

## *IRS Issues New Guidance on PPACA Changes to OTC Medical Expenses*

On September 3, 2010, the Internal Revenue Service (IRS) issued Notice 2010-59, a guidance reflecting statutory changes related to the use of health reimbursement arrangements (HRA) and health flexible spending arrangements (FSA) for payment of over-the-counter drugs and medications.

Related to accident and health plans that are provided by employers, including FSAs and HRAs, The Patient Protection and Affordable Care Act (PPACA) revised the definition of medical expenses. The definition of qualified medical expenses for Archer Medical Savings Accounts (MSA) and Health Savings Accounts (HSA) were also revised by PPACA. This will involve several changes for over-the-counter drug reimbursement, cafeteria plans, HRA and FSA debit card usage, etc..

Incurred expenses for non-prescription over-the-counter medications and drugs bought on or before December 31, 2010 can be reimbursed without taxes in accordance with the employee plan. However, as of January 1, 2011, an employer-provided health plan, such as an FSA or HRA, can only pay or reimburse the cost of drugs and medications under the following circumstances:

- The medication is insulin
- A prescription is required for the medication
- The individual acquires a prescription for a medication available without a prescription (over-the-counter medication.)

Note that a prescription is defined as a hand written or electronic medication order for a particular individual to have a particular medication or drug. It must abide state legal requirements and be composed by a healthcare professional that is legally authorized to issue prescriptions for the state it was written in.

HRAs and FSAs that use a debit card will also have new special rules. The IRS notice purports that current debit card systems are not capable of recognizing and maintaining that over-the-counter medications were in fact prescribed by a healthcare professional - as in compliance with the new definition of payable/reimbursable over-the-counter medication medical expenses. As a result, health HRA and FSA debit cards should not be used to buy over-the-counter drugs or medications after December 31, 2010. In an effort to smooth and facilitate the transition, the IRS will not be challenging FSA and HRA debit card usage for incurred expenses through the 15th of January in 2011. Thereafter, plans are required to ensure cards have been reprogrammed so that they can not be used in the purchase of over-the-counter drugs or medications.

Those with a health FSA should be careful, as some FSAs contain a grace period provision to allow use of unused funds not spent by December 31 of a given year to reimburse incurred expenses for the initial 2 ½ months of the subsequent year. Even if an individual's existing FSA includes this grace period provision,

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## Looking at the Near-Term Financial Impact of Health Care Reform

Employers are bracing for the financial impact of the new health care reform law, according to a survey from Mercer. A quarter of the nearly 800 employers surveyed said they expect compliance with the first round of mandates included in the law to add at least another 3% to their projected 2011 plan costs; 28% expect an additional increase of 1-2%, and 13% project an additional increase of less than 1%.

Three of the “immediately” effective health care reform provisions-effective for plan years beginning after September 23, 2010 (January 1, 2011, for calendar year plans)-are discussed below. Given that these and other health care reform provisions include requirements for coverage expansion, for certain types of benefits and for restrictions on benefits limitations, concerns about cost increases are well-founded.

Three health care reform provisions that are likely to have some immediate financial impact on employers are:

- Expansion of coverage to employees’ young adult children. The health care reform law requires that plans that provide coverage for dependent children now make that coverage available until a child turns age 26. (Until 2014, grandfathered plans can limit this coverage expansion to adult children not eligible for other employer-provided coverage.) In the Mercer survey, 20% of employers said this provision of health care reform was a significant or very significant concern to them. The impact of this coverage expansion will vary, of course, depending in large part on an employer’s demographics-and for some employers, adding a group of young, healthy individuals could possibly help their plan cost. To moderate the impact of this piece of health care reform, employers should take steps to ensure that only truly eligible dependents are on the plan,

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by conducting dependent audits. As indicated by the Mercer survey, other steps employers said they are considering to blunt the impact of this mandate include requiring proof that dependents do not have coverage available through their own employers (49%); adding contribution tiers based on the number of dependents covered (20%); and imposing higher premium shares for all dependents (16%).

- Elimination of lifetime limits on benefits. The law prohibits lifetime dollar limits on “essential” health benefits-and this list is long, encompassing most of the types of benefits found in the typical health care plan (e.g., ambulatory patient services, emergency services, hospitalization, maternity/newborn care, mental health and substance abuse benefits, prescription drugs, etc.). (This provision phases in to apply to annual limits, which are banned after 2013.) In the Mercer survey, 21% of employers said this provision was a significant or very significant concern.
- Preventive care benefits. Plans must cover certain preventive care services without any cost-sharing (deductibles, copayments) required for the employee or dependent receiving the service. Many plans-in particular consumer-directed health plans-already provide full coverage for certain types of preventive care, as a strategy to enable the detection and treatment of illness or disease in the early stages, and as a means to alert employees to lifestyle issues that may be harming their health. Whether this provision “costs” all employers is yet to be seen; some research shows that preventive services, especially when part of a comprehensive health promotion and wellness strategy, generate a return on the investment that an employer makes in the program.

Noncompliance with these or other provisions in the health care reform law also has a cost for employers, in the form of excise taxes and penalties. Therefore, it’s essential to review the pending mandates, not only to ensure compliance, but also to determine how to fold them into an effective and comprehensive health care cost management strategy.

## Preparing for a Workers' Compensation Audit

Just the mention of a workers' compensation audit engenders fear into the heart of man. If you are scheduled for a workers' compensation audit, there is no need to dread it or be fearful. A small amount of preparation and common sense can save you a lot of aggravation and money.

Devoting a few hours of your attention now can save you a lot of time in the future. You need to give your full attention to the auditor and remain with him/her throughout the entire process. The process may take a couple of hours to complete. So, make sure that the time and date of the scheduled audit is convenient for you. Call to reschedule the audit if it has been scheduled at an inopportune time.

Begin to collect and organize payroll records, overtime payroll records, classification divisions, and insurance certificates as soon as you learn of the audit. This should give you plenty of time to compose a summary of each, which will help you to better communicate important data during the audit process. Information that is well organized will also expedite the process. If you can reconcile your calculations to payroll records, such as W2's and payroll stubs, the auditor might be more comfortable trusting your data.

You will also want to make any needed adjustment to payrolls; for example, subtracting bonus pay from overtime pay. If applicable, you will need to apply the maximum and minimum payrolls to the calculations. This part may take a little research, since the minimum and maximum will vary based on state; career; and even among sole proprietors, partners, and executive officers.

Before the audit, you should apprise yourself on the different employee job classifications and make sure that each employee is correctly classified. This is a key element to ensure that the audit flows smoothly. If there is any question about how to classify an employee, call your broker or agent. The auditor is most likely going to be asking you about the classification and job duties for multiple different employees. So, be prepared and armed with knowledge.

One last important preparation is concerning subcontractors. Payments issued to subcontractors can go against your workers' compensation in the event that the subcontractor did not have a certificate of workers' compensation. You can get a copy of the certificate, but make sure that it is current and shows coverage during the time the subcontractor worked for you.

Once the audit arrives, you will be glad that you took a little time collecting, organizing, and summarizing your information. You will also find that the auditor is not a nemeses, especially when you provide honest answers and organized paperwork.

At the conclusion of the audit, ask the auditor for the audit worksheet. Ask your broker or agent to review the accuracy of the final audit. You have a legal right to ask for a corrected audit anytime you think there were any errors. If any overpayment was made under the last three preceding audits, you also have a legal right to recover it.

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over-the-counter medications bought without a prescription (after the deadline) will not be eligible for reimbursement under the new rules outlined in the IRS notice.

Finally, cafeteria plans may also need revising to adhere to the new over-the-counter medication requirements. Despite the tenet against retroactive

amendments, this notice allows an amendment to conform cafeteria plans to requirements adopted by June 30, 2011. For incurred expenses after January 1, 2011 or HRA and FSA debit purchases after January 15, 2011, the amendment may be retroactively effective.

## *Voluntary Benefits Are More Than an Accessory to an Employer's Core Benefits*

Today, more employers than ever before are offering at least one type of voluntary employee benefit. The growing interest in voluntary benefits reflects tight human resources budgets, the changing face of employer-sponsored health insurance, and the varied and multi-faceted needs of a workforce that is ever-growing in diversity.

A study from Eastbridge Associates found that, overall, 66% of employers offered at least one voluntary benefit in 2009, compared with 54% that did so in 2006. The growth in voluntary benefits offerings has been especially noticeable among the smallest employers (10 - 100 employees), with 65% offering at least one type of voluntary benefit in 2009, compared with only half that did so in 2006.

A separate survey from the International Foundation of Employee Benefit Plans characterizes voluntary benefits as a "fundamental" part of employers' benefits packages, a "significant part of plan sponsors' strategic benefits approach." In that study, 84% of the surveyed employer group offered voluntary benefits.

What's making voluntary benefits more popular... and more important? Here are some of the reasons-

- Tight benefit budgets have constricted the growth of employer-paid-for benefits. Voluntary benefits enable workers to have access to coverages that are popular with employees-such as vision and dental-when the employer can't afford to include these in the basic benefits package, either on a contributory or noncontributory basis.
- The shift from employer paternalism to employee responsibility that began with the introduction of 401(k) plans has continued in full force, with employees now firmly in control of providing for their families' financial security. Thus, popular voluntary benefits include supplemental life insurance, disability insurance and long-term care insurance-coverages that come into play when potentially cash-draining life events occur.
- In workplaces where consumer-directed health plans are offered, employees who are enrolled in these plans may turn to voluntary supplemental medical coverages to fill in the gaps left by these

plans. Vendors have developed products that do just this, helping employees who buy the coverage to offset the higher deductibles or coinsurances of the underlying plan.

- Other types of supplemental medical plans have long been offered on a voluntary basis and they continue to play a role. These include plans that cover the indirect costs of an injury or illness, such as critical illness insurance that pays a cash benefit upon the diagnosis of a life-threatening disease or condition, and which can be used by the insured, or the insured's survivors, for any purpose they see fit; disease-specific insurance, such as cancer insurance, that may provide coverage beyond the primary medical plan for treatments associated with the disease; and hospital indemnity insurance, which supplements the primary plan in the event of an illness that requires a hospital stay.
- A primary driver of the voluntary benefits market has been the growing demographic diversity of the workplace, and the recognition that today's workers have a wide range of needs. Voluntary coverages that address this include long-term care insurance, financial planning, pet insurance, a sampling of life insurance products, and childcare and eldercare assistance.
- Another marker of today's workforce is how time-pressed employees are, and certain types of voluntary products directly address this reality. For example, by bringing products that most individuals need-such as auto insurance and homeowners/renters insurance-into the workplace, employees save the time of researching these necessary coverages on their own, and also enjoy the convenience of paying for the insurance through payroll deduction and the cost savings of a group rating.

Though the voluntary insurance marketplace has been around for some time, it is growing in importance for the reasons noted above. Today, voluntary benefits are more than an accessory to an employer's core benefits; they are a seamless, strategic and essential component of a total compensation package.