Understanding Affordability and Safe Harbors

This guide details the three safe harbor provisions and explains affordability related to the Affordable Care Act (ACA) employer shared responsibility provision.

Version 4.5 | July 2025

The Affordable Care Act employer shared responsibility provision ("employer mandate" or "play or pay") requires applicable large employers to offer health coverage to full-time employees.

See Employer Guide to ACA Play or Pay Rules for definitions and a discussion of who is a full-time employee or what is an applicable large employer.

Affordability and Safe Harbors

If a full-time employee receives a government subsidy for individual insurance through an Exchange (Marketplace) due to the employer's failure to offer adequate coverage at work, the employer may be assessed with one of two types of penalties.

A large penalty may apply if the employer did not offer coverage to at least 95% of all full-time employees and their dependent children. If the employer did offer coverage, but the coverage did not meet standards for minimum value and affordability, a smaller penalty may apply.

Affordability is simply based on the employee contribution requirement for self-only coverage divided by the employee's income. The maximum allowable percentage is based on the plan year as adjusted for inflation:

- For plan year beginning in 2025: 9.02% of income
- For plan year beginning in 2026: 9.96% of income

Most employers won't have access to an employee's actual household income, so the regulations allow an employer to define income using any of three different safe harbor methods:

- Federal poverty level
- Rate of pay
- W-2 wages

Use of the safe harbor methods is optional. Employers may use any one of the methods or use different methods for distinct classes of employees if the chosen method is applied uniformly to the class; for example, using a different method for all employees in a certain job category or location, or using one method for hourly employees and another for salaried employees.

Extensive details are available as published in the *Federal Register*: Shared Responsibility for Employers Regarding Health Coverage.

Safe Harbor #1: Federal Poverty Level

Using this safe harbor, annual income is defined as the federal poverty level (FPL) amount determined by the Department of Health and Human Services (HHS) for a single-member household. Most employers use the mainland amount, regardless of where the employee is located in the United States. For 2025, a calendar year plan would use $15,060, and a non-calendar year plan should use $15,650. This method is very simple, but it will generate the lowest income amount.

The HHS updates the FPL in mid- to late January every year, so the new amount cannot be used for a calendar year plan that had already started a few weeks earlier on January 1. In that case, employers may use the FPL chart in effect within six months before the date the health plan year begins. This approach provides adequate time to establish premium amounts in advance of the plan's open enrollment period.

View the current HHS Poverty Guidelines. **Note:** The employee's actual earnings, or any changes in earnings, are not relevant when using the FPL safe harbor method.

Example Calculation

For a plan year beginning January 1, 2025, coverage is automatically deemed to be affordable if the employee's self-only coverage cost does not exceed $113.20 per month ([$15,060 x 0.0902]/12 months).

If a 2025 plan begins on or after February 1, 2025, the employer should use the 2025 federal poverty level (FPL) of $15,650. To meet ACA affordability standards, coverage will be considered affordable if the employee's contribution for self-only coverage does not exceed the affordable amount calculated as follows:

Affordable amount = [$15,650 × 0.0902]/12 months

Safe Harbor #2: Rate of Pay

This safe harbor is based on the rate of pay at the beginning of the coverage period (i.e., the plan year).

For salaried employees, ***rate of pay*** means the employee's monthly salary amount. This method cannot be used if the monthly salary is reduced.

For hourly employees, ***rate of pay*** means the employee's hourly rate times 130 hours per month. This is true regardless of the number of hours the employee works. Many employers will find this method to be the most convenient way to determine income in order to calculate whether the coverage is affordable, particularly for employees paid on an hourly basis. This method should not be used for tipped or commissioned employees.

The rate of pay method does not require monitoring actual earnings or hours worked, as long as the employee's hourly rate (e.g., $11/hour) does not reduce. If an hourly employee's pay rate reduces during the year, the applicable rate of pay would be the lowest rate of pay in effect at the start of the plan year or the month being reported.

Hourly Wage	Maximum Affordable Monthly Cost: 2025 Plan Year*	Maximum Affordable Monthly Cost: 2026 Plan Year*
$7.25	$85.01	$93.87
$12.00	$140.71	$155.38
$15.00	$175.89	$194.22

**Maximum affordable monthly cost = hourly wage × 130 hours × 9.02% (2025) or 9.96% (2026)*

Safe Harbor #3: W-2 Wages

Income under this method is defined as the amount reported in Box 1 of the employee's Form W-2 for the current year. Note that pre-tax § 125 contributions and § 401(k) or § 403(b) deferrals are not included in the Box 1 amount, so this method may understate the employee's actual income.

The W-2 method may be used for both hourly and salaried employees, but using the rate of pay safe harbor for hourly employees is recommended because it is more reliable and accurate.

Annual Salary	Maximum Affordable Monthly Cost: 2025 Plan Year*	Maximum Affordable Monthly Cost: 2026 Plan Year*
$16,000	$120.26	$132.80
$25,000	$187.92	$207.50
$60,000	$451.00	$498.00

**Maximum affordable monthly cost = (annual salary/12 months) × 9.02% (2025) or 9.96% (2026)*

While the amount in Box 1 is an annual amount, affordability is determined monthly. Therefore, Box 1 wages are used to calculate a monthly amount (based on the number of months in which the employee was employed and required to be offered coverage) from which affordability can be determined.

This method requires the employee contribution to remain a consistent percentage or amount throughout the calendar year.

Employers using this method often ask whether they can adjust the contribution during the year to ensure that the employee's cost always meets the affordability threshold. Employer health plans usually are part of a cafeteria plan subject to rules under § 125 of the Internal Revenue Code, which generally restrict changes after the plan year starts. Therefore, to accomplish the employer's objective, care must be taken in the language of the cafeteria plan document.

The self-only coverage contribution amount (e.g., employee's payroll deduction amount) should be outlined in the plan document as X% (for example, 9.96% for 2026) of W-2 Box 1 monthly wages but not to exceed $Y. For instance, if an employer wants to set the employee contribution amount at $250/month, the contribution described in the 2026 plan would be 9.96% of W-2 Box 1 monthly wages but not to exceed $250 per month.

Partial Year Offers of Coverage

In cases where an employee was not employed for the full calendar year, employers must determine affordability by multiplying employee wages for the year by a fraction equal to the number of calendar months the employee was offered coverage over the number of months the individual was actually employed during the year.

Example Calculation

Nahal is hired by Acme Co. on May 15, and is offered coverage after her waiting period is completed on August 1. Her wages, according to Box 1 of her W-2, are $20,000. Since Nahal was not employed for the entire year and was subject to a waiting period before coverage was offered, the calculation is as follows:

W-2 wages x (calendar months offered coverage/ months of employment) = $20,000 x (5/8) = $12,500

The W-2 wages used in the affordability calculation are adjusted to $12,500 for the five months Nahal is offered coverage. Acme Co. will be considered to offer affordable coverage if Nahal is not charged more than $249.00 per month for coverage ([$12,500 x 0.0996]/5 = $249.00).

Frequently Asked Questions About Affordability

How does an employer decide which safe harbor to use?

There are pros and cons to each safe harbor depending on the employer and employee demographics. Considerations when deciding which safe harbor to apply include:

- Employer budget
- Employer support in payroll and benefits administration
- Base salary for lowest paid employees (hourly and salary)
- Hourly employee turnover
- Hourly employees that consistently work 40 hours per week
- Hourly employees that are now full time, mostly due to 30 hours per week
- Hourly employees with busy seasons and overtime opportunities

If you offer multiple health plan options, you only need to test the lowest-cost option that is offered to the full-time employee.

If employee contribution is too high to use the FPL method, consider using either the W-2 method or rate of pay method for each category of full-time employees (e.g., hourly, salaried).

When reporting data on Forms 1094/1095-C, how does an employer determine which safe harbor was used for cost-sharing, if they don't know?

You must have set the cost sharing (employee contribution rates) before the plan year started (e.g., at renewal). You will need to do an analysis to determine which safe harbor was used and/or which one may be most advantageous for the highest number of employees. Also, review the information and factors in the previous question. Mineral cannot make this determination for employers.

Are there any special cases related to affordability that employers should be aware of?

Wellness program rewards that reduce the employee contribution rates are disregarded in the affordability test, unless the wellness program is related to tobacco use. In that case, assume all employees qualify for the reward before determining affordability.

Flex credits or cash-in-lieu benefits may affect the determination of affordability. Employers with cafeteria plans that offer these types of options should review the specific provisions with legal counsel.

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