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Maintaining Grandfathered Plans Under Health Care Reform: Is it Worth the Bother?

BY CHARLES C. SHULMAN

The Patient Protection and Affordable Care Act of 2010 (''PPACA'') Section 1251 as amended by the Health Care and Education Reconciliation Act of 2010 (the ''Reconciliation Act,'' and collectively the ''Affordable Care Act'') Section 2301, provides that plans in effect on March 23, 2010 (date of enactment of PPACA) that have not materially changed are grandfathered and thereby exempt from some but not all of the requirements of the Affordable Care Act.

Charles C. Shulman has over 20 years of experience in employee benefits and executive compensation. He is admitted to practice in New Jersey and New York and may be reached at cshulman@ebeclaw.com, (201) 357-0577, or (212) 380-3834.

- Many companies are attempting to keep their health plans grandfathered—at least for the time being. (A survey by the Congressional Research Service notes that numerous comments to grandfather regulations show a desire of many companies to keep their health plans grandfathered.[1])
- With high health care inflation, many companies may find that grandfathering the plans (which precludes many cost-saving changes) is too expensive.
- The uncertainty of health care reform—judicial and legislative challenges and the delay of certain rules (nondiscrimination)—may be a reason to take a second look at whether grandfathering the plan is worth the cost.

Determination of Grandfathered Status

Treasury Regulation § 54.9815-1251T [2] provides the following rules for determining if the health plan coverage is grandfathered.[3] These regulations became effective June 14, 2010. The regulations were amended effective Nov. 15, 2010, as described below.[4]

(i) ***In Existence on March 23, 2010.*** The health coverage must have been in existence on March 23, 2010.[5]

(ii) ***New Insurer or New Contract Can Still be Grandfathered.*** As provided in the amended regulations, which

[1] See 38 Pens. & Ben. Rep. (BNA) 114 (Jan, 18, 2011) (9 PBD, 1/13/11; 38 BPR 114, 1/18/11).

[2] There are corresponding Department of Labor and Department of Health and Human Services regulations.

[3] 75 Fed. Reg. 34,538 (June 17, 2010).

[4] 75 Fed. Reg. 70,114 (Nov. 17, 2010).

[5] Treas. Reg. § 54.9815-1251T(a)(l)(i).

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are effective as of Nov. 15, 2010, health insurance coverage does not cease to be grandfathered merely because a new contract is entered into after March 23, 2010.[6]

■ A new insurer or a new contract with the existing insurer may continue to keep the plan grandfathered (as long as they do not materially change the benefits as outlined below).

■ These amended rules will generally not help for new contracts that became effective after June 14, 2010, but prior to Nov. 15, 2010.

■ In general, grandfathering applies even to new employees and family members who join a grandfathered plan after March 23, 2010.[7]

(iii) ***Each Benefit Package Considered Separately.*** The grandfathered rules apply separately for each benefit package, so that one benefit package under the plan may be grandfathered even if other benefit packages are not.[8]

■ For example, if a group health plan includes an HMO and a PPO, the loss of grandfathered status for PPO coverage will not blow grandfathering for the HMO coverage.

(iv) ***Statement That Administrator Believes Plan Is Grandfathered; Model Notice.*** The plan materials (e.g., the SPD) must contain a statement that the plan administrator believes that the plan is grandfathered.[9] The regulations contain a model notice satisfying the above requirement.[10]

(v) ***Records Showing Coverage as in Effect on March 23, 2010.*** The plan must maintain records—which must be made available on request—showing the coverage as in effect on March 23, 2010. Under the Nov. 17, 2010, amendments to the regulations, if there is a new policy, the new insurer must be given the prior plan terms (including benefits, cost-sharing, employer contributions, and annual limit) so that it can determine if the plan is still grandfathered.[11]

(vi) ***Anti-Abuse Rules.*** Under anti-abuse rules contained in the regulations:

(a) If the principal purpose of a merger or acquisition is to cover new employees under a grandfathered plan, it will lose grandfathered status.

(b) If employees are transferred from a grandfathered plan of the employer to another (less rich) grandfathered plan of the employer, this may cause loss of grandfathered status.[12]

■ Thus, although in general, grandfathering applies even to new employees who join a grandfathered plan, if the principal purpose of a transaction is to cover new employees in a grandfathered plan, or if employees are transferred to a different grandfathered plan for the purpose of changing the terms of their coverage, grandfathered status will be lost.

Maintenance of Grandfathered Status

The following rules apply regarding maintenance of grandfather status and when change to the terms of a plan will cause loss of grandfathered status:

(i) ***Reduction in Scope of Benefits.*** The elimination of any necessary element of benefits to diagnose or treat a particular condition will cause a loss of grandfathered status.[13]

■ For example, elimination of counseling for a mental health condition, or excluding necessary AIDS treatments would cause a loss of grandfathering.

(ii) ***Increase in Percentage of Coinsurance.*** An increase in the percentage of cost-sharing (coinsurance) will cause loss of grandfather status.[14]

■ For example, an increase in patient coinsurance for hospital bills from 20 percent to 25 percent would cause loss of grandfathering.

■ Note that an increase in the amount of coinsurance but no increase in percentage of coinsurance will not cause loss of grandfathering.

(iii) ***Increase in Deductible or Out-of-Pocket Limit by More Than 15 Percent Plus Medical Inflation.*** An increase in the fixed cost-sharing amount (other than copayment), i.e., the deductible or out-of-pocket limits, will cause loss of grandfathered status if such increase is more than 15 percent plus medical inflation above the March 23, 2010, amounts.[15]

■ For example, an increase in the participant annual deductible from $500 in 2010 to $600 in 2011 (a 20 percent increase) would be permissible if the medical inflation from 2010 to 2011 is, e.g., 6 percent, since 6 percent + 15 percent is more than the 20 percent increase in the amount of the annual deductible.

(iv) ***Increase in Office Copay Amount by More Than 15 percent (or $5) Plus Medical Inflation.*** An increase in the fixed-dollar copayment that exceeds the March 23, 2010, copayment amount by the greater of: (a) $5 increased by medical inflation or (b) medical inflation percentage plus 15 percent, will cause loss of grandfathering.[16]

■ For example, if the office visit copay is increased from $25 in 2010 to $40 in 2011 (a 60 percent increase), this would cause loss of grandfather status, assuming medical inflation is 6 percent, because 6 percent + 15 percent or $5 plus 15 percent both do not reach the 60 percent increase in office visit copay.

(v) ***Decrease in Employer Premium Contribution Rate Based on Cost or Formula by More Than 5 Percent.*** A decrease in the employer contribution rate for premiums based on cost of coverage (i.e., the employer contribution as percentage of total cost of coverage) or based on a formula, by more than 5 percent below the contribution rate on March 23, 2010, will cause loss of grandfathering.[17]

■ For example, if the employer decreases its share of premium payment from 80 percent to 75 percent (a 6.25 percent decrease), this decrease exceeds 5 percent and will cause loss of grandfather status.

(vi) ***Changes in Annual Limit.*** Changes in annual limit, including (a) the addition of an annual limit where there

[6] Treas. Reg. § 54.9815-1251T(a)(1)(i) & (ii) as amended in 75 Fed. Reg. 70,114 (Nov. 17, 2010).
[7] Treas. Reg. § 54.9815-1251T(b)(1).
[8] Treas. Reg. § 54.9815-1251T(a)(1)(i).
[9] Treas. Reg. § 54.9815-1251T(a)(2).
[10] Treas. Reg. § 54.9815-1251T(a)(2)(ii).
[11] Treas. Reg. § 54.9815-1251T(a)(3), as amended in 75 Fed. Reg. 70,114 (Nov. 17, 2010).
[12] Treas. Reg. § 54.9815-1251T(b)(2). See also § 54.9815-1251T(b)(3) Examples.
[13] Treas. Reg. § 54.9815.1251T(g)(1)(i).
[14] Treas. Reg. § 54.9815-1251T(g)(1)(ii).
[15] Treas. Reg. § 54.9815-1251T(g)(1)(iii).
[16] Treas. Reg. § 54.9815-1251T(g)(1)(iv).
[17] Treas. Reg. § 54.9815-1251T(g)(1)(v).

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was no annual or lifetime limit before, (b) the addition of an annual limit where there already was a lifetime limit (but no annual limit), as long as the new annual limit is less than the lifetime limit, or (c) a decrease in the annual limit for a plan that had a higher annual limit will cause loss of grandfathering.[18]

Transition Rules for Grandfathering The following transition rules apply:

(i) ***Changes That Were Instituted Before March 23, 2010.*** If there are changes to plans that were effective after March 23, 2010, but such changes were pursuant to a legally binding contract, pursuant to a filing with a state insurance department prior to March 23, 2010, or pursuant to written amendments that were made prior to March 23, 2010, the health insurance will remain grandfathered under transition rules.[19]

(ii) ***Changes Made After March 23, 2010, and Adopted Prior to Issuance of Regulations.*** If changes were made to the health insurance after enactment of PPACA (March 23, 2010) and prior to adoption of the regulations (June 14, 2010), but the changes are reversed for plan years beginning on or after Sept. 23, 2010, the grandfather status may be retained.[20]

(iii) ***Good Faith Interpretation Prior to Regulations.*** Where good faith reasonable interpretation of the grandfather requirements prior to issuance of the regulations (June 14, 2010) only modestly exceed the changes permitted by the regulations, the grandfather status can be retained.[21]

Provisions Already in Effect for 2011, Provided Plans Are Not Grandfathered

Provisions of the Affordable Care Act that become effective for plan years beginning on or after Sept. 23, 2010, *only if the plan is not grandfathered*, include the following:

(i) ***External Review.*** New procedures for claims, appeals, and external review under the Public Health Service Act (''PHSA'') Section 2719 are not applicable to grandfathered plans.

(ii) ***Preventative Care.*** Coverage of preventive care without any deductibles, e.g., immunizations or screenings, under PHSA Section 2713, is not applicable to grandfathered plans.

(iii) ***Nondiscrimination; Subsequently Delayed.*** Prohibition on discrimination in favor of highly-compensated individuals even for insured plans under PHSA Section 2716 (tax code Section 105(h) expanded beyond just self-insured plans) is not applicable to grandfathered plans.

■ (Notice 2011-1) (Dec. 21, 2010), however, delays the effective date and provides that the Internal Revenue Service, DOL, and HHS have determined that compliance with the nondiscrimination rules under PHSA Section 2716 will not be required, nor will sanctions be applied, until after regulations or other administrative guidance has been issued.

(iv) ***Primary Care Doctor.*** Right to select a participating primary care provider or pediatrician, and to see an obstetrician without a referral under PHSA Section 2719A is not applicable to grandfathered plans.

Provisions Already Effective Even for Grandfathered Plans

Provisions of the Affordable Care Act that become effective for plan years beginning on or after Sept. 23, 2010, *even for grandfathered plans* include:

(i) ***Restriction on Imposing Pre-Existing Condition Limit for Children Under 19.*** The prohibition on preexisting condition exclusion or discrimination based on health status under PHSA Section 2704 is effective for children under age 19 for group health plans even for grandfathered plans.

(ii) ***Rescission.*** Prohibition on rescissions after coverage begins except in the case of fraud or intentional misrepresentation under PHSA Section 2712 applies even to grandfathered plans.

(iii) ***Restriction on Annual Limits.*** Restrictions on annual limits for group health plans or lifetime limits under PHSA Section 2711 apply even to grandfathered plans.

(vi) ***Extension of Dependent Coverage Until Age 26.*** Requirement for health insurance issuers that provide dependent coverage to make it available for adult children until age 26 under PHSA Section 2714 already applies with regard to group health plans if the dependent is not eligible for other employer coverage, and applies even to grandfathered plans.

Uncertainty Regarding Health Care Reform

Federal district courts in Virginia and Florida have found the Affordable Care Act's insurance mandate unconstitutional,[22] with the Florida court voiding the entire law because of this. Other federal courts have upheld the law and its insurance mandate.[23] This conflict will likely have to be resolved by the Supreme Court. Legislative challenges to overturn the law have for the most part been unsuccessful, but continue. If the law is overturned, efforts to maintain the grandfather will be for naught.

As discussed above, a notice issued in December 2010 delayed nondiscrimination requirements that had already been in effect. Thus, employers who had taken the effort to maintain the grandfather found that at least with regard to nondiscrimination requirements, this was unnecessary.

Conclusion

Plans that can afford to adhere to the restrictions on decreased benefits and increased costs—and thereby maintain grandfather status—will be able to avoid application of certain Affordable Care Act requirements (such as external review, preventive coverage, nondiscrimination, and right to primary care doctor) that would otherwise have already gone into effect. Other

[18] Treas. Reg. § 54.9815-1251T(g)(1)(vi).
[19] Treas. Reg. § 54.9815-1251T(g)(2)(i).
[20] Treas. Reg. § 54.9815-1251T(g)(2)(ii).
[21] Preamble to final regulation 75 Fed. Reg. 34,538, 34,569 (June 17, 2010).

[22] *Commonwealth v. Sebelius*, 728 F. Supp. 2d 768 (E.D. Va. Dec. 13, 2010); *Florida v. U.S. Dep't of Health and Human Servs.*, 2011 WL 285683 (N.D. Fla., Jan. 31, 2011).
[23] See, e.g., *Thomas More Law Center v. Obama*, 720 F. Supp. 2d 882 (E.D. Mich. Oct. 7, 2010); *Liberty Univ. Inc. v. Geithner*, 2010 WL 4860299 (W.D. Va. Nov. 30, 2010).

Affordable Care Act requirements (such as restriction on pre-existing condition limit for children under 19, prohibition on rescissions after coverage begins, and restrictions on annual limits) do apply already even to grandfathered plans. The uncertainty of the Affordable Care Act due to judicial and legislative challenges, and delayed effective date of certain provisions, have caused some to question whether paying the increased costs to maintain the grandfather will in the end be cost productive.

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