

March 8, 2007

Important BlueFund Information: HSA Updates and More

Market: BlueFund Plans

Since the initial launch of CareFirst BlueCross BlueShield's (CareFirst's) first Consumer Directed Health (CDH) Plan product, our BlueFund options have become quite popular. Research indicates that CareFirst CDH plans – particularly those with a Health Savings Account (HSA) – are nearing a tipping point in terms of widespread adoption and success.

Expediting this surge is President Bush's *Tax Relief and Health Care Act of 2006*, which enhanced many of the benefits already available through Health Savings Accounts.

New Rules for 2007 (Resulting from the *Tax Relief and Health Care Act of 2006*)

The following is a summary of the changes enacted, effective January 1, 2007, as part of the *Tax Relief and Health Care Act of 2006*.

- 1. Eliminates “lesser of” deductible and statutory limit rule by allowing HSA contributions up to the full statutory maximum without regard to individuals HDHP deductible amount.**

Old Rule: Maximum contribution capped at plan's annual deductible

- New regulations allow members to contribute up to the legal maximum of \$2,850 for individual coverage and \$5,650 for all other levels. The prior regulation capped HSA contributions at the level of the member's annual deductible.
- Even participants who establish their HSA mid-year can put in the maximum amount

- 2. Allows full-year contributions for individuals who enroll in a HDHP mid-year provided certain conditions are satisfied.**

Old Rule: The maximum contribution applies to contributions made in the calendar year. The maximum contribution amount was prorated for accounts opened mid-year.

- New regulation allows members to contribute up to the legal maximum as long as their coverage is in place and their HSA is opened by December 1st.
- **If a members enrolls mid-year and contributes more than the prorated amount (i.e., up to the legal maximum), the member must stay enrolled during the IRS testing period. For example, if a member's coverage is effective on February 1, 2007, the member has to stay in the plan through Dec 31, 2008. Regardless of the member's effective date, the member must be enrolled during the period from December 1st of the current year until December 31st of the following year.**

Example: Sam enrolled in a family HSA compatible health plan on July 1, 2007. He can contribute \$5,650 to his HSA even though there are only 6 months remaining in the calendar year. However, he must remain in this plan until December 31st, 2008, to ensure his full contribution remains nontaxable.

3. Allows one-time tax free rollover of Health FSA and/or HRA amounts to an HSA provided certain conditions are satisfied.

Old Rule: HRA and/or Health FSA amounts not transferable to HSA on a tax-free basis

- New Rule allows the employer to allow his/her employees to make a one-time tax-free transfer of an “applicable balance” to an HSA anytime before January 1, 2012
- The applicable balance = lesser of balance as of 9/21/06 OR the balance as of the date the transfer is made.
- This transfer is not counted against the maximum annual contribution amount (\$2,850 or \$5,650) and requires member to remain in the HSA-based health plan for 13 months.

4. Allows one time tax free transfer of IRA funds to an HSA, provided certain conditions are satisfied.

Old Rule: Individual Retirement Account funds not transferable to HSA on tax-free basis

- New Rule allows a one-time tax-free transfer of IRA funds to a health savings account, provided it is done on a trustee-to-trustee basis.
- This transfer is limited to the annual contribution maximum of \$2,850 or \$5,650.

5. Eliminates the negative impact of Health FSA grace period on HSA eligibility for a Health FSA participant that has a zero balance on the last day of plan year or who transfers entire balance by way of Qualified HSA Distribution

Old Rule: For participants in a general purpose FSA (w/grace period) - on last day of plan year, participant is not permitted to establish an HSA until the first day of first month following the end of the FSA grace period, even if the participant has no money in their FSA account.

- New rule states that an FSA grace period does not disqualify participant, provided that the individual has a zero balance in that FSA.

6. Allows greater contributions for non-highly compensated employees without violating the HSA comparability rule.

Old Rule: Employers who contribute to employees’ HSA must make comparable (same exact amount or same percentage of the deductible) to all “comparable participating employees” equally.

- New rule allows the employer to contribute greater contributions for non-highly compensated employees without violating the HSA comparability rules.
- Note: Most employers offer the HSA through the cafeteria plan where the comparability rule does not apply.

7. Requires Treasury to publish cost of living adjustments (COLA) for HSA no later than June 1 of the preceding year.

Old Rule: Allowed Treasury to post cost of living adjustments as late as December for January 1 implementation.

- New rule provides ample opportunity for insurers to update materials and alert clients of changes.

Please note these changes have resulted in our need to update our existing BlueFund FAQ documents and BlueFund resources. These updates will appear shortly in the broker section of www.carefirst.com in the Solution Center, under the *BlueFund Resources* link.

Additionally, we would also like to remind you of eligibility requirements for HSA enrollment:

HSA Enrollment Eligibility: Who Can (and cannot) enroll in an HSA Plan

- Open to everyone enrolled in a qualified high-deductible health plan
- Individuals cannot be covered under another health plan that is not a qualified high-deductible plan
- Individuals must not be enrolled in Medicare
- Individuals must not be eligible to be claimed as a dependent on another person's tax return
- Domestic Partners can be covered on health plan but cannot use HSA funds

Please contact your Broker Sales Representative with any questions.



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