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EMPLOYEE BENEFITS & EXECUTIVE COMPENSATION UPDATE

Health Care Reform Impacts Grandfathered Employer-Sponsored Group Health Plans: Now What?

This bulletin discusses certain provisions of The Patient Protection and Affordable Care Act as signed into law by President Obama on March 23, 2010 and The Health Care and Education Reconciliation Act of 2010 as signed into law by President Obama on March 30, 2010. This bulletin is the first in a series that will examine the impact of the legislation on employer-sponsored group health plans.

The Patient Protection and Affordable Care Act and The Health Care and Education Reconciliation Act of 2010 (together, the "Reform Legislation") impact the design and administration of employer-sponsored group health plans. This bulletin describes how the Reform Legislation impacts employer-sponsored group health plans that were in effect on March 23, 2010 ("grandfathered health plans").

- Additional requirements of the Reform Legislation that apply to employer-sponsored group health plans other than grandfathered health plans are not covered in this bulletin.

The Reform Legislation defines a "grandfathered health plan" as a group health plan or health insurance coverage in which an individual was enrolled on March 23, 2010. In the case of health insurance coverage maintained pursuant to one or more collective bargaining agreements, a group health plan is a grandfathered health plan until the last of the collective bargaining agreements relating to the coverage under such group health plan terminates. Adding additional family members and new hires to a group health plan does not affect the group health plan's status as a grandfathered health plan. However, it is unclear and further guidance is needed to determine what other actions may cause a group health plan to lose its status as a grandfathered health plan.

CHANGES APPLICABLE TO THE NEXT PLAN YEAR

The Reform Legislation includes a number of provisions that become effective for the first plan year beginning on or after September 23, 2010 (January 1, 2011 for calendar year plans).

- It is likely that the following requirements will not apply to stand-alone retiree medical plans. These requirements were added by provisions of the Reform Legislation that amended Part 7 of ERISA Title I (and the corresponding portion of the Internal Revenue Code), which does not apply to plans that cover fewer than two active employees. Similarly, the following requirements should not apply to HIPAA excepted benefits, such as limited-scope dental and vision benefits.



Prohibition on lifetime dollar limits. Employer-sponsored group health plans are not permitted to impose lifetime dollar limits on “essential health benefits,” as defined by the Secretary of the Department of Health and Human Services (the “Secretary”).

- It is unclear how this provision applies in the case of a former participant who has satisfied a group health plan’s lifetime dollar limit prior to the effective date of the Reform Legislation.

Restriction on annual dollar limits. Employer-sponsored group health plans are not permitted to impose annual limits, other than “restricted” limits, on essential health benefits. No annual dollar limits will be permitted on essential health benefits for plan years beginning on or after September 23, 2013 (January 1, 2014 for calendar year plans).

- The Reform Legislation permits per-beneficiary annual and lifetime limits on non-essential benefits. Until the Secretary provides a definition of “restricted” and “essential health benefits,” plan sponsors should assume that all annual and lifetime dollar limits are prohibited.
- It is unclear whether limits can be imposed on a subset of plan benefits, such as out-of-network benefits.

Required coverage for adult children up to age 26. Employer-sponsored group health plans that provide dependent coverage to children are required to provide coverage to children (married and unmarried) up to age 26. Until the first plan year beginning on or after September 23, 2013 (January 1, 2014 for calendar year plans), group health plans are required to provide coverage for children up to age 26 only if they are not eligible to enroll in another employer-sponsored group health plan. The details on how plan sponsors are to implement coverage for children up to age 26 and what premiums can be charged for such coverage will require further guidance.

- The Reform Legislation extends the income exclusion under Section 105 of the Internal Revenue Code to coverage for children up to age 26 so that such extended coverage should be exempt from federal income tax. State and local taxes may apply to the extended coverage.
- As a result of the age-26 requirement and the corresponding tax change, plan sponsors may choose to eliminate the full-time student status requirement for adult children. Plans that do not impose student status requirements will not be subject to Michelle’s Law.
- For plan years 2011-2014, it is unclear how coverage must be extended to an adult child who is eligible for coverage under the employer-sponsored group health plans of both parents.
- Although the Reform Legislation extended coverage for adult children, it did not amend the definition of dependent in Section 152 of the Internal Revenue Code. Therefore, plan administrators who receive requests for mid-year election changes involving adult children will need to be careful to approve such changes only when the adult child is a tax dependent of the employee.



Prohibition on pre-existing condition exclusions. Employer-sponsored group health plans may not impose any pre-existing condition exclusions on covered persons who are under age 19. Effective for the first plan year beginning on or after September 23, 2013 (January 1, 2014 for calendar year plans), pre-existing condition exclusions will be prohibited for all participants.

Prohibition on rescissions. Employer-sponsored group health plans may not rescind coverage, except in the case of fraud or intentional misrepresentation.

- The significance of this provision in the context of employer-sponsored group health plans is not yet clear.

CHANGES EFFECTIVE JANUARY 1, 2011

The following additional provisions of the Reform Legislation are effective January 1, 2011, regardless of the plan year of an employer-sponsored group health plan.

Over-the-counter drugs are ineligible for pre-tax reimbursement. Flexible spending accounts (FSAs), health savings accounts (HSAs) and health reimbursement accounts (HRAs) may not reimburse the cost of over-the-counter drugs other than insulin or those prescribed by a doctor.

- Flexible benefit plans and HRA plan documents need to be amended to comply with this provision if they currently permit reimbursement of over-the-counter drugs. In addition, summary plan descriptions for medical coverage should be reviewed to determine whether they include provisions relating to distributions from FSAs, HRAs or HSAs.
- Plan sponsors should communicate how this change will impact plan participants' FSA, HSA and HRA reimbursements soon.
 - Reimbursement for over-the-counter drug expenses incurred before January 1, 2011, even if reimbursed during the first 2½ months of 2011, are permitted from an FSA or HRA.
 - However, FSA plans that offer grace periods will be unable to use amounts from 2010 accounts to reimburse over-the-counter drug expenses incurred during the first 2½ months of 2011.
 - Distributions from an HSA for over-the-counter drugs must occur prior to January 1, 2011.

Cost of health coverage added to W-2. Employers are required to report the aggregate cost of an employee's employer-sponsored group health plan coverage for 2011 on the Form W-2 issued in January 2012. The aggregate cost is to be determined under rules similar to the rules used for calculating COBRA costs.

- Employers who offer on-site medical clinics will need to determine how to value the coverage provided by those clinics and report it on the Form W-2.



Higher penalty for non-medical expense withdrawals from an HSA. The excise tax for withdrawals of amounts from an HSA for non-medical expenses prior to age 65 increases from 10 percent to 20 percent.

- The excise tax may be described in summary plan descriptions for high-deductible health plans or cafeteria plans that provide for pre-tax HSA contributions. Plan sponsors should review these documents to determine whether updates are necessary.

Simple cafeteria plans available. Small employers (i.e., employers with an average of 100 or fewer employees in either of the two prior calendar years) may avoid the cafeteria plan nondiscrimination requirements by adopting a “simple” cafeteria plan and making an employer contribution on behalf of each eligible employee. Certain eligibility, participation and contribution requirements apply.

CLASS Act program established. The CLASS Act program is a government-run long-term care insurance program that provides benefits to participants who have a qualifying disability after the participant has contributed to the program for at least five years. Beginning January 1, 2011, employers are expected, but not required, to distribute information about the program to employees and to automatically enroll employees in the program, unless the employees affirmatively opt out of participation in the program.

RETIREE REINSURANCE

By June 21, 2010 (90 days after enactment), the Department of Health and Human Services (HHS) will establish a temporary reinsurance program to provide employer-sponsored group health plans with reimbursement for a portion of the cost of providing health insurance coverage to “early retirees” (retirees age 55 or older who are not eligible for Medicare) and their eligible dependents. To be eligible for reimbursements, an employer-sponsored group health plan must implement programs and procedures to generate cost-savings with respect to participants with chronic and high-cost conditions and apply to HHS.

- The Reform Legislation appropriates \$5 billion for this reinsurance program. However, it is anticipated that the reinsurance money will quickly be exhausted.

ADDITIONAL PROVISIONS EFFECTIVE IMMEDIATELY

Increase in limitations for adoption assistance programs. The pre-tax dollar limit for expenses paid pursuant to an adoption assistance program under Section 137 of the Internal Revenue Code is increased by \$1,000 to \$13,170 for 2010.

Automatic enrollment. Employers who offer health benefits and have more than 200 employees must automatically enroll new full-time employees in coverage and provide them an opportunity to opt out.

- The Reform Legislation does not provide an effective date for this requirement, so the requirement will likely become effective upon issuance of explanatory regulations.



- Plan sponsors should consider amending cafeteria plans to permit automatic enrollment on a pre-tax basis.

FUTURE CHANGES

The Reform Legislation includes many other changes that take effect in later years. Future bulletins in this series will address those changes, and Thompson Hine's Employee Benefits & Executive Compensation lawyers will provide additional updates on these provisions as guidance is issued and the effective dates approach.

RECOMMENDED ACTION ITEMS

- Plan sponsors should work with service providers to ensure that 2011 benefits are compliant with the Reform Legislation.
- Plan documents should be amended and summary plan descriptions should be reviewed and updated.
- Before establishing a new plan (which may include entering into a new insurance contract or renewing a collective bargaining agreement), plan sponsors should consult with legal counsel to determine the additional requirements applicable under the Reform Legislation.
- Employers who sponsor self-insured plans that impose annual and/or lifetime dollar limits should begin to assess the cost impact of the elimination of these limits.
- Plan sponsors who are interested in retiree reinsurance reimbursements should act quickly once HHS issues guidance on application for the reimbursements.

FOR MORE INFORMATION

If you would like more information about the Reform Legislation, please contact your primary Thompson Hine Employee Benefits & Executive Compensation lawyer or email us at AskUs@ThompsonHine.com. For a list of our Employee Benefits & Executive Compensation lawyers, go to www.ThompsonHine.com/practices/Employee_Benefits_Executive_Compensation/lawyers/.

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