
The Small Business Guide to Section 105 Medical Expense Reimbursement Plans

A strategy for hiring and keeping the best employees

Our story

Offering traditional group benefits sucks. Why? They're too expensive, too complex, and too one-size-fits-all. PeopleKeep is a new way to offer benefits called personalized benefits. Most people believe benefits are the services a company offers, such as a health insurance plan or 401k. With personalized benefits, it's the opposite. Companies give people tax-free money to spend on the consumer services they find most valuable. It's as simple as wages. For small businesses that think offering traditional group benefits sucks, PeopleKeep is personalized benefits automation software that makes offering benefits simple, painless, and personal for everyone.

Today more than 3,000 companies use PeopleKeep to hire and keep their people across the United States. PeopleKeep is based in Salt Lake City, Utah.

To learn more about PeopleKeep, visit www.peoplekeep.com.



Ready to see how PeopleKeep can work for your company?

Visit www.peoplekeep.com/demo to preview our software or click below to have a Personalized Benefits Advisor contact you.

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Introduction

Hire and keep the best employees

As a small business owner, you know that hiring and keeping top-quality employees is vital your business. And, after wages, benefits are the top influencer in where people choose to work—so benefits are key in your hiring and retention strategy.

Whether your business is hiring its first W-2 employee, you need a formal health benefits package to keep a critical employee, or your group health insurance is exceeding internal budgets, Section 105 Medical Expense Reimbursement Plans (MERPs) present a simple health benefits alternative to the cost and complication of offering group health insurance.

This guide provides an executive-level overview of Section 105 MERPs and how small businesses can leverage them to hire and keep the best employees.



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Table of contents

Introduction	iii
Executive summary	1
Rising costs of health care	2
What is a Section 105 Medical Expense Reimbursement Plan?	4
4 advantages of MERPs for small businesses	6
Frequently asked questions	8
How to implement a Section 105 MERP	10
Appendix A: Health reform and new opportunities for small businesses	11
Additional health benefits tools and resources	14



Executive summary

The problem

In the past, small businesses have relied on group health insurance to offer employee health benefits. However, over the last 15 years, group health insurance costs have tripled. Today, fewer than 50 percent of small businesses offer group health insurance. Recent reforms have only made it harder, and costs are expected to continue to rise.

After wages, benefits are the top influencer for where people choose to work. Yet every year fewer and fewer small businesses can use benefits to hire and keep their people.

The solution: Personalized Benefits

MERPs are a type of Personalized Benefit wherein small business owners can control the cost of their health benefits offering. To set up a Section 105 MERP, your company should:

- Cancel your group health insurance plan (if you have one).
- Define any amount you can afford for health benefits.
- Use a Personalized Benefits automation software to give each employee a fixed dollar amount to use on health insurance.

Through the MERP, employees use their allowance to purchase their own policies on the individual market.

MERPs give small businesses complete control of benefits while giving employees choice and a valued benefit. Additionally, MERPs allow small businesses to take advantage of new health reform opportunities.

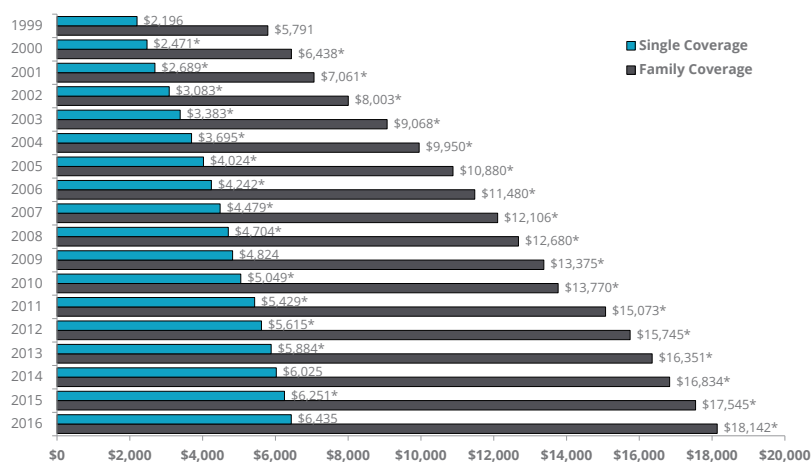


Rising costs of health care

The cost of health care for small businesses is not sustainable.

Group health insurance premium rates for single coverage increased 193 percent from 1999 to 2016, and 213 percent for family coverage. The cost continues to rise faster than wages and inflation.

Average Annual Premiums for Single and Family Coverage, 1999-2016



Average employer cost for one year of health insurance in 2016:

Single employee: \$5,306

Family: \$12,865

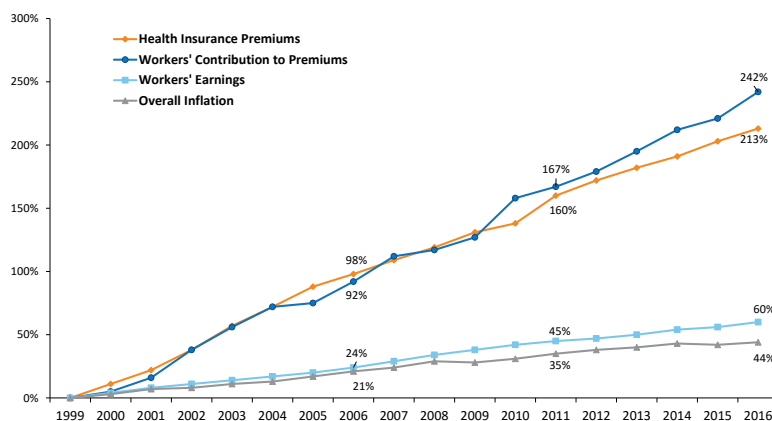
Kaiser Family Foundation, 2016.

* Estimate is statistically different from estimate for the previous year shown (p < .05).

SOURCE: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2016.



Cumulative Increases in Health Insurance Premiums, Workers' Contributions to Premiums, Inflation, and Workers' Earnings, 1999-2016

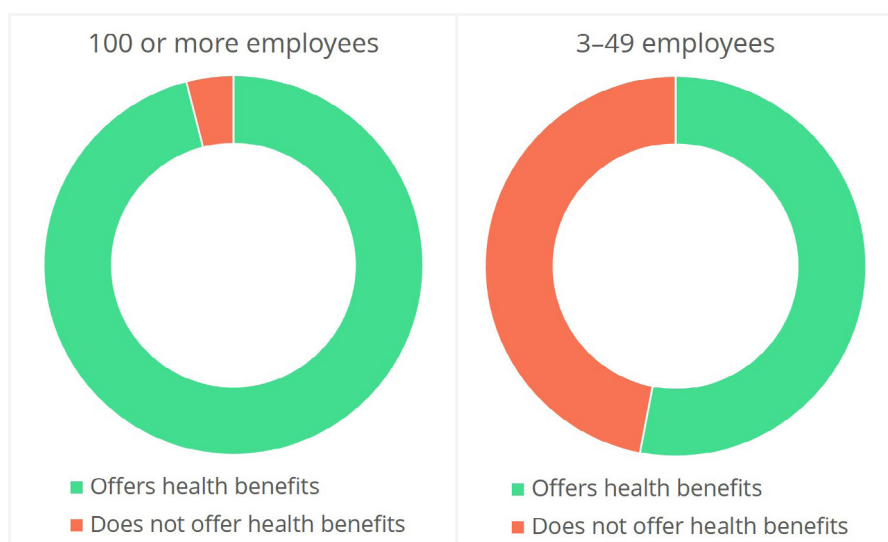


SOURCE: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2016. Bureau of Labor Statistics, Consumer Price Index, U.S. City Average of Annual Inflation (April to April), 1999-2016; Bureau of Labor Statistics, Seasonally Adjusted Data from the Current Employment Statistics Survey, 1999-2016 (April to April).



Small businesses have been hit the hardest

In 2016, a full 96 percent of employers with 100 or more employees provided health benefits for their employees. However, only 53 percent of employers with three to 49 employees provided health benefits, down from 66 percent in 2000. (The Kaiser Family Foundation, 2016.)



How has health reform helped small businesses?
See Appendix A: Health reform and new opportunities for small businesses.



What is a Section 105 Medical Expense Reimbursement Plan?

Overview of Section 105 Plans

A Section 105 Plan allows a business to reimburse employees for health insurance expenses. A common type of Section 105 Plan is a self-funded (or self-insured) health plan, where the employer self-funds (or self-insures) health benefits rather than pay premiums to an insurance company.

Section 105 Plans are also frequently found in the form of Medical Expense Reimbursement Plans (MERPs). With a Section 105 MERP, a small business would either:

1. Implement a Section 105 plan alongside a conventional group health insurance plan (to reimburse deductible amounts not covered by insurance). This is also called an Integrated Health Reimbursement Arrangement (HRA), linked HRA, or deductible HRA.
2. Implement a Section 105 plan as a stand-alone medical reimbursement plan, used to reimburse employees for individual health insurance premiums. As of 2016, companies with fewer than 50 employees can use a type of MERP, the [Qualified Small Employer HRA \(QSEHRA\)](#), to reimburse employee premiums, copays, deductibles, and expenses.

In this guide, we are referring to a Section 105 MERP used as a stand-alone health benefit.

With this type of Section 105 Plan, a small business does not offer a group health insurance. Rather, the Section 105 MERP is the entire health benefit.



Stand-alone Section 105 MERP: The basics

A Section 105 MERP is:

- An IRS-approved Section 105 self-insured ERISA plan
- 100 percent employer funded
- Tax deductible to the business and tax-free to employees

Section 105 MERPs, like the QSEHRA, are not health insurance. Rather, they are a vehicle for small businesses to reimburse employees for individual health insurance and medical expenses.

A notional arrangement

With a Section 105 MERPs, no funds are expensed until reimbursements are paid. The business reimburses employees directly through payroll, check, or other method.

Flexible and employer controlled

With a Section 105 MERP, the small business designs and controls nearly every aspect of the plan through legal plan documents, which include:

- Amount of allowances
- Who is covered (employee and dependents, or just employee)
- Employee eligibility criteria (hours worked, waiting period, etc.)

Section 105 MERPs are an IRS-approved and -compliant employee health benefits plan.



Section 105 MERPs are like business expense accounts for individual insurance and medical costs.



4 advantages of MERPs for small businesses

1. Predictable costs

With a Section 105 Plan, the business determines their maximum liability when setting plan funding amounts.

- The company doesn't disburse funds until an employee incurs an expense.
- When the employee leaves the company, accrued funds stay with the company.

Tip: If your business can contribute any amount to employees' health benefits, you can afford a Section 105 Plan. There is no minimum contribution requirement.

How? Your company can contribute any amount up to the federal allowance caps.

2. Employee choice

With a Section 105 Plan, employees choose any type of insurance plan from any carrier.

On average, individual health insurance plans are 20 to 60 percent less expensive than group health coverage for the same type of plan. The small business sees their health benefit dollars go further.

Additionally, Section 105 Plans encourage consumer-driven spending. When employees see the cost of health care, they become smarter health care consumers.

Another advantage: Individual health insurance plan choices and



affordability has expanded greatly with health reform. See Appendix A: Health reform and new opportunities for small businesses (page 11).

3. Tax advantages

Small businesses may deduct the cost of a Section 105 Plan as a business expense under IRS Code Section 162. Reimbursements to employees are pretax dollars, so the reimbursements are tax-free to employees as well, provided they have major medical insurance. Even if they don't, they can still receive reimbursements—they should just report their reimbursement amounts as part of their gross income at the end of the year.

4. Easy administration

Typically, small business owners are not health insurance experts, nor do they want to spend valuable time gaining expertise. With limited resources, the time spent comparing policies, dealing with questions or complaints, and managing the plan falls on the business owner or other key staff. This is valuable time that could be spent growing the business.

By using [Personalized Benefits automation software](#) like PeopleKeep to administer a Section 105 MERP, administration becomes as simple as wages. The business simply adds approved reimbursements to employees' paychecks. Once set up, plan administration takes 5 minutes a month.



Frequently asked questions

Can I administer the Section 105 MERP myself?

A small business can self-administer its own Section 105 MERP, but failure to comply with the minimum federal administration requirements is common without utilizing proper Personalized Benefits automation software. If a small business does not utilize proper administration software to fully comply with Section 105, ERISA, HIPAA, COBRA, and ACA regulations, the administrative cost usually outweighs the benefits. Fines for not complying with these regulations are steep.

Can I pay for employees' insurance premiums without a Section 105 MERP?

Some businesses might want to pay directly for an employee's individual health insurance plan without utilizing an ERISA and HIPAA-compliant platform, but doing so would put the business out of compliance with federal regulations, and may increase the business's (and employees') tax liability ([read more here](#)).

Can a small business owner participate in a Section 105 Plan?

Yes, a small business owner can and should participate in the business's Section 105 MERP. However, whether or not owners are eligible to receive reimbursements 100 percent tax-free depends on how the company files taxes, and the owner's status.

- **C-corporation owners:** C-corp owners may participate in a



Section 105 MERP and receive all reimbursements 100 percent tax-free.

- **Sole proprietors, partners, or S-corp shareholders that own greater than 2 percent of the company's shares:** These non-C-Corp owners can use a Personalized Benefits automation software to reimburse and track medical expenses. However, all reimbursements must be reported on the owners'/partners' wages (on their W-2 and 1040 forms) and are subject to federal income taxes, although exceptions exist if the spouse is also a W-2 employee. See our [infographic on employer eligibility](#).



How to implement a Section 105 MERP

4 easy steps

1. Complete plan setup and generate plan documents

- Complete plan setup with your Personalized Benefits automation software provider.
- Download/print required Plan Documents; sign for your business's records.

2. Enroll employees

- Enroll eligible employees online.
- Send Welcome Kits to employees (electronically or printed packets).

3. Employees choose plans and request reimbursement

- Employees choose a health plan online or through a Broker or the Health Insurance Marketplace.
- Employees submit reimbursement requests to a Personalized Benefits automation software.

4. Reimburse employees via payroll

- Once reimbursement requests are approved by Section 105 Software provider, the business simply reimburses employees tax-free via payroll... just like a business expense reimbursements.

Get a free demo of our Personalized Benefits automation software



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Appendix A: Health reform and new opportunities for small businesses

Health reform: A major change in 2016

With major Affordable Care Act (ACA) laws now fully in effect, health reform represents the biggest change in how small businesses offer health benefits, and how employees purchase health insurance. The most important recent change for small businesses was enacted as part of the 21st Century Cures Act.

The Small Business Healthcare Relief Act

The Small Business Healthcare Relief Act (SBHRA) is federal legislation that restores Stand-Alone Health Reimbursement Arrangements (HRAs), a type of MERP, for small employers effective January 1, 2017.

Signed into law in December 2016, the SBHRA ensures small business owners can use HRAs to assist employees with out-of-pocket health insurance and medical costs.

What the SBHRA does for small business

Effective January 1, 2017, the SBHRA introduces a Personalized Benefit called the Qualified Small Employer Health Reimbursement Arrangement (QSEHRA), also known as a Small Business HRA, that

- allows small employers to use tax-advantaged funding to assist employees with their out-of-pocket health insurance and related medical costs, and



- provides exemptions from current ACA compliance requirements and associated penalties.

The SBHRA provides relief on multiple fronts to small business employers by expanding affordable health care options, easing the burden of health care-related administration, and helping employers to remain competitive for purposes of hiring and keeping their people.

Additionally, the SBHRA benefits employees by affording them the flexibility and cost savings to personally choose the most appropriate health plan for their unique health care needs on the individual market.

How it works

- The HRA is available to small employers (with fewer than 50 full-time employees) who do not offer a group health plan to any of their employees.
- Small employers can use the HRA to reimburse employees tax-free for individual health insurance premiums and other out-of-pocket medical costs.
- Employer yearly contributions are capped at \$4,950 for self-only and \$10,000 for families. HRAs are 100 percent employer-funded; employees cannot contribute.
- Participants are not required to have minimum essential coverage (MEC) to receive HRA reimbursements. However, participants with MEC will receive reimbursements tax-free.
- Employees with a Small Business HRA may access premium tax credits; however, if an employee is eligible for a premium tax credit, their credit will be reduced by their allowance amount.



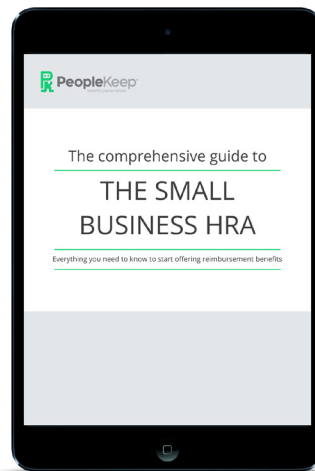
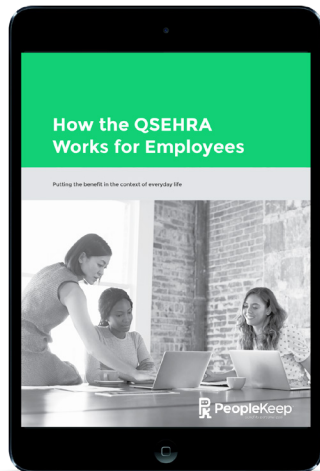
- Generally, an employer must make the same HRA contributions for all eligible employees; however, amounts may vary based on family status.

Would a QSEHRA or other Personalized Benefit MERP work for your company? Get a free benefits consultation.



Additional health benefits tools and resources

Our suite of free, in-depth materials can help you research the best benefits option for your business.



Explore our full library at www.peoplekeep.com/resources.



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