

Nondiscrimination and Health Care Reform

1. Nondiscrimination Requirements for Insured Plans Under the Affordable Care Act Delayed

Although the IRS has **delayed compliance for fully-insured plans**, the Affordable Care Act, as enacted in March 2010, extended the requirements of Internal Revenue Code Section 105(h)(2), which prohibit discrimination in favor of highly compensated individuals by self-insured medical reimbursement plans, to certain fully-insured plans. In order to comply with these requirements, the Affordable Care Act provided that rules “similar” to the nondiscrimination rules that currently apply to self-insured plans (relating to nondiscriminatory eligibility and benefits) shall apply to insured plans. These requirements do not apply to grandfathered plans.

Why the Delay?

According to Notice 2011-1, comments received raised fundamental concerns about plan sponsors’ ability to comply with the nondiscrimination requirements without regulatory guidance. In particular, guidance is needed that specifies in what respects insured plans are subject to the same statutory provisions that apply to self-insured plans and in what respects insured plans are subject to rules reflecting a different (although “similar”) application of those statutory provisions.

Timing of the Delay

Because regulatory guidance is essential to the operation of the statutory provisions, the Treasury Department and the IRS, as well as DOL and HHS, have determined that compliance with the nondiscrimination provisions should not be required until after regulations or other administrative guidance of general applicability has been issued.

In order to provide insured group health plan sponsors time to implement any changes required as a result of the regulations or other guidance, the Departments anticipate that the guidance will not apply until plan years beginning a specified period after issuance.

2. Nondiscrimination Rules for Self-Insured Medical Reimbursement Plans--IRC 105(h)(2)

The nondiscrimination requirements with respect to highly compensated individuals under a self-insured medical expense reimbursement plan are found in Internal Revenue Code section 105(h). To satisfy the nondiscrimination requirements under section 105(h)(2):

- (A) The plan must not discriminate in favor of highly compensated individuals as to eligibility to participate; and
- (B) The benefits provided under the plan must not discriminate in favor of participants who are highly compensated individuals.

Nondiscriminatory Eligibility Classifications

To satisfy the eligibility nondiscrimination requirements of section 105(h), a plan must benefit—

- (a) 70% or more of all employees, or 80% or more of all the employees who are eligible to benefit under the plan if 70% or more of all employees are eligible to benefit under the plan; or
- (b) Such employees as qualify under a classification set up by the employer and found by the Secretary not to be discriminatory in favor of highly compensated individuals.

A classification established by the employer under (b) must, based on all the facts and circumstances, be reasonable and established under objective business criteria that identify the category of employees who benefit under the plan. Reasonable classifications generally include:

- » Specified job categories,
- » Nature of compensation (i.e., salaried or hourly),
- » Geographic location, and
- » Similar bona-fide business criteria.

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Nondiscriminatory Benefits

To satisfy the nondiscriminatory benefits requirements of section 105(h), all benefits provided for participants who are highly compensated individuals must be provided for all other participants.

Due to the complexity of testing plans for compliance with the nondiscrimination rules of Internal Revenue Code section 105(h), any employer that is considering offering health benefits to only certain classes of employees should carefully review all of the provisions of that section and its accompanying regulations, and seek the advice of a knowledgeable employment law attorney for specific guidance on its particular plan.

3. Other Considerations Related to “Classing Out” — HIPAA & Other Federal Nondiscrimination Requirements for Group Health Plans

HIPAA: Distinctions Based on Health Factors are Generally Prohibited

Under the Health Insurance Portability and Accountability Act (HIPAA), an individual cannot be denied eligibility for benefits or charged more for coverage because of any health factor. Health factors are any of the following health status-related factors:

- » Health status;
- » Medical condition (including both physical and mental illnesses);
- » Claims experience;
- » Receipt of health care;
- » Medical history;
- » Genetic information;
- » Evidence of insurability; or
- » Disability.

HIPAA: Bona-Fide Employment-Based Classifications May Be Permitted

According to the FAQs regarding HIPAA's nondiscrimination requirements, distinctions among groups of similarly situated participants in a health plan must be based on bona-fide employment-based classifications consistent with the employer's usual business practice. Distinctions cannot be based on any of the health factors noted above.

Other Unlawful Discrimination Prohibited

It is also important to remember that various federal and state laws prohibit discrimination based upon race, sex and certain other factors, so eligibility requirements for participation in a group health plan should be applied equally to employees and plans should make sure that similarly situated employees are treated the same.