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2004 ERISA Advisory Council on Employee Welfare and Pension Benefit Plans Working Group on Health and Welfare Form 5500 Requirements

The following statement was submitted to be read into the record:

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Introduction

Thank you, Madam Chairman, and members of the Working Group.

I am here today to present the views and experiences of ASPPA members. ASPPA is a national organization of more than 5,500 retirement plan professionals who provide consulting and administrative services for qualified retirement plans and welfare benefit arrangements covering millions of American workers. ASPPA members are professionals of all disciplines, including consultants, administrators, actuaries, accountants, and attorneys. ASPPA's membership is diverse, but united by a common dedication to ensuring timely and effective compliance with the reporting and disclosure requirements of ERISA.

Comments

ERISA defines an employee welfare benefit plan as a plan, fund, or program established or maintained by an employer or employee organization to provide certain benefits for participants or their beneficiaries. As long as the employer maintains a plan, it may be subject to ERISA regardless of whether the employer contributes to the cost of the plan.

The first problem an employer faces is that it does not know whether a given benefit program constitutes an ERISA plan and, in many cases, may not even know enough to ask that question. As a result, Form 5500 filings are not prepared when needed.

Welfare plans come in many shapes and sizes. Some plan sponsors pay welfare benefits out of the company's general assets in a pay-as-you-go fashion. These plans are considered unfunded. Other employers have plans that provide benefits through the purchase of insurance contracts, so fall under the insured category. A larger company may use a Voluntary Employees' Beneficiary Association [a §501(c)(9) trust - or VEBA] as a funding vehicle for some or all of its welfare benefits; thus, the benefit plan is funded.

Of course, the simplified explanation above assumes the employer is responsible for 100% of the funding of the welfare benefit plan. This rarely happens today, especially with regard to medical plans. Welfare benefit plans may require contributions from the covered employees and beneficiaries and these employees' contributions may cause a plan to be treated as "funded" for reporting purposes. Fortunately, the Department of Labor has provided exceptions under DOL Technical Releases 88-1 and 92-1, along with regulations under §2520.104-44 that provide relief from funded status (for reporting purposes) solely on account of employee contributions to certain welfare plans.

Plans providing the following types of health and welfare benefits--whether

insured, funded, or self-funded--are subject to ERISA:

- Medical, surgical or hospital benefits, possibly including physical exams and some employee assistance programs;
- Sickness or accident benefits;
- Disability benefits;
- Death benefits;
- Supplemental unemployment or vacation benefits;
- Apprenticeship or other training programs;
- Day care centers;
- Scholarship funds;
- Prepaid legal services; and
- Severance pay.

As noted, this is the start of the reporting dilemma for many employers. What plans do they offer? Which plans are subject to Form 5500 filing requirements?

Let me give an example from my own experience. Engagement of my firm often starts with a compliance review. The client delivers to me all of the benefits communication materials that are normally provided to its new employees and, from that, a list of plans subject to ERISA is developed. The next step in the review involves collection of the plan documents, summary plan descriptions, and Form 5500 filings for those plans. A client typically has no difficulty presenting the documentation and filings relating to its qualified retirement plans; however, it is frequently an entirely different story for its welfare benefit plans. Although a §125 cafeteria plan document may exist, the "documents" for the medical, dental, and life plans may consist solely of the employee booklet issued by the insurance carrier. For some benefits, the only "document" may be the information presented in the employee handbook.

My approach to identifying welfare plans subject to ERISA filing requirements is not necessarily typical. Many tax form preparers do not have the skills necessary to properly advise the plan sponsor about welfare plan reporting, so merely continue to prepare only those Form 5500 filings that the plan sponsor has historically filed. Large employers often prepare Form 5500 filings for welfare plans (but not qualified retirement plans) in-house and, again, the SALY (same as last year) principal applies. No thought is given to changing circumstances and benefit structures and the impact on Form 5500 reporting.

Further complicating the identification of the plans subject to Form 5500 reporting is the ease with which welfare benefit plans change over the years. For example, in 1990 an employer may have provided employee medical and life insurance benefits through a bundled product offered by a single insurance carrier. This arrangement required only a single Form 5500 filing and the plan year was based upon the policy year. If the employer subsequently added dental benefits through a separate carrier, the employer may have just expanded the reporting on the Form 5500 reporting the medical and life coverage to include the dental coverage. Another scenario frequently encountered is that over the years all three benefits - medical, dental, and life - were unbundled and are now offered by three separate insurance carriers and, perhaps, operate on different policy years. Unfortunately, many employers in this situation continue to report all of the benefits on a single Form 5500 filing.

Form 5500 filing requirements for a welfare benefit plan hinge on two things: (1) the number of covered employees and beneficiaries and (2) whether the plan is considered funded or unfunded, insured, or a combination of unfunded and insured.

Three reporting patterns arise for filers of Form 5500 for large welfare benefit plans (more than 100 participants as of the first day of the plan year):

1. A welfare plan that is unfunded completes only the three-page Form 5500. No schedules are attached nor is an auditor's opinion and report required. These plans do not provide Summary Annual Reports (SAR) to covered participants.
2. A welfare plan that is insured - or a combination of unfunded/insured - completes the three-page Form 5500 and attaches Schedule A information from the insurance carrier(s). SARs must be distributed to covered participants.
3. A welfare plan that is funded, typically through a VEBA trust, must provide the

opinion and report of an independent accountant along with completing Form 5500, Schedule H, and other appropriate data, such as Schedule A (Insurance Information) and Schedule C (Service Provider Information). Again, SARs must be distributed to covered participants.

The welfare benefit plan filing that requires only the three-page Form 5500 (as described in 1. above) is simple in terms of data gathering and form preparation; however, it is not clear how this information provides any useful data to the government and, certainly, participants are not receiving any information about the funding of the plan. In preparing for this hearing, we surveyed ASPPA members who are routinely involved in Form 5500 preparation for welfare plans. It was unanimously agreed that these types of filings should be eliminated if, in fact, it is shown that none of the data being collected is being analyzed for any purpose.

The insured welfare plan (as described in 2. above) often presents data collection problems. For example, one of my clients has a welfare plan that covers more than 41,000 employees nationwide. The plan is a combination of insured/unfunded. Last year, the client attempted to collect approximately 160 Schedules A from the various insurance carriers that provided coverage to employees. An employee of the plan sponsor was assigned this task and began contacting insurers about two months after the end of the plan year. The due date for filing the Form 5500 was extended to June 15, 2004. As of May 31, 2004, only 147 Schedules A were received. We filed the return electronically on June 10 without the missing schedules. As a practical matter, this client has never been able to get all of the Schedule A data from all of the carriers for any plan year.

We should take a moment to elaborate on the difficulties in securing Schedule A from insurance carriers. DOL is well aware of the problem inasmuch as ASPPA has discussed this issue with the agency on several occasions; however, there is a disconnect here: insurance companies are required to provide Schedule A data to plan sponsors under ERISA §103(a)(2) but there is no apparent enforcement of this rule. Plan sponsors that are unable to secure Schedule A are being left to decide what information to provide and directed by the official instructions to note on the schedule any refusal on the part of the insurance company to provide the data. Clients tell us that Schedule A is not being sent to them automatically, that it takes multiple calls and follow up with vendors to receive this information, and often participant counts or other data are missing. It should be noted that sometimes the Schedule A information is forwarded to the broker involved in the sale of the insurance and it is their failure to send that information along to the plan sponsor that causes the gap in data collection. In any event, the practitioner preparing Form 5500 usually has little or no influence with either the broker or the insurance company and must rely on the plan sponsor's tenacity in seeking Schedule A data.

SARs are delivered to participants in these insured arrangements; however, the information presented to them is not particularly useful. Instead of showing the total premiums paid, the SAR might be more pertinent if participants are told whether all premiums were paid (and any employee contributions applied) in a timely fashion and if the coverage is currently in force.

Our survey shows preparer costs for Form 5500 filings in the first two categories (i.e., unfunded or insured/unfunded) generally start at \$500; higher fees will be charged depending upon the complexity of the arrangement and the number of Schedule A required to be filed. Some preparers reported that costs for welfare plan Form 5500 preparation may be discounted if the firm provides other, more substantial, services to the employer. The cost also depends on whether it is the responsibility of the employer or the preparer to collect Schedule A data.

The last category of welfare plan filer - a plan that requires an audit (as described in 3. above) - presents issues different from the simpler filings previously discussed. Based on our survey, costs for audits range anywhere from \$8,000 up to \$50,000. One accounting firm noted that their fees for health and welfare plans are three to four times that of §401(k) plans, and that fees have increased dramatically the past several years. One of my clients reported the annual cost relating to its welfare plans is approximately \$30,000 for one audited welfare plan and nine insured arrangements (each insured arrangement has no more than three Schedule A attached; most have only one Schedule A). That \$30,000 cost does not include any time attributable to employees of the

plan sponsor who are involved in compiling data or working through issues during the audit.

Other audit-related issues included the following:

1. Some accountants inappropriately produce a report for the trust rather than the plan, or do not reflect activity that may have occurred outside of the trust.
2. Many of the health plans under audit have activity that does not flow through the tax-exempt trust. A significant portion of audit time is spent determining that activity and, in most cases, auditing it. One auditor reported that, in many cases, welfare plan audit work involves transactions and issues that are not related to the tax-exempt trust.
3. Many companies funnel benefit payments through a VEBA trust, which triggers an audit requirement, but in fact maintain very little or no assets in the trust. In these situations, the audit does not provide any value in protecting participant contributions or benefits.
4. HIPAA. Audits of medical plans necessitate auditor access to protected health information, such as support for paid claims. Outside service providers require the auditor and the plan sponsor to sign confidentiality agreements and the plan sponsor, to comply with HIPAA provisions, also requires the auditor to sign a Business Associates Agreement. Several different accounting firms reported that it often takes months for the attorneys of the service provider, auditor, and plan sponsor to agree on the wording of these agreements.

The service providers often withhold needed claims information from the auditors, claiming HIPAA restrictions. There is much back-and-forth between the parties before reaching agreement on what information is available to the auditors.

All of these issues are multiplied by the number of service providers involved. Outside service providers change frequently, so the protocol established in one year will not necessarily apply in the following year. In addition, there is huge turnover in staff at many of the outside service providers, which adds time for the auditors and the plan sponsor.

5. When information is provided to the audit team (such as provider invoices, processing data from the administrator, explanation of benefits, etc.) the skills of the audit team are rarely compatible with interpretation of the health information. For example, the auditors have limited capacity to recognize procedural codes on an outpatient service, determine propriety of the pricing of the service codes given the geographical location of the provider, and ensure adequate network discounts were provided to the plan sponsor.

6. Preparing the financial statements is time consuming. It requires a thorough understanding of the plan, its insurance arrangements, claim payment process and the resulting accounting, and collection of data from many outside service providers as well as sources within the plan sponsor. The plan itself is an unnatural reporting entity in that the information is not available from a single source nor accumulated in a single place such as the general ledger, which accumulates the records for the financial statements of the plan sponsor.

7. Many health and welfare plans have obligations associated with them (such as incurred but not reported (IBNR) claims, post-retirement benefits, post-employment benefits, etc.). The financial accounting for these obligations as required under SOP 01-2 is not consistent with the Form 5500 reporting. Consequently, there are often many reconciling items between the Form 5500 and the audited financial statements. As a result, the auditor will spend significant resources auditing information (such as runout claims of long-term disability) that is not reported on Form 5500 and, in almost all cases, is not funded by the plan sponsor through the tax-exempt trust at the reporting date.

8. The utility of the audited financial statement is limited. Unlike the audited financial statements of defined contribution or defined benefit plans which provide important information on investment returns (for defined contribution plans) or funding levels for benefits (for pension plans), decisions of health benefit elections involve information that is not included in the statements, such as benefit coverages, deductibles, preexisting condition limitations, etc. Neither

participants nor plan sponsors particularly care about investment returns in the welfare plan context.

9. Accountants report that there are many restatements of health and welfare plan financial statements to correct errors in the prior year's financial statements. These errors are normally identified as plan operations and provisions become better understood.

These funded welfare plans must provide an SAR to covered participants; however, as noted above, the information does not really provide data that affects a participant's benefit choices or assure them of continued coverage.

This litany of issues illustrates a variety of factors that should be considered by the Working Group. One recommendation may be to apply lesser reporting requirements and auditor scrutiny to welfare plans that are "funded" but which really have no assets than to plans that maintain substantial assets and push the funding limits under IRC §419.

Several other confusing situations should be mentioned. The first involves self-insured arrangements requiring employee contributions, which raises questions about whether the employer satisfies rules under the DOL's plan asset regulations. Such arrangements may be deemed funded, fail to meet the exceptions under the regulations at §2520.104-44, and be subject to audit requirements. ASPPA members noted that sponsors of such plans generally assume compliance with the regulations without any mechanism in place for monitoring application of the employee contributions to paid claims. In short, employers assume the plan is not funded for reporting purposes and that no audit is required.

Our survey also netted multiple comments about the confusion surrounding Form 5500 reporting for §125 cafeteria plans. In Notice 2002-24, IRS formally suspended the filing of Schedule F for fringe benefit plans under IRC §§ 125 (cafeteria plans), 127 (educational assistance plans), or 137 (adoption assistance plans); however, welfare features of §125 cafeteria plans must continue to be reported on Form 5500. For example, a cafeteria or flexible benefit plan that includes a medical reimbursement feature must continue to file Form 5500 if that feature covers more than 100 participants. Similarly, if a cafeteria plan has been used as an umbrella plan for all of the sponsor's welfare benefits, the plan must continue to file under ERISA. What happened? Many people who read the Notice understood it to say that Form 5500 filings for cafeteria plans were eliminated. Several years have now passed and employers and practitioners are starting to realize they may have read the Notice too broadly and are faced with a gap in Form 5500 filings. In its simplest form, the only filing requirement is the three page Form 5500 noting the participant count (at line 7) and the type of welfare benefit (at line 8b) so the gap in information to the DOL is minimal. Yet the plan sponsor is responsible for the missed filings and that fact must be addressed by the sponsor and the professional preparer. Filings with such limited data appear to be more nuisance than informative and are certainly of no concern to the covered participants. As previously discussed, ASPPA members responding to our survey unanimously agreed that these types of filings should be eliminated if, in fact, it is shown that none of the data being collected is being analyzed for any purpose.

To make more efficient use of data, time, and other resources, the following should be considered:

The Form 5500 is primarily designed to collect information about the activity of retirement plans. If specific data is needed for analysis by the DOL, perhaps the creation of a Schedule W that specifically captures welfare plan data would be more appropriate rather than fitting a square peg (welfare plan) in a round hole (retirement plan oriented filing). Data currently provided on multiple Schedule A could be condensed to a few lines of summary data on Schedule W, and more pertinent questions could be included, such as whether the coverage is in force and premiums current, or if the application of employee contributions meets the requirements of the plan asset regulations.

Further, the SAR format should be reexamined in light of participant concerns

and consideration given to providing more useful data to participants in both welfare benefit and retirement plans. Welfare plans, in particular, are more volatile in terms of plan design. All of the new products entering the market cause frequent changes to participant costs and options. It is important to communicate meaningful information about the state of the welfare plan to the participants, rather than a recitation of global facts and figures that cannot be translated into significant information for the individual.

Finally, the DOL is interested in seeking ways to promote electronic filing of Form 5500. I presented testimony on behalf of ASPPA at the Working Group's hearing on September 20, 2002 and ASPPA has submitted comments in response to the RFC (Request for Comments) on the proposal dubbed "EFAST-2." Part of the RFC presented the possibility of building capabilities for EFAST to accept Schedule A directly from carriers. It is highly doubtful that direct filing of Schedule A is in any way feasible. Schedule A is currently delivered to plan sponsors in a variety of formats - many of which are not compatible with the Schedule A - and with missing or incorrect data, for example: plan names or numbers are incorrect; participant counts are missing; policy years are wrong. E-filing, however, is more attractive if simplified and consolidated information streamlines the collection of data, shrinks the number of filings required, and reduces the preparation time.

Conclusion

It is important to collect data about welfare plans that enables the DOL to meet its obligation to protect plan participants. It also is important to consider the differences between the information needs and concerns of welfare plan participants and retirement plan participants and to address those differences by providing them with truly meaningful information.

ASPPA sincerely appreciates this opportunity to present the views and experiences of its members. I would be pleased to answer any questions you have. Thank you.