



Regulatory Update

Prepared for

**The Kansas City Compensation
and Benefits Association**

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This regulatory update is about Medical Loss Ratio (“MLR”) Rebates under the Affordable Care Act, the first of which were received by some insured health plan sponsors on or before August 1, 2012. This update will focus on the issue of whether an ERISA covered health plan must share a portion of the rebate with participants.

Background: The Affordable Care Act requires health issuers to issue rebates to policyholders if less than a specified percentage of premiums were used to provide medical care or for expenses to improve health care quality. The MLR for the large group market is 85%. The MLR for the small group market is 80%. The rebate is calculated on the basis of the insurer’s experience for a block of similar policies in the State of issuance for the applicable period (which for the August 1, 2012 rebates is the 2011 calendar year). Rebates are not calculated on the basis of an individual plan’s claims experience. The MLR requirement does not apply to self-insured health plans.

Issue: For plans covered by ERISA that require participant contributions, employers *may* be required to either distribute a portion of the rebate to participants or apply a portion of the rebate to reduce participant premium payments, to the extent the amount of the rebate is attributable to participant contributions. However, there are two circumstances when a rebate may be retained in its entirety by the employer. They are as follows:

- 1) if (a) participants only pay a fixed amount of premiums; (b) the employer pays the remainder of the premiums; and (c) the amount of the rebate does not exceed the employer's contributions during the applicable period, then the rebate is not treated as "attributable to participant contributions" nor considered as an ERISA plan asset; or
- 2) If the employer is the policyholder and the insurance policy or contract and other documents governing the plan provide that an entire premium rebate belongs to the employer, then such document provisions will generally govern and the employer may retain the full amount of the rebate.

However, prior to the August 1, 2012 MLR rebate distributions, insurers were required to notify both employers and participants that a rebate would be paid. The same notice was sent to both employers and participants. The notice in effect was required to indicate that if a participant made premium contributions during the applicable period to an ERISA covered plan, the employer or group policyholder would be required to distribute the portion of the rebate attributable to participant premium contributions during the applicable period to participants by either reducing their future premium payments or by a cash distribution.

Special (and somewhat different) MLR rebate rules issued by the U.S. Department of Health and Human Services apply to state and local government plans.

Employer Actions: Plan Sponsors of insured group health plans need to decide whether a portion of an MLR rebate they received is attributable to participant contributions (or are ERISA plan assets) and must either be applied to reduce participant premium payments or distributed in cash to eligible participants. If so, participant premium reductions should be made or cash distributions to eligible participants should be made within three months of the employer's receipt of the MLR rebate. If not, then an employee communication of the employer's decision would be appropriate. Some employers may decide to share a portion of the rebate with participants, even if they may not be required to do so.

Here is a link to a U.S Department of Labor Technical Release No. 2011-04, which provides guidance for ERISA insured group health plans:

<http://www.dol.gov/ebsa/newsroom/tr11-04.html>

The Internal Revenue Service ("IRS") has issued frequently asked questions (FAQs) guidance which in part provides that either cash distributions of rebates or premium reductions for employees who paid their premiums during the applicable period with pre-tax salary reduction contributions are subject to income and employment tax withholding.

Here is a link to the IRS Medical Loss Ratio FAQs (with answers to fourteen questions):

<http://www.irs.gov/newsroom/article/0,,id=256167,00.html>

I hope this is helpful.