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ACA Traps For The Unwary Government Contractor

Law360, New York (November 18, 2013, 12:18 PM ET) -- In a perfect world, two separate federal laws that both require employers to provide health and welfare type benefits to employees would be consistent with each other and, if there is an apparent conflict, government agencies would walk employers through how to comply. Unfortunately, we don't live in a perfect world.

One of the laws we are referring to is the Affordable Care Act. One of the key provisions of that law is the so-called "employer mandate," i.e., the requirement that employers with at least 50 employees offer "minimum essential coverage" (also called "affordable, minimum value health coverage") to their full-time employees or make a so-called "shared responsibility payment" to the Internal Revenue Service.

For government contractors, a requirement to provide health and welfare benefits such as health insurance to employees is nothing new. Indeed, the consequences for failing to provide proper benefits can be drastic, including a three-year debarment from all government contracting. Under the Service Contract Act ("SCA"), for example, a service contractor must provide "bona fide" fringe benefits such as health insurance, a pension or 401(k) match, long or short-term disability, life insurance or extra vacation. Alternatively, the employer may provide "cash in lieu of fringe benefits." Construction contractors subject to the Davis-Bacon Act ("DBA") have analogous, though not identical, obligations.

Here's the apparent conflict, which the U.S. Department of Labor should be addressing publicly, but hasn't.

SCA regulations state, "No benefit required by any other Federal law or by any State or local law, such as unemployment compensation, workers' compensation, or social security, is a fringe benefit for purposes of the Act."[1] The ACA is an "other Federal law." The "minimum essential coverage" required by the ACA would seem to be a "benefit required by any other Federal law." Does this mean that employers won't be able to meet their SCA obligations by providing the "minimum essential coverage" required by the ACA? Will they have to provide two benefits — the SCA health and welfare benefit and the ACA health coverage?

The DOL, which enforces the SCA and DBA, has been oddly silent about this conundrum, leaving many employers worried. But there's still time, given that the employer mandate has been delayed until 2015. One solution the DOL could adopt would be to reduce the health and welfare required by the SCA to offset the ACA requirement. In fact, there's already a precedent for this. Hawaii has had mandatory employer-paid health coverage for decades, and SCA wage determinations ("WDs") in that state include a health and welfare benefit significantly lower than the benefit required in the other 49 states. As noted, though, the DOL has been mum, at least officially.

Unofficially, the DOL may be thinking that the "minimum essential coverage" required by the ACA can count toward the SCA health and welfare requirement. If this is true, it means that DOL is not viewing the ACA health coverage as a benefit required by another federal law.

The argument would go like this. Back in June 2012, the U.S. Supreme Court ruled on the constitutionality of the so-called "individual mandate" in the ACA. That provision requires most Americans to get health insurance by a certain date or to pay a penalty. One of the key issues before the Supreme Court was whether Congress has the right to force people to buy something they don't want — namely, health insurance. The Supreme Court ruled: No, Congress can't force people to buy something they don't want. (If that were allowed, the Supreme Court said, Congress could reduce healthcare costs by requiring us all to eat more vegetables — something that everyone agrees Congress can't do.)

But, said the court, Congress does have the power to tax us. And, the ACA doesn't tell individuals, "Go get health insurance." Instead, the law says, in effect, "Go get health insurance or pay a penalty in the form of higher taxes." That, said the Supreme Court, is OK.[2]

The Supreme Court was addressed the individual mandate, not the employer mandate. However, the DOL might view the latter requirement the same way the Supreme Court viewed the former requirement. Viewed in that light, the ACA doesn't require employers to provide health insurance. Rather, it gives employers a choice to provide health insurance in order to avoid paying higher taxes in the form of the so-called "shared responsibility payment." And, if the ACA doesn't require employers to provide health insurance, then the "minimum essential coverage" required by the ACA is not a "benefit required by any other Federal law" and can count toward meeting SCA requirements.

But, this leads to a follow-up question: Is a contractor that chooses to pay the IRS rather than provide minimum essential coverage a "responsible" contractor? Before a contracting officer awards a contract, he or she must make an affirmative determination that the prospective contractor is responsible. This includes a finding that the contractor has a satisfactory record of integrity and business ethics.[3]

In the mind of some contracting officers, this may include considering whether the contractor is a law-abiding citizen. Indeed, some presidential administrations in recent memory have specifically tried to make compliance with labor laws part of the responsibility determination. So the question arises: If a contractor doesn't provide the "minimum essential coverage" required by the ACA and instead makes the "shared responsibility payment" to the IRS, is that contractor a law-abiding citizen or a law-breaker who paid a penalty to the IRS?

Following the Supreme Court's logic regarding the individual mandate, the answer should be that the contractor is a law-abiding citizen. The court said:

While the individual mandate clearly aims to induce the purchase of health insurance, it need not be read to declare that failing to do so is unlawful. Neither the Act nor any other law attaches negative legal consequences to not buying health insurance, beyond requiring a payment to the IRS. The Government agrees with that reading, confirming that if someone chooses to pay rather than obtain health insurance, they have fully complied with the law.[4]

So, too, an employer that chooses to make the "shared responsibility payment" to the IRS rather than provide the "minimum essential coverage" should be considered to have fully complied with the law.

While the courts have not addressed this, it seems to be the logical result.

This is not to say that the ACA won't change the way government contractors provide health and welfare benefits. As noted above, the SCA and DBA permit employers to pay cash in lieu of fringe benefits. Anecdotal evidence suggests that a significant number of service and construction contractors do discharge their obligation in this manner — among other reasons, because it increases the employees' disposable income.

The flexibility to discharge the SCA's or DBA's health and welfare obligations by paying cash may go away once the ACA's employer mandate to provide "minimum essential coverage" takes effect. Of course, contractors that are too small to be subject to the ACA mandate shouldn't be affected. But for larger companies, the option to pay cash will remain available only if the employer can find health insurance that provides the minimum essential coverage but costs less than the minimum SCA fringe benefit, currently $3.81 per hour in most WDs.

In that case, the employer would fulfill its ACA obligation by providing the health coverage, and the difference between the cost of the ACA minimum essential coverage and the SCA or DBA health and welfare benefit can be paid out in some other form, including cash. This could happen, for example, if an employer self-insures, thus providing the minimum essential coverage, and a particular employee does not use any health benefits in a particular period.

Another change may occur with respect to those SCA WDs that do not require that all employees receive benefits, only that the contractor's workforce average a certain benefit level. For example, if the applicable WD requires an average benefit of $3.81 per hour, then the employer can comply by providing twice that amount ($7.62) to an employee who uses a great deal of health care and nothing to an employee who uses no health care.

This aspect of SCA compliance seemingly will have to change given the ACA's requirement that the employer provide minimum essential coverage to every employee. This means that the employee who previously was receiving $7.62 per hour may end up with a lower benefit. Still, it depends why the employee with no benefit was turning down coverage. For example, if he or she is covered by another policy, e.g., a spouse's health insurance policy, employers may be able to continue complying with average benefit WDs by providing no benefits to that employee. (Note that many WDs already require that every employee receive a minimum benefit.)

There's still a long way to go before the kinks in the ACA and its relationship to other laws are ironed out. Contractors shouldn't wait until the employer mandate takes effect in 2015 to consider these issues.

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[1] 29 C.F.R. § 4.171(c).

[2] National Federation of Independent Business et al. v. Sebelius, No. 11-393 (June 28, 2012).

[3] FAR § 9.104-1(d).

[4] Slip op. at 37.
