

Benefit Insights

DOL Guidance Tells How to Keep HSAs from ERISA Rules

Though established in conjunction with an employer sponsored high-deductible health plan (HDHP), a health savings account (HSA) is not considered an ERISA plan, so long as the employer's involvement with the HSA remains limited. This is important for employers, since ERISA plans would be subject to the additional compliance requirements of that law.

The Department of Labor (DOL)—the government agency responsible for ERISA enforcement—established this general principle in a Field Assistance Bulletin in 2004. More recently, it issued FAB 2006-02, which addresses, in more detail, the type and extent of involvement an employer can have and still not subject an HSA to ERISA. Also covered are actions that would result in ERISA application or trigger a prohibited transaction. Although HSAs are not ERISA plans (so long as employer involvement is limited), the Medicare Modernization Act—which created HSAs—specifically provides that prohibited transaction rules do apply to these accounts.

The DOL's initial guidance on HSAs (FAB 2004-01) stated that an employer could contribute to employees' HSAs and this would not subject the HSAs to ERISA, so long as establishment of the HSA was completely voluntary on the part of employees and the employer does not (1) limit employees' ability to move their funds to another HSA; (2) impose conditions on utilization of the HSA funds beyond those permitted by law; (3) make or influence investment decisions for HSA funds; (4)

represent that the HSA is an employee welfare benefit plan established or maintained by the employer; or (5) receive any payment or compensation in connection with an HSA.

In FAB 2006-02, the DOL clarifies that an employer can do the following and still not be considered to go beyond "limited involvement" with the HSA—

- An employer may open an HSA for an employee and deposit funds without the employee's affirmative consent. According to the DOL, this does not violate the requirement that an HSA be "completely voluntary" on the employee's part, because the employee still would have the exclusive responsibility for spending and controlling HSA funds.
- An employer may limit the HSA providers it allows to market their HSA products in the workplace, or select a single provider to which it will forward contributions.
- An employer may select an HSA provider that offers a limited selection of investment options or that offers investment options that replicate those offered under the employer's 401(k) plan, so long as employees are given a reasonable choice of investment options and are not limited in moving their funds to another HSA provider.
- An employer can realize FICA and FUTA savings by running contributions through a cafeteria plan, and this will not be considered improper "payment or compensation."

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Lambert Elected President of Southern New England Chapter ISCEBS

Paul Lambert has been elected as the 2007 President of the Southern New England Chapter of the International Society of Certified Employee Benefit Specialists. He is the first person to be elected to the position twice. The CEBS designation was developed by The International Foundation

of Employees Benefit Plans and the Wharton School of the University of Pennsylvania. The chapter conducts educational meetings focused on employee benefit programs throughout the year.



We are pleased to present to you Lambert & Carney's Employee Benefits newsletter. This newsletter is designed to give you timely and important information regarding employee benefits, government regulations, new products, and other areas of interest to employers and their employees. We value you, your employees, and your business and continue to strive to provide you with the very best products and service available.

Please contact Paul Lambert or Sean Carney at (800) 357-1840 if you have any questions.

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Massachusetts Healthcare Reform Law

Recently Massachusetts gained national attention for its attempts at universal health care by passing the **Massachusetts Healthcare Reform Law**. The state has struggled with the best method of implementation. The “Connector Authority” has been charged with working out the details of the law. Employers that have employees who live and work in Massachusetts need to be aware of the law’s provisions.

Recently, the “Connector Authority” has decided to postpone many of the requirements of the **Massachusetts Healthcare Reform Law** until July 1, 2009. One such requirement that has been postponed is the type of plan an employer must offer. The term that the authority uses is defined as a plan that is considered “creditable coverage”. The guidelines for what has been agreed upon as the minimum creditable coverage criteria or the type of plan that will be considered “creditable” is defined by the items listed below.

Minimum Creditable Coverage Criteria

(Revised and Updated – March 15, 2007)

1. *Comprehensive health benefits plan that includes preventive and primary care, emergency services, hospitalization benefits, ambulatory patient services, prescription drugs and mental health services;*
2. *No annual or per sickness benefits maximum;*
3. *No fee schedule of indemnity benefits for medical services (e.g., plan maximum benefit of \$500 per day for inpatient care, or \$50 per office visit, etc.);*
4. *Medical deductible shall not exceed \$2,000 for individual coverage and \$4,000 for family coverage;*
5. *All products that have an upfront deductible are required to cover preventive care visits prior to the deductible – at least three per individual and six per family. These preventive care visits may be subject to cost-sharing (i.e., co-payment or co-insurance) at no greater rate than applies to office visits;*
6. *If there is a separate deductible for drug coverage, the deductible may not exceed \$250 for individual coverage and \$500 for family coverage;*
7. *For health benefit plans that include a deductible and/or co-insurance, the maximum out-of-pocket spending for in-network services shall not exceed \$5,000 for individual coverage and \$10,000 for family coverage;*
8. *The out-of-pocket maximum must include any upfront deductible, all coinsurance, and all services that require \$100 or more in co-payments (e.g., inpatient admissions, ambulatory surgery). Prescription drug cost sharing need not count toward the out-of-pocket maximum; and*
9. *High deductible health plans (HDHP) that are H.S.A.-compliant shall be exempt from the above requirements and deemed to meet the Connector Authority’s minimum creditable coverage standards.*
10. *The Employer must pay for at least 33% of the overall premium of the plan.*

As noted in item 9 above the Connector Authority did decide to INCLUDE High Deductible Health Plans that are HSA compliant as creditable. This is a reversal of a previous position by the Connector.

One requirement that is taking effect on July 1 2007 is the obligation to complete an Employee Health Insurance Responsibility Disclosure or HIRD Form. This form is to be completed by the employee if he or she is considered eligible for coverage but declines to participate in the Employer plan. Again this portion of the legislation will be effective July 1, 2007 and is the most complicated piece of all. It mandates that all Massachusetts residents have insurance coverage.

Employees who are not eligible for your benefits may obtain coverage through one of the state’s “Connector” plans. If an Employer has more than eleven employees they must allow the employee to pay for this coverage through the Employer’s section 125 plan. Authority has yet to work out the details on how this will happen, but what they envision is that the Connector will notify employers to begin taking pre-tax deductions for these employees and sending the money to the Connector who will in turn send it to the health plans. This could be an administrative hassle and few think this can be put in place by July 1 2007 but at the moment that is still the plan. There are various reporting and administrative details that need to be clarified. We will of course keep you informed as these details become available.

As always if you have questions or need clarification please feel free to call or email us.

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- An employer can pay the fees associated with the HSA. On the other hand, the guidance also specifies actions that employers will want to avoid—
 - An employer that has limited the number of HSA vendors cannot receive discounts on other products from those vendors.
 - An employer that fails to promptly transmit participants’ HSA contributions may violate the prohibited transaction rules.
- With the growing popularity of HSAs, the DOL guidance is welcome. Given the consequences of inadvertently subjecting an HSA to ERISA, a thorough understanding of the DOL guidance is important for employers with HSAs in the workplace.

Three Generations of Investors View Retirement Planning Differently

According to a new study commissioned by Eaton Vance Corp, a generation gap exists when it comes to investment habits and beliefs. The investment firm hired Penn, Schoen, & Berland Associates to conduct a telephone survey of approximately 1,200 investors spanning three generations.

The first area in which the study uncovered generational differences was in 401k asset preferences. Sixty-four percent of GenXers preferred assets that primarily provide capital growth. Only 57 percent of boomers and 32 percent of seniors responded the same.



When asked what kind of asset they preferred to generate income, 34 percent of seniors and 31 percent of boomers polled chose stocks. Thirty-four percent of the GenXers who responded said they preferred real estate.

All three generations showed a preference for investing in companies that used a dividend to return cash to shareholders

as opposed to just buying back stock. In fact, 69 percent of all respondents said they preferred dividends. However, there was a distinct difference in the way each generation viewed the role of dividends in a portfolio. Forty-five percent of the seniors polled said they looked to dividends to provide income or as a source of both income and capital growth. This was in sharp contrast with the 70 percent of GenXers and 67 percent of boomers who answered that they expected dividends to provide long-term appreciation as opposed to income.

Generational investors were also divided on their expectations for dividend growth. The majority of boomers and GenXers believed that dividends would increase over the next few years. Only 44 percent of seniors felt that dividends would increase.

The generations found common ground on the subject of taxing dividends. A little over half of all three generations of investors who increased their investment in dividend-paying stocks over the last three years did so because of the 2003 tax reduction on dividend income. Almost half of all three generations of investors agreed that if Congress makes the reductions permanent, they will either start investing in dividend-paying stocks or will increase the amount invested in these stocks.

Another area of common ground among the generations is their lack of understanding about the tax implications of investing. When asked whether tax-managed stock funds, municipal bond funds, and variable annuities were better suited to be held inside or outside a qualified retirement plan, only 40 percent knew that tax-managed funds were better suited to be held inside a qualified retirement plan. Only 46 percent knew that municipal bond funds were appropriate for investment accounts held within a qualified plan; and only 39 percent knew that variable annuities were well suited to accounts held inside a qualified plan.

When asked if they would consider tax-managed investing if they could realize a 2 percent or more rate of growth annually after taxes, only the GenXers were enthusiastic about the prospect. Sixty-three percent of GenXers thought having a tax-managed account offering that rate of annual return was a desirable investment.

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By creating a situation that allows disability benefits to avoid tax, the employer helps the executive or senior level employee to narrow the gap between pre-disability earnings and post-disability benefits. An alternative—or additional—remedy looks at ways to fill that gap, by supplementing the basic company-sponsored LTD plan with additional, enhanced coverage. As noted above, typical LTD plans replace 60% of pre-disability earnings. They also may limit the maximum monthly benefit that can be paid, or exclude certain types of compensation that figure heavily into an executive's annual pay (such as bonuses or other

incentives). A supplemental plan can moderate the impact of these limits and/or exclusions, by including incentive compensation, eliminating or raising the monthly benefit cap, and raising the replacement percentage. While the executive's pre-disability income won't be matched, the gap between it and the disability benefit can be substantially reduced.

Tweaking your company's LTD plan to make it more executive-friendly can be an important element in attracting and retaining this valuable level employee.

Make Your LTD Plan More Executive-Friendly

Employer-sponsored long-term disability (LTD) plans typically replace 60% of pre-disability earnings, with some companies providing a slightly higher replacement percentage. When an employer pays the premiums for the LTD plan, benefits are taxable to the employee in the event of a disability. For executives or senior level employees with upper-range salaries—and thus upper bracket taxation—the tax hit on the disability benefit can generate a significant gap between pre-disability earnings and the amount of actual disability benefit received.

Suppose a senior level employee with an annual salary of \$200,000 becomes disabled, and the company-sponsored LTD plan replaces 60% of salary. This individual receives an annual disability benefit of \$120,000, or \$10,000 monthly. This benefit will be reduced by an additional 25%-35% (depending on the executive's other taxable income sources, deductions, the state income tax rate, etc.). So, this highly paid individual could see the monthly disability benefit fall to \$6,500, creating a huge gap between the pre-disability salary and disability benefit and causing a radical adjustment in the employee's standard of living.

What can employers do to help their executives and senior level employees fill this gap, or avoid creating such a huge gap in the first place?

The executive employee in the example was taxed on the disability benefits when paid because the employer had paid for the LTD plan premiums. If, however, the disability premium is paid by the employee with after-tax dollars, or is paid by the employer but imputed as income to the employee, any benefits paid are not subject to tax.

An Internal Revenue Service ruling (Rev. Rul. 2004-55) permits employers to allow employees to elect on a year-by-year basis whether to include any premium paid by the employer as income. The election must be irrevocable and must be made before the beginning of the plan year. An employee can make a different election for each subsequent plan year. If a disability occurs in a year when premiums are included in income, then disability benefits paid are not subject to tax. (The ruling also could be applied to short-term disability benefits.)

This approach enables employers to give executives the flexibility to determine whether, for the particular executive's financial situation, it is important that any disability benefits paid flow free from tax. Executives can change their minds, annually, in line with their current financial situation (impact of an income loss) and their perceived chances of becoming disabled (current overall health).

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