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Your Qualified Plan:

Updates, News, and Ideas

Section 125 Plans: An Even Better Deal

The Internal Revenue Service returned from Labor Day weekend with a **major** boost for Section 125 (Cafeteria) plans.

On September 2, the IRS announced in Revenue Ruling 2003-102 that over-the-counter (OTC) medicines are reimburseable under a Section 125 plan. Previously, the IRS had taken the position that only prescription medications were eligible for reimbursement through a Health Flexible Spending Account (FSA).

Interestingly, the IRS did *not* extend this principle to an individual's expenses; out of pocket costs for OTC drugs are not deductible on an individual's tax return, even for a taxpayer who reaches the 7.5% of income threshold required to deduct health care costs in general. *Only* by using an FSA can an individual take advantage of the new IRS position.

Why is this such a big deal? There are a couple of reasons. First, many popular medications have been or soon will be recharacterized from prescription to OTC availability. In the last year, for example, several very widely used allergy medications went from prescription only (and thus

reimburseable) to OTC, forcing patients to pay out of pocket and after tax. By shifting these costs into a Section 125 plan, employers can help their workers save money: a clear benefit.

Second, the new rule presents a significant challenge for plan sponsors. By eliminating the "bright line" of prescription vs. OTC availability, the IRS is requiring plan sponsors to more actively determine whether a given purchase meets the standard of "medical care."

For example, do dietary supplements meet the criteria? What about multivitamins? Plan sponsors are, more than ever, responsible for making a "facts and circumstances" decision on their employees' expenses.

Benefit Planning, Inc. has been working hard to come up with the right answers to these new questions (for the curious, the answer to both the questions in the preceding paragraph is "sometimes"). If you'd like to know more about how the rules work and when to approve – and when to deny – a participant's non-prescription drug claims, give us a call. We're here to help.

Maintaining Your Plan

The third quarter is traditionally a busy time of the year for retirement plans, as calendar year plans are required to file Form 5500 with the Department of Labor by July 31, or October 15 if on extension.

2003 was no exception; in fact, this may have been our most rushed year so far, as plan sponsors hustled to get the required information to us right up to the deadline.

While we are always happy to help, some simple good planning can greatly reduce the stress on our clients - and their "supporting cast" of CPAs, business managers, investment advisors and financial services companies.

Corporate plans that operate on a calendar year basis are required to have W-2 payroll information assembled no later than January 31 each year; if we are cc'd that information as it's compiled, we won't have to pester our clients later in the year (sole proprietors and others with Schedule C income, we know you're under a different set of rules; just make sure we get your information as early as possible).

We would also remind *all* our sponsors that we need to be copied on any brokerage statements you get from your financial services firm. Please remind your broker to send us copies, both of the monthly statements and any annual reports you receive.

A little advance work can save a world of time and hassle at the close of the administrative cycle; the modest effort required more than pays for itself when you *help us help you*.

Pension Bill Provides Short-Term Relief to DB Plans

While deferring action on the longer-term issues surrounding funding of defined benefit pension plans, the U.S. House of Representatives passed a bill in October replacing the 30-year Treasury bond with a blend of corporate bonds as the "benchmark" for Defined Benefit pension plans, at least through 2005.

Industry and labor backed the bill as a way to strengthen the defined benefit system at a time when both profits and the stock market have been growing very slowly. The retirement of the 30-year Treasury bond in 2001 aggravated the problem, driving yields down.

While the current legislation is due to expire in 2005, Rep. John Boehner (R-Ohio) says "[w]e expect to proceed immediately with efforts" to formulate and enact a permanent fix.

We'll keep you posted as this and other important legislation moves through the system.

Unforeseen Consequences?

According to a recent study by the Center for Retirement Research at Boston College, employees who are covered only by a 401(k) plan tend on average to stay in the workforce fifteen months longer than those employees covered by defined benefit pension plans.

The lack of early retirement incentives in 401(k) plans, as well as worker uncertainty about their investments and the differences in distribution forms were all cited in the study as possible explanations.

While the immediate tax benefits of a retirement plan are often the primary reason for setting up a plan, that decision can have important, and sometimes surprising, effects. If you'd like to discuss how your retirement plan may be affecting your workforce, please give us a call any time.

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