

**TECHNICAL RELEASE 2011-04**

DATE: DECEMBER 2, 2011

SUBJECT: GUIDANCE ON REBATES FOR GROUP HEALTH PLANS PAID PURSUANT TO THE
MEDICAL LOSS RATIO REQUIREMENTS OF THE PUBLIC HEALTH SERVICE ACT**BACKGROUND**

Section 2718 of the Public Health Service Act (PHSA), 42 U.S.C. 300gg-18, as added by the Patient Protection and Affordable Care Act (Affordable Care Act) (Pub.L. 111-148, 124 Stat. 119), enacted on March 23, 2010, requires that health insurance issuers publicly report on major categories of spending of policyholder premium dollars, such as clinical services provided to enrollees and activities that will improve health care quality. The law establishes medical loss ratio (MLR) standards for issuers. Issuers are required to provide rebates to enrollees when their spending for the benefit of policyholders on reimbursement for clinical services and health care quality improving activities, in relation to the premiums charged (as adjusted for taxes), is less than the MLR standards established pursuant to the statute. Rebates are based upon aggregated market data in each State and not upon a particular group health plan's experience.

The Department of Health and Human Services (HHS) has promulgated regulations interpreting and implementing the requirements of section 2718 of the PHSA (75 FR 74864, December 1, 2010 (Interim Final Rule); 75 FR 82277, December 30, 2010 (Technical Correction); and 45 CFR Part 158 (Final Rule with comment period made available to the public on December 2, 2011, and scheduled to be published in the Federal Register on December 7, 2011).¹ In order to reduce burdens on issuers and to minimize the tax impacts on participants in and sponsors of group health plans, the regulations provide that issuers must pay to the policyholder any rebates owed to persons covered under a group health plan. The regulations do not give specific instructions to policyholders who are group health plans covered by the Employee Retirement Income Security Act of 1974 (ERISA) or the sponsors of such plans regarding their responsibilities under ERISA concerning rebates. However, when rebates are issued to such policyholders, issues concerning the status of such funds under ERISA and how such funds must be handled necessarily arise.

DISCUSSION

Distributions from health insurance issuers, such as insurance companies, to their policyholders, including employee benefit plans, take a variety of forms, including refunds, dividends,

¹ Regulations published by HHS pertaining to health insurance issuers implementing MLR requirements under the Affordable Care Act are being issued contemporaneously with this Technical Release. Subpart B of the regulation addresses the requirements for health insurance issuers in the group or individual market, including grandfathered health plans, to provide an annual rebate to enrollees, if the issuer's MLR fails to meet minimum requirements.

demutualization payments, rebates, and excess surplus distributions. To the extent that distributions, such as premium rebates, are considered to be plan assets, they become subject to the requirements of Title I of ERISA. Anyone with authority or control over plan assets is a “fiduciary,” as defined in section 3(21), and subject to, among other things, the fiduciary responsibility provisions of ERISA section 404 and the prohibited transaction provisions of ERISA section 406. Further, under section 403 of ERISA, plan assets generally must be held in trust, may not inure to the benefit of any employer, and must be held for the exclusive purpose of providing benefits to participants in the plan and their beneficiaries and defraying reasonable expenses of administering the plan. However, the trust requirement does not apply to any assets of a plan which consist of insurance contracts or policies issued by an insurance company qualified to do business in a State or to any assets of a plan which are held by such an insurance company. *See* ERISA sections 401(b)(2) and 403(b).

ERISA does not expressly define plan assets. The Department has issued regulations describing what constitutes plan assets with respect to a plan’s investment in other entities and with respect to participant contributions. *See* 29 C.F.R. §2510.3-101 and 29 C.F.R. §2510.3-102. In other situations, the Department has indicated that the assets of an employee benefit plan generally are to be identified on the basis of ordinary notions of property rights.

For group health plans, a distribution such as the rebate will be a plan asset if a plan has a beneficial interest in the distribution under ordinary notions of property rights. Under ERISA section 401(b)(2), if the plan or its trust is the policyholder, the policy would be an asset of the plan, and in the absence of specific plan or policy language to the contrary, the employer would have no interest in the distribution. On the other hand, if the employer is the policyholder and the insurance policy or contract, together with other instruments governing the plan, can fairly be read to provide that some part or all of a distribution belongs to the employer, then that language will generally govern, and the employer may retain distributions.

In the Department's view, however, the fact that the employer is the policyholder or the owner of the policy would not, by itself, indicate that the employer may retain the distributions. In determining who is entitled to the distribution, one would need to carefully analyze the terms of the governing plan documents and the parties' understandings and representations.

Under ordinary notions of property rights, if a contract is ambiguous, other evidence may be used to determine the intent of the parties. In the absence of more direct evidence, the Department has looked to the sources of the insurance policies’ premium payments.² For example, where the premium is paid entirely out of trust assets, it is the view of the Department that the entire amount received from the insurer by the policyholder constitutes plan assets.³

Similarly, assuming the plan documents and other extrinsic evidence do not resolve the allocation issue, the portion of a rebate that is attributable to participant contributions would be

² *See, e.g.*, Advisory Opinions 2001-02A (Feb. 15, 2001); 99-08A (May 20, 1999); 94-31A (Sept. 9, 1994); and 92-02A (Jan. 17, 1992).

³ *See id.* and DOL Information Letter to Theodore Groom (Feb. 15, 2001).

considered plan assets. Thus, if the employer paid the entire cost of the insurance coverage, then no part of the rebate with respect to this particular policy would be attributable to participant contributions. However, if participants paid the entire cost of the insurance coverage, then the entire amount of the rebate would be attributable to participant contributions and considered to be plan assets. If the participants and the employer each paid a fixed percentage of the cost, a percentage of the rebate equal to the percentage of the cost paid by participants would be attributable to participant contributions. If the employer was required to pay a fixed amount and participants were responsible for paying any additional costs, then the portion of the rebate under such a policy that does not exceed the participants' total amount of prior contributions during the relevant period would be attributable to participant contributions. Finally, if participants paid a fixed amount and the employer was responsible for paying any additional costs, then the portion of the rebate under such a policy that did not exceed the employer's total amount of prior contributions during the relevant period would not be attributable to participant contributions.

In any case, employers that sponsor group health plans that use insurance policies to provide benefits would be prohibited by ERISA section 403(c)(1) from receiving a rebate amount greater than the total amount of premiums and other plan expenses paid by the employer. To the extent that an employer's portion of the rebate exceeds the amount of such employer's total amount of premiums and other plan expenses paid, that excess amount must be held in trust for the exclusive benefit of participants and beneficiaries.

Decisions on how to apply or expend the plan's portion of a rebate are subject to ERISA's general standards of fiduciary conduct. Under section 404(a)(1) of ERISA, the responsible plan fiduciaries must act prudently, solely in the interest of the plan participants and beneficiaries, and in accordance with the terms of the plan to the extent consistent with the provisions of ERISA. With respect to these duties, the Department notes that a fiduciary also has a duty of impartiality to the plan's participants. A selection of an allocation method that benefits the fiduciary, as a participant in the plan, at the expense of other participants in the plan would be inconsistent with this duty. See Restatement (Second) of Trusts § 183 (requiring fiduciaries to "deal impartially with beneficiaries"). An allocation does not fail to be impartial or "solely in the interest of participants," for purposes of ERISA section 404(a)(1), merely because it does not exactly reflect the premium activity of policy subscribers. In deciding on an allocation method, the plan fiduciary may properly weigh the costs to the plan and the ultimate plan benefit as well as the competing interests of participants or classes of participants provided such method is reasonable, fair and objective. For example, if a fiduciary finds that the cost of distributing shares of a rebate to former participants approximates the amount of the proceeds, the fiduciary may properly decide to allocate the proceeds to current participants based upon a reasonable, fair and objective allocation method.⁴ Similarly, if distributing payments to any participants is not cost-effective (e.g., payments to participants are of *de minimis* amounts, or would give rise to tax consequences to participants or the plan), the fiduciary may utilize the rebate for other permissible plan purposes including applying the rebate toward future participant premium payments or toward benefit enhancements.

⁴ See Field Assistance Bulletin 2006-01 (April 19, 2006); ERISA Advisory Opinion 2005-08A (May 11, 2005); and DOL Information Letter to Theodore Groom (Feb. 15, 2001).

Where a plan provides benefits under multiple policies, the fiduciary should allocate or apply the plan's portion of a rebate for the benefit of participants and beneficiaries who are covered by the policy to which the rebate relates provided doing so would be prudent and solely in the interests of the plan according to the above analysis. However, the use of a rebate generated by one plan to benefit the participants of another plan would be a breach of the duty of loyalty to a plan's participants.

Under ERISA section 403(a), plan assets generally must be held in trust until appropriately expended. However, many group health plans receiving premium rebates do not maintain trusts because their premiums are paid from the general assets of the employer (including employee payroll deductions) and all benefits are paid by the policy issuers. In ERISA Technical Release 92-01 (TR 92-01, May 28, 1992), the Department stated that in the case of cafeteria plans established under section 125 of the Internal Revenue Code and certain other contributory welfare plans, it would not assert a violation solely for a failure to hold participant contributions to the plan in trust. In the case of these types of plans, with respect to which a trust is not established in reliance on TR 92-01, the Department would treat the trust relief under TR 92-01 and the limited reporting exemptions in 29 CFR §§2520.104-20 and 104-44 as available for premium rebates that are plan assets if they are used within three months of receipt by the policyholder to pay premiums or refunds as provided in §§2520.104-20 and 2520.104-44. For other plans not otherwise subject to the trust requirements of section 403(a) of ERISA, fiduciaries may take into account the cost of creating a trust when deciding how to expend rebates. For example, directing insurers to apply the rebate toward future participant premium payments or toward benefit enhancements adopted by the plan sponsor would avoid the need for a trust, and may, in some circumstances, be consistent with fiduciary responsibilities.

In some cases, the plan involved may have terminated before the rebate is paid to the policyholder. The HHS regulation at §158.242(b)(4) describes the issuer's obligations in the event that it cannot, despite reasonable efforts, locate the policyholder with respect to a terminated plan. In cases where the issuer is able to locate the policyholder with respect to a terminated ERISA-covered plan, we believe that the policyholder must comply with ERISA's fiduciary provisions in the handling of rebates that it receives, including looking to the plan document to determine how assets of the plan are to be allocated upon termination. Under ERISA section 403(d)(2), the assets of an employee welfare benefit plan that terminates must be distributed in accordance with the terms of the plan to the extent the plan terms are consistent with the provisions of Title I of ERISA and following the terms of the plan would not violate any other applicable federal law or regulation. If the plan document does not provide direction, the policyholder may need to determine if it is cost effective to distribute the plan's portion of the rebate to the relevant former participants in the plan.

CONCLUSION

Rebates paid pursuant to section 2718 of the PHS Act, in connection with group health plans covered by ERISA, may constitute plan assets. If the plan or its trust is the policyholder, in the absence of specific plan or policy language to the contrary, the entire rebate would constitute plan assets, and the policyholder would be required to comply with ERISA's fiduciary provisions

in the handling of rebates that it receives. If the plan sponsor is the policyholder, determining the plan's portion, if any, may depend on provisions in the plan or the policy or on the manner in which the plan sponsor and the plan participants have shared in the cost of the policy. Any portion of a rebate constituting plan assets must be handled in accordance with the fiduciary responsibility provisions of Title I of ERISA.

The Department expresses no view concerning the tax consequences of any action taken by a policyholder with regard to the receipt, holding, or distribution of the rebate. Such issues are exclusively within the jurisdiction of the Internal Revenue Service.

For Further Information Contact: Office of Regulations and Interpretations, Employee Benefits Security Administration, Department of Labor, at (202) 693-8510.