A CHUBB SPECIAL REPORT:

Update on Tobacco Surcharge Litigation

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Since last year, the plaintiff's bar has filed a wave of class action lawsuits challenging the validity of employer-sponsored wellness programs in health plans that include a "tobacco surcharge." This surcharge typically requires health plan participants to pay an additional annual premium or contribution if they self-declare tobacco use.

As of June of 2025, over forty of these cases have been filed – two of which were brought by the Department of Labor ("DOL"). Over two-thirds of the cases have been filed since August 30, 2024, indicating that this new wave of litigation is likely to continue. Multiple plaintiff's firms have filed such cases, but three law firms have been the main drivers of the recent litigation: Siri & Glimstad LLP, Stueve Siegel Hanson, and the McClelland Law Firm.

Most employers appear to be challenging the allegations, with motions to dismiss. While many of these motions are still pending, the few that have been decided have been denied.

In terms of settlements, a handful of these cases have settled, with settlement values ranging from $135,000 to $4,950,000, exclusive of defense costs.

Considering the increasing number of tobacco surcharge lawsuits and the uncertain future they face, plan sponsors and fiduciaries may find it helpful to have some background on the lawsuits, the allegations and defenses asserted, and issues to watch going forward.

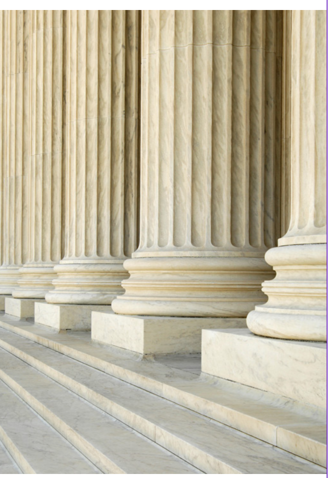
Claims Asserted in Recent Litigation

The recent lawsuits allege that these surcharges violate Section 702 of ERISA which prohibits discrimination by targeting employees based on their health status. Under Section 702, group health plans are generally prohibited from requiring participants to pay a premium or contribution that is greater than one charged to a similarly situated enrollees based on a health-status related factor. The DOL has taken the position that tobacco use is a health-status related factor because it may involve nicotine addiction.

But Section 702 provides an exception that allows employers to offer incentives, such as premium discounts or rebates, or disincentives, such as tobacco surcharges (i.e., increased health premiums), through wellness programs. Regarding tobacco surcharges, the DOL takes the position that to satisfy the exception, a wellness program must, among other things, offer a "reasonable alternative standard" to quitting smoking – such as completing a tobacco cessation program. Recent lawsuits allege that the programs in question do not meet these regulatory requirements.

Specifically, the lawsuits allege that plans with a tobacco surcharge violate ERISA in the following ways:

1. **The plans do not include a "reasonable alternative standard."** Some plans require employees to quit smoking (either immediately or upon completion of a cessation program) to receive the reward, i.e., the removal of the surcharge. Plaintiffs rely on the DOL's position that "requiring actual cessation" to receive the reward is not a "reasonable alternative standard" under the statute. Plaintiffs have also argued that wellness programs that lift the surcharge on a going-forward basis only (e.g., upon enrollment in or completion of a cessation program) and that do not provide a retroactive reimbursement for surcharge payments already made in that plan year, violate the DOL's regulations under Section 702.
2. **The plans do not sufficiently communicate the existence of a reasonable alternative.** The complaints allege that even if there was a reasonable alternative offered, that alternative was not sufficiently communicated to participants in "all plan materials."
3. **Breach of fiduciary duty.** Plaintiffs allege that by collecting a surcharge, employers have breached their fiduciary duties and enriched themselves by reducing the amount of their contributions towards the plan's administrative expenses.



Primary Defenses Asserted

Where Defendants have sought to dismiss these allegations, some of the main defenses include:

1. **Statutory/Regulatory Interpretation.** The Supreme Court's recent decision in *Loper Bright Enterprises v. Raimondo* eliminated the longstanding *Chevron* standard which required courts to give deference to agency interpretation of statutes. With that deference no longer available, some defendants have argued that the DOL's regulatory interpretation of Section 702 is not the "best reading" of the statute as required under *Loper Bright*.
2. **No entitlement to retroactive rewards.** Plaintiffs assert that no matter when a plan participant enrolls in a cessation program, they should be entitled to a retroactive refund of the surcharge for the entire year. In advocating for a retroactive rebate, Plaintiffs point to statutory language requiring a "full reward" for participation in a wellness program. Retroactive rebate appears nowhere in the statute, but the relevant statutory language does require "adherence" to a wellness program which must be designed to promote health and prevent disease. As such, defendants argue that before an employee enrolls in the cessation program, they are not "adhering" to a wellness program and are not entitled to the "reward" of lifting the surcharge on a retroactive basis.
3. **Policy rationale.** The goal of the wellness regulations is to promote health and save costs. The negative health effects of smoking are clear and well-documented. The DOL's interpretation, adopted by many Plaintiffs, runs afoul of both goals. Under their construction, a participant who smokes all year can engage in the cessation classes at the end of the year and recoup the entire year's surcharge. Their health is not improved in that scenario, and no costs are saved because they continue to be an increased economic burden on their health plan by smoking. In fact, under the DOL's and plaintiffs' statutory construction, the employer/plan sponsor is better off not offering the wellness program at all because the employer is not able to retain the surcharge, must still pay for the cessation program, and must pay the increased health care costs of a smoker.

Recommendations for Plan Sponsors and Fiduciaries

It appears likely that plaintiff's firms will continue to bring these claims, regardless of their merit. Thus, companies sponsoring self-funded group health plans that incorporate wellness programs may want to work with experienced ERISA counsel to review and assess their risk of being sued and take any appropriate steps to reduce this risk, including:

1. Plan Design Changes: Because the future of these cases is uncertain, plan design changes may be premature at this stage, given the ongoing challenges to the DOL's regulations and the potential rollback of regulations by the new administration. Nevertheless, employers may wish to review and evaluate their wellness programs to exam compliance with the current applicable regulations.
2. Retroactive Crediting of Surcharge: It would be wise for sponsors to check if the plan has a tobacco surcharge and whether that surcharge provides retroactive credit for the full year if the employee enrolls in a smoking cessation program. Although we do not believe the statutory language and the stated purpose behind wellness programs (health promotion and disease prevention) would require a retroactive refund of a surcharge for a time an employee was still smoking, not providing a retroactive credit may render the company vulnerable to a lawsuit under the legal theory promoted by the DOL and the plaintiff's bar.
3. Plan Communications: It is also advisable that sponsors review their plan materials and ensure they sufficiently communicate the existence of any smoking cessation program and the potential relief from surcharge available for participating in it.
4. Other Surcharges: Additionally, although the litigation to date has primarily focused on nicotine surcharges, other premium surcharges could face a similar risk of litigation. A couple of the recent lawsuits, for example, have targeted a plan's surcharge for unvaccinated employees in addition to the tobacco surcharge. Therefore, any review should involve looking at the plan's wellness program holistically.

Author

René E. Thorne is co-leader of Jackson Lewis P.C.'s ERISA Complex Litigation practice group and is a principal in the New Orleans, Louisiana, office. Her national practice covers the full range of complex benefit litigation matters, including representation of employers, plans, plan fiduciaries, third party administrators, and trustees. She is currently defending six tobacco surcharge class actions, including one brought by the Department of Labor. Additionally, she has handled numerous ERISA class actions alleging breach of fiduciary duty; breach of the duty of loyalty; prohibited transactions; 401(k) plan asset performance, fees, and expense issues; defined benefit plan asset issues, accrual issues, and cut-back issues; cash balance plan issues; ESOP litigation; fiduciary misrepresentation claims; sophisticated preemption issues; executive compensation litigation, both pension and welfare claims; retiree rights litigation; severance plan claims; Section 510 cases; and complex benefit claim cases. René is ranked nationally for ERISA litigation by Chambers. She has written and spoken extensively on various ERISA litigation topics and is active on the Employee Benefits Subcommittee of the Labor and Employment Section of the American Bar Association.

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