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Health Care Reform: The Shrinking World of Grandfathered Health Plans

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On June 14, 2010 the Department of Treasury (IRS), the Department of Labor (DOL), and the Department of Health and Human Services (HHS) jointly issued [Interim Final Rules](#) (Rule) for group health plans and health insurance coverage relating to the status of grandfathered plans under the Health Reform Law. This Rule will be published in the Federal Register on June 17, 2010. The purpose of this Memorandum is to outline each of the key elements of this Rule which may result in an employer-sponsored group health plan's loss of its grandfathered status under the Rule.

Background

Section 1251 of the Reform Bill (Attachment A) exempts individual and group health plans from some but not all of the requirements established under Health Care Reform. This exemption is not a blanket exemption. The exemption lasts until the plan undergoes a "change". From the inception of the law until today, benefits professionals have speculated as to the meaning of "change". Now, we know, and it's not pretty.

About the Exemption

1. **The Grandfather Status Exemption Defined.** The exemption applies to all group health plans with at least one participant (insured or self-funded) and individual health policies in effect on March 23, 2010 (date of enactment). The exemption is not effected by:
 - Policy/Plan renewals (having no benefit changes and no change of carrier);
 - Enrollment of new or existing employees of the employer;
 - Additional or removal of eligible spouse or dependents; and,
 - Collective Bargaining Agreements in effect on March 23, 2010.
2. **The Exemption's Limited Scope.** Although the ostensible purpose of the exemption is to assure plan participants and plan sponsors that their group health plans can remain in place, at least for a while, Congress deemed it necessary to introduce key reforms applicable to all plans, whether grandfathered or not. The key reforms applicable to all employer-sponsored health plans phase in as follows:



Provision	Effective
Elimination of Pre-existing condition limitations for children under age 19 (Public Health Service Act (PHSA), Section 2704)	PYB: 9/23/10
Elimination of maximum lifetime benefit limit (PHSA, Section 2711)	PYB: 9/23/10
Elimination of annual benefit limits (except for limits set by HHS in regulations) (PHSA, Section 2711)	PYB: 9/23/10
Dependent covered to age 26 (PHSA, Section 2714)	PYB: 9/23/10
Rescission of coverage (PHSA, Section 2712)	PYB: 9/23/10
IRS W-2 reporting on value of coverage (Patient Protection and Affordable Care Act (PPACA), Section 9002)	Tax Year: 1/1/2011
Health FSA annual contribution limit to \$2,500 (PPACA, Section 9005)	Tax Year: 1/1/2013
Medicare tax increase (From 1.45% to 2.35% on wages over \$200,000) (PPACA, Section 9015)	Tax Year: 1/1/2013
Waiting periods limited to 90 days; Essential Health Benefits; cost sharing, etc. (PHSA, Section 2708 et al.)	PYB: 1/1/2014

3. **Losing Grandfathered Status.** Plans which lose grandfathered status based on the newly issued Rule, will become subject to a number of additional Health Reform requirements, including two rather important provisions:

Provision	Effective
Non-discrimination Testing (PHSA, Section 2716)	PYB: 9/23/10
Preventive Care (PPACA, Section 1001(5))	PYB: 9/23/10

4. **When Does the Loss of Status Occur?** For these changes, the effective date for compliance will be on the first day of the plan year beginning on or after September 23, 2010. For calendar year plans whose changes result in the loss of grandfathered status, the non-discrimination rules and preventive care benefits mandate will take effect on January 1, 2011. Plans whose plan year begins August 1, 2010 will have until August 1, 2011 until they become subject to the discrimination rules, preventive care, and the like.

The Interim Rules

1. **The Definition of Grandfathered Health Plan Coverage Explained.** The Interim Final Rules contain some critical enhancements on the application of the Rule.
- a) The Rule applies separately to each benefit package made available under a group health plan. This would mean, in a multiple choice environment, HMO coverage may still be grandfathered, but design or contribution changes to the PPO could disqualify the PPO as a





- grandfathered plan. The PPO, then, would be subject to the non-discrimination rules and the HMO would not.
- b) To preserve its status as a grandfathered plan, the plan materials provided to plan participants must contain a statement that the plan or the coverage believes it is a grandfathered health plan within the meaning of Section 1251 of the Law. The Rule contains model language for this statement. Please refer to Attachment B.
 - c) Furthermore, to preserve the grandfathered status, the Plan Sponsor must retain complete documentation of the plan or policy terms in effect on March 23, 2010. The Plan Sponsor must make these records available to participants as well s to plan regulators and must be kept for as long as the plan asserts it is grandfathered!
 - d) The Rule also will allow a Plan Sponsor to extend coverage to another employment class not previously eligible and, in the event of an acquisition, to the employees of the acquired entity, as long as the principal purpose for the merger is not for the purpose of allowing a group to avail itself of a grandfathered plan.
 - e) If the Plan Sponsor transfers employees from a grandfathered plan into another grandfathered plan, and the benefit differences or contribution requirements fail the tests discussed in Section 2 (Fatal Design Changes) of this Memorandum, then the original plan will lose its grandfathered status. For example, if the plan left behind had a \$20.00 office visit co-pay and the new plan has a \$40.00 office visit co-pay, then the new plan loses it grandfathered status, absent a bona fide employment-based reason to transfer the employees into the new plan. The Rule states that “changing the terms of cost or coverage” will not constitute a bona fide employment –based reason (54.9815-1251T(b)(2)(ii)(C)). Similarly, reducing the benefits of a plan option to equate to the plan option from which employees are transferred will result in the loss of grandfathered status.
 - f) The grandfathered status exemption will apply to plans established pursuant to Collective Bargaining Agreements (CBA) in effect on march 23, 2010. CBAs must permit its plans to comply with all other health reforms at the same time and manner as all other health plans, generally. All collectively bargained health plans will be grandfathered for the remaining term of the CBA with regard to non-discrimination testing rules and preventive care enhancements. In the event there are multiple bargaining units in one plan, then the plan will be grandfathered until the end of the plan year (or in some instances, tax year) in which the last Bargaining Agreement expires.
2. **Fatal Plan Design Changes.** In planning for plan years beginning on or after September 23, 2010, Plan Sponsors must take note of certain plan design changes that generally will terminate the grandfathered status exemption.
- a) Elimination of all or substantially all benefits to diagnose or treat a particular condition. For example, if a plan were to cease coverage for a particular mental health condition, or only eliminate counseling for that condition, the change will result in the loss of the exemption.



- b) Increase in the “percentage” cost-sharing requirement. The Rule here is referring to a 20% co-insurance requirement for inpatient surgery changing to a 25% co-insurance requirement.
 - c) Increase in a fixed amount cost sharing (other than co-pays). The Rule is referring to an increase in a deductible or out-of-pocket limit, generally, subject to a permissible increase (medical inflation based on the medical component of the Consumer Price Index plus 15%). In the example found in the Rule, a co-insurance increase from 20% to 25% causes the plan to lose its grandfathered status.
 - d) Increase in the fixed amount of any co-pay (e.g. \$30.00 per office visit) if it exceeds the greater of medical inflation plus \$5.00. The Rule’s example would permit an increase in office visit co-pays from \$30 to \$40, based on the medical inflation definition described in the Rule. Please refer to Attachment C for the definition of medical inflation.
 - e) Decrease in the employer contribution toward the cost of the plan by more than 5% below its contribution rate on March 23, 2010. The plan will lose its grandfathered status even though the 5% change is limited to one class/tier (e.g. employee only, employee plus one, etc.) only. This rule also applies to COBRA premiums.
 - f) Decrease in the employer contribution in excess of 5% where the contribution is based on a formula such as \$3.50 per hour worked, or commission benchmarks.
 - g) Any addition of an annual overall limit by dollar value for the plan itself, where the plan has no annual limit.
 - h) A decrease in the dollar value of an annual overall plan limit, whether there is a lifetime limit or not.
 - i) A decrease in the dollar value of an annual overall limit that is lower than the lifetime limit, if any.
3. **Transitional Rules.** The Interim Final Rules provide transitional rules for plans with a change in plan terms for changes made prior to March 23, 2010 which took effect subsequent to March 23, 2010.
- a) Changes effective after March 23, 2010 pursuant to a legally binding contract entered into on or before March 23, 2010.
Comment: Since there is not further explicit description and no examples given in the Rule, it is our view that May 1, 2010 plan renewals, for example, negotiated with plan issuers or possibly plan design changes agreed upon with bargaining units where such negotiations were complete prior to March 23, 2010 may be implemented after March 23, 2010 without causing the loss of grandfathered status.
 - b) Changes to a group health policy filed with a state insurance department by its issuer for state approval, where such filing occurred prior to or on March 23, 2010 where such changes take effect after March 23, 2010 may do so without causing the loss of a plan’s grandfathered status.



Comment: Issuers licensed to do business in a state must file all master policies and policy changes (e.g. for a particular class of business such as small group) for state approval prior to the issuance of the new policy in that state. It would appear that, although not explicitly stated in the Rule, if the issuer replaces an existing policy at renewal with plan changes and where the existing plan is no longer offered, that the policyholder will not lose grandfathered status by implementing the newly approved policy. Issuers may also file group health policies for large group that are unique to a particular policyholder and implement them without first obtaining the state's approval. It would appear that if the issuer filed in early March 2010, for example, and the policy took effect on May 1, 2010 or later, even these types of policies would be exempt under the grandfathered status provisions.

- c) Changes effective after March 23, 2010 pursuant to written amendments adopted by a plan on or before March 23, 2010 may also go into effect without causing the loss of grandfathered status.
- d) Changes adopted and made after March 23, 2010 and prior to June 17, 2010 (the date the Interim Final Rules will be made available for public inspection), where such changes do not violate the rules for changes discussed in Section 2 of this Memorandum (Fatal Design Changes), will not cause the loss of grandfathered status as long as they are:
 - i. Effective before June 17, 2010, or,
 - ii. After June 17, 2010 as a result of a legally binding contract, an issuer's policy change state filing prior to June 17, 2010, or pursuant to a written amendment adopted prior to June 14, 2010.

They must, however, be revoked or modified to be in compliance by the first day of the next plan year, or the plan will lose its grandfather status.

In Brief

For Plan Sponsors who consider their group health plans as exempt from certain Health Reform rules, must do three things to preserve that status:

- a) Must provide notice to plan participants and those eligible to participate (using the model notice provided in the Rule or something similar) in all benefit materials provided to them;
- b) Must keep all records describing the plan in effect on March 23, 2010 for as long as the Plan Sponsor desires the plan to retain grandfathered status ; and,
- c) Make no plan or contribution changes which will violate the limitations described in the Rule.

For a copy of the Interim Final Rules visit:

http://www.federalregister.gov/OFRUpload/OFRData/2010-14488_PI.pdf





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HCR: Grandfather Clause

H.R. 3590

SEC. 1251. PRESERVATION OF RIGHT TO MAINTAIN EXISTING COVERAGE.

(a) NO CHANGES TO EXISTING COVERAGE.—

(1) IN GENERAL.—Nothing in this Act (or an amendment made by this Act) shall be construed to require that an individual terminate coverage under a group health plan or health insurance coverage in which such individual was enrolled on the date of enactment of this Act.

(2) CONTINUATION OF COVERAGE.—With respect to a group health plan or health insurance coverage in which an individual was enrolled on the date of enactment of this Act, this subtitle and subtitle A (and the amendments made by such subtitles) shall not apply to such plan or coverage, regardless of whether the individual renews such coverage after such date of enactment.

(b) ALLOWANCE FOR FAMILY MEMBERS TO JOIN CURRENT COVERAGE.—With respect to a group health plan or health insurance coverage in which an individual was enrolled on the date of enactment of this Act and which is renewed after such date, family members of such individual shall be permitted to enroll in such plan or coverage if such enrollment is permitted under the terms of the plan in effect as of such date of enactment.

(c) ALLOWANCE FOR NEW EMPLOYEES TO JOIN CURRENT PLAN.—A group health plan that provides coverage on the date of enactment of this Act may provide for the enrolling of new employees (and their families) in such plan, and this subtitle and subtitle A (and the amendments made by such subtitles) shall not apply with respect to such plan and such new employees (and their families).

(d) EFFECT ON COLLECTIVE BARGAINING AGREEMENTS.—In the case of health insurance coverage maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers that was ratified before the date of enactment of this Act, the provisions of this subtitle and subtitle A (and the amendments made by such subtitles) shall not apply until the date on which the last of the collective bargaining agreements relating to the coverage terminates. Any coverage amendment made pursuant to a collective bargaining agreement relating to the coverage which amends the coverage solely to conform to any requirement added by this subtitle or subtitle A (or amendments) shall not be treated as a termination of such collective bargaining agreement.

(e) DEFINITION.—In this title, the term “grandfathered health plan” means any group health plan or health insurance coverage to which this section applies.

Attachment B

Sample Model Notice: Disclosure of Grandfather Status

This [group health plan or health insurance issuer] believes this [plan or coverage] is a “grandfathered health plan” under the Patient Protection and Affordable Care Act (the Affordable Care Act). As permitted by the Affordable Care Act, a grandfathered health plan can preserve certain basic health coverage that was already in effect when that law was enacted. Being a grandfathered health plan means that your [plan or policy] may not include certain consumer protections of the Affordable Care Act that apply to other plans, for example, the requirement for the provision of preventive health services without any cost sharing. However, grandfathered health plans must comply with certain other consumer protections in the Affordable Care Act, for example, the elimination of lifetime limits on benefits.

Questions regarding which protections apply and which protections do not apply to a grandfathered health plan and what might cause a plan to change from grandfathered health plan status can be directed to the plan administrator at [insert contact information]. [For ERISA plans, insert: You may also contact the Employee Benefits Security Administration, U.S. Department of Labor at 1-866-444-3272 or www.dol.gov/ebsa/healthreform. This website has a table summarizing which protections do and do not apply to grandfathered health plans.] [For individual market policies and nonfederal governmental plans, insert: You may also contact the U.S. Department of Health and Human Services at www.healthreform.gov.]

Attachment C

Medical Inflation Defined. For purposes of this paragraph (g), the term medical inflation means the increase since March 2010 in the overall medical care component of the Consumer Price Index for All Urban Consumers (CPI-U) (unadjusted) published by the Department of Labor using the 1982 – 1984 base of 100. For this purpose, the increase in the overall medical care component is computed by subtracting 387.142 (the overall medical care component of the CPI-U (unadjusted) published by the Department of Labor for March 2010, using the 1982 – 1984 base of 100) from the index amount for any month in the 12 months before the new change is to take effect and then dividing that amount by 387.142.