DOL Provides Important Follow-Up Guidance on HSAs and ERISA Issues

The EBSA issued important guidance on HSAs and ERISA issues in the form of Field Assistance Bulletin 2006-02. FAB 2006-02 follows up on DOL's earlier guidance concerning when ERISA applies to HSAs (FAB 2004-1) and addresses a number of "recurring questions about the guidance and evolving practices regarding the offering of HSAs. HSA custodians, HDHP insurers, employers, financial institutions and service providers should take heed of this very important guidance to avoid running afoul of many frequently overlooked compliance issues.

The following is a brief overview of the issues addressed in the FAB 2006-02 question and answer (Q&A) guidance:

- **Q-1: Can an HSA be established without consent and still be voluntary?** An HSA is still "completely voluntary" (an essential element of the FAB 2004-1 safe harbor ERISA exception) even if the employer unilaterally establishes an HSA for employees and subsequently deposits employer funds in the HSA. The intent of the "voluntary" requirement in FAB 2004-1 is to ensure that employee contributions to an HSA, including salary reductions, are voluntary. NOTE: IRS Notice 2004-50 specifically allows an employer to provide negative cafeteria plan elections for HSA contributions so long as the requirements of Rev. Ruling 2002-27 are satisfied. Reading this guidance, FAB 2004-1 and the applicable IRS guidance together, it would appear that ERISA would not apply solely because an employer establishes an arrangement under which accounts are established and pre-tax salary reduction contributions are made by default. Also, it is important to ensure that state and federal banking requirements applicable to account establishment are satisfied.

- **Q-2: Employers do not trigger ERISA applicability solely by choosing one or more HSA provider to whom it will make contributions.** The DOL clarifies that employer neutrality in communicating that the HSA is an employee welfare benefit plan is a required element of the FAB 2004-1 ERISA exception; however, "endorsement" of the arrangement itself (as typically used in the ERISA group insurance arrangement exception) is not an element. Thus making contributions to a single HSA custodian, which would normally be construed "endorsement" does not by itself trigger ERISA. CAUTION: There is a thin line between endorsement (as used in the group insurance exception context) and employer neutrality in communicating the arrangement is not an employee welfare benefit sponsored by the employer. Employers will still need to take care in how they communicate the HSA to employees; ensuring that employees understand that the HSA is not an employer sponsored plan despite the fact that the employer has chosen this particular custodian to which it will make contributions.

- **Q-3 An employer is not "making or influencing investment decisions" in violation of FAB 2004-1 solely by choosing an HSA vendor who offers the same investments offered by the employer under its 401(k) plan as long as employees are afforded a reasonable choice of investments and are not limited in moving funds to another HSA.** Note, however, that a single investment option is not considered to be a "reasonable choice of investments". Does this mean that a single "certificate of deposit" or "interest bearing account" option is problematic by itself ? We hope not. One interpretation is that the guidance is referring to situations where the investments under the HSA mirror the 401(k) . Additional guidance is needed from the DOL on this issue. Also, while although not specifically addressed in the FAB, prior informal conversations with DOL officials indicate that ERISA may be triggered where the employer influences the scope of investments that the HSA custodian/trustee actually offers to its employees (e.g. where the employer requires investments be offered that the custodian/trustee does not typically offer). Finally, while not directly applicable, it remains to be seen how much of the recent Pension Protection Act guidance on investments may apply here.

- **Q-4 An employer's FICA and FUTA tax savings through a cafeteria plan are not "payment or compensation" that would trigger ERISA under 2004-1.**

- **Q-5 Employers can pay the employees' HSA fees without triggering ERISA.** Caution: Guidance is still needed from IRS as to whether direct withdrawal of fees from the HSA will be considered a non-taxable distribution.

- **Q-6 HSA Vendors may offer their employees the same HSA product that they offer "in the regular course of business" to the public without triggering ERISA.** Although good news, additional detail is still needed. For example, prior IRA related guidance from the DOL indicates that ERISA applies where IRA custodian's charge their own employees a fee. Although not directly applicable to HSAs, it raises the question as to whether employers may charge their own employees a fee if they charge non-employee HSA accountholders a fee? Informal guidance from DOL officials indicates that a market fee may be charged to employees who establish HSAs with the employer/HSA custodian without triggering ERISA. Also, since employers generally can pay HSA fees, we believe that discounted fee for employees should be permissible as well.

- **Q-7 An employer is considered to have received "payment or compensation", and thus triggers ERISA (and potential prohibited transaction issues), if it receives any discounts on other products offered by HSA vendors selected by the employer.** For example, it would appear that an arrangement where the HSA product is combined with other products offered by the HSA Vendor (e.g., other administrative services or HDHP coverage) and the vendor charges a lower fee for such products as a result of the HSA relationship than where the product is offered on a stand-alone basis would result in issues for the employer. Such receipt of compensation may also be in violation of the prohibited transaction rules.

- **Q-8 EBSA clarifies that an employer's failure to promptly forward employee HSA contributions to the HSA custodian is a prohibited transaction under IRS 4975 (without regard to whether ERISA applies).** Caution. Although not specifically stated, failure of an HSA administrator to forward such contributions to the HSA custodian would appear to also be a prohibited transaction.

- **Q-9 The class exemptions previously issued for IRAs (e.g., where the IRA custodian/trustee provided nominal incentives or reduced or no cost banking services/products to IRA owners) do NOT apply to HSAs.** Thus, any incentive provided to HSA account holders (other than those deposited in the HSA under AO 2004-09) are generally impermissible -- absent an HSA specific individual or class exemption.

- **Q-10 EBSA reaffirms the DOL's guidance in DOL Adv. Op. 2004-09A that it is not a prohibited transaction to offer a cash incentive for establishing an HSA so long as the incentive is paid directly to the HSA.** Presumably, payment to the individual's personal account would be a prohibited transaction.

- **Q-11 Addresses whether a line of credit issued by the HSA Vendor and the HSA accountholder is a prohibited transaction.** EBSA merely restated general law in this area. While certain activities are clearly prohibited (e.g., borrowing or pledging the HSA assets, or "receiv[ing] a benefit in his or her own individual capacity as a result of opening or maintaining an HSA" the mere issuance of credit by an HSA vendor in an arms length transaction and the account holder's directing HSA funds to the credit line vendor for HSA expenses paid with a credit card are not automatically prohibited. {Note: credit could not be issued on the condition that the account holder assign his rights to HSA funds to the credit line vendor, but voluntary, revocable payments directed by the account holder to the credit line vendor do not appear to be automatically impermissible.} The answer depends on the particular facts and circumstances. EBSA refers to DOL Adv. Op. 89-12A as general guidance. {In 89-12A, the DOL held that offering free checking services to IRA accountholders who invest a portion of the IRA assets with bank owned mutual funds was a prohibited transaction). Although not directly applicable to HSAs, the concept set forth in the 89-12A and the subsequent IRA rulings is that it is a prohibited transaction to provide an accountholder with consideration for his personal account as a result of establishing or maintaining an HSA or for using HSA funds.

If you have any questions, please feel free to contact John Hickman (jhickman@alston.com 404-881-7885) or Ashley Gillihan (agillihan@alston.com 404-881-7390).