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Final Rule on STLDI + Indemnity Plans



Introduction

The Department of Labor (DOL), Department of Health and Human Services (HHS), and the Internal Revenue Service (IRS), [collectively, “the Departments”] have released final rules regarding short-term medical plans and issued new notice requirements for fixed indemnity plans. The rules finalize some, but not all, of the issues included in proposed regulations issued in July 2023. The final rules, including model notices, can be found [here](#).

Short-Term Limited Duration Insurance (STLDI)

Background

Individual STLDI plans are not subject to the same requirements as comprehensive individual health insurance plans, and notably, are allowed to exclude coverage for pre-existing conditions. For many years, STLDI plans were limited to a 3-month maximum duration of coverage. In 2018, the Trump Administration issued new rules expanding STLDI plans to allow for coverage for up to 12 months with two renewals allowed, effectively allowing for a maximum coverage period of up to 36 months. However, many states impose more stringent limits on, or even prohibit, STLDI plans.

Length of Coverage Limits in Final Rules

The final rules limit STLDI plans to a maximum of 3 months of coverage with a 1-month extension allowed in some cases. The rules also limit a vendor’s ability to “stack” STLDI policies to circumvent the 3-month rule. A new expanded notice to individuals who purchase STLDI plan will also be required. The new STLDI rules are effective as of September 1, 2024.

Hospital & Fixed Indemnity Plans

Background

Hospital indemnity and fixed indemnity insurance plans pay a fixed amount for an occurrence for a specific condition and do not coordinate benefits with other insurance plans. Under current rules, these plans are treated as an “excepted benefit” and are not subject to many of the rules and regulations that apply to comprehensive group or individual health insurance plans. Regulators are concerned that some fixed indemnity type plans are being designed and sold to appear to consumers as if they are providing comprehensive coverage.

Proposed Rules

The proposed rules released in July 2023 would have made changes to indemnity plans in several ways:

- ◆ Indemnity plans sold in the individual market would be required to pay benefits on a per period basis (such as per day), not on a per service basis. This rule already applies to plans sold in the group market.
- ◆ Fixed indemnity plans would not be allowed to be integrated with a medical plan and retain excepted benefit status. This change targeted the proliferation of “preventive only MEC + indemnity coverage” plans that are being marketed as an alternative to comprehensive group health coverage.
- ◆ The proposed rules also included new notice requirements.

New Notice Requirements in Final Rules

The final rules implement a new notice requirement in both the individual and group markets, but the Departments delayed finalizing other provisions of the proposed rules, stating that they plan to release additional guidance in the future to address other concerns. The new notices are designed to make it clear to participants that indemnity policies that hospital and fixed indemnity plans are not health insurance. The Departments released model notices for both individual and group market policies. The new notice requirements go into effect for plan years beginning on or after January 1, 2025.

Tax Treatment of Hospital Indemnity and Fixed Indemnity Plans

The IRS proposed to amend existing regulations to clarify the tax treatment of indemnity plans. Under the proposed rules, benefits paid by the indemnity plan must be treated as taxable income if either of the following is true:

- ◆ Employees pay for indemnity plan coverage with pre-tax contributions made through the employer’s §125 cafeteria plan; or
- ◆ The benefits are paid by the plan without regard to the actual amount charged for medical care.

The IRS did not finalize the tax changes as described in the proposed rules and stated that they expect to release additional guidance. However, the IRS also expressed concern that some current industry practices violate existing tax rules. Specifically, the IRS has released multiple memoranda and other informal guidance clarifying that vendors offering plans claiming to save taxes by having employees pay for some undefined “wellness” or other unsubstantiated expense on a pre-tax basis would actually result in the benefits provided by those arrangements being treated as taxable income to the employee.

Summary

While many of the proposed rules were not finalized, the preamble to the final rules made it clear that additional guidance is forthcoming and that the Departments’ failure to issue final rules at this time did not indicate a change in their opinion of issues addressed in the proposed rules. Concerning tax rules in particular, employers should also consider prior IRS guidance related to the taxation of indemnity plans.