

## Responding to IRS Pay or Play Assessment Letters

### Background

The Patient Protection and Affordable Care Act (ACA) requires Applicable Large Employers (ALEs)<sup>1</sup> to make a sufficient offer of coverage to their full-time employees<sup>2</sup> (and their dependents)<sup>3</sup> in order to avoid ACA Pay or Play penalties. Pay or Play penalties can take two forms:

- The part (a) penalty can be triggered if an ALE fails to offer coverage to substantially all of its full-time employees (95%). This can result in a \$2,000 penalty (annualized, not shown as indexed) for each full-time employee minus the first 30. At least one full-time employee must also qualify for subsidized Exchange coverage.
- The part (b) penalty can be triggered if the ALE offers coverage to substantially all (95%) full-time employees, but the coverage is unaffordable<sup>4</sup> or is not at least a 60% actuarial value plan. The Part (b) penalty can also be triggered by any full-time ineligible employee outside the 95% "substantially all" threshold. This penalty is \$3,000 (annualized, not shown as indexed) for each full-time employee *that enrolls in* subsidized Exchange coverage.

The IRS determines an ALE's liability for Pay or Play penalties (and penalty amounts) based on information reported to the IRS annually on [Forms 1094-C and 1095-C](#).

### IRS Notice of Potential Penalties - Letter 226J

If the IRS determines that an ALE potentially owes Pay or Play penalties it will issue [Letter 226J](#) to initiate the penalty assessment process. Letter 226J includes:

- A brief explanation of ACA Pay or Play Penalties,
- An "Employer Shared Responsibility Penalty" (ESRP) summary table itemizing the proposed payment by month and indicating for each month if the liability is under part (a) or part (b),
- An employer response form, [Form 14764](#), "Employer Shared Responsibility Penalty Response",
- An "Employee Premium Tax Credit" (PTC) List, [Form 14765](#), which lists, by month, the ALE's full-time employees (individuals who for at least one month in the year were full-time employees) who received a premium tax credit and the indicator codes the ALE reported on lines 14 and 16 of each employee's Form 1095-C,
- A description of the actions the ALE should take if it agrees or disagrees with the proposed assessment, and
- A description of the actions the IRS will take if the ALE does not timely respond.

Under the Paperwork Reduction Act of 2024, an ALE must respond no later than 90 days from the date of Letter 226J (previously 30 days). **Extensions to the response deadline are uncommon.** The assessment process requires mastery of all applicable data and fast turnaround (offers of coverage, declinations, cost sharing, etc.)!

<sup>1</sup> Applicable Large Employers are those employers who average 50 full-time employees (plus full-time equivalents) over the prior calendar year.

<sup>2</sup> Employees who work 30 hours/week or 130/month determined using either the monthly or look-back measurement method

<sup>3</sup> The term "dependent" for this purpose does not include any individual other than children and does not include an employee's spouse.

<sup>4</sup> Employee portion of employee-only premium exceeds 9.5% (9.02% for 2025) of employee's household income.

## Employer Response Requirements

**If an employer agrees with the IRS Pay or Play penalty assessment**, it should complete, sign, and date the enclosed Form 14764 (ESRP Response) and return it to IRS along with the full penalty payment. Employers that are enrolled in the Electronic Federal Tax Payment System (EFTPS) can pay electronically instead of by check or money order.

**If an employer disagrees with the IRS Pay or Play penalty assessment**, it should complete, sign, and date the enclosed Form 14764 (ESRP Response) and return it to IRS by the response deadline noted on the first page of the 226J Letter. The response must also include:

- A signed statement explaining why the employer disagrees with part or all of the proposed ESRP. The statement should describe any changes to the information reported on Form(s) 1094C or Forms 1095C that could have resulted in an improper assessment. Employers should include documentation supporting the statement.
- The Employee PTC Listing showing any corrections to the indicator codes the employer used for lines 14 and 16 of employee 1095C statements. These are the "offer" or 1 series codes and the "safe harbor" or 2 series codes respectively.
- Any additional documentation supporting changes to Form 1094C or the PTC table reflecting 1095C coding and the proposed correction to the 226J assessment. Documents can include proof that an offer of coverage was made during open enrollment, evidence of cost sharing, or records supporting that the employee was not ACA full-time.

Timely and thorough responses are critical to correcting an improper Pay or Play penalty assessment.

**Responses should be sent in a manner where they can be tracked and receipt confirmed (by fax and by certified mail).**

## IRS Responses to Employers – Letters 227

IRS will acknowledge an ALE's response to Letter 226J with one of five versions of Letter 227. The different versions of Letter 227 acknowledge the ALE's response to Letter 226J and describe further actions the ALE may need to take based on the specific facts involved. If, after receipt of Letter 227, the ALE disagrees with the proposed or revised Pay or Play penalty, the ALE may request a pre-assessment conference with the IRS Office of Appeals. A conference should be requested in writing (by fax and certified mail) generally within 30 days from the date of Letter 227. The ALE should follow the instructions provided in Letter 227 and [Publication 5](#), Your Appeal Rights and How To Prepare a Protest if You Don't Agree, for requesting a conference with the IRS Office of Appeals. The five different 227 letters are:

- **Letter 227-J:** [Letter 227-J](#) acknowledges receipt of the signed agreement Form 14764, ESRP Response, and that the ESRP will be assessed. After issuance of this letter, the case will be closed. No response is required.
- **Letter 227-K:** [Letter 227-K](#) acknowledges receipt of the information provided and shows the penalty has been reduced to zero. After issuance of this letter, the case will be closed. No response is required.
- **Letter 227-L:** [Letter 227-L](#) acknowledges receipt of the information provided and shows the ESRP has been revised. The letter includes an updated Form 14765 (PTC Listing) and revised calculation table. The ALE can agree or request a meeting with the manager and/or appeals.

- **Letter 227-M:** [Letter 227-M](#) acknowledges receipt of information provided and shows that the ESRP did not change. The letter provides an updated Form 14765 (PTC Listing) and revised calculation table. The ALE can agree or request a meeting with the manager and/or appeals.
- **Letter 227-N:** [Letter 227-N](#) acknowledges the decision reached in Appeals and shows the ESRP based on the Appeals review. After issuance of this letter, the case will be closed. No response is required.

Importantly, Letters 227-L and M require further action if the ALE still disagrees with the penalty assessment or amount. At this stage, the ALE can request a pre-assessment conference with the IRS Office of Appeals. A conference must be requested in writing within 30 days from the date of Letter 227. Further instructions are provided in Letter 227 and [Publication 5](#), Your Appeal Rights and How to Prepare a Protest if You Don't Agree.

## Payment of Penalties- Notice CP 220J

If an employer does not timely respond to either Letter 226J or Letter 227-L or M, IRS will assess the amount of the proposed penalty and issue a notice and demand for payment, [Notice CP 220J](#). Notice CP 220J will include a summary of the penalty, instructions on how to make a payment, and will reflect payments made, credits applied, and any balance due. [Publication 594](#), The IRS Collection Process, discusses payment options, such as entering into an installment agreement. **Once IRS issues Notice CP 220J employers have very limited options to combat an incorrect assessment so thorough and timely responses to IRS are critical.** Note that the IRS can attempt to collect these penalties for up to 10 years from the date assessed.

## Amended or Corrected 1094C/1095C Filings

The initial round of 2015 Pay or Play assessment letters have brought to light many early reporting errors that were common in 2015 and likely persisted through 2016. Assuming aggressive enforcement continues, employers should correct certain early reporting errors that are now being highlighted through the Pay or Play assessment process by filing amended 1094-C and 1095-C Forms. **Once an employer has received an assessment from IRS (Letter 226J) it cannot file corrected forms but must respond through the assessment and appeal process.**

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