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Employee Benefits & Executive Compensation ADVISORY ■

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Recent Proposed Regulations Modify Requirements for Employer Wellness Programs

On November 26, 2012, the Departments of Labor, Treasury, and Health and Human Services (the "Departments") published proposed regulations (the "Proposed Wellness Rules") modifying the 2006 HIPAA wellness program regulations in light of the changes made to the statutory provisions by the Affordable Care Act (ACA).[1] Consistent with the ACA changes, the Proposed Wellness Rules increase the maximum reward that may be offered under a health-contingent program from 20 percent of the cost of coverage (as under the current regulations) to 30 percent, and up to 50 percent of the cost of coverage for tobacco cessation programs. However, for wellness plans that condition a reward on the satisfaction of a health-contingent standard—e.g., no smoking or attainment of a certain body mass index (BMI)—the Proposed Wellness Rules significantly change the way such health-contingent wellness incentive programs must be administered by adding new, stricter requirements for such plans. The proposed rules make a number of other modifications. This advisory discusses key aspects of the Proposed Wellness Rules as applied to group health plans. If finalized, the proposed rules would require changes to the design and administration of many wellness plans. Plan sponsors should review their wellness programs to determine what changes would be needed. The new rules are proposed to be effective for plan years beginning on or after January 1, 2014.

Background and Overview of Proposed Wellness Rules

As originally enacted in 1996, HIPAA's nondiscrimination rules generally prevent group health plans (and health insurance issuers offering group coverage) from discriminating against an individual based on a health factor. However, the HIPAA nondiscrimination rules do not prevent a group health plan (or health insurance issuer) from providing premium discounts, rebates, or modifications to plan cost-sharing amounts in return for adherence to programs of health promotion or disease prevention. The HIPAA statutory provisions did not provide specific rules for the implementation of the wellness program exception. Final regulations specifying the requirements for wellness programs were issued by the Departments in 2006 (the "2006 Regulations").[2]

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1 77 Fed Reg 70620 (Nov. 26, 2012).

2 Final regulations on the HIPAA wellness program rules were published on December 13, 2006, at 71 Fed Reg 75014.

The ACA changes with respect to the HIPAA nondiscrimination rules are codified in section 2705 of the Public Health Service Act (PHSA) and incorporated by reference into the Internal Revenue Code (the "Code") and ERISA. The ACA modifies the provisions regarding wellness programs in several respects, as follows:

- Key provisions of the HIPAA wellness program regulations were codified in section 2705(j) of the PHSA (which is incorporated by reference in the Code and ERISA); and
- The statute permits a reward of up to 30 percent of the cost of coverage and authorizes the Departments to increase the reward to up to 50 percent in certain cases. [3]

The Proposed Wellness Rules replace the 2006 Regulations for plan years beginning on or after January 1, 2014. Following the statutory provisions, the Proposed Wellness Rules increase the maximum permissible reward (or penalty) under a health-contingent wellness program offered through a group health plan from 20 percent to 30 percent of the "cost" of health coverage (for this purpose, "cost" is generally the COBRA rate excluding the additional two percent administrative fee). The Departments also exercised their regulatory authority by increasing the maximum possible reward (or penalty) for wellness plans aimed at tobacco use to 50 percent. The same rules apply to both grandfathered plans and non-grandfathered plans.

Most significantly, the proposed rule modifies the requirements of reasonable design and reasonable alternatives for health-contingent wellness programs by adding new, stricter requirements for such plans.

Rules for Participatory Wellness Programs

Like the 2006 Regulations, the Proposed Wellness Rules make a distinction between participatory wellness programs and health-contingent wellness programs.

Participatory wellness programs are programs that either do not require an individual to meet a standard related to a health factor to obtain a reward or do not offer a reward at all. Examples cited in the Proposed Wellness Rules include a fitness center reimbursement program, a diagnostic testing program that does not base rewards on test outcomes, a program that waives cost-sharing for prenatal or well-baby visits, a program that reimburses employees for the costs of smoking cessation regardless of whether the employees quit smoking and a program offering rewards for attending a free health education seminar.

The Proposed Wellness Rules clarify that such plans comply with the nondiscrimination requirements as long as participation in the program is available to all similarly situated individuals. There is no limit on financial incentives for participatory wellness programs, and they do not have to meet the requirements for health-contingent wellness programs.

Rules for Health-Contingent Wellness Programs

A health-contingent wellness program is defined in the Proposed Wellness Rules as a program that bases any portion of a reward on an individual satisfying a standard that is related to a health factor. The preamble also describes a health-contingent program as one that requires an individual to "do more" than a similarly situated individual in order to obtain the same reward. This includes wellness programs that require an individual to attain or maintain a certain health outcome in order to obtain a reward (such as not smoking, attaining certain results on biometric screenings or meeting exercise targets).

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[3] The ACA also extended the nondiscrimination provision to the individual market. The wellness program exception does not apply in the individual market; instead, the ACA authorizes a demonstration program for wellness programs in the individual market.

The Proposed Wellness Rules generally maintain the five requirements for health-contingent wellness programs set forth in the 2006 Regulations, but modify the requirements in certain respects. For example, the range within which permitted incentive/penalty arrangements can operate is increased generally from 20 percent to 30 percent of the cost of coverage. Perhaps more significantly, as discussed below, the Proposed Wellness Rules require that an alternative method of compliance be extended to anyone who cannot meet a health-related standard (even if they are not medically incapable of meeting the standard due to a medical condition). The Proposed Wellness Rules also require that certain alternative compliance costs (e.g., a smoking cessation clinic or obesity treatment program) be paid for by the plan. The five requirements, as modified by the Proposed Wellness Rules, are summarized below.

1. Frequency of Opportunity to Qualify

As under the 2006 Regulations, individuals must have the opportunity to qualify for a reward at least once per year. Thus, an opportunity to requalify each year must be extended even if a participant has repetitively failed to meet a goal or complete established requirements.

2. Size of Reward

In general. The total reward cannot exceed a specified percentage of the total cost of employee-only coverage, taking into account both employer and employee contributions. This is typically referred to as the "COBRA cost" of coverage, less the applicable two percent administrative charge. If dependents can participate in the plan, the reward cannot exceed the applicable percentage of the total cost of coverage in which the employee and dependents are enrolled. In addition, the Departments have requested comments as to whether (and if so, how) a reward should be apportioned among family members if the program is offered to family members and only some qualify for the reward. Such a rule, if adopted, could add more administrative complexity to wellness programs.

The 2006 Regulations capped the permissible reward at 20 percent of the total cost. In accordance with the ACA changes, the Proposed Wellness Rules generally increase the maximum reward to 30 percent.

Tobacco use. In addition, the Departments exercised their regulatory authority by proposing a reward of up to 50 percent for programs designed to prevent or reduce tobacco use. The Departments indicated they raised the limit for tobacco use to 50 percent to provide consistency with the modified community rating rules, which go into effect in 2014 and which permit health insurance issuers in the small and individual market to vary premiums for tobacco use by a similar factor. Also, to provide consistency, HHS has issued a separate, proposed rule that permits insurers in the small group market to implement a premium differential based on tobacco use only in connection with a wellness program that meets the standards set forth in the Proposed Wellness Rules. Under the Proposed Wellness Rules, tobacco use can only affect rewards/penalties from 30 to 50 percent, while other wellness-related factors can impact the initial 30 percent of the reward/penalty. The Departments left open the issue of what constitutes "tobacco use" (e.g., have/have not used tobacco in last 30 days) for purposes of the additional 20 percent reward/penalty and asked for comments on that issue.

3. Uniform Availability and Reasonable Alternative Standards

Under the Proposed Wellness Rules, the reward/penalty under a health-contingent wellness program must be available to all similarly situated individuals. Consistent with the 2006 Regulations, the Proposed Wellness Rules provide that either a reasonable alternative standard or waiver of the standard must be provided for any individual for whom it is either unreasonably difficult due to a medical condition or medically inadvisable to meet the applicable standard.

If a plan offers a reasonable alternative standard, the same full reward must be available to individuals who qualify for that alternative. Instead of implementing an alternative, a plan can also waive the standard and provide the reward, either for an entire class of individuals or on a case-by-case basis. Plans do not have to establish an alternative standard in advance of a request, but it must be provided (or the original standard waived) upon request. In addition, a participant's failure to meet an alternative standard does not excuse the plan from offering the same, or a new, standard in the future.

All of the facts and circumstances are taken into account in determining whether an alternative is reasonable. In addition, the Proposed Wellness Rules impose new cost requirements on plans by providing that the following must be satisfied for an alternative standard to be reasonable:

- If the program is the completion of an educational program, the plan must make the program available instead of requiring the individual to find one, and it cannot require an individual to pay for it.
- If the program is a diet plan, the plan or issuer must pay for a membership or participation fee, but does not have to pay for the cost of food.
- If a medical professional who is the employee or agent of the plan makes a recommendation and a participant's personal physician states that such a recommendation is not medically appropriate, the plan must provide a reasonable alternative standard that accommodates the recommendations of the personal physician. The plan may, however, impose standard cost-sharing for coverage of medical items and services under the physician's recommendations.

Plans may seek verification that a health factor makes it unreasonably difficult, or medically inadvisable, for an individual to meet the otherwise applicable standard. The Proposed Wellness Rules add that physician verification may only be allowed if it is reasonable under the circumstances to do so and that it is not reasonable, for example, for a plan to seek verification of a claim that is obviously valid based on the nature of the individual's medical condition that is known to the plan.

4. Reasonable Design

The Proposed Wellness Rules, like the 2006 Regulations, require that health-contingent wellness programs be reasonably designed to promote health or prevent disease, not be overly burdensome, not be a subterfuge for discrimination based on health factor and not be highly suspect in the method chosen to promote health or prevent disease. The Proposed Wellness Rules add that whether a design is reasonable is based on all of the relevant facts and circumstances. They state that to the extent a plan's initial standard for obtaining a reward is based on the results of a measurement that is related to a health factor such as biometric screening, the plan is ***not*** reasonably designed unless it makes available a different, reasonable means of qualifying for the reward for any individuals who fail to meet the standard. This means that the alternative must apparently be offered to everyone, even if they are not precluded from satisfying the requirement due to a medical condition.

5. Notice of Other Means of Qualifying for the Reward

Finally, the Proposed Wellness Rules require plans or issuers to disclose the availability of other means of qualifying for a reward, including the possibility of a waiver of the otherwise applicable standard, in all plan materials describing the terms of a health-contingent wellness program. The Proposed Wellness Rules clarify that a mere mention that a program is available, without describing its terms, do not trigger this disclosure requirement.

The Agencies have included the following updated sample text that plans may use to satisfy this requirement:

> Your health plan is committed to helping you achieve your best health status. Rewards for participating in a wellness program are available to all employees. If you think you might be unable to meet a standard for a reward under this wellness program, you might qualify for an opportunity to earn the same reward by different means. Contact us at [insert number] and we will work with you to find a wellness program with the same reward that is right for you in light of your health status.

Application to the Individual Health Insurance Market

The ACA applies the HIPAA nondiscrimination protections to all non-grandfathered health insurance coverage, beginning for policy years on or after January 1, 2014. However, the wellness program exception to the nondiscrimination provisions does not apply in the individual market, and the Proposed Wellness Rules would not apply in the individual market. Instead, the ACA provides for a demonstration project for wellness programs in the individual market.

This advisory was prepared by **Stacy Clark**, **John Hickman** *and* **Carolyn Smith**.

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If you have any questions or would like additional information, please contact your Alston & Bird attorney or any of the following:

Robert A. Bauman
202.239.3366
bob.bauman@alston.com

Saul Ben-Meyer
212.210.9545
saul.ben-meyer@alston.com

Emily Seymour Costin
202.239.3695
emily.costin@alston.com

Patrick C. DiCarlo
404.881.4512
pat.dicarlo@alston.com

Ashley Gillihan
404.881.7390
ashley.gillihan@alston.com

David R. Godofsky
202.239.3392
david.godofsky@alston.com

John R. Hickman
404.881.7885
john.hickman@alston.com

H. Douglas Hinson
404.881.7590
doug.hinson@alston.com

Emily C. Hootkins
404.881.4601
emily.hootkins@alston.com

James S. Hutchinson
212.210.9552
jamie.hutchinson@alston.com

Johann Lee
202.239.3574
johann.lee@alston.com

Blake Calvin MacKay
404.881.4982
blake.mackay@alston.com

Emily W. Mao
202.239.3374
emily.mao@alston.com

Douglas J. McClintock
212.210.9474
douglas.mcclintock@alston.com

Craig R. Pett
404.881.7469
craig.pett@alston.com

Earl Pomeroy
202.239.3835
earl.pomeroy@alston.com

Jonathan G. Rose
202.239.3693
jonathan.rose@alston.com

Syed Fahad Saghir
202.239.3220
fahad.saghir@alston.com

Thomas G. Schendt
202.239.3330
thomas.schendt@alston.com

John B. Shannon
404.881.7466
john.shannon@alston.com

Richard S. Siegel
202.239.3696
richard.siegel@alston.com

Carolyn E. Smith
202.239.3566
carolyn.smith@alston.com

Michael L. Stevens
404.881.7970
mike.stevens@alston.com

Daniel G. Taylor
404.881.7567
dan.taylor@alston.com

Laura G. Thatcher
404.881.7546
laura.thatcher@alston.com

Elizabeth Vaughan
404.881.4965
beth.vaughan@alston.com

Kerry T. Wenzel
404.881.4983
kerry.wenzel@alston.com

Kyle R. Woods
404.881.7525
kyle.woods@alston.com

ALSTON&BIRD LLP

WWW.ALSTON.COM

ATLANTA: One Atlantic Center ■ 1201 West Peachtree Street ■ Atlanta, Georgia, USA, 30309-3424 ■ 404.881.7000 ■ Fax: 404.881.7777
BRUSSELS: Level 20 Bastion Tower ■ Place du Champ de Mars ■ B-1050 Brussels, BE ■ +32 2 550 3700 ■ Fax: +32 2 550 3719
CHARLOTTE: Bank of America Plaza ■ 101 South Tryon Street ■ Suite 4000 ■ Charlotte, North Carolina, USA, 28280-4000 ■ 704.444.1000 ■ Fax: 704.444.1111
DALLAS: 2828 North Harwood Street ■ 18th Floor ■ Dallas, Texas, USA, 75201 ■ 214.922.3400 ■ Fax: 214.922.3899
LOS ANGELES: 333 South Hope Street ■ 16th Floor ■ Los Angeles, California, USA, 90071-3004 ■ 213.576.1000 ■ Fax: 213-576-1100
NEW YORK: 90 Park Avenue ■ 12th Floor ■ New York, New York, USA, 10016-1387 ■ 212.210.9400 ■ Fax: 212.210.9444
RESEARCH TRIANGLE: 4721 Emperor Blvd. ■ Suite 400 ■ Durham, North Carolina, USA, 27703-85802 ■ 919.862.2200 ■ Fax: 919.862.2260
SILICON VALLEY: 275 Middlefield Road ■ Suite 150 ■ Menlo Park, California, USA, 94025-4004 ■ 650-838-2000 ■ Fax: 650.838.2001
WASHINGTON, DC: The Atlantic Building ■ 950 F Street, NW ■ Washington, DC, USA, 20004-1404 ■ 202.756.3300 ■ Fax: 202.756.3333
VENTURA COUNTY: 2801 Townsgate Road ■ Suite 215 ■ Westlake Village, California, USA, 91361 ■ 805.497.9474 ■ Fax: 805.497.8804