



Section 125 Employer Guide



Employers nationwide are learning how to offset high insurance premium increases by reducing payroll tax liabilities with Section 125 Cafeteria Plans. In many cases, employer savings can add up to as much as 20 percent of every dollar being passed through the plan.

One of the most underused employee benefits for small businesses today is the Section 125 Cafeteria Plan. These plans simply allow employees to withhold a portion of their salary on a pre-tax basis to cover the cost of qualifying insurance premiums, medical expenses and dependent care expenses. Because Section 125 Cafeteria Plan benefits are free from federal and state income tax, an employee's taxable income is reduced which increases take-home pay. And because the Section 125 Cafeteria Plan reduces employee gross income for purposes of income tax, the employer also enjoys a reduction in their payroll tax liability by eliminating matching FICA taxes of 7.65%, and possibly workers' compensation (depending on your state).

In an environment where group health insurance continues to double in cost every four years, it's hard to understand why more employers don't setup full Section 125 Cafeteria Plans. Employers don't realize they can offset a good portion of the premium increases with reduced payroll tax liabilities. Seems simple; it really is. The reason more employers don't take advantage of Section 125 Cafeteria Plans is because employers think they're too difficult to setup or administer, and most CPAs don't really understand them, or offer them, and most insurance agents don't make enough commission on a Section 125 Cafeteria Plan to bother taking the time to explain the concept.

As succinctly, as possible, here's what you need to know about the three different benefits that make up a full Section 125 Cafeteria Plan (keep in mind you can implement just one or any combination of these three plans):

1. Pre-tax health insurance premium deductions, also known as a Premium Only Plan (POP). POP plans allow employees to elect to withhold a portion of their pre-tax salary to pay for their premium contribution for most employer-sponsored health insurance plans. The plan offers a simple way to obtain favorable tax treatment for benefits already offered. A POP plan is the simplest type of Section 125 plan and requires little maintenance once it's been set up through payroll. Section 125 POP plans reduce employer payroll tax liabilities. The cost to implement just a POP plan is only \$99.00. See more information at: <http://www.Core125.com>

2. Out-of-pocket unreimbursed medical expenses also known as Health flexible spending accounts (FSAs). A Health FSA, authorized under IRC Section 105 and 106, allows an employee to pay for certain medical expenses on a pre-taxed basis through salary reduction. Effectively the employee pays for out-of-pocket expenses that aren't covered by insurance (for example, annual deductibles, office co-payments, prescriptions, over-the-counter drugs and orthodontia) with dollars set aside in a tax free account. By participating in a FSA, an employee's taxable income is reduced, which increases the percentage of pay they take home. This, of course, also reduces employer payroll tax liabilities. The cost to implement a Health FSA is only \$149.00. See more information at <http://www.CoreFSA.com>



3. Dependent Care Assistance Plan flexible spending accounts (FSA).

The Dependent Care Assistance Plan (DCAP) FSA, authorized under IRC Section 129, is an attractive benefit for employees who pay for child-care or adult daycare for their parents. Many employees don't take advantage of this benefit and may be unaware of the significant tax savings. Employees may hold back as much as \$5,000 annually of their pre-tax salary for dependent care expenses, which include expenses they pay while they work, look for work or attend school full time. Qualified dependent care expenses may include, but are not limited to, the care of a child under the age of 13, daycare for parents, care for a disabled spouse or a dependent incapable of caring for himself, and summer day camps. In addition, by paying for dependent care with pre-tax dollars, your employees can save approximately 20 to 40 percent on their child-care expenses. This of course also reduces employer payroll tax liabilities. The cost to implement a DCAP FSA plan is \$149.00. See more information at <http://www.CoreDocuments.com/dcap.php>



If you purchase all three modules together as a full Section 125 Cafeteria Plan you receive a \$48 discount for a total of only \$349.00. However, employers can choose just one of the above components or mix and match only those components they need.

The best part about the Section 125 plan is most of your employees are already paying for these expenses out of their own pockets with after-tax dollars. Cafeteria plans offer them a remarkable way to save money they're already spending.

Here's how the Section 125 FSA component works:

- Prior to the beginning of each plan year, an employee estimates how much they'll spend in out-of-pocket medical expenses and/or dependent care expenses during the course of their plan year. (The plan year would be defined in their summary plan description).

Note: It's important for employees not to overestimate their annual election amounts, as the FSA is a "use it or lose it" benefit and they'll forfeit any unused balance remaining in the account at the end of each plan year. (There's a grace period for which an employee can file claims for each plan year.) If there's a FSA surplus at the end of the plan year, the remaining balance shall be retained by the employer to offset administrative expenses or future employee benefit costs.

- This amount is then deducted over the course of the plan year from their paychecks prior to being taxed and is deposited into their flexible spending account. On or after the first day of the plan year, an employee is restricted from changing or revoking the section 125 agreement with respect to the pre-tax premiums until the plan year has ended unless a "change in family status" occurs (as defined under the federal tax code) and the change is consistent with the "change in family status."
-
- Your employees would pay their out-of-pocket expenses upfront and then submit a claim and documentation to the plan administrator. A reimbursement would then be made from their own Health FSA or DCAP account with pre-taxed dollars and sent to them in the form of a check.



So what are the Section 125 Cafeteria Plan benefits to you as the employer?

- Every dollar ran through the Section 125 plan reduces an employer's payroll. Therefore, you don't have to pay FICA or workers' comp premiums (depending on your State) on those dollars. In many cases, this savings can add up to as much as 20 percent of every dollar being passed through the plan.
-
- Implementing a Section 125 Cafeteria Plan can "soften the blow" of premium increases to employees.

And what are the Section 125 Cafeteria Plan benefits to your employees?

- Participating in a cafeteria plan reduces an employee's taxable salary and increases the percentage of their take-home pay, thus increasing their spendable income.
-
- They receive a greater deduction on dependent care expenses than what's offered by a traditional tax credit at the end of year.
-
- There's less of an impact on employees from insurance increases, such as premiums, co-pays, deductibles and so on. One of the most common ways for employers to keep benefit costs down is to simply lower the benefit levels of their plan offering. While this saves you money on your premiums, your employees are then faced with greater deductibles, higher co-pays, higher prescription amounts and so on. Through the use of a Health FSA, employees can set aside money to cover these increased amounts, which lessens their out-of-pocket costs because they're setting aside tax-free dollars.

Pre-taxing Employee HSA Savings Component through Section 125 Premium Only Plans

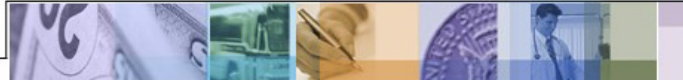
What is an HSA Plan - HSA is an acronym for the Health Savings Account. An HSA is comprised of two parts. The first part is a high-deductible health plan (HDHP) insurance policy that covers regular medical and hospital bills. The second part of the HSA allows you to make tax-free contributions to an investment account, retirement account, or HSA bank account from which you can withdraw money tax-free for medical care. Otherwise, the money accumulates with tax-free interest until retirement, when you can withdraw it for any purpose and pay normal income taxes.

HSA plans are personally owned by each participant or employee. Therefore they go with an employee when they leave one job and assume employment elsewhere.

There are two ways a Participant can take the tax-free deduction for the HSA plan:

1) *Year End Tax Return HSA Deduction:*

For the participant who will write-off their HSA bank savings amount from their annual tax return, tax-free means they only avoid paying federal income tax. They're still responsible for paying the 7.65% Medicare and Social Security taxes. This method saves the participant 15% to about 32% in federal tax write-offs depending on their tax bracket.



2) *Deducting HSA savings through a Section 125 Plan with an HSA Module:*

For HSA participants fortunate enough to have an employer with a Section 125 Plan modified to allow HSA deductions, tax-free means the participant avoids federal income tax *and* FICA taxes which include Medicare and Social Security. This method saves the employee 22.65% to about 40% depending on their tax bracket.

Core Documents has developed a HSA module for the Section 125 Premium Only Plan that allows the HSA savings component to be pre-taxed. Employers receive everything they need to establish an HSA Section 125 for only \$179.00. This package includes the Resolution to adopt, Plan Document, Summary Plan Description, Election Forms, Claim Forms, and Administrative Instructions. Core Documents is available to assist you throughout the process.

An important fact often missed by CPAs, Accountants, Payroll Companies, employers, insurance carriers and agents is how to pre-tax the HSA savings portion going into the investment or HSA bank account. This HSA savings piece can be pre-taxed through an employer's Section 125 Premium Only Plan. However, the standard Section 125 plan document should be modified or amended to allow the employee to pretax their HSA savings portion through convenient employee payroll deductions.

Employer Tax Savings:

By utilizing the Section 125 Premium Only Plan to pretax HSA savings the business owner saves matching Social Security (FICA), as well as federal unemployment taxes (FUTA) and generally, state unemployment taxes on the HSA Savings. Employer tax savings can average 7 to 10 percent more by utilizing the Section 125 Plan with the HSA module.

Administration of Section 125 Plans:

There are several administrative procedures that must be met to comply with Section 125 code legal requirements.

1. A plan document must be established. This document outlines specific details, such as a description of the employee benefits that are covered through the plan, participation rules, annual limits, election procedures, eligibility and employer contribution. It also defines the plan year.

2. A summary plan description (SPD) must be distributed to all participants. Section 104(b) of the Employee Retirement Income Securities Act of 1974 (ERISA), the basic law designed to protect the rights of participants and beneficiaries of employee benefit plans, requires that an SPD must be distributed to all participants no more than 90 days after an employee becomes a participant or within 120 days of the plan becoming subject to ERISA. The SPD summarizes specific details of the plan, claim filing procedures, and information concerning plan sponsorship and administration.

3. There's ongoing compliance that must be attended to. The laws are constantly changing and being updated. Federal legislation requires that section 125 plans can't discriminate as to eligibility and benefits being provided. Failure to meet the nondiscrimination requirements would eliminate the tax-free status of the benefits provided to the highly compensated and/or the key employees.



Frequently Asked Questions

What About Existing Section 125 Plans Already In Place That Need To Be Updated? If you already have a Plan you started years ago, you can amend and restate the Plan anytime. Our order forms address the amended and restated document dates. We simply need the original start date of your old plan so we can maintain the continuity back to the original start date. It's not unusual for a group to misplace a Plan Document and need to replace it. This is a good time to update the old plan with current plan documents. If your document was written before 2002, it certainly needs to be updated as soon as possible. So many changes have taken place in IRS Code and new laws that today's Plan Document is almost 15 pages larger than documents prior to 2002. This means you may be making administrative decisions based on outdated information.

So I've Purchased A Section 125 Plan Document, What's Next? This question is asked more frequently than any other. You'll purchase a single-use license agreement for a Section 125 Plan which can be a single Plan or a combination of any of the three components. These are not template, fill-in the blank documents. Each Section 125 Plan document is specifically prepared for each client based on the information provided in the application.



Administration of these plans is very simple. An outside administrator or software is not necessary to administer a Section 125 Premium Only Plan, however our free CoreData software will be helpful to track employee account balances for Health FSA and Dependent Care FSA plans.

Within a week you'll receive your Section 125 Plan in a one inch ring bound notebook with a Resolution to Adopt the Plan, an IRS required Section 125 Plan Document, a DOL required Summary Plan Description, Election Forms, and a complete Administrative Section. For a small additional fee you can purchase some of the documents on a CD disk.

Every employee should receive a copy of the Section 125 Summary Plan Description and an Election Form. Election Forms should be signed by employees for specific approved deductions and kept on file. For your convenience we provide you with a one page summary of all Section 125 Plan Sponsor responsibilities.

The document does not have to be filed with the IRS or the DOL, or any other government entity. Massachusetts is an exception to this rule. Annual 5500 reporting was suspended in 2002 and no longer required for all plans except Health FSAs with more than 100 employees.

You'll be required to conduct Section 125 non-discrimination testing annually. Core Documents will include DIY discrimination testing forms to assist you in this process. You'll need to sign the Section 125 Plan Document in two places and have it available in the event of an IRS audit, or the DOL asks to see a copy, or an employee asks to view the document, or you need to refer to it for administrative guidance.



Optional 125 FSA Online Administration w/Debit Cards



Why Outsource Section 125, HSA & HRA Administration?

One word - convenience. All employers want to take advantage of Section 125 and HRA tax-advantaged healthcare solutions offered by Core Documents, however some may not want to deal with the day to day administrative issues or the HIPAA liability that comes from handling employee protected health information.

For these clients Core Documents now offers a state-of-the-art online portal for Section 125 and HRA plan administration, plus the added convenience of a MasterCard® debit card for every employee. Debit cards allow your employees to instantly access their account balance.

Employees will no longer have to wait for reimbursement.

Employees can also: enroll online, make instant changes to their information, and access their account balances and information via any Internet connection, any time of the day, seven days a week. This virtually eliminates internal inquiries by employees about their plan.

How much does Section 125 and HRA Administration cost?

Unlike many administrators of Section 125 or HRA plans, Core Documents does not have a minimum monthly charge for small employers.

Section 125 FSA and HRA Administrative Fees are per employee

Group Size	Set Up Fee	Monthly Fee
1-5 employees	\$9.00	\$9.00
6-10 employees	\$8.50	\$8.50
11-19 employees	\$8.00	\$8.00
20-100 employees	\$7.00	\$7.00
100+ employees	\$6.50	\$6.50

Primary Section 125 & HRA Administrative Services include the following:

Section 125 and/or HRA Account Management

Section 125 and/or HRA Enrollment and Fulfillment

Section 125 and/or HRA Communication materials

Section 125 or HRA Customer Services

Section 125 FSA claim adjudication and reimbursement

Section 125 or HRA Compliance

Section 125 or HRA COBRA



FREE CoreData Administration Software



Many employers prefer to administer their own Health FSA and Dependent Care FSA Plans to save money. For those clients we offer CoreData, a robust Excel™ Spreadsheet Template. The software is free to clients who purchase Plan Documents.

CoreData Flex Administration software is no standard Excel™ Spreadsheet Template. You get a robust program with health flex plan and dependent care administrative capabilities designed by one of the foremost experts in Excel™ spreadsheet design. “CoreData looks and operates more like a state-of-the-art software program than an Excel™ Spreadsheet”.

Core Documents commissioned a project with one of the foremost experts in Excel™ Spreadsheet template design to build the best program for administering flex plan accounts. We spent more on the Excel™ Template design than most top of the line TPA flex software programs cost. Ease of use was the main criteria. Anyone can easily learn how to use this program in just a few minutes, experience with Microsoft Excel™ is not necessary.

Section 125 Cafeteria Plan benefit administration doesn't get any easier than this. For years flex plan administration software vendors have priced their product based on how many employees you have, however what they really want to know is how much you'll save in taxes. The price of the software was tied directly to how much you would save in taxes. Doing-it-yourself meant giving most of the tax savings to the software vendor. Not anymore!

Here's what you get with CoreData:

- A robust Excel™ template complete with three databases
- An easy to use 3 step process: Enter Employees, Enter Elections, Enter Claims
- Numerous standard reports built-in and capable of displaying all the data in the system
- Numerous automated functions to save keystrokes
- Employee, plan type, plan year, and claim drop-down menus throughout the program
- Plan year drop down menus allows you to operate in multiple years
- 25 year database takes you through 2030, simple to reprogram for the next 25 years
- The capacity to handle up to 200 employees
- Participate in Med FSA, Dependent FSA and HSA plans simultaneously



If you need help completing this application call 1-888-755-3373

Section 125 POP or FSA Application w/HSA Module



This is to request that Core Documents prepare a Resolution establishing a Section 125 Premium Only Plan and/or Flexible Spending Account (FSA), Plan Document and Summary Plan Description, Administrative Forms, Administrative Handbook, and Resolution to Adopt the Plan.

Purchaser Information (i.e. Person buying document other than the group who will use it, i.e. Agent, CPA, etc.)

First Name _____ Last Name _____
Company _____
Address _____
City _____ State _____ Zip Code _____
Phone _____ Fax _____
Email _____
Ship Document to: [] Purchaser [] Employer

Employer Information for Plan Documents

First Name _____ Last Name _____ (document signer)
Company Name _____
Address _____
City _____ State _____ Zip _____
Phone _____ Fax _____
Email _____

Form of Business: [] S Corporation [] C Corporation [] LLC [] Partnership [] Sole Proprietorship
[] Non-Profit 501(c)(3)

Employer Federal ID#: _____ State of Inc.: _____ Number of Employees: _____

Legal Name(s) of Affiliated Company(ies) that will be covered by the Plan (if any):

1) _____
2) _____
3) _____

Name of Plan Administrator: (Employer unless otherwise listed)

Name _____
Address _____
City _____ State _____ Zip _____
Phone _____

Name of Benefit Programs To Be Offered:

[] Health Insurance [] Dental Insurance [] Vision Care [] Group Term Life to \$50,000 [] Accident Insurance
[] Cancer Insurance [] Other _____

Effective Date will be:

[] a) a new plan effective date as of (date) _____
[] b) An amendment / restatement of a previously established Section 125 as of (date) _____
If this is to be amended and restated plan, state the effective date of the original plan: _____

Plan Year - The first plan year will be:

[] a) a 12 consecutive month period beginning (date) _____ and ending (date) _____
[] b) a short plan year beginning (date) _____ and ending (date) _____

Eligibility Requirements: All employees who work more than _____ hours per week.

Waiting Period: Employees can participate the first day of the month following _____ days of employment.

Please tell us how you found Core Documents: [] Search Engine [] Radio [] Magazine [] Other _____

