BENEFIT Plan Developments

A monthly report covering plan design and legislative changes

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Guidance On HSAs Is Issued By IRS, Treasury

The Internal Revenue Service (IRS) and Treasury Department have issued a notice (No. 2004-2) explaining **health savings accounts (HSAs)**. Any individual who has a high-deductible health plan may establish an HSA, which is completely portable, remains in the account until spent, and gains tax-free interest.

According to the notice, a "high-deductible health plan" or HDHP has an annual deductible of at least $1,000 with out-of-pocket expenses not exceeding $5,000 (for individuals), or at least a $2,000 deductible and annual out-of-pocket expenses not exceeding $10,000 (for families). Amounts are indexed for inflation.

The guidance also notes that a plan does not fail to qualify as an HDHP merely because it does not have a deductible (or small deductible) for preventive care. Furthermore, except for preventive care, the notice says a plan may not provide benefits for any year until the deductible for that year is met.

According to the guidance, tax-advantaged contributions to HSAs can be made in three ways: (1) the individual and family members can make tax-deductible contributions even if the individual does not itemize deductions, (2) the employer can make contributions that are not taxed to either the employer or employee, and (3) an employer with a cafeteria plan can allow employees to contribute untaxed salary through a **salary reduction plan**.

The IRS and Treasury Department said they plan to issue additional guidance in the summer of 2004. As a result, public comments are being solicited from taxpayers regarding information in the current notice, as well as on the following questions: What kinds of preventive care can be offered without a deductible in an HDHP? What relationships exist among HSAs, flexible spending accounts (FSAs), and health reimbursement arrangements (HRAs)? Should HDHPs being used in conjunction with HSAs be allowed to impose a lifetime limit on benefits? The

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notice can viewed online at http://www.irs.gov/pub/irs-drop/n-04-2.pdf

Financial Needs Analysis Helps Benefits Planning

A detailed analysis helps determine the right *insurance coverage.*

Sometimes people buy **life insurance** before performing a **financial needs analysis**. They might choose an amount that seems comfortable, without actually taking into account all the potential expenses their families might face in the event of an untimely death. If they did make an objective assessment of the possible economic consequences, they would be doing what is called a financial needs analysis.

In fact, you could analyze your *own* financial needs by following a few simple steps. First, total the value of all the things that you and/or your spouse own. These are your **assets**. (Enter amounts in one column for yourself, and in another column for your spouse.) Next, list and evaluate all expenses that you or your family may face, in the event one spouse dies. These are your potential **liabilities**. When totaling your assets and insurance, you might typically include what you currently have in **savings** and **retirement funds** (such as **IRAs, 401(k) plans,** or **TSAs,** etc.), as well as **real estate** and existing life insurance.

In order to determine how much cash is needed following the death of a spouse, take a look at these potential cash needs and assign a dollar amount to each:

1. **Immediate Money Fund.** The total cost of possible medical and hospital expenses, outstanding bills, burial costs, and attorney/executor fees. (It may be sufficient to set aside 50% of the higher wage earner's annual income for this purpose.)
2. **Debt Liquidation.** Your debt, if any, may be in the form of credit card bills, school and auto loans, unpaid notes, outstanding bills, etc. So that all debts may be cleared, record the total.
3. **Emergency Fund.** Unexpected bills not readily payable from current income, such as major home and car repairs, or even medical emergencies. (Again, 50% of the higher wage earner's annual income may be sufficient.)
4. **Mortgage/Rent Payment Fund.** How much would you need to pay off your mortgage or provide for at least ten years' apartment rent should one spouse die?
5. **Child/Home Care Fund.** Expenses created as a result of the death of a spouse who had been performing child and/or home care duties, but was not receiving any payments for it. (Estimate the cost of hired help needed to substitute your spouse's duties.)
6. **Education Fund.** The cost of funding a four-year undergraduate education or comparable vocational training for your children.

The total of all of the above costs minus your liquid assets and life insurance would give you your new *cash needs*. The numbers will be different for you and for your spouse, because assets and existing life insurance, as well as child/home care amounts, are likely to be different.

The steps noted above are a simple way for a family to figure out how much life insurance is really needed. Circumstances vary from person to person and from family to family. Analyzing your financial needs in detail is an important step toward determining the *right* coverage for you and your family.

States Adopt Contraceptive Equity Laws

A total of 20 states have enacted legislation mandating contraceptive equity in health insurance coverage and that number may increase, according to the National Women's Law Center, a nonprofit organization based in Washington, D.C.

The Center found that existing contraceptive equity laws are uniform in stating that if a health insurance policy provides prescription drug coverage, then the plan must provide coverage for any prescription drug or device that has been approved by the Federal Drug Administration as a contraceptive. In addition, the Center discovered that most existing laws state that any deductible, co-payment, or co-insurance applied to contraceptives may not be greater than those applied to other prescription drugs.

Employers that provide self-funded plans are governed by the **Employee Retirement Income Security Act (ERISA)** and are not regulated under state law. However, the Center noted that the **Equal Employment Opportunity Commission (EEOC)** has found that all employer-provided health care plans that fail to provide health insurance coverage for prescription contraceptives violate Title VII of the Civil Rights Act of 1964 because such action discriminates on the basis of gender and pregnancy.

The Center said the 20 states that currently have contraceptive equity laws are: Arizona, California, Connecticut, Delaware, Georgia, Hawaii, Illinois, Iowa, Maine, Maryland, Massachusetts, Missouri, Nevada, New Hampshire, New Mexico, New York, North Carolina, Rhode Island, Vermont, and Washington state. Meanwhile, the Center noted, another eight states have mandated that HMOs cover "family planning services." They are: Michigan, Montana, New Jersey, North Dakota, Ohio, Oklahoma, West Virginia, and Wyoming.

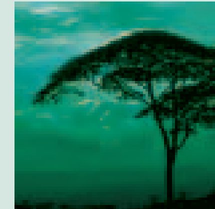
Medical 401(k)s Being Studied By Deere, Fidelity

Deere & Company is working with Fidelity Investments to develop a proposal for a **retiree medical benefits account (RMBA)** that would function like a **401(k) plan** for health care.

In advocating the need for RMBAs, Fidelity noted that, if a 65-year-old couple were to retire today without access to an employer-sponsored health care plan, they would need an estimated $175,000 to fund out-of-pocket medical expenses.

"Currently, there is no available account option that delivers the ideal combination of tax benefits, funding flexibility, portability, and investment options," said Brad Kimler, Fidelity Health and Welfare Consulting. "However, it is our hope that future regulatory changes will encourage the evolution of accounts. . .(that complement) the balance of an employer's retirement benefit offering."

Mert Hornbuckle, vice president of human resources at Deere, said his company's aim in supporting the creation of RMBAs is "to help future retirees better understand medical costs and encourage them to plan and save to meet their own needs in retirement, beyond what Medicare and/or employer-sponsored retiree benefits provide."



A new type of 401(k) for medical benefits is being studied.

Disability Income Insurance Requires Thoughtful Planning

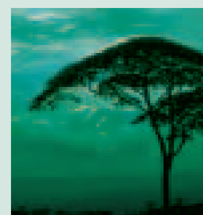
Have you ever asked yourself how your employees would manage if they were to suffer a severe accident or illness that left them unable to work? How would they pay their bills and cover their daily expenses? The likelihood of such an event may be greater than you think. According to the Insurance Information Institute (III, 2002), an employee between the ages of 40 and 65 has a *greater* chance of missing at least three months of work due to an accident or illness than of suffering an untimely death. To compound the problem, the recovery period may run as high as a lengthy two and a half years.

To be prepared for such a situation, it is important for your employees to *plan ahead.* A smart approach to help protect your employees is for them to purchase an **individual disability income insurance** policy. However, there are a few considerations your employees should keep in mind when they are choosing this coverage:

- **Definition of Disability.** Employees should carefully review their policy's definition of disability. Some policies may provide coverage if an employee is unable to work in the occupation in which he or she was employed or for which he or she was trained. In contrast, other policies may offer coverage only if your employee was unable to work in *any* occupation.
- **Residual Benefits or Partial Disability Coverage.** Under certain specified circumstances, if an employee becomes disabled and is only able to earn a *portion* of his or her previous income, residual benefits or partial disability coverage pays a portion of their benefits.
- **Guaranteed Renewable.** With this feature, the insurer cannot refuse to renew an employee's policy or change any terms, except for premium cost, as long as premiums are paid on time.
- **Guaranteed Insurability.** This provision allows employees to increase their monthly benefit, even if they experience health changes that would otherwise prevent them from obtaining additional disability coverage.
- **Cost-of-Living Adjustment (COLA).** This feature helps protect an employee's benefits against the effects of inflation during a long-term disability.

There are alternatives to having a disability income policy, although they have shortcomings. For instance, employees could self-insure. However, one year of disability could easily eliminate many years of savings for the self-insured. **Workers compensation** may be an option in some cases; however, it only covers injuries suffered on the job. Eligibility and benefits vary by state.

To qualify for **Social Security** disability benefits, your employees must be severely disabled and, even then, they will have to wait at least six months for payments to begin. Social Security disability was not intended to be an individual's sole source of disability income, thus benefits are often less than what an employee might need to cover regular living expenses.



There are multiple considerations for employees to mull when purchasing disability income insurance.