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Reapplying for RDS

Providers of prescription drug coverage to retirees eligible for Medicare Part D prescription drug coverage, may apply for a tax-free subsidy payment through the Retiree Drug Subsidy (RDS) program. Many sponsors chose this option when Medicare's prescription drug program first became effective. To continue receiving the subsidy payment, sponsors must submit a *new* application for the 2007 plan year. New applications must be submitted no later than 90 days before the start of the plan year. A one-time 30-day application extension may be requested if applied for within the 90 days before the beginning of the 2007 plan year.

The application is submitted via the RDS Website at www.rds.cms.hhs.gov. The RDS Website contains a *How to Apply* section explaining the application process.

HRA Participant Expense News

When designing Health Reimbursement Arrangements (HRAs), some employers have gone to great lengths to make employees feel ownership for their HRA balances. Unlimited carryover of unused balances; allowing an unlimited amount of time after termination of employment to spend down their balances; allowing a surviving spouse and dependent children to use the remaining HRA balance; even allowing employees to designate beneficiaries for any HRA balances are four common approaches to reinforce this notion.

This final practice — allowing an employee to designate a beneficiary to use up the HRA balance — was what the IRS considered in a recent ruling. The IRS concluded that this feature would mean all amounts paid under such an HRA would be taxable income — even if paid to reimburse medical expenses. The IRS said that it reached this conclusion because an HRA cannot provide for any current or future payment of benefits for any purpose other than reimbursing the qualifying medical expenses of employees, their spouses and their dependent children.

This ruling reinforces some HRA and FSA cautions we have offered in the past such as:

- No one other than employees and COBRA qualified beneficiaries can be participants. Persons who cannot be participants include:
 - ⇒ Partners of a partnership
 - ⇒ Two percent or more owners of an S-corporation
 - ⇒ Non-employee directors
 - ⇒ Independent contractors

The HRA or health FSA cannot reimburse expenses incurred by anyone other than a participant, a participant's opposite-sex spouse, or a participant's dependent children who meet tax code requirements. Persons whose expenses cannot be reimbursed include domestic partners (unless they qualify as dependents based on tax code criteria).

Concerned employers may want to offer Health Savings Accounts (HSAs) instead of HRAs. Although HSAs are subject to a number of technical requirements and restrictions, they truly are accounts that are owned by employees and an employee can name a beneficiary to receive any remaining HSA balance at the time of the employee's death.

Implications of Breached PHI

The *San Francisco Chronicle* reports that in less than three years one prominent national financial institution has experienced at least half a dozen major data security breaches. The most recent involved the theft of a computer and data disk from the trunk of an outside auditor's car. The disk held the Social Security numbers and names of an untold number of bank employees, along with prescription drug claims. This organization did say that the auditor is no longer auditing any of the company's plans.

To protect your employees' health information, in your hands or that of a third party administrator's, show due diligence in maintaining employees' records by:

- Treating personnel information (like SSNs) as "radioactive" by reviewing all collection, use, storage and destruction of this data.
- Segregating critical data (data required under state laws) from other data.
- Restricting access to critical data and monitor access.
- Encrypting files and databases containing critical data.
- Creating or strengthen policies of handling personal information.
- Screening, training and holding accountable all employees with access to personal information.
- Reviewing data-handling practices and safeguards with third parties.
- Developing a data-breach contingency plan.

HHS Launches Transparency Website

As part of the Bush Administration's ongoing campaign for health care transparency, the U.S. Department of Health and Human Services (HHS) has launched a dedicated website. President Bush recently issued an executive order directing federal agencies that administer or sponsor a federal health care program to take specific steps intended to make price and quality information available to federal benefi-



ciaries and employees. The order also requires the agencies and their health care contractors to promote the use of interoperable health information technology and encourage approaches that facilitate high quality and efficient health care.

Fresh Look at Health Care Costs

Employee benefit experts often blame technology advancements for rising health care costs. But according to a new MIT study, researchers said that doctors, hospitals, and patients freely adopt the latest medications and technologies because medical insurance foots the bill for them.

If MIT findings are confirmed, the data will be used to support and promote consumer directed health plans to help control costs and promote coverage. Moreover, if high-deductible plans become the norm, the findings suggest patients would be more likely to cut back on spending for expensive treatments. Such theories are not new — similar hypothesis have been promoted by economists since the late 70s. It appears that data may finally be here that supports a closer look at what medical insurance contributes to its own inflation.

Canadian Drugs: Bargain or Bogus

For many years individuals have crossed the border into Canada (and Mexico) to purchase prescription drugs at a discount. American consumers are particularly drawn to the Canadian drug market because Canadian laws fix the price of certain branded prescription drugs — often at a cost lower than the market levels charged in the United States. As the practice and generally weak FDA enforcement became more widely known, many employers (and sometimes the states themselves), set up plans to import drugs from Canada.

The FDA has repeated that the practice is not safe, citing Canadian websites where the FDA found counterfeit drugs for sale. The FDA warned that the counterfeit drugs could be toxic or may just be ineffective in treating the condition for which they were prescribed.

There is no legal method that permits employers to import drugs from Canada. Moreover, the FDA warning shows again that there is no way to know for certain that the drugs are safe.

Calling for Limits on Profits

The *Los Angeles Times* reports that the California legislature is considering two bills that would limit health insurers' profits and cap consumers' out-of-pocket expenses for medical care. Consumer advocates and lawmakers are also considering a push for universal healthcare, and others are interested in forcing health insurers to absorb further medical costs.

Health care premiums continue to rise faster than inflation, and employees are often forced to pay higher deductibles on their coverage. Doctors want to recoup further reimbursements from health insurers, which doctors claim have been stingier with claims payments in recent years. It is unclear whether current proposals in California or other states will pass, given the anticipated extensive lobbying that is expected by health insurers.

High Cost of Failing to Offer COBRA

In a recent case, a court awarded almost \$120,000 to a former employee who was not offered COBRA. This award is interesting because of the way that the court calculated it. The court first

awarded \$12,199 for unpaid medical expenses that the former employee incurred shortly after terminating employment. Then it awarded almost \$17,000 in attorneys' fees and court costs, which it said would be a caution to other employers. Finally it awarded statutory penalties of \$110 per day for the failure to notify the employee of his COBRA rights. Those statutory penalties totaled just over \$90,000.

Although courts rarely award the high penalties that were awarded in this case, it is important to remember that COBRA compliance failure can result in liabilities that far exceed a qualified beneficiary's unpaid medical expenses. In fact, courts can award statutory penalties and attorney's fees even if a failure to provide required COBRA notices did not result in any unpaid medical expenses.

Workplace Adoption Benefits

Adoption benefits are sprouting as relatively low-cost perks that spread goodwill among working parents. Companies offer adoption benefits for recruitment and retention purposes and to equalize benefit levels between workers who adopt and those who receive insurance coverage for prenatal care and delivery.

Tax implications

Adoption assistance can be a straightforward payment, like a bonus, or part of a cafeteria plan, similar to a flexible spending account. Either way, adoption assistance is not subject to federal income tax, but it is subject to Social Security, Medicare, and federal unemployment taxes.

The IRS requires that the employer's adoption assistance program not pay more than five percent of its payments during the year to shareholders or owners, or their spouses or dependents. In addition to any job-based benefits, adoptive parents may also receive a significant federal tax credit. States also may provide tax incentives for adoption.

Adopting a child can be prohibitively expensive for some families. Adoptions through private agencies can cost up to \$35,000 per child, depending on the location and type of adoption. International private adoptions tend to cost more than domestic private adoptions, due to travel expenses, visas, and other legal requirements. Adoption costs may include application fees and services that the agency provides, such as a home study, medical services for the birth mother and child, legal services, document preparation, advertising and post-placement supervision.

Status Report: Fair Share Bills

A new *Business Insurance* article reports that the number of states pushing to enact legislation requiring employers to spend a certain dollar amount on health care for their employees (or be assessed a tax) has slowed significantly. This is in large part due to the recent federal court decision that overturned Maryland's *Fair Share Health Care Fund Act*. Although passage of the Maryland "Wal-Mart" bill in January was seen as the impetus behind legislators in other states proposing similar bills — it appears that the relative speed at which the law was overturned thwarted similar efforts.

Although Massachusetts' employers still have the challenge of complying with the Health Care Reform Law and employers in San Francisco have to contend with the recently enacted ordinance that mandates employer contributions to employee health care, it looks like employers in other states will find some relief from such laws — for now.

On a related note, the Massachusetts Division of Health Care Finance and Policy has adopted, without significant changes, a regulation that establishes the standards for employers in determining whether they are making "fair and reasonable" contributions to their employees' health insurance plans in compliance with Massachusetts' Health Care Reform Law.

Under the Massachusetts' law, effective October 1, 2006, companies with 11 or more full-time equivalent employees will pass the fair and reasonable test if at least 25 percent of its full-time employees are enrolled in the company's group health plan and the employer is making contributions towards the coverage. If the employer does not pass this test, it will still be deemed to have made a "fair and reasonable" contribution if the company offers to pay at least 33 percent of the individual's health insurance premium. If the employer fails to pass either test, then the company will be subject to a \$295 per full-time employee annual assessment.

The agency has postponed taking any action on a second proposed regulation that would have imposed a surcharge on employers whose uninsured employees receive free care from the state. They also temporarily withdrew a third regulation that would have required employers to file information about the health insurance status of each of its employees.

Insurance Carriers and COBRA Obligations

The DOL has consistently taken the position that employers are ultimately responsible for COBRA procedures, even if they comprehensively delegate administration to an insurance company or third party administrator (TPA).

Given this responsibility, employers should:

- Review the content of COBRA notices.
- Standardize and document mailing procedures for COBRA notices as well as for any supplemental communication pieces that are distributed to COBRA participants.
- Implement procedures requiring review of situations in which COBRA is not offered, when coverage ends, and requiring documentation of reasons for not offering COBRA, such as for gross misconduct situations.
- Confirm duties under agreements with insurance companies and/or TPAs to make sure all COBRA functions are assigned and performance is monitored to ensure COBRA functions are being completed properly.
- Implement an audit program to review COBRA compliance at regular intervals so compliance failures can be corrected and procedures amended to ensure success.

Employers are obligated to provide COBRA continuation coverage under their group health plans, even if the insurer under the plan fails to do so. Insurers generally are not subject to direct requirements to provide COBRA coverage (except, of course, under plans they sponsor for their own employees). Although carriers do not have the same incentive that employers have to "err on the side of caution" when it comes to providing COBRA coverage, a provision in the Internal Revenue Code imposes an excise tax on certain carriers that refuse coverage. Sometimes that provision can be used to convince a balking carrier to comply.

Since You Asked: Eligibility for Employees' Children

A manufacturing firm based in the Carolinas recently asked us how expanding eligibility for employees' dependent children would affect taxation of the employees' benefits and the COBRA rights of the dependent children. The firm was planning to extend eligibility for employees' children to age 21 — even for non-students. The question was whether any of these dependent children would end up being treated like domestic partners (that is, with the employee being required to pay tax on the value of the coverage provided to the dependent child and the dependent child being denied COBRA). As often the

case with employee benefit laws, the answer is “it depends.”

Up to age 19, an employee’s child’s health benefits can be tax-free if the child resides with the employee at least half of the year, the child provides less than half of his own support, and the child is a citizen or resident of the U.S., Canada, or Mexico. After reaching age 19, an employee’s child’s health benefits continue to be tax-free if the child meets these conditions and also is disabled or is a full-time student who is under age 24. So, for those dependent children age 19 through 21 who are disabled or are full-time students, the benefits continue to be tax-free.

For employees’ children who are not disabled or full-time students when they reach age 19, their health benefits may nonetheless be nontaxable if the employee provides more than 50 percent of the child’s support, the child does not qualify as anyone else’s dependent under the tests described above, and the child is a citizen or resident of the U.S., Canada, or Mexico.

In most cases, this means that benefits provided to the children added to the plan under the new rules will be tax-free to the employee. Unfortunately, this is not automatically the case. The employer may wish to adopt a practice of having employees sign a statement at enrollment (and at annual elections) that affirms the tax status of the dependents.

COBRA Implications

Under COBRA, the child’s rights depend entirely on the terms of the plan — not on whether the child is a tax dependent. Let’s assume that the plan is amended to allow employees to cover children until age 21 regardless of student status. An employee who has previously covered his 19-year-old child decides not to enroll the child for the following year because the child’s coverage will not be tax-free for the employee. However, the child is eligible for dependent coverage of the plan, so the child does not have a COBRA qualifying event when the employee drops the child’s coverage and COBRA coverage is unavailable to the child.

Issue Spotlight: Communicating with Non-English Speaking Employees

With 35 to 40 percent of its employees not literate in English (they speak Spanish) — must an employer provide a summary plan description (SPD) and other plan documents in Spanish?

The best practice would be to provide the materials in Spanish. The materials are meant to provide information to employees and the letter and spirit of ERISA is to communicate with employees. Moreover, common sense would dictate providing the information in a language that is understandable. In addition, there may be other reasons to consider sharing plan materials in foreign languages. For example, Executive Order No. 13166, *Improving Access to Services for Persons with Limited English Proficiency* (August 11, 2000) promotes utilizing non-English languages where appropriate.

That said, there is no legal obligation under ERISA to provide the information to the employee in the employees’ native language. There *is* an obligation (in some circumstances) to provide assistance in their native language and to communicate that availability in their native language — but not to actually provide the SPD itself in their native language. In limited situations, the SPD may be provided in English but there must be a notice in their native language telling them that they can get assistance in their native language; this notice must spell out in understandable language what they have to do to get that assistance.

Example

ABC Company maintains a pension plan which covers 1000 participants. At the beginning of a plan year five hundred of ABC Company’s covered employees are literate only in Spanish, 101 are liter-

ate only in Vietnamese, and the remaining 399 are literate in English. Compliance could be achieved by preparing and distributing SPDs in each applicable language. An alternate approach would also be considered acceptable. Each of the 1000 employees receives a summary plan description in English, containing an assistance notice in *both Spanish and Vietnamese* stating the following:

“This booklet contains a summary in English of your plan rights and benefits under Employer A Pension Plan. If you have difficulty understanding any part of this booklet, contact Mr. John Doe, the plan administrator, at his office in Room 123, 456 Main St., Anywhere City, State, 20001. Office hours are from 8:30 A.M. to 5:00 P.M. Monday through Friday. You may also call the plan administrator’s office at (555) 555-5555 for assistance.”

When considering this alternative, be sure to compare the cost of translation and printing to the potential risks incurred by requiring employees to operate with less-than-readily available information.

U.S. Benefit Office Locations

Anchorage, AK (907) 562-2266	Atlanta, GA (404) 224-5000	Austin, TX (800) 861-9851	Baltimore, MD (410) 527-1200
Birmingham, AL (205) 871-3871	Boise, ID (208) 340-0645	Boston, MA (617) 437-6900	Cary, NC (919) 459-3000
Charlotte, NC (704) 376-9161	Chicago, IL (312) 621-4700	Cincinnati, OH (513) 762-7661	Cleveland, OH (216) 861-9100
Columbus, OH (614) 766-8900	Dallas, TX (972) 385-9800	Denver, CO (303) 218-4020	Detroit, MI (248) 735-7580
Eugene, OR (541) 687-2222	Farmington, CT (860) 284-6137	Florham Park, NJ (973) 410-1022	Ft. Worth, TX (817) 335-2115
Grand Rapids, MI (616) 954-7829	Greenville, SC (864) 232-9999	Houston, TX (713) 625-1023	Jacksonville, FL (904) 355-4600
Knoxville, TN (865) 588-8101	Las Vegas, NV (702) 562-4335	Long Island, NY (516) 941-0260	Los Angeles, CA (213) 607-6300
Louisville, KY (502) 499-1891	Memphis, TN (901) 248-3100	Miami, FL (305) 373-8460	Milwaukee, WI (414) 271-9800
Minneapolis, MN (763) 302-7100	Mobile, AL (251) 433-0441	Mountain View, CA (650) 944-7000	Naples, FL (239) 514-2542
Nashville, TN (615) 872-3700	New Orleans, LA (504) 581-6151	New York, NY (212) 344-8888	Omaha, NE (402) 778-4851
Orlando, FL (407) 805-3005	Philadelphia, PA (610) 964-8700	Phoenix, AZ (602) 787-6000	Pittsburgh, PA (412) 586-1400
Portland, OR (503) 224-4155	Roswell, NM (505) 317-3397	St. Louis, MO (314) 721-8400	San Diego, CA (858) 678-2000
San Francisco, CA (415) 981-0600	San Juan, PR (787) 725-5880	Seattle, WA (206) 386-7400	Spokane, WA (206) 386-7400
Tampa, FL (813) 281-2095	Washington, DC (301) 530-5050	Wilmington, DE (302) 477-9640	

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