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IMMEDIATE IMPACT OF HEALTH CARE REFORM ON EMPLOYERS

President Obama signed the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010, ("Health Care Reform Law") into law in late March. The Health Care Reform Law contains numerous provisions that will alter the responsibilities of employers with respect to providing group health plan coverage to employees. This Bulletin discusses important provisions of the Law that are currently effective, or that become applicable to employers before 2012. This Bulletin does not describe all of the provisions that become effective before 2012, and we await guidance from governmental agencies to resolve some of the issues which various provisions present.

I. Provisions Having Immediate Impact

Health Care Coverage Exclusion for Adult Children. The Health Care Reform Law adds a provision which requires plans to cover adult children until age 26, effective for plan years beginning after September 23, 2010 (January 1, 2011 for calendar year plans). A related provision of the law extends the exclusion from income for the value of health insurance coverage and benefits to children of the employee who have not attained age 27 by the end of the year. However, this latter provision is effective as of March 30, 2010. As a result of this change, plans that currently cover adult children (such as insured plans in Connecticut), or which are amended to comply early with the new coverage requirement, can exclude the value of that coverage from the income of employees beginning March 30, 2010. Many insurance companies have announced that they will permit plans to comply early with this liberalized rule relating to the coverage of adult children. Employers may also permit employees to begin making pre-tax contributions of the employee's share of premium payments under a cafeteria plan to provide for such coverage for children who have not attained age 27 by the end of the year, and may allow reimbursement under a medical flexible spending account (FSA) for the unreimbursed medical expenses of such a child. However, such changes can be effective no earlier than March 30, 2010. The IRS has announced that cafeteria plans do not have to be amended until December 31, 2010 to provide for expanded pre-tax salary reduction contributions or expanded medical FSA reimbursements, notwithstanding its general rule that cafeteria plan amendments may only be made prospectively.



If you have any questions about the issues addressed here, or any other matters involving employee benefits law issues, please feel free to contact:

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Small Employer Tax Credit. The Health Care Reform Law provides for a new tax credit for small employers, including small tax-exempt employers, beginning with the 2010 taxable year. To be eligible, an employer must have no more than 25 full-time equivalent employees, and pay average wages that do not exceed \$50,000 per full-time equivalent employee (this amount is adjusted for cost-of-living beginning in 2013). The full credit is available to employers with 10 or fewer employees and average wages per full-time equivalent employee of less than \$25,000. The maximum credit is 35 percent of the employer's premium expenses (25% for tax-exempt employers), and in order to qualify, the employer must generally subsidize, on a uniform basis, at least 50% of the cost of the coverage. Not surprisingly, there are many nuances to this provision; there is also detailed information concerning this including Frequently Asked Questions on the IRS Website, www.irs.gov. Furthermore, the IRS recently issued detailed guidance in IRS Notice 2010-44. We suggest that you review the relevant information on the IRS Website for further information, and feel free to contact us, in the event that you think your business or organization may qualify for this subsidy.

Early Retiree Medical Reinsurance Program. The Health Care Reform Law requires that the Department of Health and Human Services (HHS) establish a program to provide reimbursement to participating employment-based plans for a portion of the cost of providing health benefits for retirees aged 55 to 64 and their spouses, surviving spouses, and dependents. This program may impact you if you provide coverage to early retirees. The program attempts to encourage employers to maintain such coverage, at least until 2014, when the major coverage aspects of the Health Care Reform Law become operational. The employer is entitled to receive reimbursement of up to 80 percent of the costs, minus negotiated price concessions, for benefit claims of an individual incurred and paid in a plan year between \$15,000 and \$90,000 (indexed for inflation). Claims incurred between the start of the plan year and June 1, 2010 count towards the \$15,000 threshold, but are not eligible for reimbursement. The proceeds (paid to the plan sponsor) may be used to reduce the costs of the program to the employer and/or participants in the Plan, but may not be used as general revenue for the plan sponsor. The program will end on January 1, 2014, or when HHS has exhausted the \$5 billion allocated to the program, if earlier.

HHS released an interim final rule in early May which implements this program, with an effective date of June 1. Employers can apply to be certified for the program through HHS, and applications will be available by the end of June. The interim final rule establishes eligibility rules and guidelines for applying for the program and using the available claim reimbursements. If you maintain a plan which provides for benefits for retirees between ages 55 and 64, we recommend that you investigate the program in greater detail and consider the advisability of applying for this program. However, since the government has limited the amount allocated this program, employers should submit their applications as soon as possible. Let us know if we can assist you in that regard.

Reasonable Break Time for Nursing Mothers. Effective immediately, employers must provide a reasonable break time for an employee to express breast milk for her child for the 1 year period following the child's birth, each time the employee has the need to do so. The employer does not have to pay the employee for the time. The employer must provide a place other than the bathroom, and free from intrusion, for mothers to use. An employer that employs fewer than 50 employees will not be subject to these requirements if satisfying them would cause undue difficulty or expense. Connecticut has a similar state law which has been on the books since 2001, and state laws continue to apply as well to the extent they provide greater protections than are provided under this new law.

Retiree Drug Subsidy Taxation. When Medicare Part D became law, it included a provision which allows employers (and benefit funds) to receive a Federal subsidy if they continue to provide retirees with prescription drug benefits. The Health Care Reform Law eliminates the tax deduction for the amount of the Medicare Part D retiree drug subsidy (i.e., the employer's allowable deduction for retiree prescription drug expenses must be reduced by the amount of the tax-free subsidy payments received). Although this provision does not apply until 2013, accounting rules require an immediate recognition of the changed tax treatment in an employer's financial statements. Some major U.S. corporations have announced that they have already booked significant changes. If your company receives retiree drug subsidy, the impact of this future change upon your financial statements must be considered.

II. Provisions Effective for the First Plan Year Beginning After September 23, 2010 (January 1, 2011 for Calendar Year Plans)

Adult Coverage to Age 26. As noted earlier, the Health Care Reform Law requires group health plans that offer coverage for dependent children to make coverage available to adult children until age 26, regardless of whether the child is married. For plan years starting prior to January 1, 2014, "grandfathered" plans need not extend such coverage if the child has an offer of employer-sponsored coverage.

Many states already impose similar mandates for insured plans. For example, Connecticut has such a requirement, although Connecticut's requirement applies to unmarried children, and requires that the child be a resident of Connecticut (unless under age 19 or a full-time student).

Grandfathered Plans. There are a number of provisions of the Health Care Reform Law that apply differently to grandfathered plans. A "grandfathered plan" is any plan in which an individual was enrolled on March 23, 2010. Renewals of participation or enrolling new employees after that date will not adversely affect a plan's grandfathered status. However, the Health Care Reform Act does not address what actions taken with respect to a plan will cause it to lose grandfathered status. There are also separate grandfathering provisions for plans maintained pursuant to a collective bargaining agreement in effect on March

23, 2010 until the date such agreement expires, and it is unclear at this point how these grandfathering provisions intersect. We anticipate that guidance will be provided on the subject of grandfathered status in future regulations. Until that guidance is issued, employers must take care before making changes or amendments to existing plans, since it is likely that changes to the underlying plan will result in loss of grandfathered status. The discussions below identify where the rules apply differently to grandfathered plans.

Pre-Existing Condition Limits. Group health plans (including grandfathered plans) cannot impose a pre-existing condition exclusion with respect to enrollees under age 19. Beginning in 2014, the prohibition applies to all covered individuals.

Ban on Annual and Lifetime Limits. The Health Care Reform Law generally prohibits health plans from imposing annual and lifetime limits on the dollar value of “essential” benefits such as hospitalization, prescription drugs, mental health and substance abuse, preventive services and chronic disease management. However, prior to January 1, 2014, plans may still impose certain annual limits, and the Health Care Reform Law directs that regulatory guidance be issued as to the permitted annual limits which may apply during this period. These limits apply to grandfathered plans.

Ban on Discrimination in Favor of Highly Compensated Individuals. The Health Care Reform Act prohibits an insured group health plan from discriminating as to eligibility to participate or as to benefit levels in favor of highly compensated employees. Rules similar to those that currently apply under the Internal Revenue Code relating to discrimination under self-insured health plans will also apply to insured arrangements. However, this prohibition does not apply to grandfathered plans.

Appeals Process. The Health Care Reform Act requires group healthcare plans to establish claims appeals procedures which are generally similar to those required for plans that ERISA covers. However, there is a requirement, not currently required under ERISA but customary in the case of group insured plans, to include an external review process. The plan’s internal claims procedure must allow a participant to receive continued coverage pending the outcome of the appeals process, although it is not clear how this works in cases where claims are ultimately denied. Grandfathered plans are not subject to this appeals process requirement.

Limitation on Over-the-Counter Medications; HSA Penalties. Beginning in 2011, medical FSAs, health savings accounts (HSAs) and health reimbursement accounts (HRAs) may not reimburse for the cost of over-the-counter medications unless the purchase is pursuant to a doctor’s prescription. This applies to grandfathered plans. In addition, beginning in 2011, the penalty tax on withdrawals from HSAs which are not used for healthcare will increase from 10% to 20%.

Miscellaneous Changes. Set forth below are a number of additional changes that are effective for plan years beginning after September 23, 2010:

- No cancellation or rescission of coverage allowed by the health insurer except in cases of fraud or misrepresentation. (Applies to grandfathered plans.)
- No prior authorization required for emergency services, whether provided by in-network or out-of-network providers, and emergency services must always be paid at the in-network level. (This does not apply to grandfathered plans.)
- No cost sharing requirements (i.e., first dollar coverage required with no deductibles or co-pays) for certain preventive health services, such as immunizations. (This does not apply to grandfathered plans.)
- No referral requirement for gynecologist visits. (This does not apply to grandfathered plans.)
- No limitations on participants' choice of primary care physicians and pediatricians from available participating primary care providers. (This does not apply to grandfathered plans.)

Safe Harbor Cafeteria Plans. An employer with 100 or fewer employees can establish a streamlined cafeteria plan that will not be subject to the nondiscrimination testing requirements applicable to cafeteria plans as long as certain minimum eligibility, participation and contribution requirements are met.

W-2 Reporting. The Health Care Reform Act requires employers to report the cost of employer-sponsored health coverage on an employee's Form W-2, excluding salary reduction contributions to an FSA or amounts contributed to an HSA. The calculation of the cost will be similar to the method for calculating the cost of COBRA coverage. This information will be first reported on W-2s issued in 2012 for the 2011 year. The provision applies to grandfathered plans. It appears that coverage under stand-alone dental and vision plans, long-term care and accidental and disability insurance may not have to be included.

III. Provisions with Uncertain Effective Dates.

Advance Notice of Material Modifications. The Health Care Reform Act generally requires a group health plan to provide advance notification of a material plan modification at least 60 days in advance of the effective date of the change. Although some commentators have suggested that this provision is effective for grandfathered plans for plan years beginning on or after March 23, 2010, and for new plans, plan years beginning on or after September 23, 2010, it is likely that it is not effective until other disclosure requirements become effective in 2012. Hopefully, this issue will be clarified through guidance in the near future.

When this provision becomes effective, plan sponsors will need to keep it in mind in numerous situations, such as when renewing insurance policies, or when considering whether to change insurers. Unlike a similar requirement applicable to pension plans, it applies to any material change and not merely to reductions in benefits. Employers and insurers will need to consider renewals earlier than in the past, so that changes can be timely communicated in accordance with this 60 day advance notice requirement.

Automatic Enrollment. Employers with more than 200 full-time employees must automatically enroll new full-time employees in the plan, and must automatically continue plan enrollment of current employees. The employer must provide notice of the automatic enrollment program and the ability to opt out of coverage. The Health Care Reform Bill does not include a specific effective date for this provision. However, it is likely that the provision will not be effective until after regulations concerning the provision are issued and become effective.

Conclusion. The Health Care Reform Act makes substantial changes to the rules dealing with the delivery of healthcare benefits through plans maintained by employers. It is important for employers to determine the plan design and cost implications of the new legislation on their plans. Keep in mind that the changes summarized here are ones that are effective in the near future, and many of the more significant changes in the law will not be effective until 2014. Note as well that many issues will need to be sorted out by regulation in the coming months, and that future legislative activity in this area is also likely.

Should you have any questions concerning the Health Care Reform Law or this Bulletin, please contact Bill Keenan at (860) 240-6028 or wkeenan@murthalaw.com, Lissa Paris at (860) 240-6032 or lparis@murthalaw.com, or Elizabeth Neuwirth at (203) 653-5411 or eneuwirth@murthalaw.com.

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