



HSA / FLEX INTEGRATION

Basic Rules

Health Savings Trust Account (HSA) salary reduction contributions can be integrated into your existing Flexible Benefit Plan, however, there are several points to consider:

- The employee/participant must first own a High Deductible Health Plan (HDHP) that qualifies as an HSA compatible insurance plan. Your group insurance plan may offer only the qualifying HDHP or it might offer a dual option plan that gives the employee the choice between a traditional PPO or HMO Plan and an HDHP option.
- The employer determines which health plan coverage a participant must own to allow salary reduction contributions into the HSA Trust Account. This could include only the company's HDHP insurance or any employee-owned qualifying HDHP coverage.
- The Employer also determines whether the HSA Trust contributions will be made into a single bank or qualifying institution (selected by the employer) or if the employee can select a bank of his or her choice. NOTE: Administration costs are reduced if an employer chooses one bank to receive all deposits for the HSA Trust Accounts.

HSA Trust Contribution Limits

In addition to your group health, dental, vision and supplemental health insurance premiums and child/dependent care and/or health care spending account options, the employer can add the HSA Trust Account contributions as a tax-free salary reduction option.

The allowable salary reduction amount to be deposited into the HSA Trust, is limited to the federal limit each tax year. NOTE: the combination of the employer and employee HSA Trust Contribution cannot exceed these limits and is prorated per month based on the first day of the month following purchase of the HDHP insurance coverage.

For 2011 Federal Limits (indexed each year):	Individual	\$3,050
	Family	\$6,150

For 2012 Federal Limits (indexed each year):	Individual	\$3,100
	Family	\$6,250

PRORATION EXCEPTION: There is an exception to this rule. If an individual funds the HSA Trust to the maximum limit for the calendar year, but does not own the HDHP insurance for the full calendar year, the individual must continue to own the HDHP insurance plan for the entire next calendar year. Otherwise, the maximum contribution is prorated, based on the number of months during which the individual actually owned the HDHP insurance plan for the short year. The catch-up contribution amounts (for individuals who are 55 or older) are always prorated based on the number of months of owning the HDHP insurance during the calendar year (no exceptions).

Proration Example: The employee owns an individual HDHP that has a \$3,000 deductible. The maximum contribution for 2011 is \$3,050 (federal limit). However, the employee did not own the HDHP on January 1st but rather purchased the HDHP on June 20th. Therefore, the maximum allowable contribution to the HSA Trust is limited to the prorated values from July 1st through December 31st, or \$1,525. Otherwise, if they fund the full calendar year maximum of \$3,050 then the individual must continue to own a HDHP Plan for the entire next calendar year

(2011) in order to not be penalized for over-contributing to the HSA Trust. We recommend HSA Trust contributions be based on the number of calendar months, during which a HDHP is owned (based on the first day of any given month).

Catch Up Contributions

A “catch-up” contribution applies when an individual turns 55 years of age during a given tax year or is currently age 55 or older. This individual can contribute an additional \$1,000 prorated from the first day of the month following the purchase of the qualifying HDHP. Catch-up contributions must always be pro-rated.

Permitted Insurances

If an individual owns a qualifying HDHP, s/he can also own other insurance products as defined by the IRS, including:

- Dental
- Vision
- Long Term Care
- Auto and Home Owners Insurance
- Accident Coverage
- Specific Disease (Example: Cancer policy)
- Critical Illness (heart attack, stroke etc.), and
- Hospital Income (per diem only plans)

If a spouse and/or children are covered under a traditional indemnity, PPO or HMO Plan the employee may still purchase individual HDHP coverage and participate in the HSA Plan, if s/he is not covered under any conflicting insurance policy.

Conflicting coverage may include:

- Traditional general-use Flex Health Care Spending Account;
- Traditional general-use Health Reimbursement Arrangement (HRA); and
- Any other “non-permitted” insurance that could pay something toward the deductible under the HDHP. Under IRS guidelines, anyone owning any of these plans will be disqualified from depositing dollars into an HSA Trust.

Election Periods

When an employee enrolls in the HDHP, the election is irrevocable for a 12-month time period, unless an eligible status change occurs. For the HSA Trust, the employee may make an election change monthly - there is no required “status change” for this part of a Flexible Benefit Plan.

Note: Once elected, before-tax insurance premium deductions will continue from plan year to plan year until the employee signs a waiver form to discontinue this election. The waiver can only be signed during an open enrollment period or as the result of an eligible status change.

Group HDHP premiums are currently tax-free when paid by the employer and/or when paid by the employee through a Flexible Benefit Plan. If the employee purchases an individual HDHP policy, the premiums are paid on an after-tax basis.

Flexible Spending Accounts (FSA’s)

Dependent Care Spending Account

This reimbursement account is unaffected by the addition of an HSA Plan to the Flexible Benefit Plan options.

Health Care Spending Account

This reimbursement account must be amended and restated from a general-use Flex Health Care Spending Account (which reimburses of all Code 213(d) expenses) to become a limited-use Flex Health Care Spending Account (which reimburses only dental and vision expenses). The limited-use Flex Health Care Spending Account can also be expanded in definition to include preventive care expenses and expenses exceeding the deductible, although these two options are not recommended. The limited-use Health Care Spending Account is compatible with the new HDHP coverage with the HSA Trust Account option.

If the employer offers a dual choice health insurance plan, then a dual choice Flex Health Care Spending Account can also be offered. Employees electing a traditional group health plan (indemnity, PPO or HMO option) would continue to have the general-use Flex Health Care Spending Account, whereas, employees electing the HDHP with the HSA Trust Account would have the limited-use Flex Health Care Spending Account. The plan document must be amended to reflect this change and all changes must be proactive, not retroactive in nature.

Individually-Owned Premiums

The employer may offer a reimbursement account for individually owned health insurance policies. Premium dollars are deducted from the employee's gross pay and reimbursed to the employee for eligible policy premiums. This account is not recommended as it may violate HIPAA and ERISA rules, though it is permissible under IRS rules for Flex Plans.

However, an employer may fund, without conflict, part of the HSA Trust and allow salary reduction contributions to the HSA Trust account attached to an individually-owned HDHP. This may be a consideration when group health insurance is not offered by the company; yet the employer would like to make tax-free contributions to help defray the cost of health care.

Processing HSA Trust Election Forms

Initial Election

At the end of your Open Enrollment period, you should have an HSA Trust Account Contribution Election Form from each employee authorizing the salary reduction election for HSA contributions (in addition to your POP or Full Flex Election Form).

Election Form:

The following is an explanation of the Election Form and how it must be completed.

Employee Identification

Make sure you have all the information required for employee identification.

Boxed Election

Monthly HSA Trust Contribution

The employee specifies the value of the pre-tax dollars to be deducted from his/her gross monthly. The administrator of the plan (HR or Payroll) should then re-calculate this value, deducting the HSA Trust contributions equally from each pay date.

Be sure that the tax year values (employer and employee contributions) do not exceed the tax-year limits and that the values are properly prorated for the individual based on the 1st day of the month of owning a qualifying HDHP.

Catch-Up Election – These values must also be prorated based on the first day of the month of owning a qualifying HDHP (indexed annually).

Purpose Section

Make sure the effective date is entered and that it is the first day of a month. New hires will have varying start dates based on when the employee becomes benefit-eligible. Remember, all values are prorated for new hires and for election changes during the Plan Year.

Signatures

You must have the employee's signature on the election form dated prior to the employee's effective date.

The plan coordinator should sign on the employer signature line and date the election form prior to start of Plan Year or employee's effective date. This is a contract/agreement between the employee and the employer.

Internal Use Only Section

This section can be filled out for payroll coordination. Check initial elections and write in the effective date & first payroll date. If an employee is a new hire, has an election change or has been terminated, the necessary information can be recorded here and given to payroll department for input.

There is no required status change to make an election change in this part of the plan. This section is primarily provided for your convenience and to help with providing information to the payroll department.

Copy and Distribute the Election Form Pages as Follows:

- Original - Employee's Personnel File
- Copy - to payroll / accounting
- Copy - to employee along with Verification Memo

The **Verification Memo** gives employees a few days to make any final enrollment corrections before the election information is given to payroll. This memo also confirms that Open Enrollment is closed and reminds the employee that no other initial election changes are allowed following the verification deadline date. During the Plan Year, HSA election changes are allowed monthly.

Payroll Procedures

It is very important for the payroll person and the plan coordinator to work closely together. Open Enrollment must be completed prior to the start of a Plan Year and payroll must have enough time to make the necessary adjustments based on the employee before-tax and after-tax elections. Remember, all Flex elections are irrevocable for the entire Plan Year unless an eligible status change occurs and a new election is approved.

NOTE: The HSA Trust Contributions the rules are different. The salary reduction HSA Trust Contributions can be changed monthly. There is no requirement of a "status change" event.

All changes during the Plan Year are computed on a prorated basis. **Changes during a Plan**

Year must be elected prior to the effective date of the change.

Under a Flexible Benefit Plan the following taxes are exempted on all dollars redirected from wages to tax-free benefits:

1. Social Security contribution
2. Medicare contribution
3. Federal Withholding Taxes
4. Federal Unemployment Taxes
5. State Withholding Taxes (all states except New Jersey)
6. State Unemployment Taxes (applies to Colorado - must be verified in other states)

Colorado: For government employers under the Public Employees Retirement Association (PERA), contributions are exempted on both the employer and employee contributions. The Colorado Police and Fireman's retirement fund contributions are **not** exempted.

Worker's Compensation Insurance is **not** exempted in Colorado under the State Worker's Compensation Insurance Plan. Individual carriers may vary on requirements. Review this question with your Worker's Compensation Insurance broker for the requirements of your carrier.

Other States: The employer should verify if State Unemployment and Worker's Compensation contributions are exempted on Flexible Benefit Plan dollars in your particular state.

W-2 Reporting Procedures

Both employer and employee HSA Trust contributions, made through salary reduction, must be reported on the W-2 Form. It is recommended that the employer contribution also be tracked through the payroll to ensure ease and accuracy of reporting these dollars on the W-2 Form. The employer contribution can be designated as part of a benefit allowance that is provided to the employee, added to the gross wage and then deducted along with any additional employee designated dollars into the HSA Trust. This is the preferred way to handle the Employer HSA Contribution and the recommended way to prevent ERISA concerns. **NOTE: All HSA dollars – employee salary reduction contributions and employer contributions are considered to be “employer-paid HSA dollars” when reported on the W-2 Form.**

Banking

Flexible Spending Account (FSA) dollars from Child/Dependent Care, Health Care and Premium Reimbursement Accounts can be held in your general fund account. No special bank account is required. However, the HSA Trust Account must be established individually by each participant and is established under his/her individual Social Security Number. Until the trust account is established, medical expenses incurred will not be eligible for reimbursement from the Trust. Therefore, it is important for employees to establish their new accounts as soon as possible after purchasing the qualifying HDHP insurance plan.

The employer can determine which bank will be used for the company contributions and for the employee salary reduction contributions. The employee is then free to move the dollars to another HSA Trust at another Bank without conflict. Once the dollars are deposited into the Trust they belong to the individual account holder.

Terminations

Upon termination the employee must be provided with appropriate COBRA or Senate Bill 51 (Colorado) information and may be eligible for continuation in the HDHP (if company sponsored). However, there is no continuation of the HSA Trust contributions through salary reduction as there is no salary. (See your Flexible Benefit Plan Administration Guide Book for details on Spending Account continuation).

Ownership & Corporate Changes

Flexible Benefit Plan Coordinators need to be aware that changes in their company's corporate structure **during** a Plan Year can produce some unanticipated and unwanted results. If you know of any forthcoming mergers, acquisitions, changes from C-Corporation to S-Corporation structures, or even layoffs, please notify FlexMagic Consulting, Inc. We will help you determine what effect, if any, the change will have on Flexible Benefit Plan compliance issues.

Self-Employed Owners (non-C-Corporation owners) can contribute to an HSA Trust and pay their HDHP premiums with company dollars. However, the total cost of the premium and the amount of the HSA Trust Contribution are considered "imputed income" to the owner and are then fully deductible as self-employed health insurance premiums and HSA Trust Contributions on the individual tax return. Contact your CPA to properly set-up and track owner contributions to the Plan.