide the healthcare. Has that impacted your ability to be able to create jobs?

Mr. WINSTANLEY. Yes.

Mr. TIPTON. You are living in the real world.

You know, we just heard comment that there is no data. I will quote that, again, that there is no data that small businesses are not hiring as a result of the implementation of the president's Affordable Healthcare Act, no effect on job hiring. Is that your experience?

Mr. WINSTANLEY. No, it is not.

Mr. TIPTON. Anyone else care to comment?

Ms. WALKER. No, it is not. I see it in small businesses and large businesses.

Mr. TIPTON. The businesses are not hiring because of the Affordable Care Act?

Mr. WINSTANLEY. I believe it is draining resources from the companies that would otherwise be going to be used to grow the businesses.

Mr. TIPTON. Very interesting, because we are dealing with theoretical data. We are dealing with real life experiences. I appreciate that testimony.

I come from rural Colorado. I am a small business guy. Do you have any experience—and perhaps the CPA on the panel can address this the best—are you seeing insurance cost differences between businesses in rural areas versus urban areas? And what I can speak to is in the state of Colorado, if you punch in a rural zip code for your healthcare insurance, you are paying a 65 percent premium compared to people that are living in urban Colorado. Are you seeing those same sorts of circumstances.

Ms. WALKER. I am sorry. I am going to have to pass that to the insurance person.

Ms. BOGARDUS. That is happening and it does happen because there is less competition. There are fewer facilities in the rural areas, and they can charge what they want to charge because that is the only hospital, the only emergency room in some cases.

Mr. TIPTON. Since you have a little bit of experience with this, is it a little more typical in these rural areas to see a lower income than we do in urban America?

Ms. BOGARDUS. It is? You know, we hear a lot of talk here in Washington coming out of this administration about income inequality, but I am just hearing testimony that the administration, through its policies, are forcing you to cut the incomes of people by reducing their hours. We are hearing that people that live now in rural America, who earn less, are going to be paying more for what is now law that you must obey and buy insurance. Is that correct?

Ms. WALKER. The simple answer is yes.

Mr. TIPTON. The simple answer is yes. So effectively, what we are seeing is a system that is not affordable and we can certainly get into the accessibility issues as well.

But going back to the aggregation rules we are specifically trying to address on this, can anyone on the panel give me, small business guy, I just want to be able to produce my product, to be able to sell, to be able to provide for my family. Can you give me two sentences to be able to define the aggregation rule? Can anyone?

Ms. BOGARDUS. A parent subsidiary group where you own 80 percent of a chain of corporations, a brother-sister corporation where the same five or fewer own 50 percent and in conjunction 80 percent, and then the affiliated service group rules. Those rules do not necessarily have ownership, but if I provide management services to another business, that will be aggregated.

Mr. TIPTON. As a small business guy to have to tell you, you are a CPA, that is about as clear as mud to me to really be able to understand that.

We have had abundant testimony on this Committee that rules and regulations—and this is another one that we are talking about today—are killing jobs in America, killing job-hiring prospects in America today when we need to be able to hire people. How much more is this going to cost small businesses, like Mr. Winstanley's, who are working on a narrow profit margin, just to be able to comply with another government mandate. Any idea?

Ms. BOGARDUS. Any time you look at these rules in a situation as complicated as his with different ownership, you are going to

have to sit down with a chart. When he transfers ownership to ownership, to other people, you are going to have to go through the chart. You are going to have to ask him who does the management for his different businesses. Does the software company, in fact, do some payroll for the restaurants, those types of questions, and then you are going to put it all together. Once you reach 50 people, he will have to comply with the rules and then he knows which companies in that pot he has to provide minimum essential coverage to the workers for.

Mr. TIPTON. A lot of money.

Thank you, Mr. Chairman. I yield back.

Mr. COLLINS. Thank you.

At this point, I would like to yield five minutes to Representative Meng.

Ms. MENG. Thank you, Mr. Chair. Thank you, Ranking Member Velázquez.

I had a question. I think it was Mr. Winstanley who testified, if I heard correctly, that you believe that fewer people have health insurance now.

Mr. WINSTANLEY. I believe that fewer people are accepting health insurance now that it is available to them.

Ms. MENG. I am just curious. I know that there are a lot of good employers out there, like you, Ms. Baker, who have always provided health insurance to your employees. I represent a district in Queens, New York City, where a lot of employers have not always done the right thing, like you, Ms. Baker, and have not provided health insurance to their employees and have taken advantage of many employees around the country who do not speak English and are not familiar with rules. Statistics have shown that on Sunday and Monday alone, 29,000 people signed up for the new healthcare law just on the website in two days and I was just wondering what advice could you have given or would you give to a lot of these employees or small business employers who have not provided insurance in the past? And anyone can answer.

Mr. WINSTANLEY. Sure. We like to consider ourselves a good employer and we have provided insurance in the past. The nature of it is that the cost of insurance has risen drastically in the last few years and most of the young people who are healthy simply drop off the plan, which makes the cost go up even more. And so we have got a situation where people are not willing to pay for the insurance, despite the fact that we are continuing to increase our contribution. And it has become a situation where I have got to believe—I only know from my own experiences what we are dealing with, but I have got to believe that there are a lot of other small businesses around the country that have experienced the exact same thing. And I think if you multiply all those that the net loss is significant.

Ms. VELÁZQUEZ. Would the gentle lady yield?

I would like to relate the fact that in Massachusetts, when they passed the law and implemented it, the targeted young people were not signing up, and then later on they enrolled. So we believe that that type of trend that we saw in Massachusetts will be seen throughout the country.

Ms. BAKER. Can I answer yours?

Okay. So for my own personal situation, I am in one of the rural areas with very high health insurance and lower income. Our county has about 99,000 as a population with an average household income of middle 40,000s. So as I struggle to provide more health insurance and they aggregate the businesses to make it—if I can stay under that 50 I will—I mean, it will be extremely expensive for me. And in the meantime, to absorb a 40 to 44 percent health insurance increase, it would be much easier for me to put my employees out on the exchange. It is a lot cheaper for them to provide that than for me to absorb that additional cost within my small profit margins anyway. Thank you.

Ms. BOGARDUS. I would just comment that if the additional cost of adding each employee would be approximately \$4,000 to provide insurance to that individual at an affordable rate—it may be a smaller figure in some places, higher in others—that does stunt the job growth. I will say that the law itself is having an impact on the cost, and we are seeing people not enroll in the coverage that maybe in the past they would have enrolled in because the costs are just higher. And we do see, and traditionally have seen, young individuals not enroll in the coverage, even if it costs them \$20 a pay period. And it is a matter of individual choice. They are looking at the coverage and they are saying I would rather have the money. And in the bigger picture, in the context of wages, if people would rather have the money, the Affordable Care Act takes that off the table if they have to be offered the insurance.

Mr. COLLINS. We would like to yield five minutes to Representative Luetkemeyer.

Mr. LUETKEMEYER. Thank you, Mr. Chairman.

One of the things that I think we are seeing and you have discussed today is the problem with companies trying to deal with this. I know there was an economist in Committee here recently and they had done a small business survey, and 76 percent of the businesses that were surveyed said they were not going to hire in the next six months.

Ms. Walker, you have mentioned in your testimony here something like not hiring workers or limiting working hours. Have you seen this already with your practice that businesses are starting to limit their hours, and can you give me an idea of the number of businesses you are talking about?

Ms. WALKER. What I have seen is that businesses tend to hire new workers at less than 30 hours. So when we have to expand, we are going to expand on a part-time basis.

One of the other things I saw in a statistic yesterday for a slide presentation, if you go back two years, there were six full-time workers hired for every one part-time worker. That has flipped now and such that it is one full-time worker is hired for every four part-time workers, and those are DOL statistics.

Mr. LUETKEMEYER. Thank you for that.

Ms. Bogardus, in your comments a while ago you said that—if I got this right, correct me if I am wrong here—you made the comment that your company does not write some groups because they may not be a related business. So in other words, you are not sure if they would fall under this rule or not, so as a result you back away from doing it. Did I understand that correctly?

Ms. BOGARDUS. Actually, we are an insurance consulting and brokerage firm, so we see the insurance carriers doing that and refusing to write certain groups. And some of it may be the confusion among the carriers, but they are still exercising their leeway when they can to refuse to write a policy.

Mr. LUETKEMEYER. So even though they may technically, if they did the research and they dotted their I's and crossed their T's, may actually qualify, just the unintended consequence, just the concern about they may be in noncompliance is enough to back them away from that. Is that what you are saying?

Ms. BOGARDUS. That is correct. It may be a smaller entity, a smaller subsidiary in one state without the headquarters location, and so it could not be the location or site as for the insurance contract as a whole and they back away from it.

Mr. LUETKEMEYER. Now, you work with this every day. Are all the rules promulgated on the president's healthcare law?

Ms. BOGARDUS. No, sir. They are not. The rules we have currently on the very important issues of play or pay, the employer mandate, were issued in early January last year. We have a lack of final guidance, a lack of guidance on very industry- and employee-specific issues. There are impacts and unintended consequences of the rules that have already been issued that need to be fixed and resolved, and we do not know basic information, such as whether we will get transition relief for particular situations, such as counting the employees for purposes of 2015. We are less than a month away from the calendar year that is most at issue, 2014, starting January 1st, and an employer needs to know. So we are lacking guidance. We are kind of operating in an area of this is what we know today which is the case.

Mr. LUETKEMEYER. How can you help that company plan with the uncertainty that just sort of hangs over them with regards to the rules are not promulgated yet, as well as do not know the unintended consequences of what may or may not happen here?

Ms. BOGARDUS. We like to address that with a three- to five-year strategy and we always have a plan B. If they change the rules in this manner, then we will go this direction. But we advise, we do have some small business clients, but we advise many, many large employers. And I know that not every small employer has access to advisors with the level of sophistication that we would bring.

Mr. LUETKEMEYER. Mr. Winstanley, thank you for being here today. It is always great to have someone who deals with this on a daily basis. Ms. Baker, you as well, because you give us the real-life experience of how the consequences and unintended consequences of stuff that goes on here in Washington affects real people in the real world.

How much time and how much money do you spend on compliance with this healthcare law?

Mr. Winstanley.

Mr. WINSTANLEY. It has been a very significant distraction from our business over the last couple of years, especially as we try to ascertain where it is going to go and where things are going to land. Some of the folks that help with our administrative stuff,

they spend a lot of time. I have spent a lot of time on it. It takes a lot of our energy.

Mr. LUETKEMEYER. Ms. Baker.

Ms. BAKER. I have been flooded with questions and phone calls over the last year with my clients. There is a lot of confusion, wondering if they have to start providing the health insurance, when would it be mandated, what do they have to do. So I guess I have not tracked the time specifically, but it has definitely been a burden on my practice to try to answer all the questions that are out there.

Mr. LUETKEMEYER. And that cost and all those man-hours are all borne by your business and therefore, that is not making you any money?

Ms. BAKER. Absolutely.

Mr. LUETKEMEYER. Thank you very much for your testimony.

Mr. COLLINS. Although they have called votes, we do have time for another question or two, so at this point I will yield five minutes to Representative Hahn.

Ms. HAHN. Thank you, Mr. Chairman, Ranking Member Velázquez, for holding this hearing.

It would be nice to hold these hearings with the thought that if we did hear some unintended consequences that impact our small business that we had the belief that our friends on the other side would actually like to work on fixing some of these problems. I get frustrated in these hearings because I know the main purposes is just to have more bad stuff to talk about and to attack the Affordable Care Act. I would love for this Committee to actually work on some fixes, and I think we even heard some offers of compromises that might make it better. But I will tell you, you know, that is not going to happen. We do not have partners on the other side that actually want to look at this law, how it does impact your businesses, and take any time or effort to fix it. We are more than willing to work with our friends on the other side to fix things that maybe nobody thought about or that do have unintended consequences because being members of the Small Business Committee, we love our small businesses. We are for our small businesses. This is one of the Committees that I enjoy when I go back home to my district in Los Angeles, is talking to my small businesses and finding out what we can do here to help them out. So it is frustrating to know that there is no intention on the other side. All the testimony you give, nobody is willing to work with us to try to fix this law.

Having said that, I will ask this to Ms. Bogardus. So these business aggregation rules already apply to many aspects of business law, like ERISA and COBRA. So I know some of these small businesses found it a surprise possibly that it also included their compliance as it related to the Affordable Care Act. So maybe you can explain to us why it came as a surprise when these aggregation rules already existed and small businesses were in compliance in other areas, and maybe there are some small businesses that are having to come in contact or in compliance with these aggregation laws for the first time, and let us know why it was a surprise.

And maybe, two, what kinds of small businesses are experiencing this for the first time; what kinds of businesses that may be never had to comply with this law before even in other areas?

Ms. WALKER. Yes, Representative Hahn, thank you.

The answer to that is that while these rules have been in effect for quite some time—they affect ERISA, COBRA, Medicare secondary to a number of technical issues, including retirement plans—if a business has not offered a retirement plan and has not offered a health plan, then the analysis simply has not been done. Even if the small businesses offered a health plan, again, there has not been the analysis. The insurance carrier says, “How many employees do you have?” The small business owner answers for the group that he is covering. There is not an analysis. No one has the ability, time, or authority to sit down from the insurance carrier and work with that employer to determine its size in particular over the entire control group. And that is just simply not done. The carrier has no obligation or consideration for whether the rest of the control group is addressed or not. So it does come as quite a surprise. I think the difference is this is a mandate whereas it is providing health insurance. I can provide health insurance to just some of my workers and not others. So it has all been voluntary before.

Ms. VELÁZQUEZ. Will you yield?

Ms. HAHN. Yes.

Ms. VELAZQUEZ. And what criteria will you use to decide which workers will get health insurance? Is it driven by job retention?

Ms. WALKER. It is often driven by the industry.

Ms. VELAZQUEZ. Okay.

Ms. WALKER. It is, you know, different industries have different types of retirement plans, different types of health benefits.

Ms. VELAZQUEZ. But when people say more companies will be dropping their plans, the health care plans, I do not know what facts or empirical data or research will drive anyone to conclude that, in fact, companies will drop health insurance because when we hold hearings, one of the biggest issues that companies and small business bring to us is to find skilled workers. And I am sure that in order to retain those skilled workers, if you provide health care as one of the package job offers, then they will be more than willing to come to your company.

Thank you.

Ms. HAHN. Thank you. Before I yield back no balance of my time, I just want to throw out one more statistic today. The ADP National Employment Report, which measures private employment, says small businesses led the way in job creation with 102,000 jobs this November.

Ms. VELAZQUEZ. Two hundred fifteen thousand.

Ms. HAHN. Thank you.

Mr. COLLINS. There are never enough jobs, so I would like more jobs.

We will cut it down to the wire, but Mr. Schweikert, you are good to go.

Mr. SCHWEIKERT. Thank you, Mr. Chairman. And having just looked at those employment statistics, considering we need to be

around 300–350,000 creation every month, we are still devastated upside down when you look at our workforce participation.

Ms. VELAZQUEZ. Gentleman yield?

Mr. SCHWEIKERT. No.

Our workforce participation numbers. Because we are up against the clock, I am sure the Chairman will hand you some time when we are done.

Is it Bogardus? Am I even close?

Ms. BOGARDUS. Bogardus.

Mr. SCHWEIKERT. Just because I have heard some discussion—you have already explained it twice—I want to ask you to do it again the third time. On the aggregation rules, how different these aggregation rules are in regards to what you are seeing in the new healthcare law compared to what we have done in the past in pension and tax and mechanics. Can you sort of help explain some of the mechanics and how they are different?

Ms. BOGARDUS. I may yield part of this question to Ms. Walker as to some of the technical issues.

The mechanics are different simply because employers have not done this in the past unless they have offered the retirement plan, and in many cases, if they are operating under a safe harbor they may not have done all of the analysis or they have been able to pull out certain business classification units.

In terms of what we are seeing in actual real life, I know there has been discussion of jobs creation and whether employers are hiring or not hiring. I would caution you on the statistics that you hear and answers to surveys because I know that many of our clients will not answer that question because they have seen the fall-out in the industry, whether it is restaurants or other industries from answering and addressing questions like that, so I do not believe that you are getting a complete picture.

Mr. SCHWEIKERT. Mr. Chairman, one day that might be a complete different hearing because we had that happen once in Arizona where some voluntary surveys that were filled out turned out to being, you know, waking up and being audited the next day.

Ms. Baker, now with your background in the CPA world, or I could always turn back to our lawyer friend, let us deal with the reality of businesses trying to survive. We had a hearing yesterday about what many of the small banks are having to do to survive. Have you started to have clients with smart lawyers coming to you saying how do we have to now gain the system? Do we have to put this in a trust? Do we have to hide this, hide that? You do not have to throw anyone under the bus, but have those conversations begun?

Ms. BAKER. I think most of the businesses that I deal with, that is the first question they ask me is what do I do to avoid this.

Mr. SCHWEIKERT. So in other words, one more time as our regulatory command and control society grows out of Washington, we are going to turn a lot of our friends out their businesses into trying to find a way to game the law in many ways just to survive.

Ms. BAKER. Of course I advise them not to. But that is their first reaction, is what do I have to do to avoid this?

Mr. SCHWEIKERT. Is it Mr. Winstanley?

Mr. WINSTANLEY. Yes.

Mr. SCHWEIKERT. Now, you have actually, if I remember your testimony, some of which you wrote, you have actually reached out and invested some of your capital to start other businesses, and yet that may be now pulling you into the business aggregation. Does this become sort of a chilling effect on you helping capitalize new economic growth around you? And have you actually been approached on how to game the system?

Mr. WINSTANLEY. It is one more variable to take into account every time we do something. About gaming the system, there is always how do you figure? Where do we stand on this? How are we set up so that it is applicable, so it is not applicable? One, we have to figure it out, which is taking considerable resources and we think we understand it, but, you know, I think the issue is in the distraction from the business.

Mr. SCHWEIKERT. Mr. Chairman, just because we are down to that about three and a half minutes, we actually sort of heard a lot of this in yesterday's hearing where how do the small banks help economic growth, create jobs, take care of a lot of our brothers and sisters out there, and the arrogance that we as policymakers keep dumping onto our country and our job creators. At some point we have got to wake up and decide this is not a partisan; it actually should be about the people we represent and not the vanity here of trying to justify things that we have done that do not work.

And Mr. Chairman, with that I yield back.

Mr. COLLINS. Thank you. At this point in time we do have votes, as you can see. So we will adjourn for, I would say, give or take, 30 minutes, after which we will reconvene. So for right now we will be adjourned.

[Recess]

Mr. COLLINS. Mr. Bentivolio.

Mr. BENTIVOLIO. Thank you, Mr. Chairman.

Ms. Walker. And thank you, all of you, by the way, for coming in today and testifying.

Ms. Walker, in your practice, you advise small employers; correct?

Ms. WALKER. Yes.

Mr. BENTIVOLIO. Have you found that their situations present difficult issues under the rule, such as complicated family business arrangements, overlapping shareholders? Would you discuss some of these situations, please?

Ms. BAKER. Are you referring to me?

Mr. BENTIVOLIO. Oh, I am sorry. Walker. Right. Ms. Walker.

Ms. WALKER. I think one of the best examples is the one that Donna used. And that was an elderly woman who had invested in two restaurants. She invested in a restaurant for her son in one state and a restaurant for her nephew in another state and that required aggregation rules.

The other situation was a family business where they were making investments and one of the investments was a golf course. The golf course was not in the same area and those two businesses then had to be aggregated.

Ms. VELAZQUEZ. Mr. Chairman, we need to have the clerk here.

Mr. COLLINS. Are we missing someone?

Thank you, Ms. Velázquez. I guess we will pause momentarily. Oh, okay. We can continue. Go ahead.

Mr. BENTIVOLIO. Am I still on my time?

Mr. COLLINS. Yes.

Mr. BENTIVOLIO. Thank you.

Is it Mr. Winstanley?

Mr. WINSTANLEY. Yes, sir. Winstanley.

Mr. BENTIVOLIO. Thank you.

Do you have a tax specialist on your staff?

Mr. WINSTANLEY. No, not on our staff.

Mr. BENTIVOLIO. So who would you consult for guidance on the business aggregation rules?

Mr. WINSTANLEY. We would hire outside counsel for that. We have attempted to read them ourselves but we will have to hire somebody outside.

Mr. BENTIVOLIO. And how much is it to hire somebody?

Mr. WINSTANLEY. It ranges but it is expensive.

Mr. BENTIVOLIO. Very expensive. I mean, lawyer by the hour; right?

Mr. WINSTANLEY. Right.

Mr. BENTIVOLIO. Okay. And so it is pretty costly?

Mr. WINSTANLEY. Yes.

Mr. BENTIVOLIO. A thousand dollars? Two thousand dollars?

Mr. WINSTANLEY. I imagine with the nature of our businesses it will be significantly more than that.

Mr. BENTIVOLIO. Are you talking \$5,000? \$10,000?

Mr. WINSTANLEY. Maybe more.

Mr. BENTIVOLIO. More than that? Oh, my goodness.

Ms. BOGARDUS. Did I pronounce it right?

Ms. BOGARDUS. Yes, sir. Bogardus.

Mr. BENTIVOLIO. Thank you.

Most webinars or PowerPoint presentations on the healthcare law for small businesses do not include materials on the business aggregation rules. Do your companies?

Ms. BOGARDUS. We address the issue. We consistently refer—we are an insurance consulting and brokerage firm. We consistently refer our clients to their tax and legal advisors because it is so complicated. They will have a better understanding of any corporations, any business arrangements that they created. It also requires in many cases an analysis of options, family trusts, documents that were created for purposes other than addressing business aggregation. So it can get extremely detailed.

Mr. BENTIVOLIO. Well, how do small businesses know about these aggregation rules and how they affect them? How do they find out about this?

Ms. BOGARDUS. You know, quite frankly, their advisor, if they are working with an advisor who mentions it to them. So if they have a current relationship—

Mr. BENTIVOLIO. An advisor that costs more than \$10,000?

Ms. BOGARDUS. If they have current legal counsel, if they are working with a consultant or a brokerage firm that raises the issue to them, if they read about it on their own. I know there is information posted on the IRS website as well.

Mr. BENTIVOLIO. Now, forgive me. Are you an attorney? I did not read—

Ms. BOGARDUS. Yes, sir.

Mr. BENTIVOLIO. You are an attorney. So now the way I understand attorneys charge is they charge by the hour, and that includes research; correct?

So if I had my attorney, I want to know about the healthcare law, he would have to read thousands of pages of regulations and he would be charging me by the hour to do that?

Ms. BOGARDUS. It would not necessarily require the attorney to read the entire Health Reform Act, but it would require an analysis, and quite frankly, experience with the control group rules, which are very specific, very detailed, and that is a very specialized area of the law.

Mr. BENTIVOLIO. So if my attorney, my normal business attorney, is unfamiliar with that, I have to go find another attorney, and he is going to charge me—holy cow.

Okay. Thank you. I see my time has pretty much run out. I yield back my time. Thank you, Mr. Chairman.

Mr. COLLINS. Thank you, Mr. Bentivolio.

At this point we will yield five minutes to Representative Barber.

Mr. BARBER. Thank you, Mr. Chairman, and Ranking Member for having this hearing. I appreciate the witnesses' testimony. It is very helpful to hear directly from individuals who are affected or are trying to help others who are affected by the law.

My wife and I ran a small business in our community for 22 years, so we know a little bit about what it takes to meet a payroll, keep the doors open, keep customers coming back, and deal with regulations and taxation issues. So we are very sympathetic to small businesses on a number of levels, and we also know that businesses have to stay profitable and they have to find a way to grow. So all of these issues are very important to me. That is why I wanted to be a member of this Committee, so I could see, along with my colleagues, what we could do to help small businesses be more successful.

Since I have come here last year in June, I have been trying to partner with people on both sides of the aisle to find reasonable fixes for the Affordable Care Act. I think there are many benefits. We have realized many of them already, individuals and so on, and now we are into the larger implementation with small businesses and individuals. The benefits are real but the issues are real as well. And I think with any major piece of legislation, over the decades we have always had to make amendments and revisions to a bill of that size and magnitude. So I am clearly interested in learning more about that from you.

Clearly, as I look at this, and I have heard your testimony, and when I listen to people back home, small business owners, I am reminded that there are three Cs that they often talk about. They talk about the ACA's complexity, that it is confusing, and that it is challenging. And my job as a member of Congress, and I believe that all of our jobs is to get through all of that and help people be successful and understand the law.

So I have the same question for each of the witnesses. If you could make one change, or if you could ask one question to be re-

solved by the agencies that are responsible for the Affordable Care Act, what would your top priority be? Because I think we need to have some instruction or some ideas from witnesses about what we can do. My colleague, Ms. Hahn, was asking about let us figure out what to do that makes things better, not just talking about it back and forth arguing; let us talk about what we can do to fix things. What would those things be from each of you if you could?

Mr. WINSTANLEY. I will go first. I would position the aggregation rule to fulfill the scope that it was originally designed to fulfill, which was promoting the growth of business. I would treat the industries separately within the context of what the industry is and deal with the workforces within the context of what they are to position the law to be viable for all industries.

Mr. BARBER. Ms. Baker. It is hard to choose I imagine.

Ms. BAKER. It is. It is. I would definitely support looking at it industry by industry; looking at it by control, true control, not just ownership or indirect attributed ownership, you know, someone that is actually making day-to-day decisions. And I do think that the 50 employees is too small. It is too small.

Mr. BARBER. Thank you.

Ms. Bogardus.

Ms. BOGARDUS. With respect to the rules that impact small businesses, I would suggest taking a second look at where the rules are with respect to the insurance carriers because there is not the same level of compliance required of them that would support the employer mandate. And I think some of those gaps in the law, which make it difficult, if not impossible for businesses to actually get the coverage, would specifically need to be addressed.

If I can go off the top of small businesses, I would say it would be revisiting the definition of minimum essential coverage, and the plans that will be offered, and I am sure that some of you have read about them in the Wall Street Journal, the skinny plans. There was an article that was about six or eight months ago. They will not be sufficient coverage but they will satisfy the employer mandate. And I think when individuals realize that they have coverage that is not sufficient but it is what the law required employers to purchase and provide, there will be significant backlash, like none of the backlash that we have seen so far to date.

Mr. BARBER. Thank you.

Ms. WALKER. I take the same approach. We are looking at the insurance product. I think the real issue with healthcare in this country is that the quality of care is not what it needs to be and the ACA did not really focus on quality except in a very small segment with some research, so there is a lot more that needs to be done there.

And again, I think that the required insurance, the types of insurance, does not make it very easy for people to comply with the rules.

Mr. BARBER. Thank you for your testimony and your good answers, and I yield back.

Mr. COLLINS. Thank you.

At this point I think Mr. Bentivolio wanted to have a few add-on questions.

Oh, Mr. Huelskamp, I guess we will yield to you first.

Mr. HUELSKAMP. Thank you, Mr. Chairman. I apologize for sliding in a little late here, and I thank the witnesses for joining us today.

A couple questions or a comment at the beginning. I think it was Ms. Walker and others have mentioned that the changes you were looking for would take a legislative change in order to make that happen. And I appreciate that perspective, but what we have seen with the Affordable Care Act, that is not necessary to make the changes from this administration. We have had 10 executive actions, and the employer mandate is one of those. You know what? You have got another year. And I do not know, and Ms. Baker, when people call you, I do not know as a consultant, it makes your job really tough if you do not know what the rules are or they tell you the rules and say they might delay it for another year. I know that has happened in other arenas but we have 10 different areas of the Affordable Care mandate which is the law of the land where the administration has, by executive action, said you know what? We are not going to make employers do the reporting requirements. How do you handle that? How do you answer that question when the IRS has not finalized rules on this and they could change the rules?

I will give you one example. I had a business in Solana, Kansas. They were noted in the local paper, on July 1st they made their changes. That was the renewal period and they did everything they had to do. What a mistake. On July 2nd, the president said, "Just kidding." We are going to suspend that part for another year or delay the mandate and those kind of things. I mean, what is the answer you give to folks that definitely must be calling in saying, well, what does a one-year delay mean? And I will ask that question to Ms. Baker first.

Ms. BAKER. It does make it very difficult, especially for a small firm like mine because we have such limited resources, so when you take the initiative to communicate everything and then all of a sudden it changes, and so you reach out and have to recommunicate. So the amount of time and the expense associated with that is great.

Mr. BENTIVOLIO. Other responses from the panel?

Mr. WINSTANLEY. Sure. It consumes a phenomenal amount of energy that is not used on something else constructive. And fortunately for the restaurant side of our business, we are looking at it saying this just is not sustainable with our current business model, so something has got to be done before this gets rolled out so we can feel some level of comfort that something will happen. Hopefully that is not a pipe dream.

Mr. BENTIVOLIO. And I have yet to see anything from the White House that they want to make any changes legislatively to this act. I mean, there have been many suggestions of things we can fix. We have heard them here. Heard them multiple times in this Committee. We mention the SBA as representing the administration and no interest in changing one letter of the law unless it is by executive action, and that is certainly unacceptable to me.

One thing I would like to ask Ms. Walker on another issue as far as the trend of basically a part-time economy. The new hires, according to the Department of Labor, I did not know that they are

that bad, that in this economy four out of five new jobs—was that the figure that you had—that are created are part-time?

Ms. WALKER. For every one full-time job that is created there are four part-time jobs created.

Mr. BENTIVOLIO. So when you average the hours that is not quite four to one.

Ms. WALKER. Right.

Mr. BENTIVOLIO. That makes sense. Four out of five new jobs created.

Ms. WALKER. Well, that is surprising in and of itself to me, but the trend, and I am not sure whether it was 2010 to 2012 or what the years were, but the trend, it is flipped. It used to be six full-times to one part-time versus one to four.

Mr. BENTIVOLIO. That is really a devastating figure. I mean, it is not devastating for us in this room, definitely, it is the folks out there looking for a job, particularly young people which have been the most devastated in this lack of long-term economic recovery.

Can you describe a little more what happens, and basically this part-time economy where you are trying to work around, trying to avoid these mandates. I mean, people might say, well, why are you not providing health insurance for somebody who works 20 hours a week? There are reasons. It is costly.

Ms. WALKER. Right.

Mr. BENTIVOLIO. And trying to make those demands in a changing, uncertain environment where you have got to look and say you cannot work that much this weekend, and the reality is it is not just figures. I have heard from my district story after story of small business owners saying, you know, “Congressman, I did not hire anybody this week. I am not going to hire anybody next year because I am worried about the threshold. I do not know what the rules are going to be. I am not going to take that risk.” And these are successful businessmen and women. But the message we are sending from Washington is that we will let you know next year, and it does not work that way.

Any further comments from you all? I know I am about out of time on that, but that is the frustration I am hearing, which is matching what the panel has.

Ms. Bogardus.

Ms. BOGARDUS. Thank you. I would just add that it is an issue that is crying out for leadership, and leadership in terms of what you are doing here today, and that is seeking out the truth. What is the truth, what are the facts, and then coming to at least some sort of agreement on what you can agree on. I mean, the American people, the small business owners, the large business owners, they want to see some sort of solution to these problems other than the issues being raised and the lack of a solution just being acceptable or considered inevitable. And we need somebody, and a group of people perhaps, to step up and say something has got to change because we cannot sit back and watch the train go down the tracks with the bolts flying off because we know what is going to happen. And this is our country, our economy, our fellow citizens, the children, the young people who are trying to get jobs, people who are trying to grow a business, business owners who are trying to do

planning who are putting off expansion, putting off buildings, putting off all kinds of things that could create and generate other jobs, not just within their own businesses, construction work and other things. So it is crying out for leadership, and I would say this is a great start and I would continue down that path.

Mr. BENTIVOLIO. Thank you. And I yield back, Mr. Chairman.

Mr. COLLINS. Thank you, Ms. Bogardus. That was a great summary, actually.

At this point I would like to yield five minutes to Mr. Payne.

Mr. PAYNE. Thank you, Mr. Chairman.

Ms. VELAZQUEZ. Mr. Payne, will you yield for one second?

Mr. PAYNE. Yes.

Ms. VELAZQUEZ. I just—if not——

Mr. PAYNE. You are the ranking member. Please.

Ms. VELAZQUEZ. Go ahead and use your five minutes. I will come back. I just did not want to——

Mr. PAYNE. No, please.

Ms. VELAZQUEZ. I did not want to lose the train here.

Ms. Walker, you mentioned—a number that struck me, one out of five jobs are part-time jobs. What was the number?

Ms. WALKER. For every one full-time job created, there are four part-time jobs created.

Ms. VELAZQUEZ. There was a hearing that I mentioned before, where we had the expert witness Dean Baker from the Center for Economic and Policy Research, and he said the vast majority of people who work part-time do so voluntarily. In many cases, they have family or other obligations that make part-time employment decidable. Even with the current weak labor market, more than two-thirds of the people who work part-time report that they do so voluntarily.

Thank you for yielding.

Mr. PAYNE. Well, you know, this is an observation, and the Affordable Health Care Act is the law, very new in its infancy, and naturally there are going to be issues around the implementation. We know the problems that we have had to this point, but the meat of the act I think will revolutionize healthcare in this nation. If we look back at other large programs that have been implemented over the course of time, one being social security is probably the easiest one to mention, when it was implemented it was going to destroy this nation and we were going to socialism and how could we do this? It was going to ruin the nation. And I think most American now think social security is part of the fabric of this country. And so I see the Affordable Care Act having the same type of life in this nation.

When they started social security they used your name as an identifier. Well, guess what? They had to tweak the system because there were a lot of Donald Paynes and Ms. Bakers and what have you. So they went to a social security number. So nothing is perfect when it starts. You have to let it evolve into something that is going to work. So I like to use that example because it is probably the easiest example to use in terms of rough starts for large programs that are successful over the course of time.

And Ms. Baker, in your testimony you state that this law leads small business owners to provide health coverage in an industry

where that is not the norm. Well, let me just say that—I want to say setting the norm is precisely what the Affordable Care Act is about. Over the last decade, health insurance premiums for small firms have increased 113 percent leading to dropped coverage. The Affordable Care Act was enacted to upset this norm and make it easier for small businesses to compete and offer quality benefits. The norm prior to the law allowed insurance companies to drop coverage for employees when they needed coverage the most and discriminate against people with preexisting conditions. The law upsets this norm.

Prior to the Affordable Care Act, it was normal for an average U.S. family and their employer to pay an additional \$1,000 for insured people to cover that cost. The Affordable Care Act aims to upset this norm by bringing the uninsured into the system, driving overall costs down.

Now, there are issues with the law that need to be tweaked, but the bones and the substance of the law are good and are here to stay. Further, 96 percent of U.S. businesses have fewer than 50 employees, and according to the last census data, less than 1 percent of businesses have between 45 and 49 employees, placing them at risk of falling into the abyss of the employer mandate. Again, that is less than 1 percent.

Now, I am interested in addressing valid concerns about the Affordable Care Act and you have stated many today, such as the compliance and the burden on small businesses. However, I really find it nonconstructive to continue to play on the fears of the American people rather than work on ways to make this law better and see it implemented successfully. So over the course of the last two days I have heard the president speaking before groups and saying if you have ideas, and I believe he is reaching out to our colleagues on the other side, if you have ideas that will strengthen the law, then let us discuss it. But to continue to try to tear it down and sabotage it and not even allow it to go through its natural courses is counterproductive.

So in terms of solutions, and I am very open to the criticism and the potential of making it stronger, so I am glad to hear your testimony.

Mr. Winstanley, you mentioned—I am sorry.

Mr. WINSTANLEY. Yes, sir.

Mr. PAYNE. Did I pronounce it correct?

Mr. WINSTANLEY. Yes. Winstanley. Yes.

Mr. PAYNE. Winstanley. I am sorry.

You mention an E-FLEX coalition that advocates for greater flexibility and options within the law. I understand that the restaurant industry has a unique makeup. What proposal does the coalition have to provide flexibility while upholding the law's goal of expanding insurance coverage for all?

Mr. WINSTANLEY. Where do you see the E-FLEX? Oh, it was referenced in the regulations?

Mr. PAYNE. Yeah.

Mr. WINSTANLEY. I am not familiar enough with that. I am not familiar enough with that to speak to that. What I would like to speak to though is you mentioned social security, and to my generation and every generation behind us, what social security is

known for is being a completely unsustainable program. I would also like to mention that when I got started, I got started with a 24-hour diner. It had about 10 or 12 employees. My twin brother and I stayed up all night building that place and rebuilding it and turning it into a real business and there was nothing we wanted more than to build our business and add to it. And I have been fortunate to have some very good advice from people over the years that have done similar things, and what they have shared with me time and again, which turned out to be true in our case, is that every next step you take is harder than the step behind you, and there is significant growth burden that comes with trying to build a real business. And the 50 employees, regardless of what industry I believe you are in, the 50 employees presents an additional significant hurdle for people who are trying to build something meaningful, and I think it is counter to the spirit of this country.

Mr. COLLINS. Thank you. The gentleman's time has expired.

Mr. Bentivolio wanted to ask a follow-on question, so Mr. Bentivolio.

Mr. BENTIVOLIO. Thank you, Mr. Chairman.

Just a few short questions.

Mr. Winstanley.

Mr. WINSTANLEY. Yes, sir.

Mr. BENTIVOLIO. Healthcare law requires you to inform your employees about the health insurance choices available to them. Is this an additional burden and expense for your companies?

Mr. WINSTANLEY. I am sorry, requires us to inform them about the health care?

Mr. BENTIVOLIO. Yes, sir. There is a significant amount of education that goes on and as anybody with kids knows, it is hard to educate somebody who is not interested to hear what you are saying.

It has traditionally been very challenging for us to educate to the groups of people that we were able to provide health insurance to. And so, yeah, I see that as being very significant. Yes, sir. I see it as being a very significant challenge.

Mr. BENTIVOLIO. Now, while I was back in the District last weekend, I had dinner at a restaurant, and the waitress came over and she recognized me and a big supporter and told me her story; that she lost her job, now is working two jobs, all because of the health care. She lost it when they found out about this employer mandate, before they delayed that. Right? And they had to reduce their employees. And now she is working two jobs. Do you have a lot of waitresses or people on your staff that are working two jobs to make ends meet?

Mr. WINSTANLEY. We have a significant number of people doing that, and what we have seen is there are a lot of people who need part-time jobs and that is because wage and job growth in permanent, full-time positions has not been there while the cost of childcare and housing continue to increase.

Mr. BENTIVOLIO. Do you think that is largely attributable to the Unaffordable—excuse me—Affordable—this is really confusing—Unaffordable Health Care Act? I got it right. Washington got it wrong.

Mr. WINSTANLEY. I think it is attributable to a general slow-down, which the healthcare act is very much influencing.

Mr. BENTIVOLIO. Great. So let us see. Ms. Baker, under the aggregate rules, a controlled group is a collection of two or more corporations with common stock ownership that are connected in one of several ways. Many small businesses do not issue stock. How would the rules be applied in those cases?

Ms. Baker, CPA; right?

Ms. BAKER. Yes.

They look at ownership. So if you are not a corporation, they look at investment and equity within those companies. So in my example, when I invested in a small women's boutique just as an investment, I do not manage or operate that on a day-to-day basis. Those employees are then pulled into my CPA firm as part of the rules of aggregation.

Mr. BENTIVOLIO. And increasing the cost?

Ms. BAKER. And increasing the cost. And even though Mr. Payne mentioned the norm, I think the norm is we would all love to provide health insurance in every industry, but that is a very small women's boutique. There are very few other women's boutiques that would have to require health insurance because they are small businesses and they are not meeting the 50 employees. So for me to have to provide health insurance for them makes me not competitive in that market just because I am an entrepreneur and own businesses in different industries.

Mr. BENTIVOLIO. So let us see if we can sum up. Higher deductibles, higher premiums, additional legal costs; correct? Tens of thousands of dollars for a small business. And you are less competitive.

Thank you very much. I yield back.

Mr. COLLINS. At this point we will call the hearing to a close. I want to thank all of our witnesses for being here today. It is very timely.

I think what some people do forget is even though the employer mandate, the penalty portion has been delayed a year, the calculations as to whether or not you will have to comply with the law start in three weeks time. So on January 1st, that is the beginning of what will be 12 monthly buckets of keeping track of the hours and the employees to see if you hit the 50 FTEs or not. So it is a very timely situation. We certainly heard a lot of give and take. I think we all recognize that there will be changes that will be needed in this law and hopefully now the president would agree to make some changes. He has not up till this point in time recognized that, but I think an overwhelming number of Americans today are expressing displeasure in the law. And certainly, as we heard today, compliance with the law and the application of the complex aggregation rules is burdensome and is confusing for business, and I think it almost goes without saying that a big government, "one size fits all" set of regulations and laws that tell a business what benefits they have to offer, whether that is a restaurant, a construction company, or a high-tech manufacturing company is, in fact, a drag on the economy.

Today's hearing did highlight another example of the unintended consequences of the Affordable Care Act, namely the high cost to

business of hiring a CPA or other tax advisor to give advice on the IRS aggregation rules, money that is better spent on growth and the creation of jobs.

We on this Committee will continue to closely follow the implementation of this law and its effect on small business.

I would ask unanimous consent that members have five legislative days to submit statements and supporting materials for the record.

Ms. VELÁZQUEZ. Yes, Mr. Chairman, before we close, I would like to thank all the witnesses. It is a breath of fresh air to hear that we are talking now about fixing and looking at ways where we could improve the implementation of the health care law. So it is great to know that we are moving beyond repealing Obamacare to finding common ground to make it work because it is the law of the land. Thank you.

Mr. COLLINS. Thank you, Ranking Member Velázquez. And with that, without objection, this hearing is now adjourned.

[Whereupon, at 3:15 p.m., the Committee was adjourned.]

**A P P E N D I X**

**“The Health Care Law, The Effect of the Business  
Aggregation Rules on Small Business”**

**Testimony of:**

**Deborah Walker, CPA  
National Director, Compensation & Benefits  
Cherry Bekaert LLP  
Washington, DC**

**Before the**

**Committee on Small Business  
United States House of Representatives**

**December 4, 2013**

**The Honorable Sam Graves (R-MO), Chairman  
The Honorable Nydia Velázquez (D-NY), Ranking Member**

Good afternoon Chairman Graves, Ranking Member Velázquez and members of the Committee. Thank you for hosting this important hearing on the effect of the business aggregation rules on small business in applying the health care law. I am Deborah Walker, a CPA with over 35 years of experience in the Employee Benefits area. I am currently National Director of Compensation and Benefits for Cherry Bekiaert LLP. I welcome this opportunity to discuss this important issue and offer an alternative approach.

#### Executive Summary

In order to determine if an employer is subject to the shared responsibility rules of the Affordable Care Act, the employer must determine if at least 50 full time equivalents are employed on business days during the preceding taxable year. Prior to making this calculation, the business needs to determine what trades or businesses comprise the employer. The employer includes the business and related entities, including entities related by common ownership and by attribution of ownership from one party to another, and certain other businesses that provide services to the business. To make the determination, one needs detailed ownership rules and business relationships between the entities.

The rules used by the Affordable Care Act are the same rules used for determining if qualified retirement plan benefits are available on a nondiscriminatory basis to a fair cross section of employees. The use of bright line tests has enabled tax planners to structure arrangements to avoid the application of the rules. Because the rules have been developed over a number of years to counteract avoidance of the rules by tax planners, they are voluminous and extremely detailed.

In the health care context, this is a test that will only be used by businesses close exceeding the 50-employee limit and, as businesses grow or decline the need for applying the test evaporates. Such a complicated test for such few taxpayers is not warranted. In addition, one can expect that the employers close to exceeding the limit will make business decisions that would result in increased hiring by taking into account the increased cost of mandated health care.

An employer can choose to offer a retirement plan or not, and in so doing accepts the application of these rules. For mandated health benefits, the employer does not have a choice of whether to be involved with these rules. For this reason, these rules are not appropriate to define the employer for the Affordable Care Act. Applying the same business aggregation rules to a mandated benefit that exist for purposes of preventing discrimination for voluntary employer provided benefits can lead to inefficient and unwanted economic behavior. This behavior constrains a small business and may lead to unwanted and unwelcome business decisions including not hiring additional works that ensure the small business is not subject to the rules.

Many small employers who offer a retirement plan offer a safe harbor IRC Section 401(k) plan that does not require discrimina-

tion testing. Thus, many small employers do not have to make this determination except for determining the applicability of the shared responsibility rules of the Affordable Care Act and the groups of employees for whom minimum essential coverage is required to be provided. Because many small employers have never had to use these rules, avoiding them with the use of safe harbor qualified retirement plans or not offering a qualified retirement plan, the rules are not familiar to them. This is true for many of the advisers to small businesses. What we have here are rules that only a small subset of tax practitioners are familiar with and apply. Even those that apply the rules, as I and other benefits practitioners do, apply them on an infrequent basis, perhaps 4–5 times a year.

For determining who is the employer, I suggest an alternatives, facts and circumstances test focused on the entities controlled by a specific individual. Investors who had no control of day-to-day operations of the business would not need to be aggregated. Examples include the individual who makes hiring and firing and purchasing decisions and sets sales prices. By focusing on day-to-day operations, the business would be defined by the industry or industries with which an individual is involved regularly. Similarly, if a spouse were not involved with day-to-day operations of the other spouse's business, the businesses of each spouse would not be aggregated.

The taxpayer would evaluate the facts and circumstances of each business and a determination would be made. By using a facts and circumstances determination, the opportunity to plan to avoid bright line tests is not available. A facts and circumstances test will use business activities and characteristics with which the small business operator is familiar. The statute or IRS guidance could outline a nonexclusive list of characteristics of control. This is similar to the rules used for determining whether an individual is an employee or independent contractor and parts of the rules that determine what is a separate line of business. As there is sometimes no clear-cut answer, many people may be more rather than less conservative in making a determination.

The determination would be subject to audit by the IRS. In addition, the IRS could establish a procedure whereby taxpayers could obtain certainty by applying to the IRS for a determination of whether 2 businesses should be aggregated given specified facts.

Finally, because the existing rule is the same rule used for qualified plan discrimination testing, some employers may want to continue using the existing bright line test rule, suggesting that a new facts and circumstances rule should be an alternative.

#### Background

Under the Affordable Care Act, employers with an average of at least 50 full-time employees on business days during the preceding taxable year are subject to shared responsibility assessable penalties if 1) minimum essential coverage is not offered to full employees (and their dependents) and at least one full-time employee

enrolls in such coverage for which a tax credit or cost sharing reduction is allowed, or 2) minimum essential coverage is offered to full-time employees (and their dependents) but the coverage is not affordable or does not meet minimum value standards and at least one full-time employee enrolls in such coverage for which a tax credit or cost sharing reduction is allowed.

#### The Controlled Group Rules

To determine if an employer employs an average of at least 50 full-time employees on business days during the preceding year, all persons treated as a single employer under IRC Section 414(b), (c), (m), (n) and (o) are treated as employed by 1 employer. This rule is known as the controlled group, affiliated service group and leased employee rule. Special rules apply for employers not in existence during the preceding year, for predecessor employers and for seasonal workers. In addition, full-time equivalent employees are treated as full-time employees.

The controlled group rules were originally enacted with ERISA in 1974, modeled after the controlled group rules for consolidated return purposes. In general, the employees of a controlled group of corporations or of commonly controlled partnerships or proprietorships are treated as if the same employer employed them all. The rules have been applied for many years to qualified retirement plans and even longer for other tax purposes. Because the purpose of the controlled group rules for benefit plan discrimination testing and coverage rules is broader than the purpose for the consolidated return rules, the rules apply to noncorporate trade or business entities using the same concepts as the corporate entities. In general, the rule was originally adopted to make it impossible for the qualified plan coverage and nondiscrimination rules to be circumvented by operating businesses through separate entities rather than as a single entity. Since that time, they have been used for defining the employer for testing discrimination for all types of benefit plans.

The controlled group rules include parent-subsidiary controlled groups, brother-sister controlled group and combined groups.

#### Parent Subsidiary Controlled Group

A parent-subsidiary controlled group is one of more chains of corporations connected through stock ownership with a common parent corporation if

(A) Stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote or at least 80 percent of the total value of shares of all classes of stock of each of the corporations, except the common parent corporations, is owned (directly and through ownership of an option) by one or more of the other corporations; and

(B) The common parent corporation owns (directly and through ownership of options) stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote or at least 80 percent of the total value of shares of all classes of stock of at least one of the other cor-

porations, excluding, in computing such voting power or value, stock owned directly by such other corporations.

For determining stock ownership, attributions rules apply to attribute ownership to someone other than the legal owner of the stock. For purposes of determining whether a corporation is a member of a parent-subsidary controlled group of corporations, stock owned by a partnership is considered owned proportionally by any partner that has an interest of five percent or more of the capital or profits of the partnership, whichever is greater. Similarly, in the case of an estate or trust, other than a trust holding qualified retirement plan assets, stock owned by the estate or trust is considered owned proportionally by a beneficiary who has an actuarial interest of five percent or more in such stock. To determine the five percent actuarial interest, one assumes the maximum exercise of discretion by the fiduciary in favor of the beneficiary and the maximum use of stock to satisfy the beneficiary's rights. In addition, the grantor of a grantor trust is considered to own the stock of the trust.

For example, assume P Corporation owns 80 percent of the only class of stock of S Corporation and S, in turn, owns 40 percent of the only class of stock of X Corporation, P also owns 80 percent of the only class of stock of Y Corporation and Y, in turn, owns 40 percent of the only class of stock of X. P is the common parent of a parent-subsidary controlled group consisting of member corporations P, S, X, and Y.

Similarly, assume P Corporation owns 75 percent of the only class of stock of Y and Z Corporations; Y owns all the remaining stock of Z; and Z owns all the remaining stock of Y. Since intercompany stockholdings are not treated as outstanding for purposes of determining whether P owns stock possessing at least 80 percent of the voting power or value of at least one of the other corporations, P is treated as the owner of stock possessing 100 percent of the voting power and value of Y and of Z. Also, stock possessing 100 percent of the voting power and value of Y and Z is owned by the other corporations in the group. P and Y together own stock possessing 100 percent of the voting power and value of Z, and P and Z together own stock possessing 100 percent of the voting power and value of Y. Therefore, P is the common parent of a parent-subsidary controlled group of corporations consisting of member corporations P, Y, and Z.

When applying these rules to noncorporate entities, a parent-subsidary group of trades or businesses under common control include means one or more chains of organizations conducting trades or businesses connected through ownership of a controlling interest with a common parent organization if—

(A) A controlling interest in each of the organizations, except the common parent organization, is owned (directly and through ownership of options) by one or more of the other organizations; and

(B) The common parent organization owns (directly and through ownership of options) a controlling interest in at least one of the other organizations, excluding, in computing such

controlling interest, any direct ownership interest by such other organizations.

For purposes of these rules, a controlling interest is defined as

(A) In the case of an organization which is a corporation, ownership of stock possessing at least 80 percent of total combined voting power of all classes of stock entitled to vote of such corporation or at least 80 percent of the total value of shares of all classes of stock of such corporation;

(B) In the case of an organization which is a trust or estate, ownership of an actuarial interest of at least 80 percent of such trust or estate;

(C) In the case of an organization which is a partnership, ownership of at least 80 percent of the profits interest or capital interest of such partnership; and

(D) In the case of an organization which is a sole proprietorship, ownership of such sole proprietorship.

In determining ownership, only outstanding stock is taken into account. In addition, if the parent organization owns

(A) In the case of a corporation, 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock of such corporation.

(B) In the case of a trust or an estate, an actuarial interest of 50 percent or more of such trust or estate, and

(C) In the case of a partnership, 50 percent or more of the profits or capital interest of such partnership.

certain other stock ownership is excluded, including that held in trust for the payment of deferred compensation, subsidiary stock held by principal owners, officers, partners or fiduciaries of the parent organization, subsidiary stock held by employees if subject to a substantial restriction which limits the employees right to dispose of the stock which runs in favor of the parent organization and subsidiary stock held by an exempt organization which is controlled by the parent or subsidiary organization, by an individual, estate, or trust that is a principal owner of the parent organization, by an officer, partner, or fiduciary of the parent organization, or by an combination thereof. Whether an exempt organization is controlled is a facts and circumstances determination.

As you can see, application of this rule involves knowing stock and option ownership of all entities, applying attribution rules for stock owned by partnerships, estates and trusts and then determining if the 80% rule is met. Note that, if stock ownership is 79%, then a parent subsidiary controlled group is not formed. Corporate tax planning often involves owning 79% rather than 80% of a corporation for this reason.

#### Brother-Sister Controlled Group

A brother-sister controlled group is a group of two or more corporations if the same five or fewer persons who are individuals, es-

tates, or trusts own (directly and through the ownership of options) stock possessing

(A) At least 80 percent of the total combined voting power of all classes of stock entitled to vote or at least 80 percent of the total value of shares of all classes of stock of each corporation (the 80 percent requirement);

(B) More than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of shares of all classes of stock of each corporation, taking into account the stock ownership of each such person only to the extent such stock ownership is identical with respect to each such corporation (the more-than-50 percent identical ownership requirement); and

(C) The five or fewer persons whose stock ownership is considered for purposes of the 80 percent requirement must be the same persons whose stock ownership is considered for purposes of the more-than-50 percent identical ownership requirement.

For determining stock ownership, attributions rules again apply to attribute ownership to someone other than the legal owner. For purposes of determining whether a corporation is a member of a brother-sister controlled group of corporations, stock owned by a partnership is considered owned proportionally by any partner that has an interest of five percent or more of the capital or profits of the partnership, whichever is greater. Similarly, in the case of an estate or trust, other than a qualified retirement plan, stock owned by the estate or trust is considered owned proportionally by a beneficiary who has an actuarial interest of five percent or more in such stock. To determine the five percent actuarial interest, one assumes the maximum exercise of discretion by the fiduciary in favor of the beneficiary and the maximum use of stock to satisfy the beneficiary's rights. In addition, the grantor of a grantor trust is considered to own the stock of the trust. One also needs to attribute stock held by a corporation proportionally to any five percent or more owner of the corporation.

Finally, in the case of family attribution, stock owned by a spouse is considered owned by the other spouse unless each of the following is true:

a) the spouse owns no stock directly at any time during the taxable year,

b) the spouse is not an employee or director or participate in management of the corporation at any time during the taxable year,

c) no more than 50% of the corporation's gross income was derived from rents, royalties, dividends, interest and annuities during the year, and

d) the stock of the corporation is not, at any time during the taxable year, subject to conditions which substantially limit or restrict the owner's right to dispose of such stock which run in favor of the spouse or children who have not attained age 21.

Stock owned directly or indirectly by a child that has not attained age 21 is attributed to the parents and if an individual has not attained age 21, stock owned by the parents is attributed to the child. In addition, if an individual owns more than 50% of the total voting power or value of all classes of stock (after applying all attribution rules other than this rule and attribution from children under age 21), stock owned directly or indirectly by parents, grandparents, grandchildren and children over age 21 are attributed to the individual.

For determining a brother-sister controlled group of corporations, one needs to again determine stock and option ownership, attributed stock ownership and also common ownership (including that through attribution) and then apply the 80% and 50% test. Again, with the bright line stock ownership rules, individuals can structure ownership to avoid the rules. When applying these rules to noncorporate entities, adjustments are made which highlight that only trade or business entities are considered.

Again, certain stock ownership can be excluded for purposes of determining ownership. If five or fewer persons who are individuals, estates, or trusts own (directly and through the ownership of options) own

(A) In the case of a corporation, 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock or such corporation,

(B) In the case of a trust or an estate, an actuarial interest of 50 percent or more of such trust or estate, and

(C) In the case of a partnership, 50 percent or more of the profits or capital interest of such partnership.

certain stock ownership is excluded, including that held in a qualified retirement plan trust, subsidiary stock held by employees if subject to a substantial restriction which limits the employees right to dispose of the stock which runs in favor of the parent organization and subsidiary stock held by an exempt organization which is controlled by the by the organization, by an individual, estate, or trust that is a principal owner of the organization, by an officer, partner, or fiduciary of the parent organization, or by any combination thereof. Whether an exempt organization is controlled is a facts and circumstances determination.

The term "brother-sister group of trades or businesses under common control" means two or more organizations conducting trades or businesses if

(A) the same five or fewer persons who are individuals, estates, or trusts own (directly and through attribution as described above) a controlling interest in each organization, and

(B) taking into account the ownership of each such person only to the extent such ownership is identical with respect to each such organization, such persons are in effective control of each organization.

The five or fewer persons whose ownership is considered for purposes of the controlling interest requirement for each organization must be the same persons whose ownership is considered for purposes of the effective control requirement.

For purposes of these rules, a controlling interest is defined as

(A) In the case of an organization which is a corporation, ownership of stock possessing at least 80 percent of total combined voting power of all classes of stock entitled to vote of such corporation or at least 80 percent of the total value of shares of all classes of stock of such corporation;

(B) In the case of an organization which is a trust or estate, ownership of an actuarial interest of at least 80 percent of such trust or estate;

(C) In the case of an organization which is a partnership, ownership of at least 80 percent of the profits interest or capital interest of such partnership; and

(D) In the case of an organization which is a sole proprietorship, ownership of such sole proprietorship.

For purposes of these rules, effective control is defined as

(A) In the case of a corporation, such persons own stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of shares of all classes of stock of such corporation;

(B) In the case of a trust or estate, such persons own an aggregate actuarial interest of more than 50 percent of such trust or estate;

(C) In the case of a partnership, such persons own an aggregate of more than 50 percent of the profits interest or capital interest of such partnership; and

(D) In the case of a sole proprietorship, one of such persons owns such sole proprietorship.

For example, assume X corporation is owned by 8 unrelated shareholders, A, B, C and D each own 12% and E, F, G and H each own 13% and Y Corporation is owned by the same 8 shareholders with A, B, C and D each owning 13% and E, F, G and H each own 12%. Any group of five of the shareholders will own more than 50 percent of the stock in each corporation, in identical holdings. However, X and Y are not members of a brother-sister controlled group because at least the same five or fewer persons do not own 80 percent of the stock of each corporation.

Alternatively, assume Corporation X and Y both has voting and nonvoting stock outstanding. Individual A owns 100% of the voting stock and 60% of the value of Corporation X and 75% of the voting stock and 60% of the value of Corporation Y. Unrelated individual B owns no voting stock and 10% of the value of Corporation X and 25% of the voting stock and 10% of the value of Corporation Y. No other shareholder of X owns (or is considered to own) any stock in Y. X and Y are a brother-sister controlled group of corporations.

The group meets the more-than-50 percent identical ownership requirement because A and B own more than 50 percent of the total value of shares of all classes of stock of X and Y in identical holdings. The group also meets the more-than-50 percent identical ownership requirement because of A's voting stock ownership. The group meets the 80 percent requirement because A and B own at least 80 percent of the total combined voting power of all classes of stock entitled to vote.

These examples highlight the detail needed for determining whether a brother-sister controlled group exists. When one considers that attribution of stock ownership must be taken into account before this test is performed, it is evident how complicated the rule can be. Most tax practitioners would agree that non tax professional would not likely be able to make a correct determination of controlled group status in situations in which a number of entities are involved or where there is significant stock attribution that needs to be considered.

#### Combined Group

A combined group is any group of three or more corporations if

(A) Each such corporation is a member of either a parent-subsidiary controlled group of corporations or a brother-sister controlled group of corporations; and

(B) At least one of such corporations is the common parent of a parent-subsidiary controlled group and also is a member of a brother-sister controlled group.

A combined group of trades or businesses under common control means any group of three or more organizations, if

(1) each such organization is a member of either a parent-subsidiary group of trades or businesses under common control or a brother-sister group of trades or businesses under common control, and

(2) at least one such organization is the common parent organization of a parent-subsidiary group of trades or businesses under common control and is also a member of a brother-sister group of trades or businesses under common control.

#### **Affiliated Service Group Rules**

As noted above, provisions that use bright line tests provide practitioners and their clients with the opportunity to structure ownership to avoid the rules. That is precisely what Dr. Kiddie and Dr. Garland did when they formed a partnership owned 50% by each of them. The partnership employed nurses and other staff who, as a result of plan provisions, did not participate in the benefit plans in which the doctors participated. The IRS challenged this arrangement, but the Tax Court upheld it. As a result, Congress expanded the controlled group rules by adding the affiliated service group rules in 1980. Thus, the controlled group rules were supplemented by affiliated service group rules that focus on business relationships and activities rather than stock ownership. In

subsequent years, more statutory changes expanded the definition to include groups of management organizations and the organizations managed, even if there was no stock ownership, and broadened the attribution rules that apply. For instance, if one entity provides management services to another entity, the two entities would be part of an affiliated service group.

An affiliated service group is one type of group of related employers and refers to two or more organizations that have a service relationship and, in some cases, an ownership relationship. An affiliated service group can fall into one of three categories.

1. A-Organization groups (referred to as “A-Org”) consist of an organization designated as a First-Service Organization (FSO) and at least one “A organization”.
2. B-Organization groups (referred to as “B-Org”) consist of a FSO and at least one “B organization”.
3. Management groups.

An FSO must be a “service organization”, a corporation, partnership or other entity whose principal business is the performance of services. Proposed regulations state that the principal business of an organization is considered the performance of services if capital is not a material income-producing item. This is a facts and circumstances determination, although the proposed regulations specify that capital is a material income-producing item for banks and similar institutions. In addition, the proposed regulations note that capital is a material income-producing factor if a substantial portion of the gross income of the business is attributable to the employment of capital in the business are reflected, for instance, by a substantial investment in inventories, plant, machinery or other equipment. Capital is not a material income-producing factor if the gross income of the business consists principally of fees, commissions, or other compensation for personal services performed by an individual. In addition to non-capital intensive organizations, an organization engaged in health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting or insurance are all considered service organizations.

To be an A-Org, an organization must satisfy an ownership test and a working relationship test. The ownership test is met if the organization is a partner or shareholder in the FSO (regardless of the percentage interest it owns in the FSO) determined by applying the constructive ownership rules. The working relationship test is the organization “regularly performs services of the FSO,” or “regularly associated with the FSO in performing services for third parties. Facts and circumstances are used to determine if a working relationship exists.

To be a B-Org, the organization does not need to be a service organization. Rather, it must meet the following requirements:

- A significant portion of its business must be the performance of services for a FSO, for one or more A-Org’s determined with respect to the FSO, or for both,

- The services must be of a type historically performed by employees in the service field of the FSO or the A-Org's, and
- Ten percent or more of the interests in the organization must be held, in the aggregate, by highly-compensated employees of the FSO or A-Org.

Services will be considered of a type historically performed by employees in a particular service field if it was not unusual for the services to be performed by employees of organizations in that service field in the United States on December 13, 1980.

For example, assume Allen Averett, a doctor, is incorporated as Allen Averett, P.C. and this professional corporation is a partner in the Butler Surgical Group. Allen Averett and Allen Averett, P.C., are regularly associated with the Butler Surgical Group in performing services for third parties. The Butler Surgical Group is an FSO. Allen Averett, P.C. is an A-Org because it is a partner in the medical group and is regularly associated with the Butler Surgical Group to perform services for third parties. Accordingly, Allen Averett, P.C. and the Butler Surgical Group would constitute an affiliated service group. As a result, the employees of Allen Averett, P.C. and the Butler Surgical Group must be aggregated and treated as if they were employed by a single employer.

Similarly, assume that the Everett, Furman and Guilford Partnership is a law partnership with offices in numerous cities. EFG of Capital City, P.C., is a corporation in Capital City that is a partner in the law firm. EFG of Capital City, P.C. provides paralegal and administrative services for the attorneys in the law firm. All of the employees of the corporation work directly for the corporation, and none of them work directly for any of the other offices of the law firm. The law firm is an FSO. The corporation is an A-Org because it is a partner in the FSO and is regularly associated with the law firm in performing services for third parties. The corporation and the partnership would together constitute an affiliated service group. Therefore, the employees of EFG of Capital City, P.C. and the employees of The Everett, Furman and Guilford Partnership must be aggregated and treated as if they were employed as a single employer.

Similarly, assume Reinhardt & Associates is a financial services organization that has 11 partners. Each partner of Reinhardt owns one percent of the stock in Asbury Corporation. Asbury provides services to the partnership of a type historically performed by employees in the financial services field. A significant portion of the business of Asbury consists of providing services to Reinhardt. Considering Reinhardt & Associates as an FSO, the Asbury Corporation is a B-Org because:

1. A significant portion of its business is in the performance of services for the partnership of a type historically performed by employees in the financial services field. And,
2. More than 10% of the interests in the Asbury Corporation is held, in the aggregate, by the highly-compensated employees of the FSO (consisting of the 11 common owners of Reinhardt and Associates).

Accordingly, the Asbury Corporation & Reinhardt and Associates constitute an affiliated service group. Therefore, the employees of the Asbury Corporations and Reinhardt and Associates must be aggregated and treated as if they were employed by a single employer.

A management-type affiliated service group exists when an organization performs management functions, and the management organization's principal business is performing management functions on a regular and continuing basis for a recipient organization. There does not need to be any common ownership between the management organization and the organization for which it provides service. Any person related to the organization performing the management function is also to be included in the group that is to be treated as a single employer.

A recipient organization does not need to be a service organization. It is as organization for which management services are performed, any organization aggregated with the service organization under these controlled group and affiliated service group rules and all related organizations.

For example, assume Anson and Branch Corporations are a brother sister corporation and Crockett and Duval Corporations constitute an affiliated service group. Assume Crockett or Duval (or both) perform management functions and other services for Anson or Branch (or both) and the performance of these management functions or services satisfy the requirements of a principal business on a regular and continuing basis. Crockett and Duval are treated as a single management organization and Anson and Branch are treated as a single recipient organization. Anson, Branch, Crockett and Duval would constitute an affiliated service group.

The affiliated service group rules are very difficult to apply, because there are so many different iterations of possible structures that need to be considered. In fact, the IRS has not issued any final regulations providing guidance for applying these rules. Proposed regulations were issued in 1983 and 1987 and portions of those were withdrawn, presumably because they were broader than intended and thus unworkable, in 1993.

#### Leased Employees

At the same time that the affiliated service group rules were enacted, employee leasing rules were also enacted, which required the inclusion in the controlled group of employees leased to entities. In general, a leased employee is any person who is not an employee of the recipient and who provides services to the recipient if—

(A) such services are provided pursuant to an agreement between the recipient and a leasing organization,

(B) such person has performed such services for the recipient (or for the recipient and related persons) on a substantially full-time basis for a period of at least 1 year, and

(C) such services are performed under primary direction or control by the recipient.

These rules were designed to prevent employers using independent contractors to avoid the inclusion of individuals in benefit plans.

Finally, Congress gave the IRS broad regulatory authority to issue guidance to treat other relationships as controlled groups.

#### The Effect of the Rules on Small Employer

Many businesses develop as an entrepreneur sees an opportunity to provide a product or service. Often the businesses do not develop within the same industry and thus industry norms regarding the provision of employee benefits, including employer provided health care, are not the same. For instance, software engineers often enjoy employer provided healthcare, while retail workers and restaurant workers typically do not. It is easier to remain competitive in an industry if compensation and benefit arrangements conform to industry norms. Thus, as the entrepreneur expands into different industries it is often difficult if not impossible to use a compensation structure different than the majority of the industry.

In addition, small employers cannot as easily negotiate the purchase of health benefits for workers or self-insure benefits as they have fewer covered lives. This limits the entrepreneur's ability to provide health care.

#### A Better Alternative

Any time a test consists of specific levels, percentages or amounts, such as certain ownership percentages, there are two consequences: (1) complexity and (2) planning to avoid the "bright line" tests. With the requirement that qualified plans meet certain nondiscriminatory coverage and benefits rules, "bright line" tests make sense from a tax point of view. The tests contained in sections 414(b), (c), (m) and (o) have become increasingly complicated as Congress and the IRS have sought to prevent taxpayers from circumventing the qualified plan rules by changing stock ownership percentages. After the Tax Court upheld the structuring of arrangements to avoid aggregation, Congress adopted the affiliated service group rules and granted the IRS the authority to adopt any other rules necessary to eliminate the opportunity for taxpayers to avoid the rules. It is not appropriate to apply this test to determine the size of a business and which employees must be offered minimum essential coverage under the health care law.

Applying these controlled group rules, affiliated service group rules and leased employee rules to determine whether an employer is subject to the shared responsibility rules would appear to be a convenient approach because it is an existing set of rules. These rules, however, are exceedingly complicated and well understood by only a small subset set of tax practitioners. Applying the qualified plan aggregation rules does not take into account the different purpose of the Affordable Care Act employer mandate from the retire-

ment plan coverage and discrimination rules. Offering retirement plans is not mandated and thus, when the entrepreneur decides to offer a retirement plan, it is understood that the business aggregation rules will apply. The shared responsibility rules mandate the provision of health benefits. Applying the same business aggregation rules to a mandated benefit that exist for purposes of preventing discrimination for voluntary employer provided benefits can lead to inefficient and unwanted economic behavior. This behavior constrains a small business and may lead to unwanted and unwelcome business decisions including not hiring additional works that ensure the small business is not subject to the rules. This is the same behavior that has been exhibited by larger businesses, attempting to limit workers to less than 30 hours per week.

By its very nature, this is a rule that employers will be clearly under or clearly over, something that by its very nature changes continually as businesses grow or decline. While the test has to be applied every year, it is only relevant for businesses that are not clearly above the at least 50 employee threshold. Those clearly above or below do not need to make any calculations. Thus, for any year, the test only affects a limited number of taxpayers and the taxpayers affected each year change as businesses develop or decline. However, as noted above, taxpayers that are approaching the 50 full time equivalent employee mark may decide to delay hiring to delay application of this rule.

A facts and circumstances test, focusing on a specific individual's (or group of individuals) control of business decisions is a better aggregation test for mandated employer provided health benefits. With a facts and circumstances test, the employer will be able to determine whether the 50 full time equivalent test is met and which employees need to be covered without having to know detailed ownership information of investors and related parties, and without the cost of having to hire expensive outside consultants. Differences in industry norms can also be taken into account. The statute can include a non-exclusive list of items that need to be considered in determining who is in control of the business. Investors who had no control of day-to-day operations of the business would not need to be aggregated. Examples include the individual who makes hiring and firing and purchasing decisions and sets sales prices. By focusing on day-to-day operations, the business would be defined by the industry or industries with which an individual is involved regularly. Similarly, if a spouse were not involved with day-to-day operations of the other spouse's business, the businesses of each spouse would not be aggregated.

As with a bright line test, with a facts and circumstances test, taxpayers and the IRS have the responsibility of making a determination of whether businesses should be aggregated. The taxpayer would evaluate the facts and circumstances of each business and a determination would be made. By using a facts and circumstances determination, the opportunity to plan to avoid bright line tests is not available. A facts and circumstances test will use business activities and characteristics with which the small business operator is familiar. As there is sometimes no clear-cut answer, many people will be more rather than less conservative in

making a determination. That determination would be subject to audit by the IRS. IRS, through its enforcement process will need to understand the facts and circumstances that lead to a specific conclusion and taxpayers will need to support their conclusions.

Facts and circumstances tests, by their very nature, are less likely to be applied abusively than bright line tests. With a facts and circumstances test, individuals would understand the situation and make a determination regarding the whether the employer should be aggregated as an employer operating a business or whether 2 business operations should be viewed separately. The Employee Stock Ownership Plan (ESOP) rules offer a good example of rules intended to limit abuses that were circumvented as never expected. Under those rules determining whether the ESOP is structuring arrangements to avoid the payment of taxes involved the conversion of benefits to synthetic equity and an understanding of ownership including synthetic equity.

Facts and circumstances tests are used in many situations for determining the application of tax rules. One that comes to mind readily are the worker classification rules, determining whether someone is a common law employee or independent contractor. Those rules are set forth in regulations and other IRS guidance. In general, an employer has the right to control not only the amount of work to be done by an employee, but also how it is to be performed. This is not the case with an independent contractor. The name given to a service provider, the number of hours worked, how an individual is paid are not important.

Revenue Ruling 87-41 outlines 20 factors that need to be considered in determining whether a service recipient exercises enough control over a service provider for an employee or independent contractor relationship to exist. The ruling specifically states that not all of the factors have equal weight and that not all need to be present. Rather the factors are guides to help in determining the likelihood that someone is more closely characterized as an employee or independent contractor. While tax practitioners do structure arrangements with workers so that the classification is more likely to be certain, there is no bright line test or assurance that can be applied. Since Revenue Ruling 87-41 was issued, the IRS has outlined three categories of factors that should be considered in conjunction with the revenue ruling. These factors are behavioral control, financial control and relationship of the parties.

While this is a facts and circumstances determination, the IRS does have a process whereby either service providers or service recipients can file a request for determination of worker status by filing a Form SS-8. This form asks a number of questions regarding the relationship. In making the determination, IRS requests information from both parties and makes a final, binding decision regarding worker status. If a facts and circumstances test is applied for determining the employer for providing minimal essential coverage, a similar determination process could also be developed to all workers and service recipients to have certainty with respect to the determination.

The IRS had to address the definition of employer under these rules in the tax-exempt context. Because tax exempt organizations do not have owners, an alternative rule was devised and this test gives some examples of the types of activities that are viewed as indicators of control. Notice 89-23 specified, among other things, that in the tax exempt arena, the controlled group included each entity that provides directly or indirectly at least 80% of the contributing employer's operating funds and there is a degree of common management or supervision between the entities. A degree of common management or supervision exists if the entity providing the funds has the power to appoint or nominate officers, senior management or members of the board of directors (or other governing board) of the entity receiving the funds. A degree of common management or supervision also exists if the entity providing the funds is involved in the day-to-day operations of the entity.

Final regulations adopting the rules detailed in this guidance have since been adopted. Specifically those regulations provide, among other things, that common control exists between an exempt organization and another organizations if at least 80 percent of the directors of trustees of one organization are either representatives of, or directly or indirectly controlled by, the other organization. A trustee or director is treated as a representative of another exempt organization if he or she also is a trustee, director, agent, or employee of the other exempt organization. A trustee or director is controlled by another organization if the other organization has the general power to remove such trustee or director and designate a new trustee or director. Whether a person has the power to remove or designate a trustee or director is based on facts and circumstances. To illustrate, if exempt organization A has the power to appoint at least 80 percent of the trustees of exempt organization B (which is the owner of the outstanding shares of corporation C, which is not an exempt organization) and to control at least 80 percent of the directors of exempt organization D, then entities A, B, C, and D are treated as the same employer. While these rules have a bright line 80% test, they also indicate the type of activities that could be considered in determining whether control exists.

The qualified separate line of business rules also use a similar rule, allowing employers to determine that certain businesses qualified as separate lines of businesses and thus do not have to be aggregated for determining qualified plan coverage and discrimination testing. In general, a line of business is a portion of an employer that is identified by the property or services it provides to customers of the employer. The employer is permitted to determine the lines of business it operates by designating the property and services that each of its lines of business provides to customers of the employer.

A separate line of business is a line of business that is organized and operated separately from the remainder of the employer. The determination of whether a line of business is organized and operated separately from the remainder of the employer is made on the basis of objective criteria. These criteria generally require that the line of business be organized into one or more separate organizational units (e.g., corporations, partnerships, or divisions), that the

line of business constitute one or more distinct profit centers within the employer, and that no more than a moderate overlap exist between the employee workforce and management employed by the line of business and those employed by the remainder of the employer. There are rules for determining whether a line of business is organized and operated separately from the remainder of the employer and thus constitutes a separate line of business. These rules include an optional rule for vertically integrated lines of business.

A qualified separate line of business must satisfy the three statutory requirements including a notice requirement and a requirement to pass administrative scrutiny. A separate line of business may satisfy this administrative scrutiny rule by using a regulatory safe harbor or by requesting and receiving an individual determination from the IRS that the separate line of business satisfies the requirement of administrative scrutiny.

Finally, some small businesses may be making annual determinations of the employer for qualified plan purposes and could easily use that for determining the employer for health care reform. The facts and circumstances test could be offered as an alternative to the mechanical tests used for qualified plan purposes. For those businesses already relying on this test, certainty would exist.

To summarize, the mechanical tests used for qualified plan discrimination testing are overly complex and understood for only a limited number of tax professionals. A small business would not be able to apply those rules without professional help and many of the advisers to small business would not be familiar with the rules. In addition, the definition of employer for determining whether an employer has at least 50 employees and which workforce needs to be offered minimal essential coverage is a test that most businesses will only need to run for a few years during their life cycle. It is a mandated test and not at est that is voluntarily assumed when a retirement plan is offered to workers. As businesses come close to the 50-employee limit, the additional cost of mandated health benefits will be considered in evaluating business expansion. For these reasons, a facts and circumstances test, focusing on the businesses that an individual operates on a day-to-day basis makes more sense. The statute or committee reports could list characteristics of management control and taxpayers would be able to make a judgment regarding what operations should be considered part of the employer. This determination would be subject to audit by the IRS, as all tax determinations are.

**Formal Written Statement**

**United States House of Representatives -- Small Business Committee**

**Health Reform's "Applicable Large Employer" Standards**

**&**

**Effect of Controlled Group Rules on Small Business**

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**December 4, 2013**

**Focus: Use of Tax Code Aggregation Rules to Determine Size for Application of the Play or Pay Requirement under PPACA**

The health reform law applies existing Tax Code rules on controlled groups when determining employer size. The health reform law only applies to an "Applicable Large Employer" (some refer to them as "ALE") which is generally any employer "who employed an average of at least 50 full-time employees on business days during the preceding calendar year.... All persons treated as a single employer under subsection (b), (c), (m), or (o) of section 414 of the Internal Revenue Code of 1986 shall be treated as 1 employer." Those Section 414 rules, in turn, use the definition of controlled groups under Internal Revenue Code Section 1563(a).

The health reform law included this reference to controlled group rules for two main reasons:

1. To prevent employers from separating companies to avoid health reform requirements, and
2. To make certain companies subject to the law while smaller ones are exempt (an employer size rule is usually necessary, as you know).

This discussion is very high-level as its purpose is to create an awareness of the issue of controlled groups in the context of health reform. For additional reference, attached at the end are excerpted pages from a Tax Exempt and Government Entities discussion on "Controlled and Affiliated Service Groups" posted by the Internal Revenue Service on its website and available in its entirety at the following address: <http://www.irs.gov/pub/irs-tege/epchd704.pdf> The pages

shared here as excerpts here are representative of the issues the controlled group rules will raise, and omission of certain pages is simply for ease of reference and brevity in printed materials. Review of the complete item at the website is encouraged.

### **Commentary on Awareness, Complexity, and Confusion**

**Awareness:** While setting a size rule is necessary, as noted above, the controlled group rules continue to catch many smaller businesses unaware. These rules do apply to businesses in other contexts, but typically that is because of an action the employer has itself undertaken, such as creation of a 401(k) retirement plan. Why is the application of the rule different here?

- As with many provisions of the Tax Code, *public policy often requires businesses to “agree” to a trade off when voluntarily offering an employee benefit*; if they want to take advantage of the tax treatment for retirement plan contributions, the related employers must consider common control within the group and must treat the employees fairly across the entire group to the extent the law and regulations require. To state the effect of the main rules very simply, the controlled group rules affect which employers are considered for discrimination testing, and whether enough non-highly compensated employees are covered.
- The dynamic is different in the health reform context...these rules will apply due to a federal *requirement to provide a benefit*. The application of the controlled group rules means many small companies that have been created, maintained, and operated separately – as permitted by current tax ID numbers and the operation of other federal rules – now must be considered together.

Larger employers and some groups of smaller employers with complex corporate structures will tend to have advisors that identify the issue for them: in-house counsel, outside counsel, tax advisors such as Certified Public Accountants, or sophisticated employee benefits consultants or brokers.

However, employer awareness among small employers is lacking if they do not have these relationships. These employers may not have had the need to retain legal counsel, even via a law firm, except for specific projects, and those projects may not have involved persons with the right sort of experience to readily identify and resolve a complex tax issue.

Smaller employee benefits consulting and brokerage firms simply do not have the revenue to justify either retention of a law firm or employment of a compliance officer who might identify the issue for their clients. With the delays in the law and challenges, many advisors and employers similarly have delayed investing the capital and effort to address these issues, with many expecting at various times (including at present) that the rules would be repealed or delayed yet again.

**Complexity:** The complexity involves the somewhat mechanical application of the law. Many well-advised employers have sought the opinion of legal or tax counsel. Analysis of a simple corporate design or ownership arrangement might require 2-3 hours of work by experienced advisors, costing roughly \$1,200 based on estimates provided by a range of private law firm attorneys. More complex arrangements might be addressed with more time required, perhaps at a cost of \$2,000 to \$3,000.

The challenge is not so much the cost as *identification* of the issue. Most small employers are not aware of the issue. As noted above in the awareness discussion, we encounter small and even large businesses on a weekly basis who are unaware of the need to consider whether separate companies, divisions, etc. should be counted for purposes of determining employer size and applicability of the law.

The law applies to determine if seemingly separate employers would be treated as one employer for purposes of counting the number of employees to determine if the health reform Play or Pay rules apply. The decision is made to combine certain entities using rules under Tax Code Section 414(b), (c), (m), and (o), respectively:

- A controlled group of corporations
- A group of trades or businesses under common control
- An affiliated service group
- Certain other arrangements described in regulations

The first two bullets are often called the controlled groups rules even though they form just part of the picture, and include a parent-subsidiary analysis under Section 414(b) and brother-sister control analysis under 414(c), as well as a determination of whether there is a combination of the two types of control. Affiliated service group rules (the third bullet point, above) in 414(m) were added later to capture other employment relationships created by other arrangements. Finally, the last bullet point is a catch-all of sorts, written in part to address whether certain arrangements like employee leasing should affect retirement plans and other controlled group issues.

The controlled group rules apply differently under the four different Section 414 subparagraphs. The factors generally include percentages of ownership of either shares of voting stock or total value. (Once the status of the group as a single organization is determined, then the number of employees – full-time employees and part-time equivalents – must be counted; that issue is addressed later in this discussion on pages 5 & 6.)

#### *A Controlled Group of Corporations (Section 414(b))*

One of the easier situations is a controlled group of corporations via *stock ownership with a common parent* (Section 414(b)), but even this analysis requires an outside advisor. There is common control if:

- One or more of the corporations in the group owns (either directly or indirectly) 80% or more of the total combined *voting power* of all voting classes of stock (or 80% or more of the *total value* of all shares of all classes of stock) of each of the corporations, except the common parent corporation; and

- The common parent corporation owns, directly or indirectly, at least 80% of the total combined voting power of all classes of stock entitled to vote (or 80% or more of the total value of shares of all classes of stock) of at least one of the other corporations.

Ownership analysis is complicated by sub-rules which often make it more likely the group will be held in common control, such as disregarding stock held by other subsidiaries when determining if the parent owns the required percentage of stock of one subsidiary.

*A Brother-Sister Controlled Group Arrangement (Section 414(c))*

The rules become more complex under *brother-sister controlled group rules*. Again, an outside advisor is needed.

Brother-sister firms are companies that meet a two-part test:

- First, five or fewer individuals, estates, or trusts own (directly or indirectly) stock with at least 80% of the total combined voting power of all classes of stock entitled to vote or at least 80% of the total value of all shares of all classes of stock.
- If that threshold is met, then one must determine if those same five or fewer individuals, estates, or trusts have stock with at least 50% of the total voting power of all classes of stock or at least 50% of the total value of all shares of all stock. The stock ownership of each owner for the 50% rule is taken into account only to the extent the owner's ownership interest is identical with respect to each corporation.

These two sets of rules on stock ownership with a common parent and brother-sister controlled groups are also applied together (called a *combined group of corporations*) if each employer is in one of the two types of groups and one of them is a common parent of the parent-subsidiary controlled group and also is in the brother-sister controlled group.

Related Rules on Attribution of Ownership: Sometimes ownership is attributed to (counted toward) the ownership interests of someone else. For corporations, ownership of at least 5% in stock value means the corporation is owned by that person. Options to own stock are treated as actual ownership. According to experts in the area of controlled group rules and employee benefits, addressing ownership options is one of the trickiest areas of actual application of the law, requiring analysis of the underlying agreements relating to those options. As with so many other aspects of the controlled group rules, these arrangements and their formalizing documentation were not written or structured to address their impact other aspects of the business. The smaller the business, the more likely that is to be the case.

Similar rules and challenges apply to partnerships relative to interests in profits or capital, whichever is greater.

Family businesses create more complexity, especially when children or other descendants of the founders begin to have ownership interests. An individual is treated as also having any ownership interests of his children under 21 and (usually) of his or her spouse. If an individual has "effective control" of an organization, then he or she is considered to own interests of his parents, grandparents, grandchildren, and children (even if over age 21).

Then, at this point in the analysis, certain ownership interests are excluded but only if the result is to increase (not decrease) the ownership interests in another entity: ownership by certain employees, retirement plans, exempt organizations, deferred compensation plans, and certain interests in subsidiaries of 5% owners, officers, partners, or fiduciaries of the parent organization.

*Affiliated Service Groups (Section 414(m))*

As with the above rules, all employees of an affiliated service group under Tax Code Section 414(m) must be treated as employed by the same employer. The impact of these rules extends beyond retirement plan rules to welfare benefits such as life insurance, health plans, fringe benefits, cafeteria plans (employee pre-tax benefit plans), and continuation coverage (called COBRA) just to name a few. The affiliated service group rules were enacted to prevent circumvention of the two other controlled group rules when ownership of related companies was arranged in an artificial manner.

These related companies might perform services for another organization in the same group, or may provide management functions such as managing operations or human capital.

Attribution rules also apply to affiliated service groups; they are similar to those discussed for the more basic controlled group provisions. These additional attribution rules are beyond the scope of this discussion.

*Side Notes on Specific Types of Employers*

**Tax Exempt Organizations:** These entities are generally treated as under common control if at least 80% of the directors or trustees of one organization are either representatives of or are directly or indirectly controlled by the other organization.

**Foreign Parents:** U.S. corporations owned by a foreign parent would be considered part of the same controlled group for tax purposes under final regulations to Section 1563(a) which affects the analysis under Tax Code Section 414 subparagraphs as noted above. As a result, for example, if a French firm, group of investors, or family has sufficient ownership interests in 8 small businesses in the United States, the employees of those U.S. employers would be counted together for determining whether the employer as a whole has 50 or more employees and whether health reform applies to those 8 businesses.

**Confusion:** Even employers that do identify controlled group issue and have the requisite analysis performed still are met with many barriers to compliance. As with other aspects of health reform, these pitfalls arise because of the complexity of the systems addressed by reform, practical impacts of the law that policymakers did not foresee, and the loopholes the current law leaves open for either avoidance or interpretation.

**No Coordination of Payroll, Time Tracking, and Other Systems:** Many small businesses that health reform will impact do not have the existing infrastructure or any sort of coordinated systems to correctly and consistently track the required information necessary to determine if the group has 50 or more employees, much less to offer benefits across the population on a consistent basis.

Small businesses with different but related employers will not have a common HR department, a common payroll system, a common way to track and count employee hours, or even a single person who has

access to all such information across the group. They can usually work out the designation of a person, who then becomes the central point person responsible for requesting and compiling the information.

In the case of the health reform Play or Pay rules, the controlled group as a whole will need to have a determination made of which employees across the group are truly full-time (expected to work 30 or more hours a week) and which employees are not expected to be full-time but whose hours must be counted to determine full-time equivalents). The full-time equivalent determination requires an employer subject to the law to add all the hours worked by non-full-time employees in a month, then divide by 120 to determine the number of full-time employees it would have needed to work the same number of hours. That number of full-time equivalents is then added to the number of true full-time employees to determine if the employer or controlled group of employers is subject to the law.

If a group of employers is treated as one employer and is determined to be subject to the requirement to offer coverage, the practicalities noted below affect any given entity's ability to do. Diligent members of these combined small employers worry about whether the health benefits *can* be and *will* be offered consistently across the group. Some of our clients have met with outright resistance from other owners of related companies. ***Common control under the tax rules does not really equate to actual control over another firm within the same controlled group.*** Again, the level of cooperation is usually higher in the context of retirement plans, which the different employers often all wish to offer. Thankfully, the penalties, if imposed, will be isolated to that employer tax identification number (EIN). Small employers still fear the impact of a group-wide audit triggered by an uncooperative commonly "controlled" employer.

**Inability to Comply with Other Federal and State Laws:** The current guidance will put many employers in an untenable position: comply with one law (health reform) but to do so, you must violate another federal law and potentially some state requirements.

The controlled group rules under health reform (as they apply through Sections 4980H and 414 of the Tax Code and discussed above) are not consistent with Department of Labor rules and interpretations regarding control concepts and the status of an employer as a single entity or a multiple employer entity. While the above IRS rules are complex, the DOL rules are old and quite incomplete. While there are federal agency approval processes in place for retirement plans which provide employers with a greater sense of security, there are no similar processes for welfare plans like group health plans offered by employers. (Health plan coverage through an employer is considered a "welfare" plan because it provides for the well-being of a covered employee and his or her family members.)

Under other federal rules, health plans must only provide health insurance or health plan coverage to employees of related companies; otherwise, the plan is considered a MEWA, or Multiple Employer Welfare Arrangement as defined in Section 3(40) of ERISA. The DOL has not yet issued proposed regulations under that long-standing section of the law. While at times the DOL has indicated an intent to follow the Tax Code rules, they have cited different levels of required common ownership and also, for example, have alluded to a need for a substantial business purpose for common control. The uncertainty associated with the lack of guidance leaves employers at risk if they are to comply with Tax Code and health reform rules, but if they must do so in a manner that appears to be at odds with DOL interpretations.

Self-funded plans face even greater risks from state insurance regulators. Quite often, states will declare MEWAs to be illegal or will require them to be capitalized and licensed as insurance companies. We are now seeing groups with very few employees self-fund their plans, and that certainly now includes small businesses. State laws often say that it is illegal for employers that are not closely related enough to provide benefits to all of their employees under a single plan. Many states have taken that position in part because of firms that promise to self-fund health plan benefits for unrelated employers, often through arrangements that sound legitimate such as “unions,” but which are not ever intended to pay the promised benefits.

**Inability to Obtain Insurance:** Insurance carriers have already refused to offer insurance to groups that the law would treat as a single, or commonly controlled, employer.

Despite all the market reforms of health care reform, insurance carriers retain significant leeway to not offer insurance to small employers that collectively are subject to the health reform requirement.

Insurance carriers remain able to impose their own traditional – or new – rules regarding common ownership/control. Many insurance carriers already are refusing to provide insurance to groups of technically related smaller businesses based on the insurance carrier’s internal rules regarding which groups they will or will not write. The health insurance carriers may do so based on a number of factors (a practice which the health reform law neither addresses nor forbids), such as business ownership levels and location.

A proposed solution is not offered at the agency level because a regulatory fix likely is not possible without a change to statutory wording.

**Inability to Provide Insurance Once Offered:** Insurance carriers impose participation requirements at present. These following concerns affect small and large businesses alike, but the impact is worse for small employers – especially when they are connected as part of a controlled group where they may not operate jointly for other matters. A participation requirement means an insurance carrier may let the employer offer their insurance company’s health plan policy, but if not enough employees sign up, the insurance carrier has the right, contractually, to “pull the policy.” The carrier is under no obligation to actually provide the offered insurance.

Conversely, the insurance carrier may require the employer to pay a certain percentage of the total premium costs for the employee-only coverage or for family coverage or both. In some cases, the insurance carrier may require the employer to pay for the entire cost of single coverage, which is significantly more than the 9.5% rule and related safe harbors would require an employer to pay under the law.

Employees with other coverage often don’t count against either requirement, but because of the family glitches in the law, many employers will not provide spouses with health insurance on the same basis as in the past, and in some cases, employers won’t offer coverage to spouses at all. (The law does not allow coverage for family members to be affordable, and only children must be offered coverage with the employee, not spouses.)

In the small group context, the federal agencies have stated in regulatory and other guidance that the carriers may still impose participation requirements. The answer is expected to be the same in the context

of the large group market (defined as the market for insurance for groups with 50 or more employees or over 100 employees, depending on how the state defines the market size). Treasury Department attorneys have indicated informally they believe they have identified a way to prevent this result, but the statutory “hook” appears to be absent.

If an employer offers a policy as required by the law and the insurance carrier will not actually issue the policy because of a low level of employee participation, is the employer (small or large) subject to the fine when it is impractical / impossible to provide the coverage? Many benefits attorneys fear the answer is the penalties under the Play or Pay rules would still apply. Relief from this result would be very welcome.

Discrimination: The new health reform law requires the Treasury Department / IRS to issue and impose nondiscrimination rules on fully-insured plans similar to those imposed on self-funded group health plans. Smaller employers tend to have insured health plans and will be subject to those rules once issued, presumably on a controlled group basis. However, as noted above, insurance carriers tend to have significant leeway to interpret the rules under health reform and are not themselves subject to the discrimination rules. Depending on the location and specific situation of an employer, compliance with these to-be-issued rules across a controlled group should prove unwieldy, especially if there is common ownership but a lack of cooperation which unfortunately is often the case with very independent entrepreneurs and distantly related family members.

Additional Questions Suggested for Discussion:

What Else in Health Reform Raises Grave Concerns fro Employers?

For Individuals?

Are Employers Modifying Their Ownership to Avoid Health Reform?

Do Employers have the Guidance they Need to Prepare for 2015? What is the Timing for that Compliance?

**Definition: Controlled Group**

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**Section 414(b) and (c)** The controlled group definition is found in section 414(b) & (c). Section 414(b) covers controlled group consisting of corporations and defines a controlled group as a combination of two or more corporations that are under common control within the meaning of section 1563(a).

All employees of companies in the controlled group must be considered to determine if a plan maintained by a controlled group member meets the requirements of sections 401, 408(k), 408(p), 410, 411, 415, and 416.

Section 414(c) applies to controlled group of trades or businesses (whether or not incorporated), such as partnerships and proprietorships. Since section 1563 was written only for corporations, Treasury Regulations 1.414(c)-1 through 1.414(c)-5 mirror the section 1563 controlled group principles.

The definitions and examples used in this chapter refer to both section 414(b) and 414(c) controlled groups.

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**Three Types of Controlled Groups** A control group relationship exists if the businesses have one of the following relationships:

- Parent-subsidiary,
- Brother-sister, and
- Combination of the above

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**Definition: Controlled Group, Continued****Parent-  
subsidiary  
Group**

A parent-subsidiary controlled group exists when one or more chains of corporations are connected through stock ownership with a common parent corporation; and

- 80 percent of the stock of each corporation, (except the common parent) is owned by one or more corporations in the group; and
- Parent Corporation must own 80 percent of at least one other corporation.

Sections 1563(a) and 414(b) and (c).

**Sections  
1563(a) and  
414(b) and (c)-  
Example 1**

The following examples illustrate the parent-subsidiary rules:

**Example 1**

Redwood Corporation owns:

- 90% of the stock of Bond Corporation,
- 80% of the stock of Greene Corporation, and
- 65% of the stock of Teller Corporation.

Unrelated persons own the percentage of stock not owned by Redwood Corporation.

Redwood Corporation owns 80% or more of the stock of the Bond and Greene Corporations. Therefore, Redwood Corporation is the common parent of a parent-subsidiary group consisting of Redwood, Bond, and Greene. Teller Corporation is not a member of the group because Redwood Corporation's ownership is less than 80%.

*Continued on next page*

**Definition: Controlled Group, Continued**

Sections  
1563(a) and  
414(b) and (c)-  
Example 1  
(continued)-  
Example 2

**Example 2**

Assume the same facts as in the previous example and assume further that Greene Corporation owns 80% of the profits interest in XYZ Partnership.

Redwood Corporation is the common parent of a parent-subsiary group consisting of Redwood, Bond, Greene and XYZ. The results would be same if Redwood Corporation, rather than Greene Corporation owned the 80% interest in XYZ.

**Brother- Sister  
Group**

A brother-sister controlled group is a group of two or more corporations, in which five or fewer common owners (a common owner must be an individual, a trust, or an estate) own directly or indirectly a controlling interest of each group and have "effective control".

- Controlling interest - 1.414(c)-2(b)(2) – generally means 80 percent or more of the stock of each corporation (but only if such common owner own stock in each corporation); and
- Effective control – 1.414(c)-2(c)(2) – generally more than 50 percent of the stock of each corporation, but only to the extent such stock ownership is identical with respect to such corporation.

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*Chapter 7- Controlled and affiliated service groups***Definition: Controlled Group, Continued**

**Example-  
Brother-Sister  
Ownership Test** Adams Corp and Bell Corp are owned by four shareholders, in the following percentages:

## Percentage of Ownership

Shareholder	Adams Corp	Bell Corp
A	80%	20%
B	10	50
C	5	15
D	5	15
<b>TOTAL</b>	<b>100%</b>	<b>100%</b>

To meet the first part of the test in section 1563(a)(2)(A), the same five or fewer common owners must own more than 80% of stock or some interest in all members of the controlled group.

In this example, the four shareholders together own 80% or more of the stock of each corporation, the first test is met, since the shareholders own 100% percent of the stock.

*Continued on next page*

*Chapter 7- Controlled and affiliated service groups***Definition: Controlled Group, Continued**

<b>50 Percent Test-Example</b>	<b>Shareholder</b>	<b>Identical Ownership Percentage in both Corps.</b>
	A	20%
	B	10
	C	5
	D	5
	TOTAL	40%

To meet the second part of the test in Section 1563(a)(2)(B), the same five or fewer common owners must own more than 50% of each corporation, taking into account the stock ownership of each person only to the extent such stock ownership is identical with respect to each such corporation.

In this example, although the four shareholders together own 80% or more of the stock of each corporation, they do not own more than 50% of the stock of each corporation, taking into account only the identical ownership in each corporation as demonstrated above.

*Continued on next page*

**Definition: Controlled Group, Continued****Example-  
Brother-Sister  
Group not  
established**

The following individuals each own 12% to 13% of the stock in Tate Corp and also Ward Corp.

<b>Individual Corp</b>	<b>Percentage of Tate Corp</b>	<b>Percentage of Ward Corp</b>
A	12	12
B	12	12
C	12	12
D	12	12
E	13	13
F	13	13
G	13	13
H	13	13

Any grouping of five of the shareholders will own more than 50% of the stock in each corporation and all shareholders in any of the groupings will own identical amounts.

But, Tate and Ward are not members of a brother-sister group because, the same five or fewer individuals do not own at least 80% of each corporation's stock.

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*Chapter 7- Controlled and affiliated service groups*

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**Definition: Controlled Group, Continued**

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**Combined Group** A combined group consists of three or more organizations that are organized as follows:

- Each organization is a member of either a parent-subsiary or brother-sister group; and
- At least one corporation is the common parent of a parent-subsiary; and is also a member of a brother-sister group.

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**Combined Group- Example** A is an individual owning:

- 80% in York Partnership; and
- 90% in Sharp Corporation

York Partnership owns 85% of Tripp Corporation

York Partnership, Sharp Corporation and Tripp Corporation are each members of the same combined group of trades or businesses under common control because

- York Partnership, Sharp Corporation, and Tripp Corporation are each members of either a parent-subsiary or a brother-sister group, and
- York is:
  - the common parent of the parent-subsiary group consisting of York and Tripp; and
  - A member of a brother-sister group consisting of York and Sharp.

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*Chapter 7- Controlled and affiliated service groups***Attribution Rules**

**Introduction** Attribution is the concept of treating a person as owning an interest in a business that is not actually owned by that person. Attribution may result from family or business relationships. Section 1563 attribution is used in determining a controlled group of businesses, under section 414(b) and (c).

**Important Note** Although the following attribution rules are written in terms of stock ownership, the same principles are applied for organizations that are not incorporated.

In the case of a:	Ownership relates to the:
Trust or estate	Actual interest
Partnership	Capital or profits
Sole proprietorship	Sole proprietorship

When calculating ownership interests, use the greater of:

- Corporate ownership – voting stock or value of stock
- Partnership ownership – capital or profits

**Section 1563 Attribution** Section 1563 contains the rules of attribution used to determine “control” for the following:

- Controlled groups of corporations (section 414 (b)); and
- Trades or businesses, whether or not incorporation, which are under common control (section 414 (c)).

Also see Treas. Reg. § 1.414(c)-4.

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*Chapter 7- Controlled and affiliated service groups***Attribution Rules, Continued****General Rules  
for Family  
Attribution**

The following table is a general description of how the family attribution rules are applied to controlled groups.

**Note:** the following family attribution rules only apply to a brother-sister controlled group and do not apply to a parent-subsidary controlled group.

THE OWNERSHIP INTERESTS OF:	Are attributed to:	
Spouse	Spouse	EXCEPTION: No attribution between spouses if there is no: <ul style="list-style-type: none"> <li>• direct ownership,</li> <li>• participation in company, and</li> <li>• no more than 50% of business gross income is passive investments. See 1.414(c)-4(b)(5)(ii).</li> </ul>
Minor child (under age 21)	Parent	
Parent	Minor child (under age 21)	
Parent	Adult child (age 21 or older)	ONLY IF: Adult child owns greater than 50% of that business.
Adult child	Parent	ONLY IF: Parent owns greater than 50% of that business.
Grandparent	Minor or Adult child	ONLY IF: Minor/Adult child owns greater than 50% of that business.
Minor or Adult child	Grandparent	ONLY IF: Grandparent owns greater than 50% of that business.
Sibling	None	None

*Continued on next page*

**Attribution Rules, Continued****Examples-  
family  
attribution**

The following examples illustrate the family attribution rules:

**Example 1-  
family  
attribution**

Ada and Barton are married. Barton is a doctor owning 100% of his medical practice. Ada is also a doctor and owns 50% of a separate medical practice (the other 50% is owned by an unrelated doctor).

Barton is not an employee or owner of a direct interest in Ada's practice and less than 50% of the gross income in Ada's practice is from passive investments. Barton, however, is in charge of significant management activities for his wife's practice.

Ada does not directly own an interest or participate in Barton's practice and less than 50% of the gross income from Barton's practice is from passive investments.

- Barton is attributed the 50% interest that Ada owns in her practice (due to his participation in Ada's practice).
- Ada is not attributed any ownership interest in Barton's practice.

**Example 2**

Clare, age 25 is the daughter of Dana. Dana owns 75% of XYZ Corporation and Clare own the remaining 25%.

Since Dana owns more than 50% of XYZ, her ownership is attributed to Clare.

Since Clare does not own more than 50% of XYZ, her ownership is not attributed to Dana.

*Continued on next page*

**Attribution Rules, Continued****General Rules for Organizational Attribution**

The following table is a general description of how the attribution rules for organizations are applied to controlled groups.

<b>The ownership interest:</b>	<b>Are attributed to:</b>
From a corporation to its shareholder  <ul style="list-style-type: none"> <li>• Applicable to brother-sister controlled group only.</li> </ul>	Corporate ownership interests attributed, proportionately *, <u>to shareholders (owning at least 5% of corporate stock).</u>
From a partnership to its partners  <ul style="list-style-type: none"> <li>• Applicable to brother-sister controlled group only.</li> </ul>	Partnership ownership interests attributed, proportionately *, <u>to partners having at least 5% or more capital or profits interest.</u>
From a trust to its beneficiaries  <ul style="list-style-type: none"> <li>• Applicable to brother-sister and parent-subsidiary controlled groups.</li> </ul>	Trust ownership interests attributed, proportionately *, <u>to beneficiaries having 5% or more actuarial interest.</u>
To an organization	None

**General Rules – Organizational Attribution**

\* The interest owned is proportionate to the individual's share of the organization's value.

For example, a shareholder's interest in a corporation is proportionate share of the total stock value of the corporation.

*Continued on next page*

**Attribution Rules, Continued**


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**Organizational Attribution Rules** The following examples illustrate the organizational attribution rules:

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**Example 1** Elliott owns 70% of the stock in the Fairfield Corporation. Grant owns 20% of the stock and four other individuals who each own less than 5% own the remaining 10%. The Fairfield Corporation has a 30% stock ownership in the Hale Corporation.

The Hale stock is attributed to Elliott and Grant in proportion to their ownership interests in the Fairfield Corporation as follows:

Elliott is treated as a 21% owner of Hale Corporation.

- 70% (interest in Fairfield) x 30% (Fairfield's interest in Hale)

Grant is treated as a .06 % owner of Hale Corporation.

- 20% (interest in Fairfield) x 30% (Fairfield's interest in Hale)

Since each of the four remaining shareholders of Fairfield Corporation own less than 5%, they are not treated as owning any interest in Hale Corporation.

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**Example 2** The Isanti Group is a partnership. Jay owns a 70% interest in Isanti, and Kendall owns a 30% interest. The Isanti Group owns 50% of the stock of Lake Investments Corporation.

The Lake stock is attributed to Jay and Kendall in proportion to their partnership interests in Isanti as follows:

Jay is treated as a 35% owner of Lake Corporation (70% x 50%).

Kendall is treated as a 15% owner of Lake Corporation (30% x 50%).

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*Continued on next page*

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**Attribution Rules, Continued**


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**Other Rules under Section 1563**

After an individual is attributed the ownership of a family member, the interest *does not get attributed from the individual to another family member.*

However:

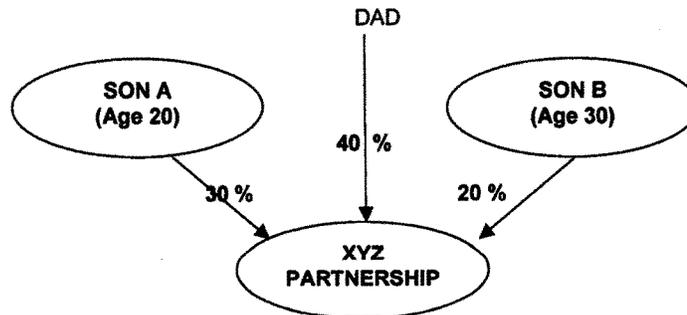
1. The ownership interests of an individual may be attributed *to more than one family member.*
2. After an individual is attributed the ownership of a corporation, partnership or trust, the interest may then be taken into account under other attribution rules.

Options to acquire stock are, generally, treated as stock ownership under IRC section 1563. Refer to Rev. Rul. 68-601 and *North American Industries, Inc. v. Commissioner*, 33 TCM 1275 (1974) for further information.

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**Example- Attribution to More than One Family Member-facts**

The following example illustrate attribution to more than one family member



An unrelated person owns the remaining interest in XYZ.

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*Continued on next page*

**Attribution Rules, Continued**


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<b>Dad-Ownership percentage</b>	<p>Dad is considered to own a total of 90% of the profits interest in XYZ Partnership as follows:</p> <ul style="list-style-type: none"> <li>• He directly owns 40% of XYZ Partnership,</li> <li>• He is considered as owning the 30% interest owned by minor Son A, and</li> <li>• He is also considered as owning the 20% interest of XYZ that is owned by his adult son. Note that generally, the stock ownership of family members who are 21 or older are not attributed to an individual. However, such attribution is required if the individual has effective control. Dad has more than a 50% ownership of XYZ. See 1.414(b)-4(b)(6).</li> </ul>
<hr/>	
<b>Son A</b>	<p>Son A is considered to own a total of 70% of the profits interest in XYZ:</p> <ul style="list-style-type: none"> <li>– He directly owns 30%, and</li> <li>– He is considered to own the 40% profits interest owned directly by Dad.</li> </ul> <p>Son A is not, however, considered to own the 20% owned directly by Son B (and attributed to Dad).</p>
<hr/>	
<b>Son B</b>	<ul style="list-style-type: none"> <li>– Son B is considered to own a total of 20% of the profits interest in XYZ:</li> <li>– He directly owns 20%, and</li> <li>– He is not considered to own the 40% interest of XYZ that is owned by his father. This is because Son B owns only 20% and he would have to own more than 50% in order for his father's interest to be attributed to him.</li> </ul>

*Continued on next page*

**Attribution Rules, Continued**

**Other Rules for Spousal Attribution under Section 1563** The following examples illustrate other spousal attribution rules

**Example 1**

Marian and Mitchell are the parents of Norton, age 25, and Oliver, age 20. Mitchell has a 45% interest in the Pitkin Corporation and his son, Norton, has a 55% interest.

**ATTRIBUTION BETWEEN SPOUSES:**

Marian is treated as owning Mitchell's 45% interest in Pitkin, assuming the spousal exception described above is not applicable.

**FAMILY ATTRIBUTION IS NOT FURTHER ATTRIBUTED TO ANOTHER FAMILY MEMBER:**

The 45% interest attributed to Marian is not further attributed to Oliver.

This rule would not prevent Mitchell's interest from being attributed to Oliver (see below).

**Example 2****FAMILY ATTRIBUTION RULES MAY BE APPLIED TO MORE THAN ONE FAMILY MEMBER:**

In addition to attributing Mitchell's 45% interest in Pitkin to his wife, Marian, using the rule for attribution between spouses, Mitchell's 45% interest is also attributed to Norton. Since Norton is over age 21 and owns more than 50% of Pitkin, Mitchell's ownership is attributed again to Norton under the family attribution rule for parents and adult children.

Since Oliver is under age 21, Mitchell's 45% interest may be attributed again to Oliver under the family attribution rule for parents and minor children.

**NO ATTRIBUTION BETWEEN SIBLINGS:**

The 55% interest owned by Norton is not treated as owned by Oliver.

*Continued on next page*

**Attribution Rules, Continued**

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**Example -  
Other Rules for  
Organizational  
Attribution  
under Section  
1563**

Assume the same facts as in Example 2. In addition, the Pitkin Corporation has a 50% interest in Rich and Riley, Inc. and Norton is married to Shannon.

**ATTRIBUTION RULES APPLIED AFTER ORGANIZATIONAL  
ATTRIBUTION:**

Norton is considered to own a 50% (100% x 50%) interest in Rich and Riley, Inc.

- Norton is treated as owning 100% of Pitkin (55% directly and 45% attributed from his father).
  - Shannon is attributed the 50% interest in Rich and Riley, Inc.
-

**Determination Letter Program: Controlled Group Plans**


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**Background** The Employee Plans (EP) Determination Letter Program provides a means whereby plan sponsors may submit their plans to the Service for review. The Service reviews the form of the plan and, if the plan sponsor elects, reviews certain operational features as well. If the plan meets the qualification requirements under 401(a) of the Internal Revenue Code (Code), a favorable determination letter is issued to the plan sponsor. The letter gives the employer reliance on the form of plan.

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**Controlled Group Pension Plans** When the sponsor of a qualified retirement plan is part of a controlled group, all employers of the group must be treated as a single employer to determine if a plan meets the requirements of sections 401, 408(k), 408(p), 410, 411, 415, 416, and 417.

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**Rev. Proc 2004-6 : Required Information** When a plan sponsor submits a determination letter application (Forms 5300, 5307, 5310 and 6406), question 6 on the applications, asks if the employer is a member of a controlled group or affiliated service group.

If question 6 is answered "Yes", Rev. Proc. 2004-6 provides certain information about the controlled group. The EP Specialist should secure for review the following information (if not present with the application):

1. All members of the group;
  2. Their relationship to the plan employer;
  3. The type(s) of plan(s) each member has; and
  4. Plans common to all members.
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**Overview: Affiliated Service Group**

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**Introduction** As you have learned, section 414(b) and (c) require that all employees of commonly controlled corporations or trades or businesses be treated as employees of a single corporation or trade or business.

By arranging the ownership of related business entities in an artificial manner, the definition of "control" under section 414(b) and (c) and the aggregation rules established by ERISA could be circumvented. In addition, the basic rule that employee plans provide an exclusive benefit for employees or their beneficiaries could be violated.

Section 414(m) was enacted to prevent such circumvention by expanding the idea of control to separate, but affiliated, entities. Proposed Treas. Reg. § 1.414(m) provides that all employees of the members of an affiliated service group shall be treated as if a single employer employed them.

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**Objectives** At the end of this section, you will be able to identify situations where the plan sponsor is a member of an affiliated service group and recognize the impact on qualified plans. Therefore, you will be able to:

1. Describe the relationship between employers and determine if an affiliated service group exists.
2. Describe the relationship between a first service organization and an A-Organization and determine whether an affiliated service group exists.
3. Describe the relationship between a first service organization and a B-Organization and determine whether an affiliated service group exists.
4. Describe a management organization situation and determine whether an affiliated service group exists.
5. Determine how these relationships affect the status of qualified plans.
6. Describe the procedure for processing a affiliated service group determination letter request.

Describe other employer/employee relationships, such as leased employees, impendent contractors, professional employee organization and management organization

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## Affiliated Service Group

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**History** The *Kiddie v. Commissioner* 69 T.C. 1055 (1978) and *Garland v. Commissioner* 73 T.C. 5 (1979) cases addressed the issue of control. The Tax Court held that where a controlled group situation did not exist, it would not be necessary to aggregate employees for purposes of testing for coverage and discrimination.

IRC § 414(m) was enacted to expand the idea of control to separate, but affiliated, entities. Proposed Treas. Reg. § 1.414(m) provides that all employees of the members of an affiliated service group shall be treated as if they were employed by a single employer.

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**Definition** An affiliated service group is one type of group of related employers and refers to two or more organizations that have a service relationship and, in some cases, an ownership relationship, described in IRC section 414(m). An affiliated service group can fall into one of three categories:

1. A-Organization groups (referred to as "A-Org"), consists of an organization designated as a First Service Organization (FSO) and at least one "A organization",
  2. B-Organization groups (referred to as "B-Org"), consists of a FSO and at least one "B organization", or
  3. Management groups.
- 

**First Service Organization** An FSO must be a "service organization":

- Performance of services is the principal business of the organization as defined in section 414(m)(3), and Proposed Treas. Reg. § 1.414(m)-2(f).
  - "Organization" refers to a corporation, partnership, or other organization.
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**Affiliated Service Group, Continued**

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**A-Org** To be an A-Org, an organization must satisfy a two-part test:

– Ownership Test

The organization is a partner or shareholder in the FSO (regardless of the percentage interest it owns in the FSO) determined by applying the constructive ownership rules as specified in section 318(a), and

– Working Relationship Test

- The organization "regularly performs services for the FSO," or
- Is "regularly associated with the FSO in performing services for third parties.

Facts and circumstances are used to determine if a working relationship exists. See Proposed Treas. Reg. § 1.414(m)-2(b).

See section 414(m)(2)(A).

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*Chapter 7- Controlled and affiliated service groups***Affiliated Service Group, Continued**

- B-Org** To be a B-Org, the organization must meet the following requirements:
- A significant portion of its business must be the performance of services for a FSO, for one or more A-Org's determined with respect to the FSO, or for both,
  - The services must be of a type historically performed by employees in the service field of the FSO or the A-Org's, and
  - Ten percent or more of the interests in the organization must be held, in the aggregate, by persons who are highly-compensated employees (pursuant to IRC § 414(q)) of the FSO or A-Org.

A B-Org need not be a service organization.

See IRC § 414(m)(2)(B).

**Performance of Services** The principal business of an organization will be considered the performance of services if capital is not a material income-producing factor for the organization, even though the organization is not engaged in a field listed in Proposed Treas. Reg. § 1.414-(m)-2(f)(2) .

Whether capital is a material income-producing factor must be determined by reference to all the facts and circumstances of each case. In general, capital is a material income-producing factor if a substantial portion of the gross income of the business is attributable to the employment of capital in the business as reflected, for example, by a substantial investment in inventories, plant, machinery or other equipment.

Capital is a material income-producing factor for banks and similar institutions.

Capital is not a material income-producing factor if the gross income of the business consists principally of fees, commissions or other compensation for personal services performed by an individual.

*Continued on next page*

**Affiliated Service Group, Continued**

**Specific fields** Regardless of whether the above subparagraph applies, an organization engaged in any one or more of the following fields is a service organization:

- Health,
- Law,
- Engineering,
- Architecture,
- Accounting,
- Actuarial science,
- Performing arts,
- Consulting, and
- Insurance.

**An organization will not be considered as performing services**

An organization will not be considered as performing services merely because:

- It is engaged in the manufacture or sale of equipment or supplies used in the above fields,
- It is engaged in performing research or publishing in the above fields, or
- An employee provides one of the enumerated services to the organization or other employees of the organization, unless the organization is also engaged in the performance of the same services for third parties.

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*Chapter 7- Controlled and affiliated service groups***Affiliated Service Group, Continued**

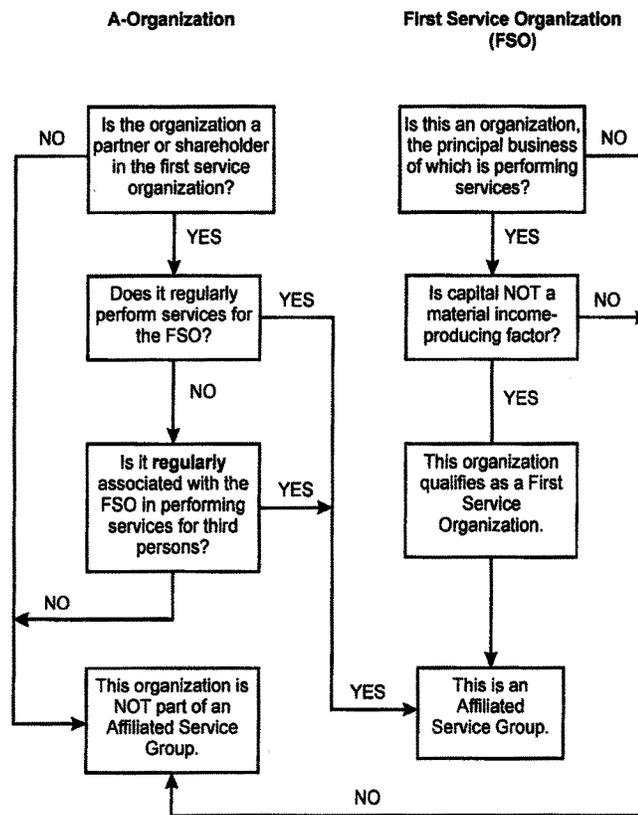
<b>Commissioner may determine other specific fields</b>	The Commissioner may determine that a specific business field, not enumerated in the proposed regulations, is engaged in performing services. In this case, the above list will be expanded, but only prospectively.
<b>“Organization” defined</b>	<p>The term "organization" includes a sole proprietorship, partnership, corporation or any other type of entity, regardless of its ownership format.</p> <p>A bona fide expense-sharing arrangement, in which the parties involved share the cost of the office overhead but are not working in unison for common business purposes, would not be considered an organization. These costs would include rent, supplies, maintenance and employees' salaries.</p>
<b>Historically Performed</b>	Services will be considered of a type historically performed by employees in a particular service field if it was not unusual for the services to be performed by employees of organizations in that service field (in the United States) on December 13, 1980.
<b>Professional Service Corporations</b>	<p>All the employees of professional service corporations that are members of an affiliated services group shall be aggregated together and treated as if they were employed by a single employer for purposes of the employee benefit requirements.</p> <p>A professional service corporation:</p> <ul style="list-style-type: none"> <li>- Is a corporation that is organized under state law for the principal purpose of providing professional services,</li> <li>- Has at least one shareholder who is licensed or otherwise legally authorized to render the type of services for which the corporation is organized, and</li> <li>- Provides the services performed by certified or other public accountants, actuaries, architects, attorneys, chiropodists, chiropractors, medical doctors, dentists, professional engineers, optometrists, osteopaths, podiatrists, psychologists and veterinarians. The Commissioner may expand the list of services.</li> </ul>

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**Affiliated Service Group, Continued**

Flowchart

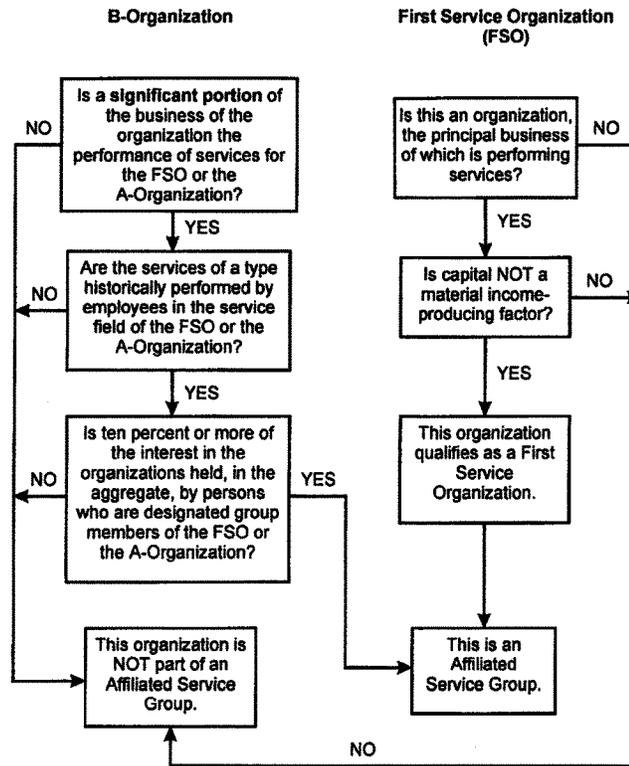
**Affiliated Service Group**



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Flowchart

**Affiliated Service Group**



**Affiliated Service Group, Continued**


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**Section 414(m)-  
Example** Allen Averett, a doctor, is incorporated as Allen Averett, P.C. and this professional corporation is a partner in the Butler Surgical Group. Allen Averett and Allen Averett, P.C., are regularly associated with the Butler Surgical Group in performing services for third parties.

The Butler Surgical Group is an FSO. Allen Averett, P.C. is an A-Org because it is a partner in the medical group and is regularly associated with the Butler Surgical Group to perform services for third parties.

Accordingly, Allen Averett, P.C. and the Butler Surgical Group would constitute an affiliated service group.

As a result, the employees of Allen Averett, P.C. and the Butler Surgical Group must be aggregated and treated as if they were employed by a single employer per section 414(m).

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**First Service  
Organization  
and an A-Org-  
Example**

The Everett, Furman and Guilford Partnership is a law partnership with offices in numerous cities. EFG of Capital City, P.C., is a corporation in Capital City that is a partner in the law firm. EFG of Capital City, P.C. provides paralegal and administrative services for the attorneys in the law firm. All of the employees of the corporation work directly for the corporation, and none of them work directly for any of the other offices of the law firm.

The law firm is an FSO. The corporation is an A-Org because it is a partner in the FSO and is regularly associated with the law firm in performing services for third parties.

The corporation and the partnership would together constitute an affiliated service group. Therefore, the employees of EFG of Capital City, P.C. and the employees of The Everett, Furman and Guilford Partnership must be aggregated and treated as if they were employed as a single employer per section 414(m).

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**Affiliated Service Group, Continued****First Service Organization and a B-Org-Example**

Reinhardt & Associates is a financial services organization that has 11 partners. Each partner of Reinhardt owns one percent of the stock in Asbury Corporation. Asbury provides services to the partnership of a type historically performed by employees in the financial services field. A significant portion of the business of Asbury consists of providing services to Reinhardt.

Considering Reinhardt & Associates as an FSO, the Asbury Corporation is a B-Org because:

1. A significant portion of its business is in the performance of services for the partnership of a type historically performed by employees in the financial services field. And,
2. More than 10% of the interests in the Asbury Corporation is held, in the aggregate, by the highly-compensated employees of the FSO (consisting of the 11 common owners of Reinhardt and Associates).

Accordingly, the Asbury Corporation & Reinhardt and Associates constitute an affiliated service group. Therefore, the employees of the Asbury Corporations and Reinhardt and Associates must be aggregated and treated as if they were employed by a single employer per section 414(m).

**Non Service Organization-Example**

Dade Properties, Inc. sells land that it has purchased and developed. Craig is a 25% shareholder of Dade and a 50% shareholder of Craig and Son Construction Company, Inc. Dade Properties regularly engages the services of Craig and Son. Although it appears that Dade Properties could be an FSO, the affiliated service group rules do not apply because Dade Properties is not a service organization.

**Affiliated Service Group: Performance of Service**

**Significant Portion** Proposed Treas. Reg. § 1.414(m)-2(c)(2) specifies that whether providing services (for the FSO, for one or more A-Org's or for both,) is a "significant portion" of the business of an organization will be based on the facts and circumstances.

The following tests may be used to substantiate the facts and circumstances:

- Service Receipts Safe Harbor Test, and
- Total Receipts Threshold Test.

For additional information, see Proposed Treas. Reg. § 1.414(m)-2(c)(2).

**Service Receipts Safe Harbor** The performance of services for the FSO, for one or more A-Org's, or for both, will not be considered a significant portion of the business of an organization if the "service receipts percentage" is less than five percent.

- The "service receipts percentage" is the ratio of:
  1. Gross receipts of the organization derived from performing services for the FSO, for one or more A-Org's, or for both, to
  2. Total gross receipts of the organization derived from performing services.
- This ratio is the greater of:
  1. the ratio for the year for which the determination is being made, or
  2. the ratio for the three-year period including that year and the two preceding years (or the period of the organization's existence, if less).

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*Chapter 7- Controlled and affiliated service groups*

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**Affiliated Service Group: Performance of Service, Continued**

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**Total Receipts  
Threshold Test** The performance of services for the FSO, for one or more organizations, or for both, will be considered a significant portion of the business of an organization if the "total receipts percentage" is ten percent or more.

The "total receipts percentage" is calculated in the same manner as the service receipts percentage, except that gross receipts in the denominator are determined without regard to whether they were derived from performing services.

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**Affiliated Service Group: Performance of Service, Continued****Service receipts- Example**

The income of Cascade Corporation is derived from performing both services and other business activities. The amount of its total receipts and its receipts derived from performing services and its total receipts from Starr Corporation and from all customers is provided below:

	Origin of Income	All Customers	Starr Corp.
Year 1	Services	\$ 100	\$ 4
	Total	\$120	
Year 2	Services	150	9
	Total	180	
Year 3	Services	200	42
	Total	240	

**Service Receipts Percentage**

In Year 2, the services receipts percentage is the greater of:

1. The ratio for that year ( $\$9/\$150$ , or 6%), or
  2. For Years 1 and 2 combined ( $\$13/\$250$ , or 5.2 %).
- = 6%

The total receipts percentage is the greater of:

1. The ratio for that year ( $\$9/\$180$ , or 5%), or
  2. For Years 1 and 2 combined ( $\$13/\$300$ , or 4.3%).
- = 5%

The services receipts percentage is greater than 5% and, therefore, the Service Receipts safe harbor is not met.

The total receipts percentage is less than 10% and, therefore, the Total Receipts threshold test is not met.

As a result, for Year 2, facts and circumstances is used to determine whether performing services for Starr Corporation constitutes a significant portion of the business of Cascade Corporation.

**Affiliated Service Group: Performance of Service, Continued**

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**Total Receipts  
Percentage**

In Year 3, the services receipts percentage is the greater of:

1. the ratio for that year (\$42/\$200, or 21%), or
  2. for Years 1, 2, and 3 combined (\$55/\$450, or 12.2%).
- = 21%.

The total receipts percentage is the greater of:

1. the ratio for that year (\$42/\$240, or 17.5%), or
  2. for Years 1, 2, and 3 combined (\$55/\$540, or 10.2%).
- = 17.5%

Because the total receipts percentage is greater than 10% and the services receipts percentage is not less than 5%, a significant portion of the business of Cascade Corporation is considered to be the performances of services for Starr Corporation.

For Year 3, therefore, the Cascade Corporation and the Starr Corporation are part of an affiliated service group within the meaning of section 414(m), and the employees of both corporations must be aggregated and treated as if they were employed by a single employer.

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**Affiliated Service Group: Performance of Service, Continued**

**Example-Total Receipts, Percentage Test** Marsha Mesa owns one-third of an employee benefits consulting firm, Benefits by Marsha. Marsha also owns one-third of an insurance agency, Mesa, Long and Toole Insurance Agency. A significant portion of the business of Benefits by Marsha consists of assisting the Mesa, Long and Toole Insurance Agency in developing employee benefit packages for sale to third persons and providing services to the insurance company in connection with employee benefit programs sold to other clients of the Mesa, Long and Toole Insurance Agency.

Additionally, Benefits by Marsha frequently provides services to clients who have purchased insurance arrangements from the Mesa, Long and Toole Insurance Agency for the employee benefit plans they maintain. Mesa, Long and Toole Insurance Agency frequently refer clients to Benefits by Marsha to assist them in the design of their employee benefit plans. Twenty percent of the total gross receipts of Benefits by Marsha represent gross receipts from the performance of these services for the Mesa, Long and Toole Insurance Agency.

Considering Mesa, Long and Toole Insurance Agency as a FSO, Benefits by Marsha is a B-Org because:

- A significant portion of the business of Benefits by Marsha (as determined under the total receipts percentage test) is the performance of services for Mesa, Long and Toole Insurance Agency of a type historically performed by employees in the service field of insurance, and
- More than 10% of the interests in Benefits by Marsha is held by owners of the Mesa, Long and Toole Insurance Agency.

Thus, Mesa, Long and Toole Insurance Agency and Benefits by Marsha constitute an affiliated service group, and the employees of both companies must be aggregated and treated as if they were employed by a single employer.

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**Affiliated Service Group: Performance of Service, Continued**

**Example-Gross Receipts Derived from Performing Services** Calvin Cameron is a 60% partner in Decatur, a service organization, and regularly performs services for Decatur. Cameron is also an 80% partner in Fleming Brothers. A significant portion of the gross receipts of Fleming Brothers is derived from providing services to Decatur of a type historically performed by employees in the service field of Decatur.

If Decatur is an FSO, then Fleming Brothers would be a B-Org because:

- A significant portion of gross receipts of Fleming Brothers is derived from performing services for Decatur of a type historically performed by employees in that service field, and
- More than 10% of the interests in Fleming Brothers is held by a highly-compensated employee, Calvin Cameron (who is a common owner of Decatur).

Accordingly, Decatur and Fleming Brothers constitute an affiliated service group. Additionally, the employees of Decatur and Fleming Brothers are aggregated under the rules of section 414(c). Thus, any plan maintained by a member of the affiliated service group must satisfy the aggregation rules of section 414 (c) and 414 (m).

The aggregation rules of section 414(c) and 414(m) require all employees of the "employer" to be aggregated and treated as if they were employed by a single employer. The "employer" is Decatur and Fleming Brothers.

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NATIONAL  
**RESTAURANT**  
ASSOCIATION



Statement  
On behalf of the  
National Restaurant Association

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HEARING: THE HEALTH CARE LAW, THE EFFECT OF THE BUSINESS AGGREGATION  
RULES ON SMALL EMPLOYERS

BEFORE: COMMITTEE ON SMALL BUSINESS  
U.S. HOUSE OF REPRESENTATIVES

BY: ELLIS WINSTANLEY  
CEO, TRADELOGIC CORPORATION

DATE: DECEMBER 4, 2013

**Statement for the hearing  
"The Health Care Law, The Effect of the Business  
Aggregation Rules on Small Employers"**

**Before the**

**Committee on Small Business,  
U.S. House of Representatives**

**By  
Ellis Winstanley,  
CEO,  
Tradelogic Corporation**

**On behalf of the  
National Restaurant Association**

**December 4, 2013**

Chairman Graves, Ranking member Velazquez, and members of the House Committee on Small Business; thank you for the opportunity to testify today on the effect of the business aggregation rules included in the health care law, on small businesses like mine.

My name is Ellis Winstanley, CEO of Tradelogic Corporation, and I own a variety of small businesses in Austin, Texas, with my brother, parents, and partners. I'm honored to share the perspective of my companies, especially my restaurants, on behalf of the National Restaurant Association.

**OUR COMPANIES**

I am a business executive with a successful track record of starting up, turning around and growing businesses in the hospitality, construction, software, printing & promotion products, and apparel industries. My brother and I are entrepreneurs who got started in this business while we were students at the University of Texas. We currently own eight restaurants with our partners, which I oversee on a day to day basis. We are partnered together with our parents in two construction and three printing and promotional products businesses which support the restaurant operations. We also own two software development companies, one of which is Tradelogic Corporation, that also serves as our management company. My brother and I are known for rescuing local and historical small restaurant brands, and turning them around to maintain their place in the community as job creators.

### **THE RESTAURANT AND FOODSERVICE INDUSTRY**

The National Restaurant Association is the leading trade association for the restaurant and foodservice industry. Its mission is to help members like me establish customer loyalty, build rewarding careers, and achieve financial success. The industry is comprised of 980,000 restaurant and foodservice outlets employing 13.1 million people who serve 130 million guests daily. Restaurants are job-creators. While small businesses comprise the majority of restaurants, the industry as a whole is the nation’s second-largest private-sector employer, employing about ten percent of the U.S. workforce.<sup>1</sup>

The unique characteristics of our workforce create compliance challenges for restaurant and foodservice operators within this law. It’s difficult for restaurants to determine how the law impacts them and what they must do to comply. Many of the determinations employers must make to figure out how the law impacts them – for example the aggregation rules and the applicable large employer determination – are much more complicated for restaurants than for other businesses that have more stable workforces with less turnover.

Restaurants are employers of choice for many looking for flexible work schedules and the ability to pick up extra shifts as available. As a result, we employ a high proportion of part-time and seasonal employees. We are also an industry of small businesses — more than seven out of ten eating and drinking establishments are single-unit operators. Much of our workforce could be considered “young invincibles,” as 43 percent of employees are under age 26.<sup>2</sup> Hence, high turnover is the norm. In addition, the restaurant business model produces relatively low profit margins of only four to six percent before taxes, with labor costs being one of the most significant line items for a restaurant.<sup>3</sup>

Business owners crave certainty, because it enables us to plan for the future and make decisions that benefit our employees, customers, and communities. One of the most difficult things to predict about the impact of this law is the choices employees will make.

Will they accept restaurant operators’ offers of coverage more than they do today?

Will our young workforce choose to pay the individual mandate tax penalty instead of accepting the employer’s offer of coverage in 2015, 2016 and beyond?

Will exchange coverage be less expensive than what is currently available and can operators afford to offer under the law?

With the younger, healthier population of the workforce, we may find that more team members will favor the tax penalty because it is less expensive than employer-sponsored coverage. This provides less certainty for employers to predictively model.

<sup>1</sup> 2013 *Restaurant Industry Forecast*.

<sup>2</sup> Bureau of Labor Statistics, U.S. Department of Labor.

<sup>3</sup> 2013 *Restaurant Industry Forecast*.

*COMPLYING WITH THE HEALTH CARE LAW IS CHALLENGING FOR RESTAURANT AND FOODSERVICE OPERATORS GIVEN THE UNIQUE CHARACTERISTICS OF THE INDUSTRY*

Since the law was enacted in 2010, the National Restaurant Association has taken steps to educate America's restaurants about the requirements of the law and the details of the Federal agencies' guidance and regulations. Through the National Restaurant Association Health Care Knowledge Center website ([Restaurant.org/healthcare](http://Restaurant.org/healthcare)), we offer one place where restaurant operators of every size can go to better understand the law's requirements and determine its impact on their employees and businesses.

The National Restaurant Association has actively participated in the regulatory process, from the beginning, to ensure that the implementing regulations and Federal agencies' guidance consider the implications for businesses that are not just one type or size. As co-leaders of the Employers for Flexibility in Health Care (E-Flex) coalition, we have partnered with other businesses and organizations with similar workforce characteristics. Together we advocate for greater flexibility and options within the implementing regulations, especially for those that employ many part-time, seasonal, or temporary employees.

The overarching challenge restaurant and foodservice operators face in complying with the law is to first understand its complicated and interwoven requirements. By far, the definition of "full-time employee" under the law poses the greatest challenge. It does not reflect current workforce practices and could have a detrimental impact on a restaurant operator's ability to offer flexible schedules for his or her employees.

In addition, the applicable large employer determination is too complex. It stifles smaller employers' ability to manage their workforces, expand their businesses and prepare to offer health care coverage. Finally, the automatic enrollment provision could cause financial hardship and greater confusion about the law for some employees, without increasing their access to coverage.

All of these factors combine to complicate what a restaurant and foodservice operator must consider when adapting their business to comply with the law.

**EMPLOYER AGGREGATION RULES**

To determine if an employer is considered a large or small employer under the health care law (and if large then subject to the Employer Shared Responsibility<sup>4</sup> and Reporting of Employer Health Insurance Coverage<sup>5</sup> provisions) an employer must first determine who the employer is. This may seem like a simple determination but due to the structure of many restaurant companies – separate legal entities owned by many of the same partners, and often

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<sup>4</sup> Internal Revenue Code §4980H.

<sup>5</sup> Internal Revenue Code §6056.

family businesses – determining the employer is more complicated than many expect in the restaurant industry.

Section 1513(c)(2)(C) of the health care law lays out Rules for Determining Employer Size. Subsection (i), Application of Aggregation Rule for Employers, states that "All persons treated as a single employer under subsection (b), (c), (m), or (o) of section 414 of the Internal Revenue Code of 1986 shall be treated as 1 employer." Section 414, (b), (c), (m), (o) of the Tax Code is often referred to as the Common Control Clause.

This is the first section of the health care law employers must look at to begin determining how the law impacts them and their businesses. Typically it is smaller employers in the restaurant industry who are unsure and struggling to understand how these complicated aggregation rules apply to them. Because the rules are so complicated they must consult a tax professional to help them determine the impact of the law, even at the very first step. Larger businesses, where each entity could be considered an applicable large employer on their own, are less concerned about determining if they are one or multiple employers. They are not struggling to understand these complicated rules as smaller employers are in the industry.

These rules have been part of the Tax Code for years, but this is the first time that many restaurateurs, especially smaller operators, have had to understand how these complicated regulations apply to their businesses. The Treasury Department has not issued, nor to our knowledge plans to issue, regulatory guidance that could be used by smaller operators to understand how Section 414 (b), (c), (m), (o) might apply to them without having to consult a tax professional. The Department of Treasury's Proposed Rule on Employer Shared Responsibility issued January 2, 2013, discusses how the aggregation rules apply when determining the size of an employer's workforce, but does not explain how to determine whether a group of businesses are one or multiple employers. On their website, the Internal Revenue Service (IRS) mentions that certain affiliated employers with common ownership or those part of a controlled group must aggregate employees. It also states that the regulation and that FAQs are available for employers on their website<sup>6</sup>, however the FAQ page, last reviewed or updated July 18, 2013, states that "Updated questions and answers will be posted soon"<sup>7</sup> and provides no additional information about the aggregation rules.

Given the lack of easily understood guidance, restaurant and food service operators are forced to hire expensive tax advisors to determine how the complicated rules and regulations associated with this section of the Tax Code apply to their specific situations. Like me, very often entrepreneurs own multiple restaurant entities with various partners, often with family members. Though these restaurateurs consider each operation to be a separate small business, many are discovering that, for the purposes of the health care law, all of the businesses can be considered one employer due to common ownership.

<sup>6</sup> <http://www.irs.gov/uac/Affordable-Care-Act-Tax-Provisions-for-Employers>, 12/2/2013.

<sup>7</sup> <http://www.irs.gov/uac/Newsroom/Questions-and-Answers-on-Employer-Shared-Responsibility-Provisions-Under-the-Affordable-Care-Act>, 12/2/2013.

**EFFECT OF THE AGGREGATION RULES ON SMALL BUSINESSES**

The application of these aggregation rules to determine the employer for the purposes of the health care law is having an impact on small businesses. Businesses, who consider themselves small, must consult a tax professional to determine if they are one or multiple employers, or they assuming they are one employer and an applicable large employer. Most of our small businesses each have less than 50 full-time employee equivalents, and independently would not be considered applicable large employers. Two of our restaurants are highly seasonal businesses and may or may not be considered applicable large employers depending on the calendar month. We are located in a college town and our customer traffic flow and hence staffing levels fluctuate depending on whether the University of Texas is in session or on break. For those restaurants, even if they are large for a few months, the seasonal exemption to the applicable large employer determination may apply if we were allowed to consider each legal entity independently.<sup>8</sup> If the seasonal exemption would apply, the two highly seasonal restaurants may also not be considered large if they were considered as separate entities. However, since my brother and I are partners and own our businesses with family members and other common partners, I believe we will be considered as one employer under the law and must consider all of the employees in all of our businesses as one group.

I have not consulted a tax professional but instead have tried to determine myself if we are considered one or multiple employers under the law. Based on my own understanding of the aggregation rules, we will be one employer and hence an applicable large employer subject to the Employer Shared Responsibility and Reporting of Employer Health Insurance Coverage provisions, among others.

The impact of the aggregation rules, and hence our status as an applicable large employer, will have an impact on each of our small businesses. Simply, the cost of doing business for each will increase, yet they must be able to stand on their own. Labor costs are typically one-third of a restaurant's expenses.<sup>9</sup> Operators only have a finite dollar amount to spend on labor costs given thin margins, including employee benefits such as health insurance coverage, and must manage these costs closely to remain viable. In the end, our status as an applicable large employer as a result of the aggregation rules means we must be extremely careful with our labor dollars and it will impact our decision-making going forward.

Since the recession, everyone has been tightening their belt to manage these costs and in Austin, we are still very much feeling the impact. This puts pressure on the staff, our vendors, our pricing, and in the end our customers. I see the cost associated with offering health care coverage as only adding to that pressure.

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<sup>8</sup> Applicable large employer status for calendar year 2015 is determined by measuring January 1 – December 31, 2014. See Applicable Large Employer Determination section.

<sup>9</sup> 2013 Restaurant Industry Forecast.

**OTHER SECTIONS OF THE LAW OF IMPACTING RESTAURANTS**

In addition to the aggregation rules, there are several other sections of the law that impact restaurant operators and small businesses. The cost of offering coverage continues to be a top concern for small businesses like me. It remains difficult to project and budget for the cost of coverage even next year. I'm also concerned about the administrative burden that compliance with the law will impose on my businesses. I fear that the administrative cost will be almost as expensive as the coverage itself, which includes having to educate our staff on the law and our health insurance coverage offerings.

***APPLICABLE LARGE EMPLOYER DETERMINATION***

Once a restaurant or foodservice operator determines what entities are considered one employer, they must determine their applicable large employer status annually. For larger employers, it may be clear that they have more than 50 full-time equivalent employees employed on business days in a calendar year. However, many small businesses will have to complete this calculation annually to determine their responsibilities under the law. That is not so easy given the number of employees' hours of service that must be tracked due to the labor intensive nature of the restaurant and foodservice business.

Unfortunately, operators on the cusp of 50 full-time equivalent employees are struggling to understand how to complete this complicated calculation each year. An employer must consider each employee's hours of service in all 12 calendar months each year. Immediately after they achieve this cumbersome calculation at the end of the year, they must begin to offer coverage January 1<sup>st</sup>.

Smaller restaurant and foodservice operators need clarification on when such employers must offer coverage in future years. Will small businesses just reaching the applicable large employer threshold on December 31, 2015, for example, be able to offer coverage a day later on January 1, 2016? Currently, the law does not allow any time to shop for coverage or conduct open enrollment once a small employer determines they are now a large employer. Congress should allow small businesses an administrative period between determining large employer status and offer of coverage, before it creates further confusion, especially in the second year of implementation and beyond.

The applicable large employer determination is complicated. Employers must determine all employees' hours of service each calendar month, calculate the number of FTEs per month, and finally average each month over a full calendar year to determine the employer's status for the following year. The calculation is as follows:

1. An employer must first look at the number of *full-time employees* employed each calendar month, defined as 30 hours a week on average or 130 hours of service per calendar month.
2. The employer must then consider the hours of service *for all other employees*, including part-time and seasonal, counting no more than 120 hours of service per

person. The hours of service for all others are aggregated for that calendar month and divided by 120.

3. This second step is added to the number of full-time employees *for a total full-time equivalent employee* calculation for one calendar month.



4. An employer must complete the same calculation for the remaining 11 calendar months and average the number over 12 calendar months to determine their status for the following calendar year.

This annual determination is administratively burdensome, especially for those employers just above or below the 50 FTE threshold who must most closely monitor their status – most likely smaller businesses. Many restaurant operators rely on third-party vendors to develop technology or solutions to help them comply with these types of requirements but, in addition to the added costs and time this requires, vendors are backlogged and solutions are not easily accessible at this time.

Congress should simplify this calculation and help small businesses more easily determine their status under the law. A more workable definition of large employer is needed as the current calculation stifles smaller employers' ability to manage their workforces, plan to expand their businesses, and prepare to offer health coverage if they are not already doing so.

*OFFERING COVERAGE TO FULL-TIME EMPLOYEES*

The health care law requires employers subject to the Shared Responsibility for Employers provision to offer a certain level of coverage to their full-time employees and their dependents, or face potential penalties. The statute defines a full-time employee as someone who averages 30 hours a week in any given month.

This 30-hour threshold is not based on existing laws or traditional business practices. In fact, the Fair Labor Standards Act does not define full-time employment. It simply requires employers to pay overtime when nonexempt employees work more than a 40-hour workweek. As a result, 40 hours per week is generally considered full-time in many U.S. industries. In the restaurant and foodservice industry, operators have traditionally used a 40-hour definition of full-time. Adopting such a definition in this law would also provide employers the flexibility to comply with the law in a way that best fits their workforce and business models.

Compliance based on a 30-hour a week definition is further complicated by the fact that, for restaurant and foodservice operators who are applicable large employers, it is not easy to predict which hourly staff might work 30 hours a week on average and which will not. Hourly employees are scheduled for more or less hours depending on several factors, including customer traffic flows.

One reason so many Americans are drawn to restaurant jobs is the flexibility to change your hours to suit your own personal needs. However, under this law, for the first time, the federal government has drawn a bright line as to who is considered full-time and who is considered part-time. As a result, employers with variable workforces and flexible scheduling must alter their practices and be very deliberate about scheduling hours. The reason being that the law imposes a greater financial impact than before in the form of potential liability for employer penalties if employees who work full-time hours are not offered coverage. If the definition is not changed to align with workforce patterns, the flexibility so many employees value will no longer be as widely available in the industry. This could result in significant structural changes to our labor market.

The National Restaurant Association supports efforts, such as Senators Susan Collins' and Joe Donnelly's bipartisan bill S. 1188, Congressman Todd Young's bill H.R. 2575, and Congressman Dan Lipinski's bipartisan bill H.R. 2988, that would define a full-time employee under the Affordable Care Act as someone working 40 hours or more a week.

We appreciate that the Treasury Department, in its January 2, 2013 proposed rule on the Employer Shared Responsibility, recognized that it may be difficult for applicable large employers to determine employees' status as full-time or part-time on a monthly basis, causing employee churn between employer coverage and the exchange or other programs. Such coverage instability is not in our employees' best interests. We are pleased that the Lookback Measurement Method is an option that applicable large employers may use.

While the Lookback Measurement Method's implementing rules are complex, it could be helpful for both employers and employees. Employers will be better able to predict costs and accurately offer coverage to employees as required. Employees whose hours fluctuate (variable hour and seasonal employees) have the peace of mind of knowing that if their hours do decrease from one month to the next, coverage will not be cut short before the end of their stability period.

*CHALLENGES FOR APPLICABLE LARGE EMPLOYERS OFFERING COVERAGE TO THEIR FULL-TIME EMPLOYEES AND THEIR DEPENDENTS*

Once an applicable large employer has determined to whom coverage must be offered, he or she must make sure that the coverage is of 60 percent minimum value and considered affordable to the employee, or face potential employer penalties.

Minimum value is generally understood to be a 60 percent actuarial test; a measure of the richness of the plan's offered benefits. This is a critical test for employers especially relating to what the employer's group health plan covers and hence what the premium cost will be in 2014. Business owners strive for certainty, and that means the ability to plan for their future costs.

Employers are eager to know what their premium costs will be under the new law. Minimum value is necessary to determining that information.

On February 25, 2013 the Health and Human Services Department included the Minimum Value Calculator, one of the acceptable methods to determine a plan's value, in its Final Rule: Standards Related to Essential Health Benefits, Actuarial Value, and Accreditation. Minimum value can now be determined using this calculator or other options, but it is still difficult to anticipate premium costs this far in advance.

Why? Rates are not usually available until a few months before the employer's plan year begins because insurance companies provide quotes based on the most current data with the greatest amount of claims history. This gives operators a short timeframe to budget and make business decisions in advance of the new plan year. Restaurant operators are eager to see premiums for 2014 and better evaluate the impact and costs associated with the employer requirements for voluntary compliance, and then full implementation in 2015.

Applicable Large Employers must also ensure at least one of their plans is affordable to their full-time employees or face potential penalties. A full-time employee's contribution toward the cost of the premium for single-only coverage cannot be more than 9.5 percent of their household income to be considered affordable. Employers will not know household income – which the statute specifies as the general standard – nor do they want to know this information for privacy reasons. Hence, employers needed a way to estimate before a plan is offered if it will be affordable to employees or potentially trigger an employer penalty.

What employers do know are the wages they pay their employees. Almost always, employees' wages will be a stricter test than household income. Employers are begrudgingly willing to accept a stricter test in the form of wages so that they know they are complying with the law and are provided protection from penalty under a safe harbor. The Treasury Department's proposed rule allows employers to use one of three Affordability Safe Harbors based on Form W-2 wages, Rate of Pay or Federal Poverty Line. The option of utilizing these methods will be helpful to employers as they determine at what level to set contribution rates and their ability to continue to offer coverage to their employees.

We encourage policymakers to address the cost of coverage so that the employer-sponsored system of health care coverage will be maintained, and businesses aren't forced to choose between plans they cannot afford and penalties they cannot afford.

#### *NONDISCRIMINATION RULES NOW WILL APPLY TO FULLY-INSURED PLANS*

The health care law applies the nondiscrimination rules that currently apply to self-funded plans to fully-insured plans in the future. These rules state that a plan cannot offer benefits in favor of their highly-compensated individuals over other employees. This rule is not in effect as the Treasury Department has put implementation on hold until further guidance has been issued in this complex area. Under the law, these rules apply to all insured plans, regardless of whether they are offered by an applicable large employer or a small business. I am watching this rule closely as it could impact our future plan offerings and compliance with the law.

Current group health plan participation rules often force operators to carve out the group of employees who will participate in the plan.<sup>10</sup> However, in many restaurateurs' experience, these are almost always a group that would be considered in the top 25 percent based on compensation.

Management carve-outs are not just for upper level executives who may receive richer benefit plans than the rest of the employees. In the restaurant and foodservice industry, management-only plans are sometimes the only option that operators have to provide health care coverage to those employees who want to buy it and pass participation requirements at the same time. As a result, these plans are quite common in the industry.

The rules the Treasury Department writes to apply non-discrimination testing to fully-insured plans could have an impact on our industry. Regardless of how they are written, restaurant and foodservice operators will need sufficient transition time to apply these rules as it could create upheaval for plans and employers alike.

#### *APPLICABLE LARGE EMPLOYER REPORTING REQUIREMENTS*

The employer reporting requirements are a key area of implementation for employers: the required information reporting under Tax Code §6055 and §6056 from the Internal Revenue Service and the Treasury Department. These employer reporting requirements are a critical link in the chain of the law's implementation. They represent what could be a significant employer administrative burden and compliance cost.

The Administration's July 2<sup>nd</sup> announcement and subsequent July 9<sup>th</sup> IRS Notice 2013-45 provides transition relief and voluntary compliance in 2014 for the Employer Reporting requirements under Tax Code Sections 6055 and 6056, and hence the Employer Shared Responsibility requirements under Tax Code Section 4980H.

The restaurant and foodservice industry welcomes this transition relief after asking the Administration and Congress for more time to receive, understand, and comply with the complex implementing regulations for Employer Reporting under Sections 6055 and 6056. As early as October 2011, the National Restaurant Association, as part of the E-Flex coalition, submitted comments to the Administration requesting transition relief and time to implement the reporting requirements under Tax Code Sections 6055 and 6056 once the rules were issued. The proposed rule from the Treasury Department concerning Tax Code Section 4980H was published in the *Federal Register* on January 2, 2013 to implement the employer mandate, and employers finally

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<sup>10</sup> The participation rate requirement cannot be applied for plans beginning on or after January 1, 2014 as guaranteed issue and guaranteed renewability apply in the individual, small group and large group markets. See Department of Health and Human Services Final Rule: Patient Protection and Affordable Care Act; Program Integrity; Exchange, Premium Stabilization Programs, and Market Standards; Amendments to the HHS Notice of Benefit and Payment Parameters for 2014, *Federal Register*, October 30, 2013.

received the critical proposed rules on Tax Code Sections 6055 and 6056 in early September 2013.

Employers need the rules for these reporting requirements to set up the systems that will track data on each full-time employee and their dependents to then report this data to the IRS annually. While the first report was not originally required to be submitted to the IRS until January 31, 2015, six months (July-Dec 2013) was too short a time frame for employers to receive the rule, set up systems or engage vendors to develop information technology systems that would begin tracking the necessary data as of January 1, 2014. We welcome the transition relief<sup>11</sup> that will allow restaurant operator to understand the rules and then implement the law.

On September 9, 2013, the IRS published the Proposed Rules on Information Reporting by Applicable Large Employers on Health Insurance Coverage Offered Under Employer-Sponsored Plans (IRC §6056) and Information Reporting of Minimum Essential Coverage (IRC §6055). The proposed rule on IRC §6056 suggests a general reporting method, which asks applicable large employers to tabulate and track offers of coverage by employee and dependent tax identification number, by calendar month. This will only add to the administrative burden of compliance with the law for applicable large employers, especially for smaller operators. While simplified methods are suggested in the proposed rule, it is not likely restaurant operators will be able to utilize these on a large scale due the characteristics of our workforce.

#### CONCLUSION

Since enactment of the law, the industry has worked to constructively shape the implementing regulations of the health care law. Nevertheless, there are limits to what can be achieved through the regulatory process alone. Ultimately, the law cannot stand as it is today given the challenges restaurant and foodservice operators face in implementing it.

We ask you to simplify the applicable large employer determination and remove the unnecessary burdens on small businesses, who must closely track their status from year-to-year. This includes a close look at how the aggregation rules apply to small businesses such as mine. The effect of the aggregation rules, and hence our status as an applicable large employer, is that the cost of doing business for each of my small businesses will increase.

Congress must address key definitions in the law: The law should more accurately reflect restaurant and foodservice operators' needs – and our employees' desire for flexible hours.

Consider the impact the administrative burden of the law will have on small businesses like mine as we work to implement the law. The Reporting of Employer Health Insurance Coverage under IRC §6056 will certainly add to the cost of compliance as well.

<sup>11</sup> "Continuing to Implement the ACA in a Careful, Thoughtful Manner," Mark Mazur, Treasury Notes Blog, July 2, 2013: <http://www.treasury.gov/connect/blog/Pages/Continuing-to-Implement-the-ACA-in-a-Careful-Thoughtful-Manner.aspx>

While I did not discuss it in detail in my testimony today, we ask you to also eliminate the duplicative automatic enrollment provision for larger employers with 200 or more full-time employees. It has the potential to confuse and financially harm employees while burdening employers, without increasing employee's access to coverage.

Thank you again for the opportunity to testify before you today regarding the health care law and the effects of the business aggregation rules on small businesses like mine.

We are both proud and grateful for the responsibility of serving America's communities – creating jobs, boosting the economy, and serving our customers. We are committed to working with Congress to find solutions that foster job growth and truly benefit the communities we serve.

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Testimony of:

Donna Baker, CPA  
Donna Baker & Associates LLC  
Adrian, Michigan

Before the

Committee on Small Business  
United States House of Representatives

December 4, 2013

The Honorable Sam Graves (R-MO), Chairman  
The Honorable Nydia Velázquez (D-NY), Ranking Member

Good afternoon Chairman Graves, Ranking Member Velázquez and members of the Committee. I am Donna Baker, a CPA with 25 years of experience. I am an Associate Professor of Accounting at Siena Heights University and have owned my own CPA firm for the last 13 years.

#### Executive Summary

The business aggregation rules in the Affordable Care Act will have a negative impact on small businesses. The aggregation rules require any group of companies under “common control” to be treated as a single employer. The primary key in determining which companies are combined is direct or attributed ownership, not operational control. The attributed ownership rules may cause unrelated businesses held by family members or trusts to be aggregated. Companies within a controlled group do not need to have the same management or operate in the same industry. All employees of the controlled group must be considered in determining if the health insurance mandate applies. These rules could cause employers to delay growth, manipulate ownership percentages or limit employees to less than 30 hours, discourage small businesses from investing in other businesses, and require health insurance coverage in industries where this is not the norm which will affect a business' ability to compete.

Also, the aggregation rules are vast and detailed. They are rarely used by small business and small business advisors. The level of complexity and the unfamiliarity could create inaccurate application of the rules.

#### Background

I live and practice in Lenawee County, Michigan, a rural area with a population of 99,000 and median household income of \$48,000. My practice includes tax and accounting services for several small businesses. I also own a small payroll company and retail store and my husband is a partner in a dairy farm.

The business aggregation rules in the Affordable Care Act will impact small businesses. The Affordable Care Act requires a business to apply the controlled group, affiliated service and leased employee rules to determine what groups of companies are to be treated as a single employer. All employees (including leased employees) of companies in the controlled group and affiliated service group must be included in the calculation of full time equivalent employees (FTEs). If the total number of full-time employees (including FTEs) for the entire group is at least 50, then each entity in the controlled group will be subject to the employer mandate rules of the Affordable Care Act and must provide the minimum essential health insurance coverage to all full time employees and their dependents.

The attribution rule applies in determining a controlled group and affiliated service group. Attribution is the concept of treating a person as owning an interest in a business that is not actually

owned by that person. Attribution may result from family or business relationships. One aspect of this rule is the family attribution rule between spouses that requires the business interest of one spouse to be attributed to the other spouse unless there is either no direct ownership, no participation in the company and no more than 50% of business gross income is passive investments.

### **Implication of Requiring Small Business to use Controlled Group Rules**

Many Small Businesses and Small Business Advisors are Unfamiliar with the Controlled Group Rules.

The controlled group rules are lengthy and complicated. These rules are typically used in determining if qualified retirement plan benefits are available on a nondiscriminatory basis. Many small employers, who offer a retirement plan, offer a safe harbor IRC Section 401(k) plan that does not require discrimination testing. Therefore, the rules are rarely applicable to small businesses. The lack of use of these rules, make them unfamiliar to both small businesses and small business advisors. Many CPA's, who work primarily with small businesses, do not have the specialized knowledge that is required to interpret the business aggregation rules. To add to the confusion, the use of "controlled group" is misleading and is often inaccurately assumed to mean "hands on control" instead of its actual emphasis on direct or attributed ownership.

Most Affordable Care Act training materials do not cover the specifics of controlled group rules. In reviewing ACA training modules from typical sources that small business advisors would use, (Michigan Association of CPA's, Michigan State University, Check-Point Learning, Thomson Reuter), most materials mention that controlled group rules apply, but do not define the rules.

Examples of Applying Controlled Group Rules and Ownership Attribution.

Example 1: This is my personal example.

I own the following businesses:

CPA firm - 100% owner and manager - 20 employees

Payroll Company - 100% owner and manager - 10 employees (and growing!)

Retail store - 50% owner (75% capital investment) - I have no management responsibility and no control over business decisions - 5 employees. This store was purchased as an investment.

My husband is a 50% owner in a dairy farm with 8 employees. I have no management responsibilities and no control of business decisions in this entity. I am not a partner; however, my name is on some of the land in the partnership, therefore the family attribution rules apply.

Based on the controlled group rules, the full time equivalents (FTE's) would be:

CPA firm—20 employees  
Payroll Company—10 employees  
Retail Store—5 employees  
Farm—8 employees  
Total FTE's—43

I am currently not at the 50 FTE's that would make the businesses subject to the shared responsibility rules of the Affordable Care Act. However, the payroll company is 1½ years old and quickly growing. I anticipate hiring 10–15 more employees in the next 2 years. Alternatively, I may consider restructuring ownership in my entities or slowing growth so that I do not pass the 50 FTE mark.

Example 2: This is one of my clients.

Jane is an elderly woman that is a 100% owner of two local restaurants. Her son manages these restaurants and makes all business decisions for both of the entities.

Jane recently provided the capital, as an investment, for her nephew to start a restaurant in Florida. The nephew manages this restaurant and makes all business decisions for this entity. Jane is a 50% partner, but provided 100% of the capital. The controlled group rules would require all three entities to be treated as one employer. The number of employees from all three entities would exceed 50 full time equivalents and these entities would be required to provide the minimum essential health insurance coverage.

The two examples above illustrate how the controlled group rules will aggregate businesses that are not directly owned by the same person, or do not have the same management, and may not be in the same industry or in the same state.

In addition, I want to mention the increased cost of my health insurance plan. I currently provide basic health insurance for my employees in the CPA firm and the payroll company. My plan is being canceled and the closest plan will have an increased cost of 40% to 44%. This new plan also has reduced benefits. My businesses are located in a lower income area which translates into a lower profit margin. The increased health insurance cost will be very difficult to absorb.

In summary, the implication of requiring small businesses to use the business aggregation rules will have the following negative effects:

- (1) Hinder growth by discouraging owners to hire.
- (2) Create an environment where owners try to manipulate ownership percentages or limit employees to less than 30 hours per week.
- (3) Discourage small business owners from investing in other businesses.

(4) Require small business owners to provide health insurance coverage in industries where this is not the norm. This additional cost would make it difficult for these companies to compete.

**Effect of the Business Aggregation Rules under the ACA  
on Small Employers**

**Submitted by Linda R. Mendel and Mark A. Bodron**

**November 22, 2013**

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*The comments provided below are solely those of Ms. Mendel and Mr. Bodron and are not submitted on behalf, and may not be the views, of their firms or any other person or entity.*

**Application of the Business Aggregation Rules under the Affordable Care Act (“ACA”)**

Starting in 2015, an employer with 50 or more full-time and full-time equivalent (“FTE”) employees will be subject to the employer shared responsibility payment rules (sometimes referred to as the “play or pay” rules) under Internal Revenue Code (“Code”) § 4980H. The ACA relies on the controlled group rules under Code § 414 to determine which businesses are aggregated and treated as a single employer for purposes of the 50-employee threshold. Businesses are aggregated if the businesses are part of: (1) a controlled group of corporations; (b) trades or businesses under common control; or (c) an affiliated service group.

The aggregation rules are complex but well established. The need to identify an aggregated group of businesses is not unique to Code § 4980H. In fact:

- Businesses must apply the same aggregation rules to determine whether they must offer COBRA continuation coverage. A business in an aggregated group with 20 or more employees is subject to COBRA.
- Businesses must apply the same aggregation rules in testing a retirement plan for prohibited discrimination. The proportion of highly paid employees in the aggregated group who are offered retirement benefits is limited by the proportion of non-highly paid employees in the aggregated group who are offered retirement benefits.

- Similar aggregation rules apply to determine whether a business' group health plan must pay primary to Medicare for health expenses incurred by a Medicare-eligible employee (or a Medicare-eligible family member of an employee).
  - If an aggregated group has 20 or more employees, the business' group health plan must pay primary to Medicare for employees entitled to Medicare on the basis of age.
  - If an aggregated group has 100 or more employees, the business' group health plan must pay primary to Medicare for employees entitled to Medicare on the basis of disability.
- Similar aggregation rules also apply for purposes of federal income taxes.

### **Suggested Change to the Definition of a “Small Employer”**

We do not think it is the complexity of the Code § 414 aggregation rules, but rather the complexity of Code § 4980H, that presents the challenge for smaller businesses facing the possible application of the play or pay rules. Smaller businesses tend not to have in-house expertise or ongoing relationships with outside experts to assist them with the changes that may be required to avoid the Code § 4980H penalties. Many smaller businesses are unequipped to even determine their responsibilities. That is the problem regardless of whether a small business is structured as a single entity or a group of aggregated entities.

Our suggestion is to increase the threshold for the application of Code § 4980H from 50 full-time and FTE employees to a higher number. For example, Congress could consider a modest increase from the current threshold of 50 full-time and FTE employees to a threshold of 101 full-time FTE employees. We suggest the 101-employee threshold because it corresponds to the threshold for small employer status for the SHOP Exchanges and the small group health insurance market. Starting in 2016, the SHOP Exchanges and the small group insurance market will be available to aggregated groups with up to 100 full-time and FTE employees; an aggregated group with 101 or more full-time and FTE employees will be considered large. (In fact, the same method for counting employees applies to Code § 4980H, the SHOP Exchanges, and the small group health insurance market. The only difference is the employee threshold for status as a small employer.) It would make sense for an employer that is considered small for purposes of the SHOP Exchanges and the small group insurance market to also be considered small for purposes of Code § 4980H.

### **Suggested Simplification of Penalties under Code § 4980H**

To reduce the burden on smaller businesses, we suggest that Congress consider simplifying Code § 4980H by repealing the “no-offer” penalty under Code § 4980H(a).

There are two employer pay or play penalties under Code § 4980H:

- The “no-offer” penalty under Code § 4980H(a) applies when an employer fails to offer its full-time employees health coverage and one or more full-time employees buys health insurance through a Marketplace with premium assistance. The penalty is \$2,000 multiplied by the number of full-time employees (including any full-time employees who were offered and enrolled in health coverage sponsored by the employer).
- The “unaffordable/inadequate coverage” penalty under Code § 4980H(b) applies when an employer offers health coverage to its employees but that coverage is either unaffordable or inadequate and one or more full-time employees buys health insurance through a Marketplace with premium assistance. The penalty is \$3,000 multiplied by the number of full-time employees receiving premium assistance.

The no-offer penalty under Code § 4980H(a) and the unaffordable/inadequate coverage penalty under Code § 4980H(b) are both applied separately to each business within an aggregated group; provided, however, that with respect to the unaffordable/inadequate coverage penalty, the amount is the same regardless of the structure of the group. (While the penalties are applied separately to each business within the aggregated group, the threshold issue of whether an employer has 50 or more full-time and FTE employees, and thus is subject to Code § 4980H, is based on the aggregated group.)

To avoid the unaffordable/inadequate coverage penalty under Code § 4980H(b), an employer must offer its full-time employees a group health plan that actually provides reasonable access and protections. In contrast, to avoid the no-offer penalty under Code § 4980H(a), an employer can offer a group health plan at inaccessible contribution levels and/or with very limited protections for employees. (Such plans are in fact being marketed for this explicit purpose.) In other words, the no-offer penalty is driving group health plan design but will not actually benefit employees, a result that we think is contrary to the purposes of the ACA. Yet, the implementation of the no-offer penalty raises issues for an aggregated group that would not have to be resolved if the sole penalty under Code § 4980H was the unaffordable/inadequate coverage penalty.

The no offer penalty is complex in its application to aggregated groups of all sizes. For example, it is not clear how the no-offer penalty should apply to shared employees or where one entity within the aggregated group offers health coverage to employees of another entity in the aggregated group. The reporting to support the no-offer penalty will require monthly identification of the aggregated group, taking into account acquisitions and dispositions that change the composition of the aggregated group.

We suggest asking the Congressional Budget Office to estimate the economic impact of the implementation of the unaffordable/inadequate coverage penalty without the no-offer penalty. If the unaffordable/inadequate coverage penalty is sufficient inducement for businesses to maintain group health coverage for lower income employees (i.e., employees who are potentially eligible for subsidies

in the Marketplaces), we think Congress should consider the repeal of the no-offer penalty.

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We appreciate the opportunity to provide the above comments above to the Committee. We would be pleased to provide additional information at your request on this issue or other ACA issues.

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