Flexible Spending Accounts

Eligible employees may establish flexible spending accounts (FSAs) to use pre-tax income to pay for eligible healthcare and dependent-care expenses. These are IRS-sanctioned accounts that allow you to authorize monthly deposits to your account from your before-tax salary. Then, as you incur eligible expenses, you request tax-free withdrawals from your account to reimburse yourself.

You may enroll for the accounts within 60 days of your initial date of hire, during Open Enrollment, or within 60 days of and consistent with a qualified status change. These are annual accounts; you can close them or make changes to deposit amounts midyear only because of and consistent with a qualified status change.

Following are examples of qualified status changes:

- Your marriage, final divorce or legal separation
- Birth, adoption or placement for adoption of a dependent
- Death of your spouse or dependent
- A change in your spouse's employment status
- A change in legal custody agreement
- Cost changes by, or change of, dependent care provider (for dependent care FSAs, only).

IRS Rules for FSAs

FSAs are annual accounts that operate under IRS rules. Under these rules, you must enroll annually to establish an account for the coming plan year. And the accounts operate under the "use-it-or-lose-it" rule.

In the past, participants could be reimbursed with plan-year deposits only for eligible expenses incurred during the plan year. If they didn't incur as much in eligible expenses during the plan year as they deposited to the account during that year, they forfeited any dollars remaining in the account.

The IRS now allows a "grace period" for FSAs that gives you a cushion if you overestimate the amount you will need for reimbursement of eligible expenses during the plan year. The 75-day grace period runs from January 1 through March 15 in the year following the plan year. If you have funds remaining in your plan-year account and you incur eligible expenses during the grace period, those expenses may be reimbursed using plan-year deposits.

The grace period should not be used as a carryover you plan for, but rather as backup for unanticipated situations. Let's say you establish a healthcare FSA for the 2006 plan year. You plan to have lasik eye surgery in the fall of 2006, so you elect to deposit the maximum amount – $5,000 – to the account during the year. Come November, you find out that your lasik treatment will have to be postponed until January 2007. Instead of losing the considerable amount that could remain in your account on Dec. 31, 2006, you can confidently reschedule your surgery for January and use the dollars you deposited during 2006 for reimbursement.

But FSAs are still "use it or lose it" accounts. You will have 90 days after the end of the plan year to submit reimbursement claims to the FSA administrator. After this 90-day run-out period, any dollars left in the account will be forfeited.

Tax Alternatives?

You may have alternative options in the current IRS system. If your out-of-pocket healthcare expenses for the year are greater than 7.5 percent of your adjusted gross income, you may be able to deduct the amount above that threshold. For example, if your adjusted gross income was $25,000 you could deduct healthcare expenses higher than $1,875. That threshold may make a healthcare FSA a better option.

If you use a dependent care FSA to pay for your dependent care expenses, your use of the federal and Oregon child-care tax credits will be limited. Before you enroll for a Dependent Care FSA, determine which tax program will be better for you. Generally, if you expect that your adjusted gross annual income (including spousal income) will be more than $25,000, you will most likely be better off using reimbursement through an FSA. If you expect that your adjusted gross annual income (including spousal income) will be less than $25,000, you will most likely be better off taking the tax credits and not participating in a Dependent Care FSA.

Please note that PEBB cannot guarantee favorable tax results. If you need additional information or assistance, contact your attorney, accountant or other tax advisor.

Starting an Account

You start an account by enrolling online or by completing the enrollment form and submitting it to your agency.

These are annual accounts, so you must re-enroll during Open Enrollment if you want to continue to participate from year to year. You begin each year with a zero balance for that plan year. You determine your deposits for the next year with each enrollment.

Ending the Account

When you enroll in an FSA, you are electing to participate for a full year. However, you may stop making deposits to the account because of a qualified status change. Deposits to your account automatically terminate if you end state service. To ensure a deduction is not taken from your final paycheck, notify your payroll office as soon as you know you will be leaving state service. If you terminate employment with the state, you are still eligible to claim reimbursement for expenses you incurred during the year while you were a state employee. Expenses incurred after your termination are not eligible.

Questions?

If you have questions about flexible spending accounts, call a PEBB benefits analyst at (503) 373-1102 in Salem or (800) 788-0520 statewide. Or send e-mail to inquiries.pebb@state.or.us.

Special Instructions for OUS Employees

Your first monthly deduction will be taken from your Dec. 31, 2005, paycheck, and the last deduction will be taken from the Nov. 30, 2006, paycheck.

Nine month employees (includes classified academic year employees) who are not enrolled in the 12-month payroll distribution plan will have only 10 deductions taken for the 2006 plan year. Dependent care FSA participants cannot claim expenses they incur when they are not working. Contact your campus benefits office to request dependent care FSA information.

Healthcare Flexible Spending Account

Any eligible employee may establish a healthcare FSA. A healthcare FSA helps you save money on your out-of-pocket healthcare expenses. Because you pay for these expenses with pre-tax dollars, you save a percentage of each dollar you spend out of pocket. Eligible expenses include most of the medical, dental and vision services and drug costs not fully covered in PEBB plans.

Eligible expenses include:

- Copayments and coinsurance amounts (for services and prescriptions)
- Costs over maximum coverage (for example, for glasses and orthodontia)
- Over-the-counter (OTC) drugs for treating medical conditions.

Ineligible expenses include:

- Insurance premium payments
- Costs covered by PEBB medical, dental and routine vision plans
- Any healthcare expense you itemize as a deduction on your tax return
- Vitamins, herbal preparations and dietary supplements (unless prescribed by your provider for a diagnosed medical condition)
- Health club memberships.

Please see the Eligible and Ineligible Expenses list for more detailed information.

How Much to Deposit?

The annual contribution limit for PEBB's healthcare FSA is $5,000. If your spouse also has a healthcare FSA through the state or another employer, your individual contribution limit is still $5,000. Your contribution will be deducted monthly from your pay and deposited to your account.

Remember, this is a "use it or lose it" account. So, before you establish your healthcare FSA, carefully estimate what you expect your out-of-pocket expenses to be for the coming year. You might want to be conservative in your estimate.

Ask your pharmacy and healthcare providers for a printout of your expenses for this year. As an alternative, you can review receipts, insurance forms, credit card statements and cancelled checks to determine this year's out-of-pocket costs.

Then think about any additional expenses you are likely to incur in the coming year. Are any surgeries likely? Will someone in the family be getting braces? Ask the providers for estimates. Will you need new glasses or contacts more frequently or that are more costly than your medical plan covers? Estimate that cost, as well.

Use these estimates to calculate your anticipated out-of-pocket costs and monthly deposit amount on the worksheet provided here.

Healthcare FSA Estimate Worksheet	
Anticipated annual expenses for you and your dependents	**Estimated amount**
Medical care coinsurance or co-payments	$
Dental care coinsurance or co-payments	$
Prescription drug coinsurance or co-payments	$
Medical care not covered in the plan	$
Dental care not covered in the plan (such as implants)	$
Prescription drugs not covered in the plan	$
Vision care more frequent than or beyond plan allowance	$
Vision care not covered in the plan (such as laser surgery)	$
Travel for healthcare	$
Over-the-counter drugs for healthcare (such as aspirin)	$
Annual total (below $5,000)	$
Divide by 12 and enter the monthly deposit amount.	$

Here's an example of how a hypothetical PEBB member saves dollars with a healthcare FSA. She gets paid $1,500 a month. After taxes, her take-home pay is $1,050. But then she has to pay $200 per month for healthcare services and supplies – dollars she has already paid taxes on. Now, her actual spendable monthly income is only $850. Then, she opens a healthcare FSA, so the $200 she'll spend on healthcare isn't taxed, and her spendable income goes up to $910. She saved $60 in taxes.

Tax Savings Comparison		
	Without FSA	With FSA
Gross monthly salary	$3,000	$3,000
Pre-tax FSA deposit	$0	-$200
Adjusted monthly salary	$3,000	2,800
Taxes, calculated at 30%	$900	$840
Net take-home pay	$2,100	$1,960
After-tax medical expenses	$200	$0
Spendable monthly income	$1,900	$1,960

Near the end of the year, you may want to match any remaining dollars with current needs for preventive or ongoing care. Examples include health screenings, routine vision care and maintenance prescriptions.

Filing for Reimbursement

With the healthcare FSA, in most instances you have access to the total amount you elected for the year as soon as you incur eligible expenses and a deposit has been made to the account. This does not apply in the case of orthodontia, however. For orthodontic (braces) expenses, you must submit a reimbursement request for the initial deposit and thereafter with an invoice from the orthodontist.

You may print a copy of the claim form from www.benefithelpsolutions.com/pebb/fsa.shtml. Or you can register there to submit claim forms electronically.

To file for reimbursement, complete a reimbursement form and attach receipts or other proof of goods or services incurred and payment made for each eligible expense. Documentation must include:

- Date of service
- Provider's name
- Type of service
- Amount charged
- Prescription number (if for prescription drug)
- Name of over-the-counter product on the receipt.

An explanation of benefits form from your insurance carrier can act as proof. The IRS does not accept canceled checks as proof of expense or payment. A receipt from the provider should state the goods or services and the date they were provided; the amount of the expense; and the

Healthcare FSA	
Eligible Expenses	**Ineligible Expenses**
• Healthcare co-payments, coinsurance • Prescription drug co-payments, coinsurance • Charges in excess of usual, customary, reasonable • Orthodontia beyond the maximum allowed • Dental implants • Routine eye exams, eyeglasses and contact lenses beyond the maximum allowed • Cataract surgery or any other surgical process to correct your vision such as laser surgery • Hearing aid costs beyond the maximum allowed • Speech and physical therapy • Nursing services • Wheelchairs • Prosthetic and orthopedic devices • Nursing home care for treatment of illness or injury • Prescription drugs not covered by the plan • Over-the-counter products for medical care • Crutches • Guide dog or other animal for blind or deaf individuals • Travel to receive care	• Cosmetic surgery • Health or fitness club fees • Personal care items • Prescription drugs used for cosmetic purposes • Most weight reduction programs • Amounts reimbursable by other sources • Expenses for which a federal itemized deduction is taken • Insurance premiums • Maternity clothes • Illegal operations or treatments • Funeral and burial expenses • Vitamins or supplements taken for general health purposes • Cosmetics, toiletries • Tooth-whitening procedures • Custodial care if in an institution • Household or domestic help, even if recommended by a doctor • Marriage or family counseling fees • Long-term care services

provider's name. Send the form and supporting documentation to the address on the form.

Appeals

If your claim is denied, notification of the denied claim will set out the specific reasons for the denial and the specific Plan provision on which the denial is based; and will further advise you of what steps, if any, you might take in order to validate your claim. The notification will advise the following: (a) your right to appeal the denied claim by requesting an administrative review; (b) your right to review (on request and at no charge) relevant documents and other information; and (c) your right to file suit under ERISA (where applicable) with respect to any adverse determination after appeal of your claim. If you ***do not*** appeal on time, you will lose your right to appeal.

You (or your authorized representative) may request a review any time within 180 days of the notice that your claim was denied. Your written appeal should state the reasons that you feel your claim should not have been denied. It should include any additional facts and/or documents that you feel support your claim. You will have the opportunity to submit comments and have them considered. Your appeal will be reviewed and decided by someone who was not previously involved with your claim. The decision regarding the review will be made no later than 60 days after you submit the appeal. If the decision on review affirms the initial denial, you will be furnished with a notice of adverse benefit determination on review setting forth:

- The specific reason(s) for the decision on review;
- The specific plan provision(s) on which the decision is based;

- A statement of your right to review (on request and at no charge) relevant documents and other information;
- A description of any specific rule, guideline, protocol, or other similar criterion or a statement that such a rule, guideline, protocol, or other similar criterion was relied on and that a copy of it will be provided free of charge to you upon request.

Send your appeal to: **BenefitHelp Solutions, FSA Appeals, PO Box 67230, Portland, OR 97268**

Dependent Care Flexible Spending Account

Eligible employees may set up a dependent care FSA if they are:

- Single with an eligible dependent, and the expenses are necessary for the employee to work
- Married with an eligible dependent, and the expenses are necessary for both the employee and the spouse to work
- Married with an eligible dependent, and the spouse is either disabled, actively seeking employment, or a full-time student at least five months during the year.

According to IRS regulations, expenses that qualify for reimbursement are expenses for the care and well-being of the employee's dependent child under the age of 13 or for the care of a disabled dependent of any age who is incapable of self-care and who spends at least eight hours per day in the employee's home.

Eligible expenses include charges for:

- A licensed or registered day care facility or nursery school
- An individual (other than a spouse or a qualified dependent under age 19) who provides care for a qualified dependent.

Ineligible expenses include those for:

- Education (including kindergarten)
- Overnight camps
- Food and transportation, when billed separately
- A dependent's healthcare.

Please refer to IRS Publication 503 for further information on eligible and ineligible dependent care expenses. You can find it online at www.irs.gov.

How Much to Deposit?

Carefully estimate how much you will spend on dependent care during the year. Following are the maximum participation amounts:

If you are:	Maximum annual amount
Single	$5,000
Married, filing jointly	$5,000
Married, filing separately	$2,500
Married, with spouse who is disabled or a full-time student	$2,400 per dependent up to $4,800

If you or your spouse earns less than the amounts shown, the maximum amount you may deposit is either your monthly income or your spouse's monthly income, whichever is lower. If you both participate in a dependent care FSA (through the same or different employers) the $5,000 limit applies to the combination of both FSAs.

Filing for Reimbursement

With a dependent care FSA, you may not be reimbursed for more funds than you have available in your account. You can file for reimbursement as soon as you incur eligible expenses during the plan year and a deposit has been made to the account.

You may print a copy of the claim form from www.benefithelpsolutions.com/pebb/fsa.shtml. Or you can register there to submit claim forms electronically.

To file for reimbursement, complete a reimbursement form and attach receipts or other proof of services incurred and payment made for each eligible expense. The IRS does not accept canceled checks as proof of expense or payment. A receipt from the provider should state the dates dependent care services were provided; the amount of the expense; and the dependent care provider's name, address, and Tax Identification Number or Social Security Number. (Your provider should complete a Form W-10, which is available from the IRS.) Send the form and other documentation to the address on the form.