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Employee Benefits | Life Insurance | Risk Management

**TO: Clients of Sitzmann Morris & Lavis Insurance Agency**

**RE: MLR Rebates**

The time has come for the medical loss ratio (MLR) rebate checks! As reported in the January issue of *Insurance Brief*, based upon the Department of Health and Human Services' final regulations and the Department of Labor's Technical Release No. 2011-04, our recommendation to clients is to use the rebate money to provide a reduction to current plan participants' contributions.

Key Provisions:

Under ERISA any monies attributable to employee payments are considered plan assets and must be used for the exclusive benefit of plan participants. If the employer pays 100% of employee and dependent premiums then there are no plan assets and the full rebate remains with the employer. The rebate must be used within 90 days of receipt or the employer will need to hold the money in a trust.

If payments to MLR year participants are not cost-effective (e.g., are "de minimis" or create tax consequences) the rebates may be used for other permissible purposes including premium reductions, cash payments or benefit enhancements. Under general principles, cash payments are W-2 wages for FICA and federal income tax withholding purposes.

Different rules apply to public agency and church plans. For these plans, only a reduction in premiums or refunds to employees is permissible. Benefit enhancement is not an option. In addition, church plans must enter into an agreement with the issuer to make a distribution.

What Portion of Rebate Goes to the Participant?

The employer must calculate both the amount of premiums paid by the employer and the amount paid by employees, as a percent of total premiums for the MLR year, calendar 2011. If the rebate is not for all policy designs with the carrier the calculation should only include those premiums paid for the rebated policy(ies). Please refer to our example below. Also note, that if the rebate is less than \$5 per participant, there is no duty to distribute it.

Allocation of the rebate to the individual participants need not reflect the exact contribution amount paid by the participant. This means that the same amount *can* be paid irrespective of age-banding or coverage tiers. However, you can also do the allocation based on share of premium paid if you want. The employer should document their allocation method. This will be yet another area that will fall under DOL audits.

If the plan has multiple policies, the rebate from one policy (PPO 20, PPO 30, HMO 25, etc.) should generally benefit only those covered by that policy. For example, if Anthem is only rebating their HMO 25 product then the employee share should be distributed to the HMO 25 participants only.

**Example:** Employer receives rebate check for Anthem HMO totaling \$1800. In 2011 the total premium for the HMO was \$100,000. The employer paid \$60,000 and the employees paid \$40,000, for a 60/40% split.  $\$1800 \times 60\% =$  employer share and  $\$1800 \times 40\% =$  \$720 in plan assets. Today there are 10 contributing participants in the Anthem HMO. The employer can reduce their contributions by a total of \$72 in lump sum or spread over two but not more than three months.

If a policy has been terminated and there is no successor policy, the regulations allow the employer to keep the rebate. They are under no obligation to distribute the rebate to former plan participants. If there is a replacement or successor policy, the employer may elect to use it to reduce future employee contributions to the replacement/successor policy or to enhance benefits.

Deadline: Rebates should be used within three months of receipt to pay premiums or refunds. If an employer fails to distribute the rebate within this time they will trigger a requirement to set up a trust account to hold the rebate monies and complete a 5500 filing for that trust.

If you cannot spend all of the rebate through premium reductions within the three month period paying a cash refund is recommended. Under this option all current participants receive a taxable payment which would be included on their W-2.

As always, contact your SML Account team if you have any questions.

The information provided in this legislative update for our clients and colleagues is for general guidance only and is not intended to be, and does not constitute, tax or legal advice. We recommend that you consult with your tax and legal advisors for the interpretation or application of any laws for your particular circumstances and situation.