

Section 125 Cafeteria Plans	
	Continuous Education

History	
	<ul style="list-style-type: none"> • Enacted in 1978 • Employee Benefit Program • Choice between cash and a variety of non-taxable benefits • Salary Reduction Agreement

Benefits Offered Under 125	
	<ul style="list-style-type: none"> • Section 105 and 106 Accident and Health Insurance (including disability insurance) • Section 79 term life insurance • Section 129 dependent care • Section 132(f) transportation

How Does it Work? - Employee		
	Without 125	With 125
Salary.....	\$3,500	\$3,500
Flex Dollars.....	0	800
Taxable Income.....	3,500	2,700
Income Tax.....	525	405
State Tax.....	175	135
Social Security.....	268	207
Income After Taxes.....	2,532	1,953
Medical Premium.....	300	
Medical Expenses.....	100	
Dependent Care.....	\$ 400	\$ 0
Take-Home Pay	\$ 1,732	\$ 1,953
Net Increase		\$ 221
Pay Periods		x 12
Annual Increase		= \$2,652*

*This is for illustration purposes only. Actual savings may vary.

How Does it Work? - Employer		
	Without 125	With 125
Salary.....	\$1,600	\$1,600
Flex Dollars.....	0	400
Taxable Income.....	1,600	1,200
Income Tax.....	240	180
State Tax.....	80	60
Social Security.....	128	96
Income After Taxes.....	1,152	864
Dependent Care.....	\$ 200	\$ 0
Take-Home Pay	\$ 710	\$ 833
Net Increase		\$ 123
Pay Periods		x 12
Annual Increase		= \$1,476*

Employer's Savings

\$400 x 12 months = \$4,800 x 0765 = \$367.20

*This is for illustration purposes only. Actual savings may vary.

Benefits to 125	
	<ul style="list-style-type: none"> • Tax Savings WIN-WIN • Recruiting/Retaining Employees • A benefit most everyone can use

Health FSA Eligible Expenses*	
<p>Acupuncture Alcoholism Ambulance hire Artificial limbs/teeth Birth control pills Birth prevention surgery Braces Braille - books and magazines Care for handicapped child Chiropractors Christian Science fees Co-insurance Communication equipment/deaf Contact lenses and cleaning solution Crutches</p>	<p>Deductibles Dental fees Dentures Diagnostic fees Drug and medical supplies Education for the blind Eyeglasses, including exam fee Healing service fee Hearing devices and batteries Home improvements motivated by medical consideration Hospital bills/hospitalization insurance Insulin Laboratory fee Lasik Eye Surgery</p>
<p>* This list is to serve as a reference only. It is not a complete list of deductible expenses, nor is it an item-by-item approved list of expenses by the Internal Revenue Service (IRS), as determinations made by the IRS may vary from year to year.</p>	

Eligible Expenses Cont'd	
<p>Laetrile by prescription Lead base paint removal for children with lead poisoning Membership fee in association with furnishing medical services, hospitalization and clinical care Needed medical supplies, prescribed by doctor Nurses' fees Obstetrical expenses Operations Orthodontia Orthopedic shoes Osteopaths Over-the-Counter (OTC Drugs) Oxygen Prescribed medicines Psychiatric care Psychologist fees</p>	<p>Routine physicals and other non-diagnostic services "Seeing Eye" dog and its upkeep Sterilization fees Stop Smoking Programs Surgical fees Therapeutic care for drug/alcohol addiction Therapy treatments Transportation expenses primarily for rendition of medical services Tuition at special school for handicapped Wheelchair Wigs (prescribed by a physician) X-rays</p>

Type of 125's
<ul style="list-style-type: none"> • Premium Only Plans <ul style="list-style-type: none"> – Most common – almost everyone has – Only benefit offered is – Health Related Insurance Premiums – Low Cost to implement – Low maintenance – Good starting point

Type of 125's
<ul style="list-style-type: none"> • Full Cafeteria Plan <ul style="list-style-type: none"> – Variety of Benefits "a-la-carte" <ul style="list-style-type: none"> • Health Related Medical Premiums + Dependent Care + Transportation + Non-Employer Sponsored Health Related Premiums + HSA – More Complex <ul style="list-style-type: none"> • Enrollment Process • Moving of payroll funds to TPA • Claim Processing & Payments • Compliance

Business Qualifications
<ul style="list-style-type: none"> • Filing Status should be taken into account <ul style="list-style-type: none"> – Sole Proprietor – Partnership – LLC – Corporations (including S-Corps) • Along with what the Plan objectives are <ul style="list-style-type: none"> – Do the owners want to participate?

Compliance & 125
<ul style="list-style-type: none"> • Plan Documentation • Shared Risk <ul style="list-style-type: none"> – Use it or Lose it (Employee Risk) – Uniform Coverage (Employer Risk) • Non-Discrimination Testing • HIPAA

Plan Documentation

- Have to have it!
- Outlines the parameters of the plan
- Provides specific “Plan Design” options
 - Benefits Offered
 - Who is Eligible and When
 - What are the Plan Year Dates
 - Etc

Use it or Lose it Rule

- What does it mean?
- #1 Reason Employees do not participate
- Overcoming that objection – What is the TAX Savings – the \$ Lost?
- Grace Period – Changed the Perception!
 - 75 days of additional time to spend!
 - Employer controls 0-75

Left Over Funds

- Employee who “lost” money to Employer
What can the Employer Do or Not Do with that \$?
 - Can NOT give back to employee(s) who lost
 - Can give back to ALL employees who participated - equally
 - Can use for employee welfare (parties, donation to charity, etc)
 - Can keep and absorb into financials

Uniform Coverage

- Proposed Reg § 1.125-2(Q&A7)(b)(2)
Uniform coverage throughout coverage period.
The maximum amount of reimbursement under a health FSA must be available at all time during the period of coverage (properly reduced as of any particular time for prior reimbursements for the same period of coverage). Thus, the maximum amount of reimbursement at any particular time during the period of coverage cannot relate to the extent to which the participant has paid the required premiums for coverage, under the health FSA, for the coverage period. Similarly, the payment schedule for the required premiums for coverage under health FSA may not be based on the rate or amount of covered claims incurred during the coverage period.

Uniform Coverage

- What does that mean for the Employee?
 - My total Medical FSA election is available to me day 1 of Plan!
- What does that mean for the Employer?
 - If I quit on day 2, after spending it all on day 1 – the employer has to assume that dollar amount!

Uniform Coverage

- Uniform Coverage – Controlled Risk
 - Employer sets the maximum amount you can elect each year
 - Employer sets who is eligible (allowing to exclude the more risky groups – seasonal, part-time etc)
 - Most likely for someone an employer “loses” on – and employee will “lose” to cover the difference!

Uniform Coverage

- Can the employer recoup their loss?
 - Caution!
 - Room for interpretation – some will say yes, IF you collect from everyone – positive and negative.
 - Some will say no, don't go there – this is the least complicated and is sure-fire compliant!
 - Remember – there is RISK to employer and employee (IRS) – by withholding you are removing that RISK.

Non-Discrimination Testing

- A.K.A. – Highly Compensated Testing
- Done annually
- There are a variety of tests
- IRS is non-specific
- Range from 15%-45%
- Calculating at what level a high comp'd employee can participate in benefits.

Non-Discrimination Testing

- Who is considered Highly Comp'd
 - Any Officer of the Corporation, or
 - Making over \$100,000 and in top 20%, or
 - Employees who are spouse/offspring (not necessarily "IRS-defined dependants") of an employee meeting 1, 2 or 3

Non-Discrimination Testing

- **IMPORTANT!**
 - Intention behind Non-Discrim Testing was to create a "safe harbor"
 - Passing means your plan is non-discriminatory
 - Failing does not necessarily mean you are discriminatory
 - Other factors may exist
 - Plan can most likely continue, seek counsel

HIPAA

- Section 125 Plans must be HIPAA compliant
- Health Protected Information (HPI) is part of the process

Self-Administration vs. TPA

- Being Assured of Compliance
- Accounting
- FSA Processing
- COBRA
- Customer & Client Services
- Administrative benefits communication
- Enrollment Processing/Meetings

Available Features of 125's

- Debit Cards
 - Instant Reimbursement
 - Easy to use
 - Increases Participation (National Average is 70% increase)
- Direct Deposit
 - No trip to the bank
 - No hassle
 - Faster! – Eliminate mail time

Available Features of 125's

- On-Line Tools
 - Many TPA's have variety of online tools available
 - Enrollment
 - Claim Processing
 - Account Balances
 - Reporting
 - Compliance

HSA's & FSA's

- Individuals can participate in both if:
 - FSA is Limited Purpose (limited reimbursement to preventative, vision, dental etc)
 - FSA is a Post Deductible Plan (reimbursement happens only after HDHP is met)

HRA's and FSA's

- Health Reimbursement Accounts (HRA)
 - Can be done in conjunction with FSA
 - Employer Defined Contribution Plan
 - Combat rising health care costs with "Consumer Driven Health Care" options

Questions?