

BenAlert

BENEFIT TRENDS AND LEGISLATIVE UPDATES

NOVEMBER 2008



HOWITT
Benefit Services

Howitt Benefit Services is pleased to provide you with periodic updates on benefit trends and legislative updates. As part of our valuable services, we want to ensure that you are in compliance and well-informed of the ongoing changes in our industry.

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2008 Plan Year End: Compliance Highlights

The purpose of this BenAlert is to provide you with a turnkey list of benefits issues that requires attention between now and the end of 2008, whether or not your plans are calendar year plans. For some of you, 2009 benefits are fixed and open enrollments have begun or are about to begin. 2009 plan design and communication strategies are in place. For others, budget constraints are calling for significant changes in plan design. Regardless of which stage you are in, at some point before year-end you must address your plan compliance obligations. Here is your checklist.

1. **New Compliance Required.** Plan Sponsors must address the following:
 - **Cafeteria Plans:** Compliance with new regulations
Click [here](#) to see the BenAlert previously sent regarding the following two topics.
 - New Medicare Secondary Payer reporting requirements;
 - New Medicare Part-D Notice content (must be completed by Nov 15th).
2. **Year-end Federal Tax Compliance.** This Memorandum provides you with an overview of IRS rules regarding the following:
 - Taxation of group term life insurance coverage in excess of \$50,000;
 - Tax treatment of coverage for same-sex marriage partners and domestic partners;
 - Tax treatment of coverage provided to over-age dependents.

3. **Annual and Event-related Notice Requirements.** See Attachment A for a list of required notices you must provide employees/plan participants either annually or upon the occurrence of a specific event.

DETAILS: NEW COMPLIANCE

1. **New Cafeteria Plan Rules.** For those of you who offer calendar year cafeteria plans with health care and/or dependent care spending accounts, January 1, 2009 is a very important date. By that time your cafeteria plan documents must comply with new rules and, if needed, must be amended by January 1, 2009. These new cafeteria plan rules prohibit retroactive plan amendments; so, get it right, before the plan year starts.

Written Plan Document. There must be a written plan document in place on or before the first day of the cafeteria plan year. The IRS will disqualify a plan if the plan document does not meet legal requirements.

Notable New Provisions. The new regulations contain a number of provisions a Plan Sponsor must incorporate into the plan document as well as new benefit choices available to the Plan Sponsor, at his/her discretion:

- **Common Law Employee (mandatory):** Explicit provision prohibiting participation in the plan by any individual who is not a common law employee of the Plan Sponsor.
- **Amendment and Termination Provision (mandatory):** Any amendment to a cafeteria plan must be made before the beginning of a plan year.
- **Orthodontia (voluntary):** The plan may permit reimbursement for advance payments to orthodontists even though it is for services not yet performed.
- **Dependent Care (voluntary):** The plan may permit reimbursement to terminated participants for dependent care expenses incurred after termination of employment where an account balance remains available.
- **Adoption Assistance (voluntary):** The plan may include pre-tax contributions toward the cost of adoptions which qualify under IRC Section 137..
- **Non-discriminatory Plan.** On audit, the IRS will test a plan for passing non-discrimination tests as of the last day of the plan year. Although a Plan Sponsor may want to test for non-discrimination (using IRS rules found at IRS regulation 1.125-6) at the beginning of or during the plan year to assure compliance, the IRS, on audit, will only test as of the last day of the plan year.

Recommendation. If you have a cafeteria plan, review the existing plan document and make any necessary amendments by December 31, 2008.

2. **Medicare Secondary Payer Requirements.** As of January 1, 2009, insurers and third party administrators (TPAs) must collect and report information on all Medicare eligible plan participants, their coverage election including type of coverage (e.g., HMO, PPO, etc), group policy numbers (if applicable) and other data specifically on drug plan availability. See <http://www.howittins.com/> and look under Quicklinks.

3. **Medicare Part-D Notices (Due no later than November 15, 2008):**

Notice Requirement. The Center for Medicare and Medicaid Services (“CMS”) recently updated the model notices required under Medicare Part D, including the model notices of creditable and non-creditable coverage to be used by employers to notify health care plan participants whether the prescription drug benefits available under the employer’s health plan is a satisfactory substitute for Medicare Part-D.

See <http://www.howittins.com/> and look under Quicklinks.

The Deadline is November 15, 2008!

DETAILS: FEDERAL TAX COMPLIANCE

As you prepare your W-2s you may need to include additional income for those employees with employer provided group term life insurance in excess of \$50,000, as well as imputed income for domestic partner coverage, same-sex marriage partner benefits, and coverage provided to over-age dependents.

1. **Group Term Life Benefits.** Each calendar year the cost of group term life insurance benefits provided by the employer in excess of \$50,000 is taxable to the employee. The IRS uses a table to determine the amount of income per \$1,000 per month of coverage. This imputed income is to be included on the employee’s W-2 for the year in which the coverage is provided. Although rare, it is also possible that a group term life benefit discriminates in favor of the highly compensated, resulting in the cost of all group term life insurance (using IRS Table 1 rates) to be included in the highly compensated employee’s wages. We provide you a chart shortly.
2. **Domestic Partners / Same-sex Marriages.** Since federal law does not recognize domestic partnerships or same-sex marriages for federal income tax purposes, Plan Sponsors must impute income on the value of the health and other benefit coverage provided to the partner or same-sex marriage partner. The amount to impute is the fair market value of the employer provided coverage

(usually health care benefits) offset by any employee after-tax contributions toward the domestic partner / same-sex marriage partner's coverage. The fair market value traditionally used is either the premium amount for single coverage or the premium amount for employee plus spouse minus the employee premium. To calculate the imputed income, please refer to the imputed income calculator Attachment B.

For example, single coverage \$350; employee and spouse coverage \$650: imputed income would be \$300 per month (offset by the employee's after-tax contribution, if any). Since the amount of imputed income over the year can be substantial, it is important to include it in each pay check. Regardless of how you include it, this income must appear as wages on the W-2.

3. **Over-age Dependents.** Effective January 1, 2005, Congress amended and replaced IRC Section 152 with a new definition of dependents which may impact your health plan eligibility rules for dependent children. The new rule defines a dependent child to include a child who has not reached the age of 19 (unless handicapped) or age 24 (for full time students). For purposes of taxation, any benefit (coverage) a child receives after the date he/she turns age 24 is taxable for federal income tax purposes.

For example, if Suzanne, a full-time student, turns 24 on July 27, 2008, the employer provided group health care coverage provided from July 28, 2008 through December 31, 2008 must be reported on the employee's W-2 based on the fair market value of his/her coverage for the period. State income tax rules in this situation vary by state.

Recommendation. Conduct a dependent status audit based on enrollees who request coverage for dependent children who are age 18 or older. To assure responsiveness, some employers reserve the right to terminate dependent coverage in the absence of a complete response.

To make the audit effective, it is important to review and, if needed, clarify dependent eligibility rules as they appear in all plan documents, including the official plan document and the summary plan description or evidence of coverage. If there are changes, you must provide notice of the change to plan participants.

ACTION ITEMS FOR ALL PLAN SPONSORS

1. Review your welfare plan documents and enrollment materials for consistency and inclusion of appropriate notices.
2. Review your cafeteria plan documents and amend as needed, prior to December 31, 2008 (or by the first day of the plan year thereafter).
3. Determine your compliance on imputed income and on withholding for that income as it applies to domestic partner or same-sex marriage benefits.
4. Conduct an over-age dependent status audit.
5. Determine your compliance with Medicare Part-D Notice (by November 15, 2008) and your annual notice requirements.

For more details on any of these developments, please call Larry Seiden, our Compliance Officer, at 408-997-3019.

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