Employee Benefits Report

AFFORDABLE BENEFIT SOLUTIONS
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Retain Top Talent with “Golden Handcuffs”

Even in a difficult economic environment, employers need to attract and retain top talent. One way to to do this is by offering high-level executives a non-qualified deferred bonus plan, also known as a supplemental executive retirement plan (SERP).

Unlike qualified retirement plans, nonqualified SERPs allow your company to provide benefits to your key employees on a selective basis. You decide who participates, what benefits will be provided, and how and when benefits will become vested.

Most importantly, key employees find SERPs attractive because they permit higher retirement savings. Nondiscrimination rules that apply to qualified plans, such as 401(k)s, allow them to contribute only a certain amount above and beyond what other employees choose to set aside—typically 125 percent of rank-and-file employees’ contributions, or two percentage points higher, whichever amount is larger. Even if your talented $300,000-a-year execs want to contribute 10 percent or more of salary, their contributions might be capped at five percent because other employees save an average of only three percent. A SERP allows you to work around this reverse discrimination and reward talented top executives.

SERP benefits for employers:

- ✔ Recruit, retain and reward key employees
- ✔ Selectively single out plan participants
- ✔ Determine individual benefit levels
- ✔ Continue existing retirement plans without change
- ✔ Minimize filing and reporting requirements.

SERP benefits for employees:

- ✔ Increase retirement savings with no change in current compensation
- ✔ Obtain survivor benefits during employment and/or retirement, depending on plan design
- ✔ Can receive additional or accelerated benefits upon a change in corporate control or ownership.

A SERP is considered a “top hat” plan and therefore exempt from many ERISA requirements. A plan qualifies as a top hat plan if it is created for the purpose of providing benefits to a select group of top management or highly compensated employees.

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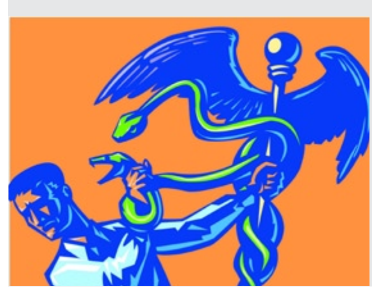
This Just In…

Congress has extended federal COBRA subsidies for an additional six months for beneficiaries whose nine-month COBRA premium subsidy has run out. Previously, employees who lost their jobs after Dec. 31, 2009 would have been ineligible for the subsidy. The new legislation extends the 15-month subsidy to those who lose their jobs through February 28, 2010. Under the program, the federal government pays 65 percent of COBRA premiums and the beneficiary pays the remaining 35 percent.

The legislation requires employers to notify current and future COBRA beneficiaries of the new 15-month premium subsidy. An estimated 7 million COBRA beneficiaries took advantage of the subsidies from March through December 2009; many of them would not have bought COBRA coverage without the subsidy.



Design Your Own Health Plan with an HRA

What healthcare plan allows employers to set their own maximum for employee healthcare costs, can be structured to cover 100 percent of preventive care for most employees, and gives employees greater incentive to manage their healthcare costs?

The answer? Health reimbursement arrangements, or HRAs. As one of the most flexible healthcare benefits, it's no surprise that many employers offer HRAs.

HRAs offer tax advantages for both employees and employers. HRAs do not involve insurance—rather, the employer agrees to reimburse eligible employees up to a certain amount each year for qualified healthcare expenses for themselves. HRAs can also cover spouses and eligible dependents, if the employer wishes.

To meet the definition of a qualified HRA, the IRS requires them to (1) be funded solely by the employer and not by salary reduction, and (2) provide benefits only for substantiated medical expenses. In other words, the HRA can only reimburse employees when they provide proof of eligible medical expenses. (3) Only employees or former employees and their spouses and dependents can participate; owners cannot (including owners of partnerships, LLCs, LLPs and S-corporations).

HRAs Offer Flexibility

Employers can tailor HRAs to their needs and those of employees. HRAs can work with other benefits, such as high-deductible health plans (HDHPs) and flexible spending accounts (FSAs). For example, by combining an HRA with a high-deductible health plan, you can provide low-cost health benefits for your employees that will cover 100 percent of preventive care expenses for most employees, such as routine physicals and child immunizations.

HRAs give employers more flexibility in funding and plan design than health savings accounts (HSAs). While HSAs are funded accounts, the employer does not need to set aside funds at the beginning of the year for an HRA. Instead, you can pay reimbursements out of cash flow as need arises. Further, you can allow employees to roll

HRA balances over from year to year, if you choose, as well as allowing retirees to participate.

As reimbursement plans, HRAs work better than many other health plans to raise employees' awareness of the real costs of healthcare, while giving them greater decision-making control over their healthcare spending.

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HRA Rules to Remember

✔ Only employer dollars can be used to fund an HRA, not including funds that are considered employer dollars as a result of an election under a Section 125 plan. Funds may roll over from year to year.

✔ The HRA may not be tied to any salary reduction or deferred compensation program, although an accompanying insurance plan may be tied to a salary reduction plan. But the salary reduction may not exceed the actual cost of the insurance plan and may not be pegged to any level of HRA contribution.

✔ The employer sets parameters for the type of healthcare expenses the fund will reimburse. Reimbursements may include items allowed under IRS Section 213(d), or simply expenses not covered by the high-deductible health plan, such as deductibles, coinsurance, co-pays and other cost sharing. HRAs can also reimburse employees for health insurance premiums, such as medical plans, long-term care insurance, dental insurance and dependent coverage. Disability policies do not qualify.

✔ HRAs must be available for COBRA continuation on the same basis as other health plans.

✔ Employers can elect whether to make HRAs available to terminating or retired employees.

✔ Unused HRA funds remain with the employer when an employee terminates. Employers may not bonus terminating employees an amount equivalent to the dollars that remain in their HRA.

✔ HRAs can coexist with flexible spending accounts (FSAs) and cafeteria plans as allowed under Section 125. The notice requires that the HRA be exhausted before the FSA pays. However, an employer may set up the HRA plan document to require FSA exhaustion first.

✔ Many of the timing rules of an FSA do not apply to an HRA, so a mid-year enrollment is allowed, as well as reimbursements that cross calendar years or plan years.

✔ The same non-discrimination rules that apply to other health benefit programs apply to HRAs. ■

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Setting up a SERP

SERPs are relatively easy and inexpensive to set up and administer. Your company and the key employee enter into an agreement that says you will pay the employee a certain amount of money, either over a period of time or in a lump sum upon death, retirement or termination of the plan. You must notify the Department of Labor in writing within 120 days of the adoption of the plan. When the SERP benefit comes due, the executive receives taxable ordinary income and your company receives a tax deduction.

You Can Finance the SERP in a Number of Ways:

- ✔ Company cash flow. While this may be the easiest method, the company must earmark future cash flow or assets to make payments over potentially long periods of time.
- ✔ Accumulation fund. Create an investment fund out of which benefits will be paid. However, the fund will be subject to market risks and gains may taxable.
- ✔ Company-owned life insurance. The company buys life insurance on the executive; the plan can draw benefit payments from either the death benefit or internal growth of cash values. This method offers a number of income tax advantages: cash values grow income tax-free; death benefits are generally paid income tax-free; and cash values may be sufficient to recover the costs of funding the plan. As a result, it can cost significantly less to finance a plan with life insurance.

One caveat to consider: While they come with less red tape than stock or qualified plans, you most likely will want a specialist to administer it (usually the same firm that set it up). That's because executive benefit plans are covered by section 409(a) of the tax code, meaning that they require an experienced adviser who can avoid potential penalties or unexpected taxation. For more information, please contact us. ■

Section 162: Fast and Easy

One popular type of SERP is a Section 162 life insurance plan. Under this agreement, the employee purchases a cash-rich insurance policy and names himself as owner. This policy may be issued on a single insured basis or a joint insured basis, such as a husband and wife together. The employee controls the policy, including naming the beneficiary and the cash value.

The company pays the premiums, which are fully tax-deductible as a business expense and considered compensation to the employee. Because the premiums are considered taxable income to the employee, often the employer will 'double bonus' the employee.

Life insurance's tax advantages include tax-free accumulation, tax-free income through loans and withdrawals and tax-free transfer at death.

If the employee is also a stockholder of the company and his/her tax bracket is less than the corporate tax bracket, the 162 is attractive to the employee-stockholder who wishes to withdraw profits from the corporation. ■

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Advantages of HRAs for Employers:

- ✔ You choose how much to set aside per employee each year, and what types of qualified expenses the HRA will cover, whether preventive care, out-of-pocket expenses, dependent costs or health insurance premiums.
- ✔ You can deduct reimbursements of qualified claims as a business expense.
- ✔ You know at the beginning of the year the maximum amount your employee healthcare benefits will cost.
- ✔ You can offer HRAs with other benefits, including flexible spending accounts.
- ✔ You will have minimal paperwork and administrative burdens, compared to the costs of self-insuring.

Advantages of HRAs for Employees:

- ✔ They can exclude reimbursements from gross income.
- ✔ They may be able to accumulate unused funds for use in future years, depending on plan structure.
- ✔ They do not have to be covered under any other health care plan to participate, unlike a health savings account (HSA), which requires a high-deductible health plan (HDHP).
- ✔ They can use funds to be reimbursed for premium payments for a healthcare plan that meets their or their families' specific needs, as opposed to a standard company plan.

Instead of designing a health plan for a few high-end users, you can design an HRA for the 80 percent of most companies' employees who are low-end healthcare users. To discuss the uses of HRAs in benefit design, please contact us. ■

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- ✔ **Allow Female Employees to Pump Breast Milk.** A 2007 Institute of Medicine report on childhood obesity noted "more widespread availability of convenient and private rooms for pumping breast milk at a worksite could potentially facilitate mothers' continued breastfeeding of their infants for the recommended 4 to 6 months."

Employers can do only so much, but by encouraging healthier habits in the workplace, you may see the results in the bottom line. ■

It's Time to Battle Obesity in the Workplace

People who are obese spent 42 percent more for medical care in 2006 than did normal-weight people, found a study by RTI and the U.S. Centers for Disease Control.

And the problem is getting worse: Two-thirds of adults are now either overweight or obese. Childhood obesity rates have nearly tripled since 1980, from 6.5 percent to 16.3 percent. The proportion of all annual medical costs due to obesity increased from 6.5 percent in 1998 to 9.1 percent in 2006, the study said.

For employers, here's the most alarming news of all: employee obesity costs U.S. employers approximately $45 billion annually, according to a 2006 estimate by the Conference Board and RTI International.

Many experts believe that America has been slow to deal with obesity because many see it as a matter of personal responsibility. But employers can help solve the problem. By encouraging employees to slim down, your employees will be healthier and the company can reduce its healthcare costs.

As part of the National Strategy to Combat Obesity, the non-profit Trust for America's Health (www.healthyamericans.org) suggests employers consider the following actions:

- ✔ **Offer Wellness and Disease Prevention Programs and Benefits.** Offer employees programs and health benefits that help them stay healthy, including nutrition, physical activity, and obesity counseling; subsidize health club memberships and provide insurance discounts for preventive services. Investing in employee health not only improves productivity but also cuts down on absenteeism.
- ✔ **Provide Opportunities for Employees to Be Active During the Day.** Maintain clean, well-lit stairwells to encourage employees to take the stairs, and focus on providing healthy food options in vending machines and in cafeterias.
- ✔ **Replace Smoke Breaks with Fitness Breaks.** Encourage employees to engage in physical activity on their lunch hours and breaks. Employers have long allowed smokers to step outside for a cigarette break. Consider offering "walking breaks" instead, whereby employees can leave their desks for 10 minutes or so to walk around the office. Walking breaks can improve mental focus in addition to physical health.
- ✔ **Advocate for Prevention Services.** Generally, physicians do not receive enough support, resources or reimbursement from insurance companies to prescribe preventive care for patients with chronic diseases. Employers can ask their insurers to offer plans that cover nutrition counseling, weight loss and weight management programs to decrease obesity and prevent the development of chronic diseases.

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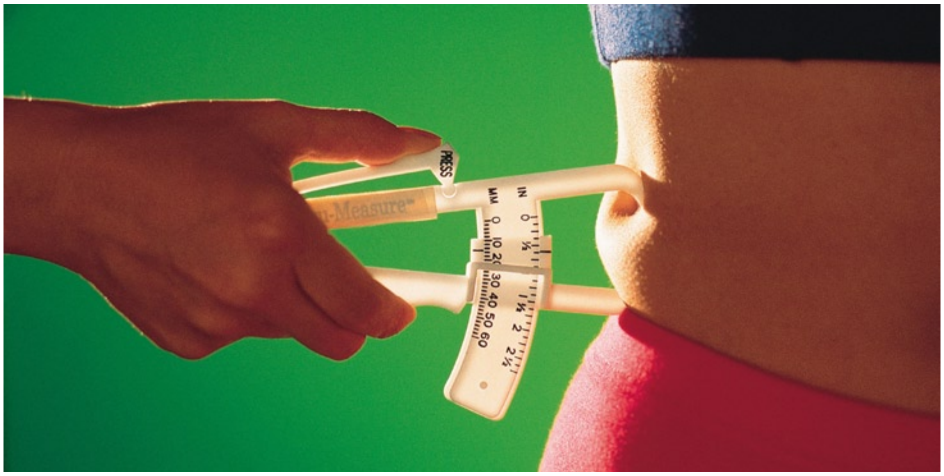

The Safeway Miracle

As a self-insured employer, the grocery store giant Safeway has a vested interest in keeping employee healthcare costs down. During the last four years, its per capita healthcare costs have remained flat while most American companies' costs have increased an average of 38 percent over the same four years.

How did Safeway do it?

Safeway capitalized on two key insights, according to an article in *The Wall Street Journal.* The first is that 70 percent of all healthcare costs are the direct result of behavior. The second is that 74 percent of all costs are confined to four chronic conditions: cardiovascular disease, cancer, diabetes and obesity.

Armed with these facts, Safeway instituted a voluntary Healthy Measures program that now covers 74 percent of the company's insured nonunion workforce. Employees are tested for measures related to the four conditions cited above and receive premium discounts off a "base level" premium for each test they pass. Data is collected by outside parties and not shared with company management. If they pass all four tests, annual premiums are reduced $780 for individuals and $1,560 for families.

Today, Safeway obesity and smoking rates are roughly 70 percent of the national average. When surveyed, 78 percent of Safeway employees rated their health plan as good, very good or excellent. In addition, 76 percent asked for more financial incentives to reward healthy behaviors. ■