



JANET  
LETOURNEAU

*QPA, CFCI, is the chief compliance officer at MHM Resources, in Leawood, KS. She draws upon more than 18 years of experience with flexible benefits plans and tax laws to perform consulting services and monitor quality control.*

*LeTourneau is a frequent speaker to employer groups and conferences and is a board member of the Cafeteria Plan Advisors Council (CPAC). She is the lead instructor for the Section 125 administrators training workshop.*

*LeTourneau was one of the first people in the country to earn the CFCI designation sponsored by the Employer's Council on Flexible Compensation. She is a certified trainer in the Certified in Flexible Compensation Instructor (CFCI) program.*

*LeTourneau can be reached at MHM Resources, 11440 Tomahawk Creek Parkway, Leawood, KS 66211. Telephone: 913-234-1083. Email: [janl@mhbiz.com](mailto:janl@mhbiz.com).*

# Consumer-Directed Health Plans

**H**igher-deductible health insurance plans are a practical strategy for many employers looking for cost-effective and flexible health care solutions for their groups.

*Are you proposing higher-deductible health plans to your employers now?*

*Are many of your groups thinking about implementing higher-deductible health plans in the future?*

If you answered "yes" to either of these questions, then the following information is for you. Some people call the higher-deductible health plans consumer-driven health care plans, while others refer to them as consumer-directed health plans (CDHP).

A typical consumer-directed benefit has two components in addition to the higher-deductible health plan: (1) a tax-free side account to pay expenses the health plan does not cover and (2) consumer tools and information to help employees understand how to make the most of their plan. These additional components are what employers and their employees need in order to take full advantage of a CDHP.

A CDHP will only be truly complete when employers offer employees a non-taxable way to pay their portion of the health plan premiums and tax-favored side accounts to pay for expenses the health plan does not cover.

A side account allows employees to save 25 to 40 percent on qualified expenses

when they elect to pay those expenses with voluntary payroll deductions on a pretax basis. And for account contributions made by the employer, employees will avoid 100 percent of the costs.

## Account Options

**Premium-Only Plans (POPs).** Like other health plan premiums, higher-deductible health plan premiums paid by employees may be paid on a pretax basis through a POP. It helps everyone—both employees and employers save money. Employees save because they don't have to pay federal, Social Security (FICA), state or local taxes (where applicable). Employers don't pay the matching FICA.

**Health Savings Accounts.** HSAs pay for health care expenses that either accumulate toward the deductible of the qualified higher-deductible health plan or expenses that are not covered by the health plan—such as dental and vision expenses.

HSAs are like IRAs, only for health care, the funds roll forward from year to year, are owned by the individuals, are portable if an individual leaves his current employer, and can be funded pretax through a POP.

The lower premiums typically associated with a higher-deductible health plan can help fund an HSA. Contributions can be made to an HSA by employees, employers or both. And keep in mind, contributions are only available as deposits are made. In other words, the account holder's qualified

expenses are not subsidized by an outside provider.

A newly established HSA will not likely have accumulated enough contributions to pay for medical expenses incurred in the early stages of a CDHP program. This fact must be carefully weighed by anyone choosing an HSA side account.

**Flexible Spending Accounts.** FSAs pay for expenses that are not covered by a health plan. Like an HSA, these include dental and vision expenses. POP plans can be expanded with an FSA plan to include medical expenses not covered by a health plan and other voluntary products. Employees utilize FSAs in order to budget for medical expenses.

Like an HSA, contributions can be made to the FSA by employees, employers or both. However, unlike an HSA, the entire FSA annual election is available to participants at the beginning of the plan year.

Although contributions may be deposited to an FSA on each payroll, employers are obligated to pay eligible expenses that exceed the cash balance in the account.

The good news is that a POP can be upgraded to an FSA at any time during the year.

**Health Reimbursement Arrangements.** HRAs are employer-owned health care reimbursement accounts. Contributions to an HRA are made by employers, and

employers set the annual limit that can be available on the first day of the plan or funds may be made available to participants on a periodic basis.

An HRA bridges the gap for employees moving to a higher-deductible health insurance plan with more employer control. Employers direct what expenses may be paid from a plan, whether unused balances may roll forward from year to year or are forfeited to the plan, and if a plan will cover terminated and/or retired employees.

**Other Voluntary Products.** Employees appreciate choice and value for their hard-earned income. Offering other voluntary benefits can enhance a benefit package, save employers as well as employees additional tax dollars, and make employees happy.

To complement a CDHP, an employer should think about adding a child or adult daycare account, adoption assistance plan, or transportation and parking benefits. Expenses normally paid by employees for these types of services can be paid with pretax dollars.

For employees who share in the cost of insurance premiums through payroll deduction or who purchase voluntary insurance products, certain premiums can be paid on a pretax basis. Premiums paid for cancer, accident, dental, disability, employer-sponsored group term life, and hospital

per-diem policies can all be purchased with pretax dollars through a POP.

According to a report issued by the Centers for Medicare and Medicaid Services, health care is expected to account for one of every five dollars spent in the United States within 10 years. Out-of-pocket expenses are estimated to rise 5.3 percent a year during that time, and the cost of health insurance may rise 6.4 percent annually.

A study by the Government Accountability Office (GAO) imparted these findings: CDHP coverage increased from three million at the beginning of 2005 to between five and six million at the beginning of 2006; employers offering CDHPs rose from 1 percent (2004) to 4 percent (2005); and effectively communicated CDHPs draw more participation.

Premium-only plans can save employers hundreds—if not thousands—of dollars annually. By combining other CDHP accounts with a higher-deductible health plan, employers can see a significant rise in their tax savings. And employees will have the confidence in their CDHP that only a total benefits package can provide. 🌐

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