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Wellness Incentives - Tax and Compliance Considerations

In an age of increased health risk awareness and ever-increasing health care costs, programs that promote wellness have become an important element of our society. Many workers in the United States have access to these programs through their employer's benefits packages. Wellness programs are considered to be an important component of employer benefit packages because they offer workers and their families access to programs to increase health and ultimately contribute to the development of less costly benefit packages.

An ever evolving body of law applies to wellness and disease prevention programs. Wellness programs featuring financial or other incentives are popular among employers, but there may be a tendency to overlook the federal and state laws that must be considered before implementation. Employers will need to keep an eye on the continuing legal developments and evaluate whether their wellness programs need any modification due to changing regulations. Since specific facts, program designs, and state laws raise different legal issues, employers should consult with legal counsel to determine the final compliance status of any wellness program.

Employers must take care to design their programs within various legal guidelines:

The Health Insurance Portability and Accountability Act: HIPAA prohibits group health plans from discriminating in eligibility, benefits, premiums or contributions because of an employee's health condition. For example, denying plan eligibility for smokers or requiring higher premiums for those with an elevated body mass index would be prohibited by HIPAA.

HIPAA does allow some exceptions for wellness programs. Only wellness programs that are, or relate to, a group health plan must comply with the HIPAA nondiscrimination rules. Wellness programs that provide incentives to promote healthy behaviors, but do not require an individual to meet specific health-related standards, do not violate the HIPAA nondiscrimination rules. Examples include fitness center reimbursements; incentives for attending health education classes; diagnostic-testing rewards that aren't based on test results; and reimbursements for the cost of smoking-cessation aids, regardless of whether the person quits smoking.

In terms of incentives, the US Department of Labor (DOL) issued very specific regulations relative to what wellness programs can and cannot do. The intent of the regulations is to ensure that no plan member is discriminated against by virtue of their being unable or incapable to participate in or benefit from a wellness incentive. For example, if the wellness plan requires one to walk or

exercise in order to enjoy a wellness incentive, those with physical limitation who are unable to do so would be discriminated against. A DOL Field Assistance Bulletin (FAB) 2008-02 provides guidance in the form of a checklist on the final regulations relating to the wellness provisions of HIPAA. The DOL has also issued a Frequently Asked Question document on the HIPAA nondiscrimination requirements.

The Americans with Disabilities Act and Other Federal Laws: There are various legal "wellness" concerns under the ADA and other federal laws. A Congressional Research Service report entitled Wellness Programs: Selected Legal Issues discusses "wellness" issues under nine federal laws: the Patient Protection and Affordable Care Act (the new health reform law), HIPAA, the ADA, the Genetic Information Nondiscrimination Act (GINA), the Age Discrimination in Employment Act (ADEA), Title VII of the Civil Rights Act, the National Labor Relations Act, the Internal Revenue Code, and Medicaid. The report operates as a general checklist to evaluate a wellness program's compliance with various federal laws.

State Laws: State law obligations depend on the facts of each wellness program. Employers are advised to consult local legal counsel to confirm compliance. A variety of factors affect whether a wellness program is subject to state law, including whether cash rewards or other wellness incentives are offered outside of a health plan; whether the wellness program or underlying health plan is insured or self-funded; whether incentives are provided through an ERISA plan; and what, if any, health-status factors (such as smoking) are targeted by the program. Common state requirements affecting wellness programs include smoker and other employment nondiscrimination laws, as well as restrictions on insured plans' premiums and eligibility incentives. Hawaii's Prepaid Health Care Act, which applies to both insured and self-funded plans, also presents some unique challenges to wellness programs. Self-insured ERISA plans are largely exempt from state insurance or employment nondiscrimination laws because of ERISA pre-emption. However, non-ERISA plans (such as self-insured governmental or church plans) may need to meet state nondiscrimination laws.

Tax Consequences: Some employer-sponsored wellness incentives have tax consequences. Employers that offer incentives should review these potential tax consequences with legal counsel. The general rule is that any compensation provided by an employer to its employees is taxable unless a specific Internal Revenue Code provision excludes it from income. Some wellness programs provide financial incentives such as gift certificates, cash, premium reductions, or dollars in a health reimbursement arrangement (HRA), flexible spending account (FSA) or health savings account (HSA). When the incentive is cash or a cash equivalent (no matter how small), such as a gift certificate, gift card, check, coupon or cash bonus, the incentive will be treated as fully taxable wages. The amount must be included as taxable income on the employee's form W-2 for the year, and federal employment taxes must be paid. Certain employer-provided "de minimis" fringe benefits, such as water bottles, t-shirts, baseball caps or one-day health club passes, are not taxed (as it would be unreasonable or administratively impracticable to account for them). When an incentive is related to a group health plan, such as reduced cost-sharing (premium reduction) or contributions or a payment into a health FSA, HRA or HSA, then the incentive may be excluded from taxation.

Healthcare reform: Federal healthcare reform also impacts wellness programs. The healthcare reform law has a variety of provisions aimed at encouraging wellness and disease prevention. For example, effective January 1, 2014, employers can offer premium discounts of up to 30% of the

cost of employer and employee premiums under the plan, for employees who participate in wellness programs that require the employee to satisfy a health standard. Existing wellness regulations under HIPAA limit wellness incentives to 20% of the total premium, provided certain conditions are met. Health care reform also allows government agencies to increase the discount up to 50% if they determine such an increase is appropriate. This change will give employers greater latitude in designing their wellness programs. In addition, the new law creates a $200-million, five-year program to provide grants to certain small employers (fewer than 100 employees) for comprehensive workplace wellness programs. The law also mandates a host of requirements and designs for almost all group health plans, so employers adopting a wellness program that qualifies as a group health plan or is part of a broader plan should make sure the program meets the new mandated reforms.

As additional information becomes available on this topic, Conner Strong & Buckelew will issue updates. We encourage you to contact your Conner Strong & Buckelew account representative toll-free at 1-877-861-3220 for assistance with wellness programs and design. For a complete list of Legislative Updates issued by Conner Strong & Buckelew, visit our online Resource Center.

connerstrong.com 877-861-3220 news@connerstrong.com Change My Preferences

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