BENEFIT
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529 Plans—Helping Employees Save For Education

Most employers recognize that, for many of their employees, saving for a child's education is a top priority. With the cost of a private four-year college education ranging upwards of $100,000, saving early has become paramount in helping to ensure a child's schooling and, for many employees, their own continuing education. In particular, 529 college savings plans—named for Internal Revenue Code 529—are a popular way to set aside money for college and graduate school.

In response to the warm welcome these tax-advantaged savings vehicles are receiving, particularly after favorable changes made by the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), employers seeking innovative ways to attract and retain a qualified workforce have begun offering the 529 plan as an incentive in their benefits packages. Furthermore, to ease the process for employees and to encourage a disciplined approach to saving, many companies allow contributions to be easily made through payroll deduction.

Not to be confused with prepaid tuition plans, 529 college savings plans are state-sponsored investment accounts that offer two distinct tax advantages: 1) the potential for earnings to grow free of federal income tax; and 2) the opportunity for withdrawals to be made free of federal income tax, if funds are used for qualified education expenses, such as tuition, fees, room, and board. Certain state taxes may apply, though. Nonqualified withdrawals may be subject to a 10% federal income tax penalty. Prior to EGTRRA, beneficiaries of a 529 plan had to pay federal income tax on any earnings. However, this provision is scheduled to "sunset" on December 31, 2010, and if Congress does not act in the interim, regulations governing 529 plans revert back to their status as of tax year 2001.

Contribution limits vary by state and in most states exceed $200,000. As an employer-sponsored payroll deduction, employees contribute a percentage of their pay to a 529 account (similar to a 401(k) plan).

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While contributors are not eligible for any federal income tax deductions, some states allow for certain state income tax deductions. A person's residency status in the state sponsoring the plan generally affects his or her state tax benefits, which may affect employees of companies with offices in different regions. For example, suppose a company has an east coast office and a west coast office. The main office, which is on the east coast, offers a 529 college savings plan from that east coast state. This would allow east coast employees to reap state tax benefits, as well as any qualified federal tax benefits. However, employees from the west coast office, while sharing the potential for earnings free of federal income tax, would not qualify for any state tax benefits.

For contributors in all states, federal gift taxes may also apply, but a special provision applies to 529 plans. Any individual may gift $11,000 per year ($22,000 for married couples) to another individual without incurring gift taxes. However, individuals contributing to a 529 plan are allowed to make a lump-sum contribution of $55,000 ($110,000 for married couples), using five years' worth of gifting. While this method limits tax-free gifting for the next five years, it may allow funds a longer time for potential compound earnings.

Investment options vary by plan but often include a selection of mutual funds. Generally, diversification—a strategy used to manage risk and maximize potential earnings—of the portfolio's assets is based on the beneficiary's age or number of years until the beneficiary begins college. The portfolio's investment strategy may be changed once during a calendar year without incurring any federal income tax penalties. Also, the account holder may change the designated beneficiary at any time without incurring federal income tax penalties.

In addition to understanding the federal and state tax issues affecting 529 plans, it is also important to understand the associated fees and expenses. These vary by state and plan, but often include enrollment fees, maintenance fees, sales charges, management fees, and fund expenses.

For many employees, sending children to college or continuing their own education is a significant life goal. Offering a 529 plan, with payroll deduction as part of a benefits package, may boost employee satisfaction and help the business owner retain a valuable workforce.

Health Savings Accounts Popular, But Not Universally Available

The majority of consumers who have signed up for tax-advantaged Health Savings Accounts (HSAs) are satisfied with their health care coverage, according to a survey by the Blue Cross and Blue Shield Association (BCBSA). But a recently published study by the Galen Institute found that, nearly two years after HSAs first became available, many states still have legal barriers to the efficient delivery of HSA plans in place.

BCBSA conducted an online survey of 3,000 consumers enrolled in both consumer-driven health plans (CDHPs) and conventional plans. Among the HSA-eligible enrollees responding to the survey, 68% indicated they are satisfied with the performance of their insurer, 71% said they are satisfied with their access to preventive care and wellness services, and 69% said they are satisfied with the health benefits information provided by their insurer. These satisfaction levels compared favorably with those of enrollees in traditional insurance plans, according to BCBSA researchers.

The survey also showed that 65% of the HSA-eligible enrollees who purchased their coverage directly and 61% of those who obtained coverage through their employers would recommend CDHPs to others.

The age and health status of the HSA-eligible enrollees who participated in the survey did not differ significantly from that of enrollees in traditional insurance products, researchers noted. The two groups were also found to be equally likely to request generic drugs, choose not to go to a doctor, delay seeing a doctor or having a medical procedure, delay or fail to fill a prescription, and take a lower than recommended dose of a prescribed drug.

The HSA-eligible enrollees were, however, found to be twice as likely as participants in traditional plans to have been previously uninsured. Results further showed that HSA-eligible enrollees were more likely than traditional plan enrollees to make use of information and services provided by the insurer, such as drug price comparisons, cost-tracking tools, and online wellness programs.

"The success of HSAs and other consumer-directed health plans is predicated on consumers pursuing information and applying that knowledge to their health care decisions. The survey shows that consumers enrolled in HSAs are beginning to do just that," said Maureen Sullivan, senior vice president, Strategic Services, BCBSA.

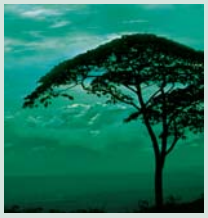
Growing numbers of businesses are interested in offering HSAs coupled with high-deductible plans to their employees, but state regulations often get in the way, David Hogberg concluded in the Galen Institute report "HSAs and the States: Lifting the Barriers."

While most states have changed their income tax codes to accommodate HSAs, eight states—including California, New Jersey, Wisconsin, and Pennsylvania—continue to tax contributions, according to the report. "There is little excuse for the delay," Hogberg said, observing that changing a tax code is relatively easy to do and that the eight states currently taxing HSA contributions can afford the exemptions.

Another barrier to HSA take-up in many states, the report said, are first-dollar coverage mandates, which require insurance to cover certain conditions and treatments from the "first dollar," before any deductible is met. Because most non-preventive care mandates conflict with the IRS regulations governing HSAs, Hogberg said, states will be required to eliminate some types of first-dollar coverage mandates by the end of this year. Hogberg called upon states to repeal these mandates or, barring that, exempt HSA qualifying insurance from such mandates.

A further problem for HSA providers are the community rating regulations of 27 states and the guaranteed issue regulations of 5 states, the report said. The community rating process, which averages all the premiums in a given region when setting premiums for individuals, discourages healthy people from buying health insurance, according to Hogberg. Guaranteed issue rules, which stipulate that an insurance company may not refuse coverage to individuals with health problems, tend to limit the number of insurance providers willing to offer individual policies. The report noted that HSAs are not available at all in any of the five states with guaranteed issue rules. Hogberg recommended eliminating these regulations or creating exceptions for HSA plans.

An additional obstacle faced by insurance providers in most states is the need to seek approval of the state department of insurance before selling a policy. While some of these processes are relatively simple, the report said, they can be more complex in the case of HSAs because many companies are still developing their policies. To avert delays in providing coverage, Hogberg advised, states should streamline their procedures, and state legislatures should pass laws allowing insurance providers to start selling a policy if the department of insurance fails to either approve or deny it within 60 days.



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Older Women May Be Discouraged From Working

While the percentage of older women who participate in the workforce is expected to grow over the next several years, a recently published report by the Center for Retirement Research at Boston College asserts that married women in particular are discouraged from working by a variety of factors, including relatively low earning power, high tax rates, and barriers to earning Social Security benefits.

In their report, "What Makes Older Women Work," researchers Alicia Munnell and Natalia Jivan said the share of women aged 55–64 in the labor force rose from 43% in 1970 to 52% in 2000 and is expected to jump to 61% by 2012. This increased labor force participation among older women, the report suggested, is likely due to improvements in health status and the rising incidence of divorce.

At the same time, however, the financial incentives for older married women to work are not as great as for other groups, Munnell and Jivan observed. In 2002, they noted, the median earnings for female full-time employees were 78% of that of their male counterparts, and women earned less than men at every level of education and across occupational categories.

In addition, the researchers pointed out, married women tend to face higher marginal tax rates than men or single women because, in 76% of married households in which both partners work, husbands earn more than their spouses. Women who earn less than their husbands receive a lower return on their wages because they are taxed at higher rates.

A woman whose husband earns significantly more than she does may also be discouraged from working because, under current rules, her continued employment generates little or no additional Social Security income. An estimated two-thirds of women age 62 or older receive Social Security benefits based entirely or partially on their husbands' earnings. Moreover, the report added, family responsibilities and a desire to stop working when their husbands retire may pull married women out of the labor force.

After examining the factors that keep women in the workforce, Munnell and Jivan found that older women are more likely to be employed if they are divorced, have no younger children, lack substantial financial assets, or earn more than their partners. Women who could improve their Social Security benefits through employment were shown to be 14% more likely to work than women with lower projected benefits.

As women of all ages participate in greater numbers in the labor force, more older women will have greater incentives to work than in the past, the researchers concluded. As women become more likely to earn their own Social Security benefits and less likely to be the marginal earner in the household, Munnell and Jivan predicted, "their work decisions and careers [will] look more like those of men."

The researchers added, however, that while current trends suggest both women and men will have insufficient resources to retire early, causing them to continue working until their mid-60s, "the challenge is greater for women given their weaker attachment to the labor force and smaller financial incentives."

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