Stay Alert to New Guidance in 2012

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Federal government activity is already affecting employers that offer flexible benefits. The IRS hit the ground running: just a few days into 2012, it issued Notice 2012-09, which replaced Notice 2011-28 and addresses reporting health coverage on Form W-2. Following are more things we can expect from the federal government this year.

• Affordable Care Act (ACA), Part I: Health FSA Cap. Under §9005 of the ACA, health FSAs will be subject to a $2,500 limit on contributions related to salary reductions, starting with the 2013 taxable year.

The big question is how this affects FSA plan years that do not start on Jan. 1. In addition, it would be good to receive confirmation that employer contributions are not subject to the limit, even if the figure is based on the amount of employee contributions (for example, matching contributions). The limit increases each year by a cost-of-living adjustment, rounded to the nearest $50, but we don’t know the timing of the annual announcement. Expect guidance on this issue before July 1, 2012, when many non-calendar year plans renew.

• ACA, Part 2: Nondiscrimination Testing for Fully Insured Plans. In late 2010, the IRS issued Notice 2011-1, which delayed indefinitely the effective date of Section 2716 of the Public Health Service Act (PHSA). This provision imposes the same nondiscrimination testing requirements applicable to self-insured plans on fully insured plans. Code Section 105(h) nondiscrimination testing applies to self-insured plans, including health savings accounts (HSAs) and health reimbursement arrangements (HRAs).

Guidance on this provision should appear sometime in 2012, and may shed additional light on how this testing applies to self-insured plans. Most likely, the effective date will be some time after this guidance arrives on our doorstep.

• ACA, Part 3: Summary of Benefits and Coverage (SBC). In a late 2011 FAQ update, the IRS, the Centers for Medicare and Medicaid Services (CMS) and the Employee Benefits Security Administration delayed indefinitely the effective date of Section 2715 of the PHSA. This provision requires health plans to provide an SBC to participants annually and at other times. The government has provided a template. It is unclear how — or if — this requirement applies to HRAs.

• ACA, Part 4: Free Rider Penalty. Under ACA Section 1513, applicable large employers must pay a penalty if they do not offer minimum essential health coverage. The penalty equals $2,000 per year, per participant and starts in 2014. Applicable large employers have at least 50 full-time employees. How flexible benefits will play into the calculation is unclear. Recently, the Obama administration announced that states will take the lead in determining what constitutes minimum essential health coverage.

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health benefits, which will make it hard on multi-
state employers.

• ACA, Part 5: Minimum Essential Coverage Reporting. The IRS also has indicated that it will be providing information on how employers report their coverage on an annual basis, as required by §1514 of the ACA.

• Cafeteria Plan Regulations. The IRS issued the proposed regulations in August 2007. We could see the final version before the end of the year.

• HIPAA Privacy and Security Regulations. Already in 2012, we have seen one set of HIPAA regulations issued on transaction standards for health care electronic funds transfers and remittance advice. The Office for Civil Rights (OCR) very well could issue final rules on the revisions to accounting of disclosures as a result of the HITECH Act (the proposed rules were issued in May 2011) and breaches of unsecured protected health information (PHI) (the Department of Health and Human Services withdrew an interim final rule on this in August 2010). In addition, we may see final guidance on HIPAA enforcement, updating proposed regulations issued in July 2010. In short, 2012 could be a very busy year on the HIPAA front, with foreseeable changes to the three major HIPAA documents:

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the business associate agreement, the notice of privacy practices and the accounting of disclosures.

• Regulations on HSA Contributions Made Through a Cafeteria Plan. In its Priority Guidance Plan for this year, the Treasury Department said it planned to undertake a project to clarify the interaction of Code Section 4980G and Code Section 125 regarding comparable employer contributions to employees’ HSAs. Recall that employer contributions made through a Section 125 cafeteria plan do not have to comply with the comparable contribution restrictions. These contributions are subject to Treas. Reg. §1.125-7 nondiscrimination testing, though, just like any other qualified benefit.

• Use-or-Lose Rule. This long-established rule is a result of regulatory guidance, not law. The rule originally was implemented decades ago as an extension of the prohibition on deferred compensation, which is law. As a result, the IRS has the authority to change this rule or remove it altogether. Several years ago, the IRS amended the use-or-lose rule when it allowed a grace period of up to two and one-half months after the end of the plan year. The IRS reportedly is considering further change to this rule; details may emerge in 2012.

This is not necessarily an exhaustive list of what may affect flexible benefits this year. Still, it does serve as a useful reminder: stay alert to benefit changes in 2012.

Why Offer an FSA?

Flexible spending accounts (FSAs) are a common feature of employee benefit plans. But why would an employer offer an FSA plan to its employees? Here are some key reasons why an employer may decide it wants to add an FSA plan to its benefits program.

• Health FSAs are not always subject to COBRA. Generally, an overspent health FSA is not subject to COBRA. Health FSA COBRA coverage only lasts through the end of the current plan year in most cases.

• Health FSAs can cover adult children. Because of the Patient Protection and Affordable Care Act, participants can cover their adult children on a health FSA until the year in which the children turn age 27.

• You can save on orthodontia. Typically, an orthodontist provides a discount if payment is up front, instead of month to month. Health FSAs may now reimburse orthodontia expenses when paid, instead of when they are incurred.

• Dependent care expenses are a no-brainer. Dependent care expenses are usually a fixed cost that easily exceeds the $5,000 FSA limit in a year, even for just one child. Tax-free reimbursement makes a lot of sense.

• Debit cards make it even easier. Debit card auto-substantiation rates are usually more than 90 percent, virtually eliminating the hassle of keeping receipts and waiting for reimbursement.

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