

NONDISCRIMINATION REQUIREMENTS IN A NUTSHELL



NOTE *The effective date for the Section 105(h) nondiscrimination requirements for fully-insured groups has been delayed indefinitely pending the release of regulations.*

- *Self-funded plans will continue to be required to comply with Section 105(h) requirements.*
- *ANY group health plan taking pre-tax premiums must continue to comply with Section 125 nondiscrimination requirements.*
- *Fully-insured groups only are not required to comply with the Section 105(h) requirements below until regulations are released.*

Section 105(h) for Fully Insured and Self-Funded Group Health Plans	Section 125 Cafeteria Plans for Pre-Tax Premiums
<p>Highly Compensated Individuals (HCI)=</p> <ul style="list-style-type: none"> • One of the five highest-paid officers; OR • A more than 10% shareholder or his/her spouse/dependent; OR • One of the highest-paid 25% of all employees. <p>The plan cannot discriminate in favor of HCIs. A plan that provides greater benefits to HCIs is a top-heavy plan and will not pass the required nondiscrimination tests.</p>	<p>Highly Compensated Individuals (HCI)=</p> <ul style="list-style-type: none"> • An officer of the company; • A more than 5% shareholder; • An employee who earns \$110,000+ for 2010; & • A spouse/dependent of any of the above. <p>The plan cannot discriminate in favor of HCIs. A plan that provides greater benefits to HCIs is a top-heavy plan and will not pass the required nondiscrimination tests.</p>
<p>Basic Plan Design Considerations:</p> <ol style="list-style-type: none"> 1. Required employee contribution levels must be identical for each benefit level. 2. The maximum benefit level cannot vary based on age, years of service, or compensation. 3. The same benefits that are available to HCIs must be available to non-HCIs. 4. Waiting periods to be eligible to participate must be uniform for all employees. 5. Amending a plan in a way that favors HCIs is prohibited. 6. For self-insured plans, benefits reimbursed for HCIs must also be reimbursed for non-HCIs. 	<p>Basic Plan Design Considerations:</p> <ol style="list-style-type: none"> 1. Only employees of the sponsoring employer may participate. 2. NOT eligible to participate: self-employed individuals, partners in a partnership, more than 2% shareholders in an S-Corp, members of an LLC, outside directors, spouses/dependents of any of these. 3. Benefits that can be offered on a pre-tax basis: coverage under accident/health plan, health FSA, dependent care account, group term life insurance up to \$50,000, paid time off, 401(k), adoption assistance, HSA plans 4. Plan document must be in writing and formally adopted before the beginning of the plan year. 5. Waiting periods to be eligible must be uniform for all employees. 6. Employees who otherwise meet all eligibility requirements must be allowed to enter the plan no later than the 1st day of the 1st plan year beginning after the date eligibility requirements are met. 7. The same benefits must be available for all similarly situated (for example, geographic location, level of coverage selected) participants at the same price. 8. Available employer contributions for similarly situated participants must be the same, and all participants must have the same option to use them.



Must benefit (meaning that the employee actually elects coverage):

1. 70% or more of all employees;
2. 80% or more of all employees who are eligible to participate if 70% or more of all employees are eligible to participate; or
3. A nondiscriminatory classification of employees based on objective business criteria (such as specific job categories, salaried vs. hourly, geographic location). The classification must not result in HCIs receiving a greater benefit than non-HCIs.

Must benefit (meaning that the employee actually elects coverage):

1. 70% or more of all employees;
2. 80% or more of all eligible employees if 70% or more of all employees are eligible to participate; or
3. A nondiscriminatory class of employees based on objective business criteria (such as job categories, geographic location); the class must not result in HCIs receiving a greater benefit than non-HCIs.

Utilization: Percent of HCIs that actually elect coverage cannot exceed percent of non-HCIs that elect coverage.

Key Employee Concentration: Benefits for key employees (officers with annual compensation greater than \$160,000 in 2010, more than 5% owners, & more than 1% owners with compensation greater than \$150,000) cannot exceed 25% of benefits provided for all employees under the plan.

Penalties for Noncompliance:

Self-Insured Plans

Amounts considered to be “excess reimbursements” to HCIs will be taxable.

Fully Insured Plans

- Penalties for failing to comply with the Public Health Services Act (PHSA), as amended by the Patient Protection and Affordable Care Act (PPACA) apply, including excise taxes of \$100 per day for each individual affected by the failure (imposed on the plan sponsor). The excise tax is generally a minimum of \$2,500 or \$15,000 for violations that are more than de minimis. The excise tax must be self-reported and paid using IRS Form 8928.
 - The excise tax may not need to be paid if plan sponsor can demonstrate that they did not know of the failure and would not have known even in exercising due diligence. The tax may also be avoided if the plan sponsor can demonstrate that the failure was due to reasonable cause rather than willful neglect and corrected within 30 days of first being discovered. Additional guidance needed.
- Health and Human Services (HHS) penalties of \$100 per day per failure may be assessed against the sponsoring employer of a nonfederal government plan.
- Civil Remedies: Private-sector employers may face enforcement action by the Department of Labor and participant lawsuits.
- It does not appear that failure will result in adverse tax consequences to HCIs (further guidance needed).

Penalties for Noncompliance:

- HCIs and Key Employees, as applicable, will lose the favorable tax treatment of the plan. Amounts contributed to the cafeteria plan will be included in gross income for the taxable year.
- Cafeteria plan nondiscrimination tests cannot be satisfied through corrections made after the plan year.
- Non-HCI and non-Key Employees are not affected by the failure to pass the nondiscrimination tests. The plan will continue to be a valid plan.

Safe Harbor for Simple Cafeteria Plans:

Reform allows eligible small employers to establish a simple cafeteria plan for plan years beginning on or after 12/31/10. Simple cafeteria plans will be treated as meeting nondiscrimination rules as long the following requirements are met:

1. **Employer size.** Employer (including affiliated employers) must have an average of 100 or fewer employees in either of the two preceding years. Includes full-time, part-time, temporary, or seasonal employees.
2. **Eligibility.** Generally all employees with at least 1,000 hours of service during the preceding plan year (other than excludable employees) must be eligible to participate. Each eligible employee must be able to elect any benefit available under the plan.
3. **Required employer contributions.** Each employee who is not a key/HCI must receive a “true” employer contribution of at least 2% of employee’s compensation for the year, or the lesser of 6% of employee’s compensation for the plan year or twice the employee’s salary reduction.

