METRO NEWS – Report #66
July 31, 2007

To our clients and friends:

This is another in a series of newsletters designed to keep you clearly informed of current events in the area of employee benefit plans.

New quarterly statement requirement – second notice due:

Last year's pension law (PPA) created new quarterly reporting rules for 401k plans. We sent clients a mailing on this a few months ago. The first quarterly report to plan members was due 5/15/07. This is to remind you that the next report will be due 8/15 and so on. As you may recall from that mailing, there are 7 items to be reported (some of them are silly). For plans on a mutual fund platform, the fund family usually reports all items so you need not do anything. For other plans, we have provided you with the required handout. Please call if uncertain.

How much can I deduct?

Most of us are familiar with the 401k annual limit of $ 45,000 per year. (plus $5,000 more if you are over age 50.) Remember that there are other types of plans available to you, such as the (dreaded) defined benefit plan. These plans can allow an annual contribution of over $ 200,000 per year per person, based upon age. There is some "baggage" with these plans, since they are a "pension plan", which envisions an annual recurring contribution. They are typically more expensive to administer, since an actuarial valuation is needed each year. Nevertheless, a huge tax deduction like this will cover a lot of "baggage"!

Actuarial Corner - Want to live to be 100?

The recent "North American Actuarial Journal" has an article about this topic. (Authors: Gavrilova and Gavrilova, 1/07 edition). Here are a few key findings:

- Normally I wouldn't burden you with a long title like this, but the article is titled: *"Search for predictors of human longevity: using computerized genealogies and internet resources for human longevity studies"*. By cross referencing Social Security records, public internet records, and US census records, the authors have tried to "clean up" the data related to old people. You can imagine how "iffy" the records are for centenarians.
- Having a farm background (did your parents own a farm?) and growing up in the West may help, as a "lower burden of sickness during childhood may have far-reaching consequences for survival to extreme old ages".
- How old was Mommy when you were born? I would not have guessed it, but this appears to be a major factor in determining your chances of survival to age 100. If a mother is younger than age 25 at the birth of a child, then that child has a 1.8 times greater chance of living to age 100 than later-born children. Remember that this study is looking at people who were born a long time ago, when child mortality was very high. It is possible that a younger parent had more resources and energy to invest in their newborn than would an older parent.
- It is fun being an actuary because (among other reasons) you get to think about these concepts. Yes we may look geeky but we may have some redeeming characteristics. Plus, we have a good feel for probability, which helps us navigate through some of life's issues (but not poker yet) more easily. Be nice to your actuary today.

Health FSA's, HRA's and HSA's -- Which one is right for you? (by Diane M. Barton, CPC)

(Preface – Diane is Senior Vice President at Metro Benefits, Inc. Among other duties, Diane oversees our cafeteria plan department, and prepared this article to provide an overview of current trends in plan design.) Please see the attached pink sheets for Diane's article.

You may be surprised to know that…..

Metro's biggest client is the United States Department of Labor! This is because they entrust us with many of their "orphan" plans. Let me explain.

Most of the 401k plans that you know of operate smoothly. Money goes in. Money comes out. Investments grow over time. Life is good.

Believe it or not, there are some 401k plans that do not operate this smoothly. Sometimes the Employer is unable to overcome the temptation of ready cash, and they "borrow" employee or employer 401k funds to run their business. Sometimes the company just dissolves, and there is no "Trustee" left to sign the papers so that the employees can take their money out.

When these problems occur, the DOL has the authority to go to Court, and to replace the Plan Trustee. Metro Benefits has taken over Trusteeship on over 30 of these plans so far. We play the role of "Independent Fiduciary", and we become responsible for liquidating plan assets and coordinating the termination of the plan. As you might imagine, we do not always have clear records of how much money belongs to each plan member, so we may need to recreate old records or make estimates.

The DOL does not want us to spend money on "paperwork" like revising plan documents or preparing annual tax returns for these "orphan plans". By avoiding these expenses, we can preserve more of the plan assets to pay out. (It is interesting to note that healthy plans are required to jump through these same hoops, however.)

While we normally do not seek fiduciary responsibility, we have found this to be an interesting niche for us. By placing ourselves on the "employer's" side of the desk, we gain a different perspective.

Please join me in congratulating….

…. Diane Barton as a new minority owner of Metro!! Diane has been with Metro since 1989, and will become an owner of Metro Benefits. With her great commitment, professionalism, and leadership, Diane has earned this opportunity!

Best Wishes, David M. Lipkin, F.S.A., Editor

Metro Benefits, Inc. is a regional consulting and administration firm, based in Pittsburgh, PA. We provide a wide range of services for employee benefit plans. While we make every effort to verify the accuracy of the information that we present here, you should consult with your Plan attorney or other advisor before acting upon it.

Health FSA's, HRA's and HSA's -- Which one is right for you?

by Diane M. Barton, CPC

Many employers looking to reduce or cap rising health care costs may want to consider implementing a consumer driven health plan arrangement such as a Health FSA; an HRA or an HSA plan. The basic premise of these plans is that the employees (the consumers of the health care) will be more prudent with their health care expenses if they have a financial stake in the costs and benefits of the underlying arrangement.

Below is a short synopsis of each of these types of plan design arrangements:

Health FSA's (Flexible Spending Accounts)

Health FSA's are a reimbursement arrangements that are part of a Section 125 Cafeteria Plan. They allow employees to contribute pretax dollars to be used to pay for eligible expenses under Section 213 of the Internal Revenue Code that are not covered by insurance, as well as for insurance co-payments and deductibles. Many plans also allow for the reimbursement of over the counter medications that are available without a prescription.

Under a Health FSA each employee sets aside a dollar amount to be contributed at the beginning of the year. This amount is deducted from their salary on a pro-rata basis over the course of the year. The employee pays the expenses up front as they are incurred and then submits a claim form to the Employer for reimbursement.

Contributions made by the employee for their Health FSA expenses are excludable from income for Federal income tax purposes, and are not subject to Social Security and Federal unemployment taxes. The Employer also saves on their share of the Social Security taxes for the contributing employees.

Any contributions that the employee does not use by the end of the year (plus a 2 -1/2 month grace period, if the plan allows) must be forfeited. Therefore, it is important for the employee to plan out their annual contributions carefully.

Section 125 Cafeteria Plans can also allow for reimbursement of dependent care assistance benefits as well as for the payment of the employee cost of the Employer provided group insurance premiums on a pre-tax basis.

HRA's (HEALTH REIMBURSEMENT ARRANGEMENTS)

HRA's are a type of Employer provided defined contribution health plan. The Employer sets aside a fixed dollar amount they are willing to contribute toward healthcare expenses. It does not necessarily need to be tied into the actual cost of a specific health insurance benefit.

HRA's are funded by the Employer only. No employee contributions are allowed.

The employee pays for the expenses up front as they are incurred and then submits a claim form to the Employer for reimbursement.

Tax-free distributions from the HRA are allowable for qualified medical expenses under Section 213 of the Internal Revenue Code that are not deducted or reimbursed by insurance as well as for insurance premiums, insurance co-payments and deductibles. Many plans also allow for the reimbursement of over the counter medications that are available without a prescription.

Unlike a Health FSA which must have a "use-it or lose it" provision for unused contributions, the balance in the HRA may be carried forward from year-to year.

Under the HRA, the employee becomes more aware of their health choices as they customize the plan to fit their individual needs.

(HSA's) Health Savings Accounts

HSA's are trust/custodial arrangements that are established to pay for qualified medical expenses. Unlike the Health FSA and HRA which are plans established only by Employers, HSA's can be established by either an individual or by an Employer.

In order to participate in an HSA there are four requirements that must be met:

1. The individual must be covered by a High Deductible Health Plan (HDHP);

2. An individual may not be covered by any other non-HDHP, except for certain permissible benefits not covered by the HDHP;

3. An individual must not be eligible for Medicare benefits; and

4. The individual may not be claimed as a dependent on another person's tax return.

Annual limits are imposed by the IRS on the amount that can be contributed to an HSA during the year depending upon whether the individual has self-only coverage or family coverage. In addition, individuals age 55 or older may make additional catch-up HSA contributions.

Contributions made by an individual are deductible and not subject to the

7-1/2% threshold that normally applies to medical expense deductions. Contributions made by an employee are excludable from income for Federal income tax purposes and are not subject to Social Security or Federal unemployment taxes. The Employer also saves on their share of the Social Security taxes for the contributing employees.

Unlike the Health FSA and the HRA, which are typically unfunded arrangements, the HSA is a funded plan. Distributions of any contributions and the associated investment earnings on the account are tax-free so long as they are used to pay for qualified medical expenses; insurance co-payments and deductibles. Many plans also allow for the reimbursement of over the counter medications that are available without a prescription.

Distributions not used for qualified medical expenses will be taxed and a 10% additional tax will apply except if the distribution is taken after the individual dies or becomes disabled, or the individual becomes entitled to Medicare benefits.

Because HSA's are funded arrangements, HSA's have a dual purpose – to provide for current health coverage and to provide a savings vehicle for future health coverage. Individuals can limit medical expenses today to save for expenses they will incur in the future.

Designing a health benefit plan that meets the needs of the Employer and the employees can be a challenge. There are many other issues to consider regarding each of these types of plan arrangements including, but not limited to, documentation requirements; restrictions on the ability of sole proprietors and partners to participate; annual non-discrimination testing; specific plan design limitations; etc. For further information contact our office and we'll be glad to discuss these plans in more detail.