ROBINSON & COLE LLP
Employee Benefits & Compensation

Over-the-Counter Drugs can now be Reimbursed through Flexible Spending Accounts

A recently issued IRS Ruling significantly expands the types of expenses that can be reimbursed through health care flexible spending accounts. Over-the-counter drugs, such as antacids, allergy medications, pain relievers and cold remedies, can now be reimbursed through flexible spending accounts. Toiletries, cosmetics and dietary supplements, such as vitamins, continue to be ineligible for reimbursement. This expansion of eligible reimbursable expenses may result in increased popularity for flexible spending accounts. As the IRS did not set an effective date for this change, it can be implemented immediately if plan documents permit.

As with the case of prescription drugs, the purchase of over-the-counter drugs must be properly substantiated. Although the IRS has not defined what constitutes substantiation, an itemized receipt has generally been found sufficient with respect to prescription drugs. An itemized receipt would likely be sufficient for over-the-counter drugs when combined with a representation that the drug was purchased to treat the employee, a spouse or a dependent. Obtaining an itemized receipt could be problematic since some pharmacies may not provide itemized receipts for non-precription purchases.

Although reimbursement for over-the-counter drugs is now permissible, plan sponsors are not required to reimburse these expenses. In making a decision as to whether or not to permit reimbursement of over-the-counter drugs, plan sponsors should consider whether obtaining substantiation for these expenses would be administratively burdensome. After a decision has been made as to whether or not over-the-counter drugs will be reimbursed under a flexible spending plan, the plan document and the SPD should be reviewed and revised as necessary so that it is clear which expenses can be reimbursed under the plan.

If over-the-counter drugs will be eligible for reimbursement under a plan, this change should be communicated as soon as possible so that employees can take advantage of this opportunity.

DOL Provides Guidance on the Reallocation of Employer Stock in a Master Trust

The DOL has issued an Advisory Opinion relating to the reallocation of employer stock among an employer's qualified plans. Under the facts of the opinion, an employer sponsored five defined benefit plans that were all funded through a master trust that was funded in part with employer stock. The master trust's assets, including the employer stock, were allocated among the five plans for funding and recordkeeping purposes and for purposes of satisfying plan liabilities. The value of the employer stock as allocated under the trust did not exceed 10% of the fair market value of the assets of any one of the plans.

In order to facilitate the merger of one of the plans funded by the master trust, the employer proposed to reallocate the employer stock held under the merging plan to the four remaining plans. ERISA prohibits a defined benefit plan from acquiring employer stock if immediately after the acquisition the fair market value of employer stock held by a plan exceeds 10% of the fair market value of the assets of the plan. In this case, the reallocation of the employer stock among the four plans could have resulted in the value of the employer stock held by the remaining plans exceeding 10% of the fair market value of the assets each plan. The DOL stated that the reallocation of one plan's interest in employer stock to the remaining plans participating in a master trust would be an acquisition of employer securities under Section 407(a) of ERISA. The DOL stated that if the reallocation resulted in any plan holding more than 10% of its assets in employer stock, the transaction would violate ERISA.

IRS Extends Deadline for Determination Letter Applications for Adopters of Master and Prototype or Volume Submitter Plans

A sponsor of a Master and Prototype or Volume Submitter Plan is required to amend its plan to comply with GUST before September 30, 2003. If an employer amends a standardized or non-standardized prototype plan for GUST before September 30, 2003, generally no additional action is required and the plan does not need to be submitted to the IRS for a favorable determination letter. Adopters of volume submitter specimen plans who have made modifications to the plan must submit the plan to the IRS and obtain a favorable determination letter.

The IRS recently announced that if a plan sponsor timely amends and restates its plan to comply with GUST before the September 30 deadline, the deadline for applying for a determination letter is extended to January 31, 2004. If a sponsor fails to adopt a GUST amendment prior to September 30, 2003, the sponsor can amend the plan, pay a $250 compliance fee, and apply for a favorable determination before January 31, 2004. The $250 compliance fee is paid in addition to the normal determination letter user fee. Therefore, although generally a plan sponsor using a standardized or non-standardized prototype plan would not apply for a determination letter, if such a plan is not timely amended before September 30, 2003, then the plan must be submitted for a favorable determination letter, together with the compliance fee, before Janaury 31, 2004.

Final Regulations on Split-Dollar Arrangements Issued

The IRS has issued final regulations regarding split-dollar life insurance policies. The regulations supercede previous IRS guidance regarding the tax treatment of split dollar arrangements. Under the new rules, which are consistent with the last proposed supplemental rule issued by the IRS, if the executive is the owner of the policy, the employer's premium payments are treated as loans to the executive. Thus, unless the executive is required to pay the employer market rate interest on the loan, the executive will be taxed on the difference between market rate interest and actual interest. If the employer is the owner of the policy, the employer's premium payments are treated as providing a

taxable benefit to the executive.

The new rules do not alter the taxation of key man life insurance arrangements where the employer purchases the life insurance contract and also retains the rights and benefits of the contract. The new rules apply to split-dollar arrangements entered into after September 17, 2003, and also apply to existing arrangements that are materially modified after that date.

DOL Provides Guidance on Providing Prospectuses to Participants to Satisfy ERISA 404(c) Requirements

Under Section 404(c) of ERISA, if a participant exercises control over the investment of his or her account and certain administrative requirements are met, plan fiduciaries will generally not be liable for any participant investment losses. In order to secure Section 404(c) protection, a participant must be provided with or have the opportunity to obtain sufficient information to make an informed decision regarding the investment alternatives provided under the plan. In the case of mutual funds, the regulations require the plan fiduciary to provide participants with a copy of the most recent prospectus either immediately before or immediately following the participant's initial investment. Additionally, at any time the participant requests, he or she must be provided with a copy of a prospectus. The Department of Labor has issued an Advisory Opinion stating that the delivery of a Profile (a brief summary of the prospectus, generally two to four pages long) will satisfy the prospectus requirement of Section 404(c). However, the plan sponsor must provide the full prospectus upon a participant's request.

For participants who find the information contained in a prospectus to be overwhelming, receipt of the summary Profile will be a welcome change. It is important to note that the Advisory Opinion only permits the use of mutual fund Profiles and did not address whether a Profile could be provided in lieu of a prospectus in the case of investment in securities.

NEW ARRIVAL

CONGRATULATIONS TO ATTORNEY KERRI WILLIS AND MATT BUDZIK ON THE ARRIVAL OF BABY CAITLIN DELANEY BUDZIK