BLOG

MLR Rebate Considerations for Employers

By Erica Honig, J.D., Compliance Director, Employee Benefits

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This compliance bulletin discusses:

- What are MLR rebates and when they are distributed
- ERISA and tax considerations for MLR rebates
- Options available to employers that receive MLR rebates

Medical Loss Ratio (MLR) rebate season is quickly approaching and employers sponsoring fully insured group health plans are required to review their options on how to use or distribute these rebate funds within three months of receipt. Read on for more information.

MLR Rebate Background

Medical Loss Ratio (MLR) is the percentage of premiums health plan insurance carriers spend on claims and expenses that improve health care quality for plan participants. The MLR regulation within the Affordable Care Act (ACA) requires insurance companies to pay annual rebates if the MLR for groups of health insurance plans issued within a state is less than 85 percent for large employer group health plans and 80 percent for most small employer group health plans and individual policies. The goal of the MLR regulation is to ensure that a minimum percent of premiums is used to pay health plan claims by limiting the amount that insurance carriers can spend on plan administration, marketing, and profits. Insurance carriers that fail to meet the applicable state MLR thresholds are required to pay back excess profits in the form of rebates to their plan enrollees.

Since MLR rebates are calculated using aggregate data over an insurer's entire book of business within each applicable market segment in every state the insurer operates, MLR rebates are not based on the unique claims experience of an individual employer group health plan.

MLR rebate requirements apply only to **fully insured plans** and not self-funded or excepted benefit plans.

MLR Rebates & ERISA Plan Assets

MLR rebates for a particular year (commonly referred to as the rebate year) are calculated based on medical costs incurred during the *previous* calendar year. Insurance carriers are required to distribute MLR rebates and rebate notices to the policyholder of an ERISA[1] group health plan, typically the employer sponsoring the plan. This distribution deadline is **September 30th** of the rebate year. Employers who receive MLR rebates must determine what to do with these rebate funds and if the rebate is considered a plan asset under ERISA.

To determine if an MLR rebate (or any portion of it) is an ERISA plan asset, review the ERISA plan documents and insurance contracts. The language in these documents should address how to allocate MLR rebates from carriers. If the plan document or insurance contract is silent with respect to MLR rebates, then allocation of the rebates is determined by contribution toward plan premiums for the year related to the rebates. The Department of Labor (DOL) has provided guiding principles regarding allocation of MLR rebates in DOL Technical Release 2011-04. Generally, if a plan premium is 100% employer-paid, the MLR rebate is not considered an ERISA plan asset and the rebate may be retained by the employer. However, if plan participants contribute toward the premium, then a corresponding portion of the premium is treated as a plan asset and cannot be retained by the employer. For example, if an employer pays 75% of the plan premium cost and employees pay 25% of the cost, then 25% of the MLR rebate would be a plan asset.

MLR rebates that are considered plan assets under ERISA must be used for the benefit of plan participants and beneficiaries through one of the following methods:

- Pay a direct cash refund to plan participants;
- Provide current plan participants with a premium discount or premium holiday; or
- Use the plan assets to enhance plan benefits (such as adding a disease management or wellness program).

Group health plan fiduciaries may choose which method outlined above to handle MLR rebates as long as the method is fair, reasonable, and objective. For example, if a fiduciary finds that the cost of distributing proportional amounts of a rebate to former participants (i.e. terminated employees) approximates the amount of the proceeds, the group health plan fiduciary may properly decide to allocate the proceeds to current participants based upon a reasonable, fair, and objective allocation method.

MLR rebates typically must be used or distributed as soon as possible, but no later than **three months** after they are received.

Tax Treatment of MLR Rebates

The tax implications of MLR rebates for group health plans are outlined below:

- If employees paid their plan premiums through a Section 125 plan on a pre-tax basis, then any MLR rebate amount distributed to the employees will be treated as taxable income.
- If employees paid their plan premiums on a post-tax basis, then any MLR rebate distributed to the employees will ***not*** be treated as taxable income in the year in which it is received.

MLR Rebates for Multiple Insurance Policies

Certain employers sponsor ERISA health plans with several options under multiple insured policies. In these situations, MLR rebates should be allocated solely for the benefit of the participants covered under the specific insured policy receiving the rebate. For example, an employer's ERISA group health plan offers both a PPO and HMO plan option and the employer receives an MLR rebate in connection with the PPO plan. If any portion of that MLR rebate for the PPO plan constitutes plan assets, then that portion must be allocated for the sole benefit of the participants in the PPO plan and not for participants in the HMO plan.

Next Steps for Employers

As the MLR rebate distribution deadline of September 30th approaches, health plan insurance carriers are required to send a notice to the employer policyholder of the fully insured group health plan and to the enrolled members of the plan with details explaining the MLR rebate and how it was calculated for that rebate year. As a result, employers should be prepared to receive questions directly from employees who receive the insurance carrier notice regarding the MLR rebate. Moreover, employers may want to consider providing their own notice to employees explaining how the MLR rebate will be used, especially if the employer is not anticipating providing direct cash refunds to employees.

Reach out to your Risk Strategies account team with any questions regarding MLR rebates and for further assistance.

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[1] Employee Retirement Income Security Act of 1974 (ERISA)

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