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Distribution of MLR Rebates

New final Medical Loss Ratio (MLR) rules direct group health plan issuers to provide rebates owed under a plan, if any, to the group policyholder (usually the employer) for distribution to the employees. The new rules make fundamental changes for insured employer-sponsored group health plans, including revised rules on who receives the rebates and how such amounts may be applied. Additional detailed rules address how plans sponsored by ERISA and non-federal governmental employers must distribute these rebates received from insurers. Insurers will be required to make the first round of rebates to consumers in 2012. Rebates must be paid by August 1st each year.

As background, the MLR rules are designed to ensure that health insurers in the individual and group market spend 80% to 85% of consumers' premiums on direct care for patients and efforts to improve care quality, and not on income, overhead and marketing. Insurance companies that fail to meet the new standard are required to provide a rebate to policyholders if the issuer has an MLR that is less than 85% in the large group market, or less than 80% in the small group market and individual market.

Rebate Guidance for Plans Subject to ERISA

Effective January 1, 2012, issuers must pay to the policyholder any rebates owed to persons covered under a group health plan. But the handling of rebates by ERISA-covered plans is not subject to HHS regulation, so instead, the DOL has provided technical release guidance giving instructions to policyholder/sponsors of group health plans covered by ERISA regarding their responsibilities under ERISA concerning rebates. Employers sponsoring ERISA-governed plans must determine if any portion of the rebate qualifies as ERISA “plan assets.” According to the guidance, if a group health plan (or its trust) is entitled to rebates under the MLR rules as a policyholder, rebates issued may constitute “plan assets,” and as such, the policyholder would be required to comply with ERISA fiduciary provisions for handling the rebates. However, if the plan sponsor is the policyholder (as opposed to the plan or the trust), then determining the plan's portion, if any, may depend on provisions in the plan on the manner in which the plan sponsor and the plan participants have shared in the cost of the policy. Here’s how this would work:

- According to DOL, if the employer is the policyholder, and the insurance policy (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. However, DOL cautions that 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, the terms of the governing plan documents and the parties' understandings and representations must be carefully analyzed.

- Assuming the plan documents and other extrinsic evidence do not resolve the allocation issue, DOL states that the portion of a rebate that is attributable to participant contributions would be considered plan assets. Specifically:
    - If the employer paid the entire cost of coverage, then no part of the rebate would be attributable to participant contributions. However, if participants paid the entire cost of coverage, then the entire amount of the rebate would be attributable to participant contributions and would be considered 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 that does not exceed the participants' total amount of prior contributions during the relevant period would be attributable to participant contributions.
    - If participants paid a fixed amount and the employer was responsible for paying any additional costs, then the portion of the rebate that did not exceed the employer's total amount of prior contributions during the relevant period would not be attributable to participant contributions.
- Any portion of a rebate that does constitute plan assets must be handled in accordance with ERISA's fiduciary responsibility provisions. Among other things, plan assets may not inure to the benefit of any employer, and must be held for the exclusive purpose of providing benefits to plan participants and their beneficiaries and defraying reasonable expenses of administering the plan. In deciding on a method of allocating rebates to plan participants, 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 so long as the method is reasonable, fair, and objective. Examples of allocation methods mentioned in the guidance include refunds to participants or reductions in future participant contributions or benefit enhancements. 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. Similarly, if distributing payments to any participant is not cost-effective—such as if payments are of de minimis amounts, or would give rise to tax consequences to participants or the plan—the fiduciary may use the rebate for other permissible plan purposes, including applying the rebate toward future participant premium payments or toward benefit enhancements.
- If a plan provides benefits under multiple policies, the fiduciary must 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, so long as if doing so would be prudent and solely in the plan's interests. 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.
- In addition, this Technical Release provides that prior DOL Technical Release 92-01 (which generally excuses insured group health plans from the obligation to hold participant contributions in trust and from the obligation to file Form 5500 as a funded plan) will be treated as applying to MLR rebates, provided they are used within three months of receipt to pay premiums or refunds.

Rebate Guidance for Non-federal Governmental Plans

Group health plans maintained by non-federal governmental employers (such as state and local governments) are not subject to ERISA, so HHS has issued separate [interim final regulations addressing non-federal governmental plans](). Under these regulations, the plan policyholder is required to use the portion of rebates attributable to the amount of premium paid by subscribers under the plan for the benefit of plan subscribers. This portion of the rebate must be used, at the option of the policyholder, either to reduce employee premium contributions or to provide cash refunds to employees covered by the group health policy on which the rebate is based. In either case, however, the rebate is to be used to reduce premiums for (or pay refunds to) employees enrolled during the year in which the rebate is actually paid (rather than the MLR reporting year on which the rebate was calculated).

Rebates Under Terminated Plans

In some cases, a plan may have terminated before the rebate is paid to the policyholder. DOL says that where the issuer is able to locate the policyholder of a terminated ERISA-covered plan, 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, the assets of an employee welfare benefit plan that terminates must be distributed in accordance with the terms of the plan to the extent that 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 plan participants.

Employer Next Steps

The MLR rules will likely make receipt of insurance company payments a more common occurrence for plan sponsors. In the past, this has been generally limited to experience-rated insurance policies and other special situations, like insurer demutualization distributions. Both ERISA-covered and non-ERISA plan sponsors should consult counsel to determine the best approach for handling rebates. ERISA plan sponsors unfamiliar with the applicable ERISA fiduciary rules may wish to consider what steps might be advisable in advance of the August 1, 2012 due date for the first rebates. ERISA sponsors will need to determine if any portion of a rebate qualifies as ERISA “plan assets” and then be clear as to how the plan assets portion of a rebate can be used (e.g., using the plan assets portion of a rebate for plan administrative expenses paid by the employer).

Should you have questions about this or any aspect of healthcare reform, contact your Conner Strong & Buckelew account representative toll free at 1-877-861-3220. For a complete list of Legislative Updates issued by Conner Strong & Buckelew, visit our online [Resource Center]().