



Medical Loss Ratio Rebate Checks

A Case Study on Rebate Distribution to Employer Group Plan Participants

A group health plan subject to ERISA is offered to 20 employees. The total cost the group plan paid for premiums in 2011 was \$90,000, and of that total, the employer paid \$72,000 (80%) and the employees paid \$18,000 (20%). The employer received a medical loss ratio rebate check in July of 2012 for \$500.

The employer's first step should be to review existing plan documents to verify if the plan has a policy for addressing premium refunds and rebates. Assuming that there isn't one (as is the case for most group plans) the employer may keep \$400 as it represents the share of the total rebate check directly attributable to the costs the company pays towards all employees and their dependents. The employer may wish to check with a tax advisor to determine how best to deal with the rebate funds attributable to the employer. The portion leftover is \$100 and the employer has the responsibility to treat it as "plan assets" and handle it in accordance with ERISA's general standards of fiduciary conduct. Among other things, this means that the employer must handle distribution of the rebate funds within three months to avoid having to establish an ERISA trust account for these plan assets.

Within the group, four employees have declined or waived coverage, so they are not entitled to a rebate. This means 16 total employees are covered by the plan, but one is a new employee who joined the plan in 2012. Since that employee was not on the plan in 2011, he is not entitled to a rebate either. Of the remaining 15 employees, five employees have single coverage and the employer pays 100% of their premiums. Five employees have self plus spouse coverage and their share is \$100/month. The five other employees have family coverage and pay \$200/month. All of the employees who pay into the plan contribute on a pretax basis via a section 125 cafeteria plan.

Total Employees in 2012	20
<i>Employees who have declined or waived coverage (not eligible)</i>	<i>-4</i>
<i>Employee joining plan in 2012 (not eligible)</i>	<i>-1</i>
<i>Employees with employer-paid single coverage (not eligible)</i>	<i>-5</i>
Total Employees to consider for rebates	10

Rebate Distribution Option One:

The employer may decide to fairly and equitably split the remaining rebate funds between the employees who pay into the group plan. If this is the employer's decision, then the five employees who pay nothing towards their costs because they have single coverage get no share of the rebate. The employer should split the \$100 left among the ten paying employees in a fair and equitable way. So, the employer could give the 10 employees who pay into the premiums each \$10 or the employer could give the five employees who pay towards spousal coverage \$6.66 each and the five with family coverage \$13.33 each.

The employer then has the choice of how to distribute these funds. The employer could reduce the premium contribution employees pay toward the plan for one pay period. The employer could also issue each a separate check or include the rebate amount in a future paycheck. In all cases, since the employees originally paid their premiums on a pre-tax basis, the rebate is taxable income. If a direct check is issued, the check is subject to all payroll and income tax deductions. If a premium credit is applied to the employee's share, then their monthly salary will correspondingly go up and be taxed at the higher amount.

Rebate Distribution Option Two:

Alternatively, since the amount of the total rebate attributable to employees is very small, the employer has the option of providing an enhanced benefit to the entire group plan with the money. So for example, the employer could use the \$100 total employee share of the rebate to hire a nutritionist to give a "lunch and learn" presentation to employees and provide them with a healthy lunch. This option could benefit all plan participants generally and would not lead to any tax consequences for employees.

No matter which choice is made, the employer should document all actions taken regarding the rebate.