
Employee Benefits Nondiscrimination Rules



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Agenda

- ▶ **Traditional Employment Discrimination Considerations (Title VII, etc.)**
- ▶ **HIPAA Nondiscrimination**
- ▶ **105(h) Nondiscrimination for Self-Funded Plans**
- ▶ **125 (Cafeteria Plan) Nondiscrimination**
- ▶ **Nondiscrimination of Underlying Benefits (FSA, DCAP, HSA, Life Insurance)**
- ▶ **Retirement Plan Nondiscrimination**

Employment Discrimination

- ▶ **Title VII (as amended by Pregnancy Discrimination Act of 1978)**
 - Prohibits employment discrimination based on race, color, religion, sex (including pregnancy), or national origin
 - PDA – Generally must cover pregnancy, childbirth, and related conditions on same basis as coverage for non-pregnancy-related conditions
 - Applies to employers with 15 or more employees for each working day in each of 20 or more calendar weeks in the current or preceding calendar year

Employment Discrimination

- ▶ **Title VII** – Application to group health plans:
 - Title VII regulates “health insurance benefits” that are provided under a “fringe benefit” program – includes health and many other types of benefits
 - Contraceptives – EEOC’s position is that coverage is required; courts’ positions have been mixed
 - Coverage of same-sex spouses generally required
- ▶ **Interaction with ACA Section 1557** – Coverage of gender affirming care:
 - 2020 Regulations – Remain in effect but are subject to ongoing litigation; among other things, narrowed 1557 applicability so that entities not principally engaged in providing health care (e.g., most insurers) are regulated only to the extent their health care activities are funded by HHS (rather than their entire operations, as under the prior regulations)

Employment Discrimination

▶ GINA:

- Prohibits discrimination based on genetic information
- Places limitations on requests for such information

▶ ADA:

- Prohibits discrimination based on a disability
- Reasonable accommodation required for wellness programs

▶ ADEA:

- Prohibits discrimination based on age
- Standard is whether the allegedly discriminatory act would not have occurred “but for” employee’s age

HIPAA Nondiscrimination

- ▶ **May not discriminate based on “health factors” with regard to eligibility, benefits, or premiums/contributions**
- ▶ **Health factors:**
 - **Health status, medical condition (including both physical and mental illnesses), claims experience, receipt of health care, medical history, genetic information, evidence of insurability*, or disability**
- ▶ ***Evidence of insurability includes—**
 - **Conditions arising out of acts of domestic violence; and**
 - **Participation in activities such as motorcycling, snowmobiling, all-terrain vehicle riding, horseback riding, skiing, and other similar activities**

HIPAA Nondiscrimination

Eligibility

- Requires same eligibility conditions for *similarly situated individuals*

Benefits

- Benefits provided under a plan must be uniformly available to all *similarly situated individuals*

Premiums

- May not require an individual to pay a premium or contribution that is greater than the premium or contribution for a *similarly situated individual* enrolled in the plan based on any health factor that relates to the individual or a dependent of the individual

“Similarly Situated Individuals”

- ▶ Distinction between groups must be based on a bona fide employment-based classification consistent w/ employer’s usual business practices
- ▶ Based on all the relevant facts and circumstances
 - Relevant facts and circumstances include whether employer uses the classification for purposes other than qualification for health coverage (e.g., determining terms of employment or eligibility for other benefits)
 - Examples of bona fide employment-based classifications: full-time vs. part-time, geographic location, membership in a collective bargaining unit, date of hire, length of service, current vs. former employee status, and different occupations
 - A classification based on any health factor is not a bona fide employment-based classification
- ▶ Wellness Program – Exception to HIPAA nondiscrimination rules

Treatment of Two or More Companies as One “Employer” – Controlled and Affiliated Service Groups

Parent-Subsidiary Controlled Groups	A parent-subsidiary controlled group consists of a parent corporation and its at least 80% owned direct and indirect subsidiaries
Brother-Sister Controlled Groups	A brother-sister controlled group exists when the same five or fewer individuals (incl. estates or trusts) own an at least 80% “controlling interest” in two or more entities and the same five or fewer individuals “effectively control” more than 50% of each entity
Combined Parent-Subsidiary and Brother-Sister Groups	A combined group exists when three or more organizations are each a member of either a parent-subsidiary or a brother-sister group and where one entity is the common parent of a parent-subsidiary group and is also a member of a brother-sister group
Affiliated Service Groups	In addition to common ownership, look for situations where services are performed for one another on a regular basis, or where one company provides management services to the other on a regular basis

Treatment of Two or More Companies as One “Employer” – Why It Matters

- ▶ **Separate companies that are in the same controlled group or affiliated service group are treated as one employer for various benefits and tax purposes**
- ▶ **Family and Organizational Ownership Attribution Rules**
- ▶ **Implications include:**
 - **Qualified Retirement Plan Compliance**
 - **Health and Welfare Benefits Compliance (e.g., MEWA status)**
 - **ACA Employer Mandate and ACA Reporting**
 - **Nondiscrimination Rules**

Section 105(h) Nondiscrimination Rules

- ▶ Nondiscrimination requirements for self-funded (*aka*, self-insured) group health plans
- ▶ Self-funded plans may not discriminate in favor of Highly Compensated Individuals (“HCIs”)
- ▶ Applies with respect to Eligibility and Benefits
- ▶ Consequence of failure = HCIs are taxed on the value of otherwise tax-exempt benefits received

Section 105(h) Nondiscrimination Rules

Two 105(h) Tests

Eligibility Test

Benefits Test

105(h) Highly Compensated Individuals include—

5 highest paid Officers

**More than 10%
shareholders**

**Highest paid 25% of all
employees**

Section 105(h) Nondiscrimination Rules

► Eligibility Test

- 1. The plan benefits 70% or more of all nonexcludable employees**
- 2. The plan benefits 80% or more of all nonexcludable employees who are eligible to benefit — IF 70% or more of all nonexcludable employees are eligible to participate under the plan**
- 3. The plan benefits a nondiscriminatory classification of employees. This requires (1) a bona fide business classification for any exclusion; and (2) a sufficient ratio of benefiting non-HCIs to benefiting HCIs.**

Section 105(h) Nondiscrimination Rules

▶ Benefits Test

- Plan benefits will not satisfy the nondiscriminatory benefits requirements unless all the benefits provided for participants who are HCIs are provided for all other participants
 - Two components of the Benefits Test —
(1) nondiscrimination on the face of the plan, and
(2) nondiscrimination in operation
- ▶ **Common Issue – Varying Premium Levels**
- ▶ **Satisfying the Benefits Test through disaggregation**

Section 125 (Cafeteria Plan) Nondiscrimination

- ▶ Cafeteria Plans may not discriminate in favor of Highly Compensated Individuals (“HCIs”) or Key Employees as to eligibility, contributions, or benefits.
- ▶ Consequence of Failure:
 - In general, HCIs/Keys who made pre-tax salary reductions will be taxed on the amount of those salary reductions.
- ▶ Testing generally must be run on the last day of the plan year
 - Of course, employers should monitor compliance with testing criteria during the plan year
 - Employers cannot fix nondiscrimination problems after year-end
- ▶ *Concept: Cafeteria Plan “party”...*

Section 125 Nondiscrimination

Three Cafeteria Plan Tests

Eligibility Test

Contributions and Benefits Test

Key Employee Concentration Test

“Highly Compensated Individuals” include—

Officers

More than 5% shareholders

Highly compensated under Code § 414(q) (\$135,000 in 2022; \$150,000 in 2023)

Spouses or dependents of the above

125 Nondiscrimination – Eligibility Test

(1) Employment Requirement

- No employee may be required to complete 3+ years of employment, and the same employment requirement applies to all employees (but the employer could have separate cafeteria plans...)

(2) Entry Date Requirement

- Participation must commence no later than the first day of the first plan year beginning after the date the employment requirement was satisfied

(3) Two-part Nondiscriminatory Classification Test

- Bona fide business classification for those included or excluded from the plan; and
- Sufficient ratio of eligible non-HCIs to eligible HCIs (a numeric test)

125 Nondiscrimination – Eligibility Test

- ▶ ***Eligibility Test: “Have enough non-HCIs been invited to the party?”***
- ▶ **Two-Part Nondiscriminatory Classification Test:**
 1. **Cafeteria plan does not discriminate in favor of HCIs if it benefits a group of employees who qualify under a “reasonable classification”**
 - **Examples – Specified job categories, salaried vs. hourly, geographic location, and similar bona fide business criteria**
 2. **Group of employees included in the classification must satisfy either the “safe harbor” or “unsafe harbor” percentage test**
 - **Premium Only Plan (“POP”) Safe Harbor**
 - **Issues for which current IRS guidance provides no clear answer:**
 - **Which employees can be excluded for testing purposes?**
 - **What does it mean to “benefit” under a cafeteria plan?**

125 Nondiscrimination – Contributions and Benefits Test

- ▶ **Contributions and Benefits Test – Two Parts:**
 1. **Availability Test**
 - *“What drink options are available to each person and at what cost?”*
 2. **Utilization Test**
 - *“How much is each group drinking?”*
- ▶ **Nondiscrimination in Operation – Cafeteria plan also must not discriminate in favor of HCLs in actual operation**
- ▶ **Contributions and Benefits Test Safe Harbor**

125 Nondiscrimination – Contributions and Benefits Test

- ▶ **Either qualified benefits and total benefits, or employer contributions allocable to qualified benefits and total benefits, must not discriminate in favor of HCPs.**
- ▶ **Tests are run based on “similarly situated” participants:**
 - **When determining whether participants are “similarly situated,” reasonable differences in plan benefits may be taken into account, such as variations based on geographical location or to employees with family coverage versus employee-only coverage.**
- ▶ **Are benefits or contributions available to similarly situated participants on a nondiscriminatory basis?**
- ▶ **Actual utilization (election) of benefits or contributions must not be disproportionate by HCPs vs. non-HCPs.**

125 Nondiscrimination – Key Employee Concentration Test

- ▶ **Key Employee Concentration Test**: If the qualified benefits provided to Key Employees exceeds 25% of the total qualified benefits provided for all employees under the plan, the plan will fail the Key Employee Concentration Test
- ▶ “Key Employees” include—
 - Officers with annual compensation in excess of the dollar limit for that year (\$215,000 for 2023)
 - More-than-5% shareholders
 - More-than-1% shareholders with annual compensation greater than \$150,000 (not indexed)

Nondiscrimination of Underlying Benefits

▶ Health FSAs (105(h) Tests):

- Eligibility Test
- Benefits Test

▶ DCAPs (aka Dependent Care FSAs):

- Eligibility Test
- Contributions and Benefits Test
- More-Than-5% Owners Concentration Test
- 55% Average Benefits Test

▶ Health Savings Accounts (HSAs):

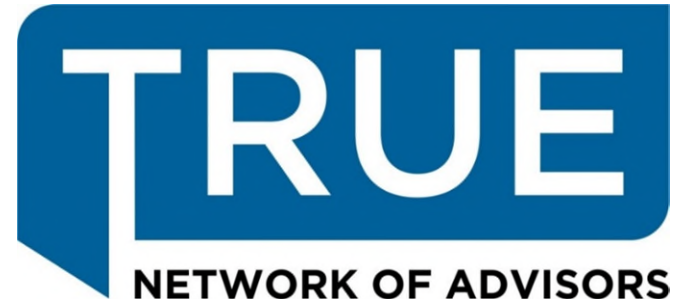
- Comparability Rules

▶ Group Term Life Insurance:

- Eligibility Test
- Benefits Test

Retirement Plan Nondiscrimination

- ▶ **Minimum Coverage Requirements under Code § 410(b)**
- ▶ **General nondiscrimination principles under Code § 401(a)(4) and top-heavy rules under Code § 416**
- ▶ **Actual Deferral Percentage (ADP) and Actual Contribution Percentage (ACP) Testing**
- ▶ **Safe Harbor Plan Designs – ADP and ACP Safe Harbors**
- ▶ **Correcting Retirement Plan Nondiscrimination Mistakes:**
 - **IRS’s Employee Plans Compliance Resolution System (EPCRS) – SCP, VCP, or Audit CAP**
 - **DOL’s Voluntary Fiduciary Correction Program (VFCP)**



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