



Rising ERISA Class-Action Lawsuits Over Tobacco Surcharges in Health Plans

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A wave of ERISA class-action lawsuits is challenging tobacco surcharge programs in employer-sponsored health plans across the U.S. These cases center on potential fiduciary breaches, with plaintiffs arguing that surcharges added to tobacco users' premiums are not compliant with federal laws such as the Employee Retirement Income Security Act (ERISA), the Affordable Care Act (ACA), and the Health Insurance Portability and Accountability Act (HIPAA). Designed to encourage wellness, tobacco surcharges are increasingly viewed as potentially punitive rather than supportive, prompting employers to reevaluate these programs' structures.

Understanding Tobacco Surcharges and Wellness Program Requirements

A tobacco surcharge, permitted under the ACA, is a premium differential for tobacco users. However, the ACA and HIPAA require that such surcharges be part of a compliant wellness program, providing tobacco users with a clear path to reduced premiums by meeting a reasonable alternative standard (RAS), such as enrolling in a cessation program.

To impose a tobacco surcharge that complies with federal law, employers must meet five requirements:

- 1. Annual Opportunity:** Offer employees at least one opportunity per year to qualify for the incentive. Regular access ensures tobacco users can benefit from premium reductions by quitting or participating in cessation support programs.
- 2. Incentive Limits:** Tobacco surcharges cannot exceed 50% of the total coverage cost, with a 30% cap for other health-contingent incentives, ensuring financial fairness and alignment with ACA limits. For this purpose, the total coverage cost includes both employee and employer contributions.
- 3. Health-Focused Program Design:** Wellness programs must aim to promote and improve health or prevent disease, not to penalize the participant. This requires designing incentives that support achievable health goals without excessive burdens.

4. **Reasonable Alternative Standard (RAS):** An RAS, such as a cessation program, must be available for employees unable to meet the primary health standard. This standard ensures inclusivity and prevents penalties against those unable to quit immediately. For example, if the primary health standard is to be a non-smoker, then an RAS must be available for smokers (e.g., completion of a smoking cessation program).

5. **Clear Communication of Alternatives:** All wellness program materials must disclose the RAS and provide contact information. This transparency ensures employees understand their options to avoid surcharges.

Failing to meet these requirements can lead to HIPAA compliance issues and increase the likelihood of ERISA-based legal challenges. Additionally, employers should verify whether state-specific laws impose additional restrictions on implementing tobacco surcharges.

Regulatory Framework for Tobacco Surcharges

The ACA and HIPAA jointly govern tobacco surcharges, requiring compliance with wellness program standards, and ACA provisions allow group health plans to apply tobacco surcharges up to 50% more than non-tobacco users' premiums. In addition, ERISA requires plans to operate for the exclusive benefit of participants, enforcing fiduciary standards that include transparent and fair program administration.

HIPAA and the Americans with Disabilities Act (ADA), meanwhile, impose additional protections to prevent discrimination and maintain voluntary participation in wellness programs. If a wellness program requires medical screening or information collection, ADA standards mandate that participation remains voluntary with no penalty for non-participation, ensuring excessive surcharges do not coerce employees.

Rising Lawsuits and Employer Liability

Recent lawsuits allege that some employers' wellness programs fail to provide adequate alternatives or sufficient communication around tobacco surcharges, resulting in potential ERISA fiduciary breaches.

Some large employers, including prominent retail companies, are now facing litigation for wellness programs that allegedly do not meet federal compliance standards under ERISA, the ACA, and HIPAA. For instance, the U.S. Department of Labor (DOL) filed a recent lawsuit against a large employer claiming that a tobacco surcharge should be waived if a smoking cessation program is completed – regardless of whether the participant actually quit smoking.

These cases argue that tobacco surcharges linked to group health plan premiums disproportionately impact tobacco users by increasing their costs without providing sufficient means to avoid the surcharges. As a result, these lawsuits allege that these employers potentially violate ERISA's fiduciary obligation to act solely in the participants' best interests.

Employers should be aware of the following litigation claims:

- **Lack of Reasonable Alternatives:** Surcharges are viewed as discriminatory and punitive when employers do not provide clear, accessible, reasonable alternative standards (RAS), such as participation in smoking cessation programs.

- **Insufficient Transparency and Disclosure:** Failure to adequately communicate the availability of alternatives and how to access them within wellness program materials can lead to non-compliance with ERISA’s fiduciary standards and HIPAA requirements.
- **Increased Costs for Participants:** Plaintiffs argue that wellness programs may breach ERISA fiduciary duties if surcharges are imposed without a clear health-promoting purpose, resulting in increased costs for participants that may not align with the program’s stated wellness goals.

In light of these lawsuits, employers should reassess their wellness program design, focusing on transparency, accessible alternatives, and compliance with fiduciary standards to mitigate legal risks under ERISA and other federal laws.

Proactive Steps for Plan Sponsors and Fiduciaries

Plan sponsors and fiduciaries should proactively ensure their wellness programs meet ERISA and other federal standards. Six key actions include:

1. **Regular Compliance Audits:** Conduct periodic reviews to ensure wellness programs align with ACA, ERISA, HIPAA, and ADA requirements. Given the rise in litigation, a proactive compliance review can mitigate potential legal challenges.
2. **Track Ongoing Litigation.** Many of the current lawsuits involve agency interpretation of regulations. Given the recent rejection of Chevron deference by the Supreme Court, decisions for current litigation could alter compliance requirements.
3. **Transparent Program Communication:** Ensure all wellness program materials detail the availability of reasonable alternatives and contact information, allowing employees to access resources and avoid surcharges.
4. **Health-Driven Program Design:** Maintain a genuine health improvement focus in the program’s structure. Avoid designs that could be viewed as punitive, making sure that surcharges are part of a broader health-focused initiative rather than a financial penalty.
5. **Offer Accessible Alternatives:** Providing reasonable alternatives, such as a smoking cessation program, makes the wellness program fairer and more inclusive while allowing employees to achieve premium reductions through realistic health goals.
6. **Ongoing Training for Fiduciaries:** Continuous education on regulatory requirements and compliance best practices can help plan sponsors make informed decisions that support employee wellness and align with legal standards.

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