

# Eleven for 2011: A Short List for Flex Plans

By Rich Glass, JD



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Now that you are used to writing “2011” instead of “2010,” it’s a good idea to sketch out a general “to do” list for this year.

The general rule with lists is to stop at 10 because it is a nice, round number. However, the following list has one more: 11 things for 2011 that flexible benefit professionals should keep on their radar.

**1) Keep an eye on over-the-counter (OTC) drug expenses.** IRS Notices 2010-59 and 2011-5 put several new wrinkles into the general prohibition against reim-

bursing non-prescribed OTC medicine and drugs. (See ¶322 of the *Handbook* for more on OTC medications.) The Affordable Care Act (ACA) ushered in this change. Plan administrators will want to ensure that all participants — employees, covered spouses and children — understand the new rules.

Two situations will warrant special attention.

First, you will need to examine carefully the prescriptions that substantiate an OTC drug to make sure they comply with the requirements the IRS set forth. At a minimum, the prescription should be from a standard prescription pad, signed and dated by the physician, and clearly indicate the drug, quantity and duration needed for the patient. Depending on the state’s definition of “prescription,” other requirements may need to be met.

Second, you will need to examine whether debit card purchases of OTC drugs follow the procedures outlined in Notice 2011-5 (see story on p. 4). For example, an OTC purchase may be auto-substantiated at the point of sale if the pharmacist assigns a prescription number to an OTC drug, records the details of the transaction and agrees to make the records available to the plan upon request.

Bottom line is that both IRS notices should be within arm’s reach (or fingertips’ reach). They are available on the IRS website at <http://www.irs.gov/pub/irs-drop/n-10-59.pdf> and <http://www.irs.gov/pub/irs-drop/n-11-05.pdf>.

**2) Get up to speed on W-2 reporting of health coverage.** The ACA requires that health coverage be reported on Form W-2. Notice 2010-69 delayed this mandate from the 2011 tax year to the 2012 tax year. The IRS plans to issue guidance this year on how to meet this requirement. Plan administrators will need to understand how to calculate the cost of coverage for various insured and self-funded health plans (except health flexible spending accounts (FSAs)) and test how this reporting ties into employers’ payroll systems. Even though employers generally are not required to send the 2012 Form W-2 until the end of January 2013, employees who terminate in 2012 will have the right to request an early copy of their W-2s.

**3) Start preparations for the \$2,500 FSA contribution limit.** Yet another ACA concern is the employee contribution limit on health FSAs that starts Jan. 1, 2013. That date will be here before you know it, and 2011 is a good time to start participant awareness of that

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provision. As of this writing, the IRS has yet to issue guidance on the \$2,500 limit. One aspect that remains unclear relates to FSAs that have non-calendar plan years: Does the effective date apply to plan years that start on or after Jan. 1, 2013, or any plan years that contain at least a portion of 2013?

**4) Keep SIMPLE cafeteria plans in mind.** Jan. 1, 2011, came and went without too much fanfare related to this new type of cafeteria plan, created by the ACA. The eligibility requirements for employers (typically, 100 or fewer employees) and for participants (all employees with at least 1,000 hours of service in the prior plan year) restrict the availability of these plans. The complicated minimum contribution requirements may have caused some employers to steer clear from SIMPLE cafeteria plans for the time being, but the ultimate reward may be worth the effort in some cases: The nondiscrimination testing requirements (see Tab 700) for the cafeteria plan and all benefits offered through it are eliminated.

**5) Don't forget the cafeteria plan regulations.** Issued in August 2007 as proposed regulations, these rules replaced varying pieces of regulatory and other IRS guidance that dated back to the early 1980s. Word was that we were supposed to see the final version in early 2010, but health care reform pushed back their release.

The joint Treasury Department/IRS Priority Guidance Plan for 2010-2011 calls for these regulations to be issued in final form. Once that occurs, anticipate a flurry of activity as cafeteria plans scrutinize what has changed since the original guidance was issued four years ago, particularly in the area of nondiscrimination testing for cafeteria plans (Treas. Reg. §1.125-7). A copy of the plan is available at [http://www.irs.gov/pub/irs-utl/2010-2011\\_pgp.pdf](http://www.irs.gov/pub/irs-utl/2010-2011_pgp.pdf).

**6) Expect guidance on COBRA premiums.** The Priority Guidance Plan also included another project that is a carryover from years past: Guidance under Code Section 4980B on how to calculate the applicable premium for COBRA continuation coverage. This is particularly an issue with self-insured plans like health reimbursement arrangements (HRAs), for which the true cost of coverage (which is the basis of the COBRA premium) is not simply what the employer commits to contributing each year. The current tax Code provision provides

two methods for arriving at this cost: a past cost method and a reasonable actuarial calculation. Plan administrators have struggled for a long time on how to apply these approaches practically.

**7) Monitor the health care reform traffic.** Congress went through an extreme makeover of sorts when it reconvened in January 2011. We will see plenty of House action on various parts of the ACA, including the expanded Form 1099 filing requirement that is due to become effective in 2012. Bills that pass the Senate, where Democrats hold a slight majority over Republicans, will probably be signed by the president. Thus, the key viability test for legislation will occur in the Senate. In the House of Representatives, expect Speaker of the House John Boehner (R-Ohio) to further challenge health care reform on two other fronts. First, funding of some ACA programs will likely become a subject of hot debate. Second, committee chairs will probably hold many hearings on the economic impact of some ACA provisions.

Benefits and insurance professionals also will want to watch lawsuits filed against the ACA, particularly in Florida and Virginia. Preliminary decisions favoring repeal of the ACA on constitutional grounds will work their way through the appellate system to the U.S. Supreme Court.

**8) Reach out to your elected representatives.** If you have not done so already, this should be the year that you get acquainted with your three elected representatives in Congress — your two senators and your member of the House. It is very easy to communicate with them electronically. Sending regular mail is a much slower process due to security concerns. These people need to hear from professionals who are on the front line of health care, who have the pulse of participants and employers.

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# Plan Administration

## IRS Issues Guidance on FSA/HRA Debit Cards

Employees whose plans issue debit cards for use in paying for prescribed over-the-counter (OTC) medications will continue to be able to use them, thanks to guidance the IRS issued Dec. 23. Notice 2011-5 allows continued use of health flexible spending account (FSA) and health reimbursement arrangement (HRA) debit cards for purchasing prescribed OTC medicines and drugs (see box). (See ¶292, ¶311 and ¶328 of the *Handbook* for more on FSAs and HRAs; see ¶328 for more on electronic cards.)

Under Notice 2010-59, which the IRS issued in September 2010, the cost of OTC medications and drugs

can no longer be reimbursed without a physician's prescription, effective Jan. 1, 2011. (See November 2010 newsletter for more on Notice 2010-59.) Notice 2011-5 modifies previous guidance to make it possible for those with electronic cards to use them to cover purchases of OTC medications.

Under Notice 2011-5, the use of debit cards must comply with procedures reflecting those that pharmacies or drugstores follow when selling prescribed medicines or drugs. These procedures include requirements that a prescription for the medication must be shown to the

**See *Debit Cards*, p. 5**

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If possible, try to schedule a visit to Washington. It is very straightforward to schedule a meeting.

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It is clear that 2011 will be a critical year of decision and execution for employers offering flexible benefits.

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#### **9) Make sure no HSA rollovers occur after 2011.**

The Tax Relief and Health Care Act of 2006 put in place the ability to roll over health FSA/HRA balances to an HSA. The amount of the rollover was limited to the lesser of the current balance or the balance on Sept. 21, 2006, and was subject to a 12-month clawback provision. If you are considering this option, you must do it this year because these rollovers will no longer be allowed after Dec. 31, 2011.

#### **10) Consider alternatives to the usual benefit mix.**

Right now, about the only thing staying the same is this: Employer-provided benefits are in a constant state of change. Employers that still want to offer meaningful benefits must keep up. Study what is working. Consider offering more choice and flexibility. Considerable financial pressure is being put on the insurance industry. Medical loss ratio rules are only the beginning.

The result is that simply relying on pre-tax medical insurance as the primary health care option may not work in the brave new world. Is this the year to introduce HSAs or couple an HRA with your health FSA? Or would a seed contribution to the health FSA work?

**11) Start planning for 2014.** Circle Jan. 1, 2014, on your mental calendar. It is the date on which many of the health care reform changes take effect, as follows:

- *State health exchanges come into existence.* These exchanges are primarily for individuals; employers with 100 or fewer employees may participate. For the first two years, states can restrict employer participation to those with 50 or fewer employees.
- *Auto-enrollment kicks in.* Employers with 200 or more full-time employees have to enroll all new hires automatically after providing sufficient notice and an opportunity to opt out.
- *Individual mandate will go into effect.* Most Americans must carry minimum essential coverage or pay the penalty.
- *Employer mandate will go into effect.* Employers must offer minimum essential coverage or pay the penalty.
- *Free choice vouchers must be available.* Employers offering minimum essential coverage must also provide these vouchers to qualified employees to buy coverage through the exchange.
- *Additional health insurance reforms become effective.* These include no pre-existing condition exclusions, guaranteed availability and renewability, waiting periods of no more than 90 days and limits on out-of-pocket expenses.

With these factors in mind, it is clear that 2011 will be a critical year of decision and execution for employers offering flexible benefits. 🏠