

BenAlert

Benefit Trends and Legislative Updates



December 2006

Howitt Insurance 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.

New HSA Provisions

Delivering on healthcare goals in President Bush's January State of the Union Address, a new bill, HR 6111 (Tax Relief and Health Care Act of 2006), was passed by Congress this week and is expected to be signed by the President before the holidays. This bill will allow consumers with FSAs, individual retirement plans and health reimbursement arrangements to transfer funds into their HSAs.

The passing of this bill greatly enhances the rules governing HSAs. It also expands funding sources for HSAs. The HSA provisions will go into effect on January 1, 2007.

If you are presently offering an HSA plan to your employees, you need to communicate to your employees these new regulations which may benefit them.

The bill allows an employee a one-time opportunity to roll over unused funds from an existing Flexible Spending Account (FSA) and/or Health Reimbursement Arrangement (HRA) to deposit in their Health Savings Account.

For FSAs and HRAs, the rollover must meet these requirements:

- The rollover amount must be no more than the FSA balance on September 21, 2006, or at the time of distribution.
- The transfer must be directly from the employer to the HSA and take place no later than December 31, 2011.
- The rollover can occur only once from that particular account.

For IRAs, the rollover must meet these requirements:

- The rollover amount is counted against the annual maximum limit for HSA contributions.
- The transfer must be directly from the IRA trustee to the HSA.

- The rollover can occur only once from the IRA, unless the first rollover was during self-only high-deductible health plan (HDHP) coverage, and the later rollover is with family HDHP coverage.

For both types of rollovers, HSA participants need to continue HDHP coverage for a testing period of 12 months or else the rollovers will be includible in gross income and subject to an additional 10% tax. This does not apply if the reason for terminating HDHP coverage is disability or death. The HRA/FSA rules go into effect the day the bill becomes law. The IRA rules are effective on January 1, 2007.

HSA participation may occur during FSA grace periods. The former rule stated that the mere existence of an FSA grace period precluded participation in an HSA. Thus, if an employer was moving from a calendar-year plan with a 2½-month grace period to an HSA, HSA enrollment could not occur until April 1. Under the new rule, HSA participation may begin earlier in either of two scenarios:

- * The participant has a zero balance at the end of the plan year (e.g., December 31 for calendar-year plans); or
- * The participant rolls over the remaining FSA balance to the HSA.

Simplifies and Expands the Annual Limits on HSA Contributions

One of the complaints about HSAs was the complexity of determining the annual contribution limit: the lesser of the HDHP deductible or a statutory limit that is adjusted annually. H.R. 6111 removes these complications. First, the annual maximum contribution limit is no longer based on the HDHP deductible. For 2007, these limits are \$2,850 (self-only coverage) and \$5,650 (family coverage).

Another rule complicated matters further: if an HSA participant began in the middle of the year, the limit was prorated (e.g., 7/12 of the annual limit for a June 1 HSA start date).

This will help people who begin their HSA-qualified coverage part way through the year and who are subject to the entire calendar-year deductible by allowing them to make a full annual contribution, rather than pro-rating their contribution for the number of months of HSA-qualified coverage. Taxpayers would be required to maintain a high deductible plan for a full year beginning in the month the HSA begins or pay tax on the contribution and a 10 percent penalty.

Additional Flexibility for Employers to Help Lower Paid Workers

Allows employers to make additional contributions for lower-paid workers. The bill provides an exception to the current “comparability rules” that require companies to make equal dollar contributions to all HSA-eligible employees with similar coverage (single or family) and work status

(full-time or part-time). This provision will give employers flexibility to provide greater assistance to their lower-paid workers in the form of contributions to their HSA accounts.

Earlier Notification of Cost of Living Adjustment

Under current law, the minimum deductible and out-of-pocket limits for HSA-qualified policies, as well as the annual contribution limits are indexed for inflation. The bill requires the Secretary of the Treasury to announce adjustments to the amounts by June 1st of each year. Currently, the adjustments are not announced until November each year. Earlier notification will simplify planning decisions for insurance companies, banks, credit unions, employers, and taxpayers.

HSA comparability rules are loosened. If an employer does not make HSA contributions through a cafeteria plan, existing rules required contributions to be comparable, i.e., the same amount or percentage of the deductible. H.R. 6111 provides an exception: employers may contribute more to the HSAs of non-highly compensated employees than the HSAs of highly compensated employees.

Please call us at 408-323-1436 if you have further questions.

Bill information courtesy of HSA Clearing Corp and Infinisource

Howitt Insurance Services (HIS) is not an attorney firm and HIS is not giving legal advice or interpreting the IRS Code.