

LAW & POLICY GROUP

GRIST**MORE STATES APPROVE PATHWAY 2
ASSOCIATION HEALTH PLANS**

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Oct. 21, 2019*

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New state laws allow small employers to form “Pathway 2” association health plans (AHPs) in Arizona ([2019 Ch. 194](#)), Florida ([2019 Ch. 129](#)) and North Carolina ([2019 Ch. 202](#)). However, all three measures rely on a 2018 AHP rule ([29 CFR § 2510.3-5](#)), which a federal court ruling struck down earlier this year (*New York v. US Dep't of Labor*, No. 18-1747 (D.D.C. March 28, 2019)). Other states are considering whether to enact the similar legislation, although some — like Virginia — may reject efforts to allow Pathway 2 AHPs.

EFFORTS TO EXPAND AHPS

Before the Trump administration issued a final rule last year, long-standing Department of Labor (DOL) guidance distinguished between “bona fide” and other AHPs. Bona fide AHPs, now commonly referred to as “Pathway 1 AHPs,” have a single plan at the association level. Under other AHPs, each participating employer in an association separately sponsors its own ERISA plan.

Pathway 1 AHPs. Bona fide AHPs have enjoyed certain advantages relative to other AHPs under the Affordable Care Act (ACA) and ERISA. For example, bona fide associations are treated as a single employer under ERISA and may avoid certain plan restrictions that apply to small employer groups. But the guidance sets a high bar for bona fide AHP status: Members must not only control the plan but also have a common interest (e.g., same industry) and a shared economic or representation purpose — unrelated to benefits — for forming the association.

Pathway 2 AHPs. The 2018 final AHP [rule](#) offers small businesses and “working owners” a new way — Pathway 2 — to form employer groups or associations offering large group health plans. Under Pathway 2 AHPs, small groups must have a “commonality of interest,” such as a shared location — a principal place of business in the same region within a single state or a metropolitan area (even if the metropolitan area spans multiple states). Unlike earlier “bona fide associations,” Pathway 2 allows groups to form for the

express purpose of purchasing health insurance. In addition, working owners with no common-law employees may participate in AHPs under some circumstances.

LAWSUIT HALTS 2018 FEDERAL RULE

In March, a federal district court struck down several aspects of the 2018 rule, finding they unreasonably expanded ERISA’s definition of “employer” (*New York v. US Dep’t of Labor*, No. 18-1747 (D.D.C. March 28, 2019)). The decision sets aside the revised rule — including the commonality of interest based on location and working owners’ participation — pending appeal. The US Court of Appeals for the District of Columbia will hear arguments in the case next month.

While the future of Pathway 2 AHPs under federal law is uncertain, Pathway 1 AHPs developed under prior guidance — primarily DOL advisory opinions and earlier court rulings — aren’t affected by the decision. This brief table outlines what types of AHPs are allowed or prohibited in the wake of the court’s ruling:

PROHIBITED AHPs	ALLOWED AHPs
AHPs whose member employers share only the same geographic location (such as a state or metropolitan area)	Bona fide AHPs whose member employers have a common interest and genuine organizational purpose unrelated to providing benefits <ul style="list-style-type: none"> Facts and circumstances determine commonality, which can’t rely solely on geography.
AHPs with working owners (members with no employees)	AHPs that don’t allow working owners (all members have employees)
AHPs sponsored by associations that have the primary purpose of purchasing health coverage, but also have a substantial business purpose	AHPs sponsored by associations that have a genuine business/organizational purpose and function unrelated to providing benefits

STATE AHP ACTIVITY

Three states — Arizona, Florida and North Carolina — have recently enacted legislation authorizing Pathway 2 AHPs. These states join others with laws that purport to permit Pathway 2 AHPs: Arkansas ([2019 Act 919](#)), Hawaii ([2018 Sess. Law 199](#)), Iowa ([2018 Act 1063](#)), Kansas ([2019 Sess. Law 54](#)), Kentucky ([2019 Act 165](#)), Oklahoma ([2019 Sess. Law 265](#)) and South Dakota ([2019 Sess. Law 212](#)). However, Virginia’s governor rejected legislation that would have allowed Pathway 2 AHPs.

Arizona

Effective Aug. 27, Arizona’s new [law](#) recognizes Pathway 2 AHPs whose members mainly have geography in common, as permitted under the 2018 federal regulations. If the federal court’s ruling rejecting those regulations is upheld, the state law will no longer have any federal authority to follow, raising issues about ERISA compliance for a Pathway 2 AHP in Arizona. The Arizona law also eliminates a five-year “seasoning requirement” that had required associations to exist for five years before sponsoring an AHP.

Florida

Effective June 25, Florida amended its [law](#) on multiple-employer welfare arrangements (MEWAs) to allow AHPs based on geography and including working owners. Like the Arizona law, the Florida measure cites the now-invalid federal regulations, raising compliance questions unless the lower court's ruling is overturned. The Florida law also eliminates a one-year seasoning requirement for associations to sponsor an AHP.

North Carolina

Effective Oct. 1, a state [law](#) allows small employers to offer a self-funded or fully insured AHP by forming a "Pathway 2" association, based on the 2018 federal rule. This would permit AHPs that share a common geography (or the same trade/industry) and include working owners.

Unlike Arizona or Florida, North Carolina has enacted a fallback provision if the court's ruling invalidating the 2018 federal regulations is upheld. The state's Department of Insurance would conduct a study to explore obtaining a [Section 1332 state innovation waiver](#) from the US Department of Health and Human Services (HHS) to allow Pathway 2 AHPs. The Insurance Department would report the study's findings and recommend any necessary legislation to state lawmakers.

Virginia

Earlier this year, Virginia's governor [vetoed](#) a bill that would have permitted Pathway 2 AHPs. In his veto message, the governor expressed concerns that AHPs do not have to cover essential health benefits (EHBs) like maternity care and prescription coverage; can set different premium rates based on characteristics like age, gender, job and preexisting conditions; and would undermine efforts to stabilize Virginia's health insurance marketplace.

DOL NONENFORCEMENT POLICY

In the wake of the court ruling striking down the 2018 AHP rule, the DOL has issued a nonenforcement policy for Pathway 2 AHPs. Under that [guidance](#), the DOL and HHS won't pursue enforcement action against Pathway 2 AHPs formed between publication of the final rule and the court's decision, as long as the AHPs relied in good faith on the final rule and continue to pay health benefit claims as promised.

Employers participating in insured AHPs generally should maintain that coverage through the end of the plan year or, if later, the contract term. For the next plan year or contract term, issuers may renew Pathway 2 AHPs only if the coverage complies with the relevant ACA market requirements for that employer's size (e.g., the EHB and premium-rating rules for small employers). Unless an appeals court reinstates the 2018 rule, however, groups cannot establish new Pathway 2 AHPs going forward.

NEXT STEPS FOR AHPs

Although a few states have adopted legislation that would allow Pathway 2 AHPs, these laws raise issues about ERISA compliance as long as the 2018 rule remains invalidated. AHP members should continue to monitor federal litigation over the 2018 AHP rule. If the lower court's decision is upheld, states might file for state innovation waivers to allow Pathway 2 AHPs, although HHS might decline to issue such waivers. Pathway 1 AHPs, on the other hand, are allowed.

RELATED RESOURCES

Non-Mercer Resources

- [2019 Ch. 202](#) (North Carolina General Assembly, Aug. 26, 2019)
- [2019 Ch. 129](#) (Florida State Library and Archives, June 25, 2019)
- [Association Health Plans Q&As — Part Two](#) (DOL, May 13, 2019)
- [2019 Sess. Law 54](#) (Kansas Legislature, May 9, 2019)
- [2019 Ch. 194](#) (Arizona Legislature, May 8, 2019)
- [Governor's Veto Statement](#) (Virginia Legislative Information System, May 2, 2019)
- [2019 Sess. Law 265](#) (Oklahoma Secretary of State, April 19, 2019)
- [2019 Act 919](#) (Arkansas Legislature, April 11, 2019)
- [2019 Act 165](#) (Kentucky Legislature, March 26, 2019)
- [2019 Sess. Law 212](#) (South Dakota, Feb. 14, 2019)
- [2018 Sess. Law 199](#) (Hawaii Legislature, July 10, 2018)
- [2018 Act 1063](#) (Iowa Legislature, April 2, 2018)
- [New York v. US Dep't of Labor](#), No. 18-1747 (D.D.C. March 28, 2019)
- [Final Rule: Definition of 'Employer' Under Section 3\(5\) of ERISA-Association Health Plans](#) (Federal Register, June 21, 2018)
- [29 CFR § 2510.3-5](#) (US Government Publishing Office)
- [Section 1332 State Innovation Waiver Request](#) (Centers for Medicare & Medicaid Services)

Mercer Law & Policy Resources

- [New Push for ACA Innovation Waivers Aims To Rekindle States' Interest](#) (May 21, 2019)
- [Litigation, Legislation Leave AHP Guidance in Flux](#) (May 2, 2019)
- [Final Association Health Plan Rule Offers New Options for Employers](#) (Nov. 8, 2018)

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