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Expansion of association health plans (AHPs) – DOL final rules pave the way

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Primarily of interest to small employers and business owners with 50 or fewer employees, AHPs may also be of interest to some large employers

In October 2017, President Trump directed the Department of Labor (DOL) to issue new guidance that would allow more employers to form association health plans (AHPs). AHPs offer an opportunity for otherwise unrelated small employers (i.e., employers that do not have adequate common ownership) to group together to be considered a single large group health plan, thus avoiding certain Affordable Care Act (ACA) rules otherwise applicable to small group plans. Thus, AHPs are primarily of interest to small employers (50 or fewer employees), although some large employers may also have an interest in AHPs, such as a franchisor sponsoring an AHP for its franchisees.

In June, the DOL issued a final rule on AHPs. The final rule follows up on a proposed rule issued in January. The final rule provides a pathway toward more use of AHPs. Nevertheless, some issues still remain, including the application of state law.

Background

AHPs have been in existence well before now. If applicable rules are satisfied, the association is considered the "employer" under ERISA, with the result that the AHP is considered a single health plan. If applicable rules are not satisfied, then each participating employer is treated as the sponsor of a separate group health plan. Fully insured small-employer group health plans are subject to additional ACA requirements that do not apply to large group or self-funded plans, such as the requirement to offer essential health benefits (EHBs) and modified community rating. Through an AHP, a small employer may be able to avoid these additional requirements, potentially resulting in lower cost coverage (although possibly a narrower set of benefits).

Before the final rule, guidance as to when an association was considered the employer under ERISA was contained in DOL "sub-regulatory" guidance, such as opinion letters and bulletins, as well as case law. This pre-rule guidance generally sets forth two tests that must be satisfied for an association to be considered the "employer" for health plan purposes. First, the employer members of the association must have sufficient "commonality of interest." Second, the employers must exercise "control" over the association. Under the pre-rule guidance, it can be difficult to satisfy these tests. The final rule relaxes these requirements in many respects, particularly the "commonality of interest" rule, making it easier to form AHPs.

Highlights of key provisions in the final rule

The primary purpose of the association may be to offer health coverage, but the association must also have at least one substantial business purpose unrelated to providing benefits. This aspect of the final rule is somewhat more restrictive than the proposed rule, which would have allowed associations whose only purpose was to provide benefits. Many associations, however, will not find it difficult to satisfy the final rule because of the various ways the existence of a substantial business purpose may be demonstrated. The final rule does not define the term "substantial business purpose" but does provide a safe harbor under which a substantial business purpose is considered to exist if the association would be a viable entity even in the absence of sponsoring an employee benefit plan. The business purpose does not have to be a for-profit purpose. Examples of what may be considered a business purpose include providing conferences or other educational services to association members, acting as a standard-setting organization to establish business standards or best practices, engaging in public relations activities on issues of interest to members unrelated to health benefits and advancing the well-being of the industry in which association members operate through substantial activity in addition to providing health coverage. If an organization has operated with an active membership before offering benefits, the DOL considers that compelling evidence of a substantial business purpose.

Nondiscrimination rules generally prohibit different rating or eligibility rules for each employer member. The final rule aims to prevent discrimination based on health conditions by preventing AHPs from discriminating among and between employers or employees with regard to health status, including for eligibility or rating. An AHP may not treat member employers as distinct groups for applying the nondiscrimination rules, although certain other bona fide business distinctions other than health risk are permitted. Examples of bona fide business distinctions that may serve as a basis for charging different premiums for different employer groups (provided the distinction is not based on a health factor or directed at individual participants) include different occupations within a retail industry association (e.g., cashiers, stockers, sales associates) and industry subsectors within a geographically based association (e.g., construction, education, financial services). In addition, within any employer, different premiums may be based on nondiscriminatory factors such as part-time and full-time status.

"Working owners" such as sole proprietors and partners can participate if certain requirements are met (even if the business has no employees other than the owner and spouse). The final rule relaxes the requirements that must be satisfied for working owner participation compared to the proposed rule. A working owner must work on average at least 20 hours per week (or 80 hours per month in the business enterprise) or have income from the trade or business at least equal to the cost of coverage under the AHP. The final rule drops a provision in the proposed rule that would have prohibited a working owner from participating in an AHP if the working owner had access to other employer subsidized group health plan coverage, such as coverage through a spouse's employer. Initial eligibility of working owners must be determined by a plan fiduciary and eligible status must be monitored periodically through a reasonable process.

Relaxed commonality of interest test allows for geographically based AHPs. The final rule retains a modified version of the pre-rule AHP commonality of interest test. Under the pre-rule guidance, employers in the same line of business and same geographic location have been found to have requisite commonality of interest; however, employers that share only a common general interest, size or geographic location have been held not to demonstrate sufficient commonality. Thus, for example, pre-rule, the DOL found that a local chamber of commerce was not the "employer" (and therefore was not the proper sponsor of an AHP), where the primary economic nexus between the member employers was a commitment to private business development in a common geographic area. Under the final rule, the employers participating in an AHP will have commonality of interest if they are in the same trade, industry, line of business or profession. Additionally, the employers will have a commonality of interest under the final rule if their principal place of business is in the same geographic region within a single state or metropolitan area. For example, all employers in North Dakota would have commonality of interest, as would employers in the metropolitan Washington, D.C., area, regardless of whether they are in D.C., Maryland or Virginia. Those employers would not be required to share any additional business connection other than their location.

Control test is similar to pre-rule guidance. Historically, the DOL has not found that participating employers exercise control unless they have the authority to direct, replace, and supervise the plan's insurer/administrator and have the ability to amend the plan. Further, the DOL has typically required that each participating employer must be involved in designing and administering the plan offered to their employees. Typically, it has been difficult to determine if the participating employers satisfy the control test. Even the courts have had difficulty making this determination. In the final rule, the DOL confirms that the control test is intended to be consistent with the pre-rule guidance. Thus, the final rule does not significantly relax the pre-rule standard. The employer members must exercise control over the association and health plan in both form and substance, but this does not require that the employer members manage the day-to-day activities of the association or the plan. Pre-rule guidance generally requires regular nomination and election of directors, officers or representatives that control the AHP, as well as bylaws or similar formalities. An AHP will need to ensure the active involvement of participating employers.

Continued applicability of pre-rule guidance as an option. Associations that meet the requirements of the pre-rule guidance are not required to satisfy the requirements of the final rule in order for the AHP to be considered a single group health plan. There are two primary implications of organizing an AHP under pre-rule guidance compared to the more relaxed tests in the final rule. First, the nondiscrimination rule described above (which expressly provides that separate employer members may not be treated by the AHP as distinct groups for rating and other purposes) does not apply to AHPs that meet the requirements of the pre-rule guidance. Rather, whether such an AHP may treat employer members as distinct groups of similarly situated individuals is subject to HIPAA and depends on whether the creation or the modification of the classification is directed at individuals based on a health factor. In addition, the final rule clarifies that working owners without employees are not eligible to participate in AHPs organized under the pre-rule guidance. The DOL has explained that the more restrictive nondiscrimination rules are a trade-off for more flexible rules for treating the AHP as a single group health plan.

Effective dates are staggered. The effective date of the final rule is staggered based on the type of arrangement in order to give associations and plans time to adjust to the new rules. For fully insured AHPs, the final rule is effective on Sept. 1, 2018. For self-funded plans in existence on June 21, 2018 (the date the final rule was published), that meet the requirements of the pre-rule guidance and that choose to become an AHP as defined in the final rule, the final rule is effective on Jan. 1, 2019. In other situations where the association is being formed under the final rule, it is effective on April 1, 2019.

Specific Additional Compliance Concerns

Several important issues remain under the final rule, including:

State laws still apply to AHPs. AHPs are multiple employer welfare arrangements (MEWAs) under both pre-rule guidance and the final rule. Thus, an AHP is a MEWA even if it is considered a single plan at the association level rather than separate plans sponsored by each participating employer. One of the most significant consequences of this status is that ERISA has specific preemption provisions that allow states to regulate MEWAs, including self-funded MEWAs. Under ERISA, if the AHP is fully insured, state laws that require specified levels of reserves or contributions may apply to the AHP. Consequently, states can impose significant reserve and contribution requirements that might make it difficult to maintain a fully insured AHP in a state. Note, in addition to regulating the AHP, states may regulate insurance companies and insurance policies issued to an AHP.

If the AHP is self-funded, all state laws regulating insurance may apply to the extent such laws are not inconsistent with ERISA. Consequently, a self-funded AHP may be treated by a state the same as an insurance carrier issuing an insurance policy within that state, including but not limited to the requirement to provide "mandated" benefits. Currently, some state laws go so far as to prohibit self-funded MEWAs entirely or require significant registration and reserve requirements.

ERISA provides the DOL with the statutory authority to issue regulations exempting self-funded MEWAs from certain state laws (other than state laws relating to contribution and reserve requirements). However, the DOL has not previously issued any exemptions and similarly does not do so in the final rule. It is possible that there will be more cases challenging state laws as applied to self-funded AHPs as a result of the attempt to expand AHPs under the final rule.

Current state insurance laws might also present challenges to the formation of AHPs, even in states that are interested in expanding AHPs. For example, most states require that the association already be in existence for a certain number of years (typically five years) and organized for purposes other than providing insurance. Some states have minimum participation requirements. For example, North Carolina requires an association to have a minimum of 500 persons. Some states limit the types of entities that can form AHPs.

Those considering forming AHPs will need to consider state law carefully. Although some state legislatures might change their laws to match federal requirements, these changes may occur slowly.

Other federal laws may still apply. MEWAs are subject to the ACA insurance sector fee tax – regardless of whether they are self-funded or fully insured. This tax applies in 2018, is suspended for 2019 and will again apply after 2019, absent further congressional action. Questions also arise as to how certain federal laws based on employer size apply in the AHP context. For example, there is an exception to the parity requirements of the Paul Wellstone and Pete Domenici Mental Health Parity and Addiction Equity Act (MHPAEA) for small employers with no more than 50 employees during the preceding calendar year. In the final rule, the DOL states that this exception will be based on the total number of employees of all association members, rather than on the size of each employer member. As another example, the COBRA health care continuation rules do not apply if all employers maintaining a plan normally employed fewer than 20 employees on a typical business day during the preceding calendar year. DOL plans to consult with the IRS on the COBRA issue, and further guidance is expected in the future.

Federal law, through the Public Health Service Act (PHSA), requires that fully insured coverage provided to an employer through a bona fide association must be renewed by the insurer unless the employer's membership in the association terminates. The definition of "bona fide association" in the PHSA is narrower than the definition of association under the proposed rule. Thus, even if an AHP is considered a single large group health plan under the DOL guidance, the guaranteed renewal requirement would still apply unless the association meets the PHSA's definition of bona fide association. That definition requires, among other things, that the association has been in active existence for at least five years and was formed and maintained in good faith for purposes other than obtaining insurance.

Conclusion

The final rule paves the way for expansion of AHPs; however, it is still too early to tell just how quickly changes will occur and the extent to which various states will accommodate the new AHPs. AHPs formed under the final rule may be a favorable option for many small employers, whether they currently offer health coverage to employees or not. As with any health coverage, employers who consider participating in an AHP should carefully review what it may mean for them and consult their own advisors before making a final decision.