**Employee Benefits**

ALERT

# HIPAA Administrative Simplification Rules Apply to Health Care Flexible Spending Accounts

## HHS Decides HIPAA's Administrative Simplification Provisions Apply To Health FSAs

The United States Department of Health & Human Services ("HHS") has determined that health care flexible spending arrangements and cafeteria plans paying for medical care ("health FSAs") are generally covered by the privacy rule and the other administrative simplification provisions of the Health Insurance Portability and Accountability Act of 1996 ("HIPAA") as "group health plans." See "Questions and Answers" posted on April 24, 2003 by HHS on its website, www.hhs.gov.

The deadline for compliance with HIPAA's privacy rule was April 14, 2003 for large plans..."small health plans" have until April 14, 2004.

### What Does This Mean?

HIPAA's administrative simplification provisions – its privacy, security and "electronic data interchange" or "EDI" rules – apply only to "covered entities," which include "group health plans." A group health plan is an employee welfare plan that provides medical care (on an insured or uninsured basis) to employees or their dependents and that *either* has 50 or more participants *or* is administered by an entity other than the sponsoring employer. According to the HHS, health FSAs will qualify as group health plans (unless they are self-administered by the employer *and* have fewer than 50 participants), and are thus covered by HIPAA's privacy, security and EDI rules.

*Self-insured* group health plans are generally subject to substantive regulation under HIPAA's privacy rule. However, *fully insured* group health plans administered by insurance carriers or other third party administrators are generally exempt from most privacy rule requirements. Because health FSAs are by their nature almost always self-insured, they are potentially subject to the full range of HIPAA's privacy rule. This may be burdensome to employers, particularly small or mid-sized employers, whose health plans are otherwise fully insured and thus escape much of the impact of the privacy rule.

### Compliance Deadlines

The deadline for compliance with HIPAA's privacy rule was April 14, 2003 for large plans (plans with more than $5 million in annual receipts). "Small health plans" have until April 14, 2004 to comply with the privacy rule. The security rule does not take effect until April 21, 2005; again, small health plans have an extra year, to April 21, 2006, to comply. The deadline for the EDI rule was October 16, 2002 -- October 16, 2003 for small health plans and large plans that requested an extension.

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If a health FSA is a "group health plan," full compliance with HIPAA's privacy rule, security rule and, under certain conditions, EDI rule is required.

### Exceptions and Other Relief

In order to evaluate HIPAA administrative simplification compliance obligations, employers who sponsor health FSAs must first determine if their plans are group health plans and, if they are, decide if they are eligible for the delayed effective dates for small health plans.

Only those health FSAs that pay for medical care are covered as group health plans. Plans such as dependent care assistance programs or health insurance premium pre-tax payroll deduction arrangements are not covered. In addition, health FSAs that are self-administered by the employer *and* have fewer than 50 participants are not covered group health plans.

As noted above, certain delayed effective dates apply to "small health plans." A small health plan is defined as a health plan with annual receipts of $5 million or less. "Annual receipts" are total annual premiums (for insured plans) and total claims (for self-insured plans). The question of whether a health FSA is considered a single plan or whether it must be aggregated with other group health plans of the employer for purposes of determining if it qualifies as a small health plan is one that should be discussed with legal counsel. One significant factor is whether the employer treats the health FSA as a stand-alone plan for annual reporting under ERISA (Form 5500) or whether it includes the plan in a Form 5500 filing with other group health plan(s).

### What Does Full Compliance Mean?

If a health FSA is a "group health plan," full compliance with HIPAA's privacy rule, security rule and, under certain conditions, EDI rule is required.

- *Privacy Rule*

  Very briefly, the privacy rule, provides that covered entities, including group health plans, may not use or disclose an individual's "protected health information" without the affected individual's authorization, unless such use is required or permitted by the privacy rule itself. The rule requires or permits use or disclosure of protected health information only for purposes of payment, treatment or health care operations or for certain specified public health and public policy reasons. Even where a covered entity may use or disclose protected health information it must take reasonable steps to limit the use or disclosure to the minimum amount necessary to accomplish the intended purpose of the use or disclosure. For a more complete discussion of HIPAA's privacy rule, please refer to this Employee Benefits Alert available on our site,
  http://www.bingham.com/Bingham/updates.asp –Employee Benefits
  (March 7, 2003).

- *Security Rule*

  Covered entities, including group health plans, must comply with HIPAA's security

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rule by April 21, 2005, except for small health plans, which have until April 21, 2006. The security rule establishes a standard for the security of all protected health information that is maintained or transmitted electronically. It requires all covered entities to ensure the confidentiality, integrity and availability of electronic protected health information that they create or maintain and to protect it from reasonably anticipated improper uses or disclosures. The security rule includes a proposed rule for electronic signatures which describes standards for the authentication and permanence of electronic signatures.

- *Electronic Data Interchancge ("EDI") Rule*

  HIPAA's EDI rule requires covered entities, including group health plans, to process certain specified health care transactions (such as transmittal of health claims, coordination of benefits and enrollment and disenrollment information) in an electronic format in accordance with specified standards. For a more complete discussion of the EDI rules, please refer to this Employee Benefits Alert available on our site, http://www.bingham.com/Bingham/updates.asp –Employee Benefits. (September 26, 2002). However, the EDI rules only apply to transactions between plans and health care providers or between plans, not transactions between plans and participants or between plans and employers. Most health FSAs are administered by third party administrators without the employer's involvement; the administrator will directly receive claims from participants and directly reimburse participants for covered expenses, transactions for which EDI format is not required. However, some third party administrators may require employers by contract to forward plan information (for example, enrollment and disenrollment information) to them using EDI format.

For assistance, please contact the following attorneys:

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