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LFN 2011-34

November 23, 2011

Local Finance Notice

2011 Health Benefit Reform Supplemental Guidance

This Local Finance Notice provides local units supplemental guidance on implementing the health care reforms enacted in P.L. 2011, c.78. It summarizes and supplements Notice 2011-20R which replaced Notice 2011-20. Local officials responsible for human resource or payroll administration are obligated to carefully review the revised Local Finance Notice 2011-20R. Both this Notice and 2011-20R should be shared it with other appropriate local officials.

The Division may issue further guidance, and interested parties should check the Division's website periodically for updates. Additional guidance will be issued through the Division's GovConnect system and through DLGS E-Mail News.

Employee Contributions

The following guidance is provided to all local units concerning when the employee health benefit contribution takes effect:

- As of 6/28/11 the minimum health benefits contributions established under Section 39 are not negotiable or locally set for four years, or four years from the expiration of any contracts in effect on 6/28/11.
- All employees receiving health benefits will contribute to the cost of health benefits, sooner or later.
- The employee health benefit contribution takes effect:
  - Immediately (subject to necessary administrative actions for collection being implemented by the employer) when a CNA expired before 6/28/11 and a successor agreement had not been agreed to; or,
  - As soon as a CNA that was in effect on the effective date expires.

  The fact that a successor CNA of an expired contract may have been negotiated or was in some stage of approval (including pending or interest arbitration awards that were not implemented) or a successor agreement for a contract that expired after June 28 was approved and ready for implementation, has no impact on required health benefit contributions. In these cases, the c.78 health care contributions take effect immediately.
- When a contract that requires a health benefits contribution higher than c.78 expires, the contract provision remains in effect until a subsequent contract amends or removes it, or until the c.78 requirement is greater.
- When a CNA that was in effect on 6/28 expires or is in almost any way modified, the contribution required by section 39 is phased in at 25% a year.

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Existing Employment

The date the c.78 contribution commences varies; it is on the effective date for employees not under a CNA and the day after a CNA ends for CNAs in effect on June 28, 2011. Employees employed on the date the health care contribution commences are subject to a four year phase-in of the full contribution amount. The following describes employment circumstances that may affect whether the phase-in applies to certain employees.

An employee is someone who appears on the employer's regular payroll and receives a salary or wages. (N.J.S.A. 52:14.-17.26). An existing employee includes:

- An employee who has not been formally terminated, but continues to receive employer-paid benefits while not receiving salary and has rights to return.
- 10-month school employees who continue to receive employer-paid health benefits over the summer until employment resumes in September.
- Employees receiving worker compensation benefits.
- Employees on voluntary unpaid leave who have rights to return and who maintain health benefits through COBRA payments.

Conversely, an employee is not an existing employee when terminated for economic reasons and the determination to return is the employer's, not the employee's, notwithstanding that the employee makes COBRA payments. Similarly, an employee who ceases employment over the summer and there is a formal break in the employment relationship, i.e., the employee receives unemployment compensation, would not be treated as an existing employee.

The employer needs to review the individual circumstances involved for each employee and make decisions based on those facts. In these cases, if the employee is represented by a collective negotiations agreement, a dispute over the employer's action on the matter may be the subject of an appropriate filing with the Public Employment Relations Commission.

Individual Employee Agreements

Employees with individual employment agreements begin phasing in c.78 of the effective date (and subject to implementation), unless local legal counsel determines that, under the facts and circumstances of the particular IEA, applying c.78 would result in an impermissible contract impairment.

Employees Changing Organizations

If an employee is transferred or assigned to another government employer through an agreement between employers (i.e., shared services, inter-government transfer, service consolidation, etc.), and the work being performed is effectively continuous, the change would not trigger a break in employment and the employee would not be treated as a new employee for c.78 purposes.

Calculation of Premiums for Self-Insured Programs

An employer that provides a benefit on a self-insured basis must develop a premium or periodic charge for each self-insured benefit provided to employees in order to calculate the total benefit costs under section 39. The calculation guidance under "Impact on Local Unit Self Insurance Programs" in Section 2 of LFN 2011-20R continues to apply for the calculation or premiums or periodic charges.

Inclusion in Cost of Benefits

Employer contributions toward employee benefits that are insurance policies, such as long-term care, or disability policies are not included in the non-SHBP/SEHBP cost of coverage.

"Reopening" of Contracts

Chapter 78 (sections 40-42) requires that any "extension, alteration, re-opening, amendment, or other adjustment to a CNA" in effect or expired on 6/28/11 is treated as a new CNA, requiring immediate implementation of c.78. Questions have been raised about the impact of this clause on circumstances such as adding new job titles and setting their wage rates, agreeing to continue previously negotiated sidebar agreements that may be expiring in ongoing contracts, or negotiate concessions to avoid layoffs.

While guidance on such individual circumstances cannot be provided by State agencies, they should be addressed by the legal advisors of the parties based on their particular circumstances and contract language.

Employees who are on Workers' Compensation, Disability or Family Leave

During the period in which they are not actively at work, these employees should continue to contribute as if they were receiving their regular salary. The appropriate health care contribution method and amount under c. 2, c. 78 or a greater local contribution requirement would continue based on their pre-leave salary. All adjustments to the contribution amount, due to increased coverage costs or employee salary changes, would take effect as if the employee continued in active service.

Supplemental Information on Section 125 Plan Issues

Pre-Funding Flexible Spending Accounts

All public employers must now establish Section 125 Flexible Spending Accounts to allow employees the option of using pre-tax dollars to satisfy their required contributions to health benefits costs under c. 78, PL 2011. See Local Finance Notice 2011-20R for basic information about these plans and complying with the statute.

Local employers need to be aware that a Flexible Spending Account may require an employer to pre-fund a portion of the employee accounts at the inception of the program and annually at the beginning of each plan/budget year. The pre-funding is necessary to have funds available to pay/reimburse claims during the initial period until employee salary deductions are sufficient to pay these claims. IRS rules require that the full amount of an employee's annual deduction be available for use at any time as of the first day of the plan/budget year, regardless of the amount actually contributed by the employee. The employer is not required to actually fund the entire annual amount for each employee, only to

provide an amount to cover anticipated claims during the initial period. It is unlikely that many, if any, employees will require the full amount of their annual contribution early during the coverage period. An initial amount may be repaid by the plan provider once sufficient funds are accumulated through the deduction process. Regardless, in the event the program needs pre-funding, an interfund transfer is the appropriate method of providing the short-term funding for the program to be operational. The transfer should be reversed once the fund achieves a level sufficient to maintain itself.

At the employer's discretion, the plan may include a grace period of up to two and a half months after the end of the plan year. If there is a grace period, any qualified medical expenses incurred during that period can be paid from any amounts left in the employee's account at the end of the previous year. At the end of the plan/budget year the employer retains the unexpended balance of the employees' contributions. These monies can be used in the subsequent year as pre-funding to cover the initial expenses of that year allocated to pay the employer's administrative costs, or to recoup the pre-funding amount advanced at the start of the year. The employer is not permitted to refund any remaining balance to the employees. It is important to note that the full amount of an employee's annual contribution can be used at any point in the year. If this occurs during the initial period, the entire amount could be claimed. If the employee does not return to work or is terminated, he does not have to repay the money to the employer.

Under the FSA (and the Premium Option Plan that is also required by c. 78), both the employee and the employer benefit from the pre-tax treatment of the monies. Payroll taxes (Federal Income Tax, Social Security Tax and Medicare) are not paid on the portion of salary deposited into the FSA. The means the employer appropriation for FICA and related taxes can be reduced by the taxes that would otherwise accrue to the employer by the anticipated FSA deductions for the year.

Together, the retained balance at the end of the plan year, plus the savings in employer payroll tax obligation is expected to offset the costs of providing the plan and any losses from employees who use their entire contribution and terminate employment prior to the end of the year. Based on this, the law anticipates that the employer will bear the costs of providing the plan.

Domestic Partners and Civil Union Partners under Section 125 Plans

The Section 125 Plan allows the employee to use pre-tax dollars to receive health benefits for themselves and their spouses or other dependents. However, the Internal Revenue Code does not recognize Domestic Partners and Civil Union Partners in the same way as a spouse and does not automatically recognize them as dependents for tax purposes. Accordingly, the cost of coverage for a civil union partner or domestic partner may be subject to federal taxation and the employer would be required to withhold federal income tax, Social Security and Medicare taxes on its value.

See Internal Revenue Service Publication 503 – Child and Dependent Care Expenses for detailed information about dependent status for federal tax purposes.

Affected employees and local employers, whether participants in the State Health Benefits and School Employee Health Benefits Plans or not, should also review the appropriate sections of SHBP Fact Sheet #71 (Domestic Partners) and Fact Sheet #75 (Civil Union Partners) for additional information on the taxation of health benefits. While directed to SHBP participants, the tax implications also apply to non-SHBP employee and employer use of Section 125 Plans and coverage provided for Civil Union or Domestic Partners.

Employees may also wish to consult a tax professional for advice regarding the qualification of a Civil Union Partner or Domestic Partner as a dependent.

Approved: Thomas H. Neff, Director, Division of Local Government Services

Table of Web Links

Page	Shortcut text	Internet Address
1	DLGS E-Mail News	http://www.nj.gov/dca/lgs/dlgs-newssubscribe.shtml
3	Local Finance Notice 2011-20R	http://www.nj.gov/dca/lgs/lfns/11lfns/2011-20R.doc
4	IRS Publication 503	www.irs.gov\pub\irs-pdf\p503.pdf
5	Fact Sheet #71 (Domestic Partners)	www.state.nj.us/treasury/pensions/epbam/exhibits/factsheets/fact71.pdf
5	Fact Sheet #75 (Civil Union Partners)	www.state.nj.us/treasury/pensions/epbam/exhibits/factsheets/fact75.pdf

Appendix A – Definition of "employee"

(pertinent part in italics)

§ 52:14-17.26. Definitions relative to health care benefits for public employees

As used in this act [*C.52:14-17.25* et seq.]:

…

(c) (1) The term "employee" means an appointive or elective officer, a full-time employee of the State of New Jersey, or a full-time employee of an employer other than the State who appears on a regular payroll and receives a salary or wages for an average of the number of hours per week as prescribed by the governing body of the participating employer which number of hours worked shall be considered full-time, determined by resolution, and not less than 20.

(2) After the effective date [May 21, 2010] of P.L.2010, c.2, the term "*employee" means (i) a full-time appointive or elective officer whose hours of work are fixed at 35 or more per week, a full-time employee of the State, or a full-time employee of an employer other than the State who appears on a regular payroll and receives a salary or wages for an average of the number of hours per week as prescribed by the governing body of the participating employer which number of hours worked shall be considered full-time, determined by resolution, and not less than 25, or (ii) an appointive or elective officer, an employee of the State, or an employee of an employer other than the State who has or is eligible for health benefits coverage provided under P.L.1961, c.49 (C.52:14-17.25 et seq.) or sections 31 through 41 of P.L.2007, c.103 (C.52:14-17.46.1 et seq.) on that effective date and continuously thereafter provided the officer or employee is covered by the definition in paragraph (1) of this subsection*. For the purposes of this act an employee of Rutgers, The State University of New Jersey, shall be deemed to be an employee of the State, and an employee of the New Jersey Institute of Technology shall be considered to be an employee of the State during such time as the Trustees of the Institute are party to a contractual agreement with the State Treasurer for the provision of educational services. The term "employee" shall further mean, for purposes of this act, a former employee of the South Jersey Port Corporation, who is employed by a subsidiary corporation or other corporation, which has been established by the Delaware River Port Authority pursuant to subdivision (m) of Article I of the compact creating the Delaware River Port Authority (*R.S.32:3-2*), as defined in section 3 of P.L.1997, c.150 (*C.34:1B-146*), and who is eligible for continued membership in the Public Employees' Retirement System pursuant to subsection j. of section 7 of P.L.1954, c.84 (*C.43:15A-7*).

For the purposes of this act the term "employee" shall not include persons employed on a short-term, seasonal, intermittent or emergency basis, persons compensated on a fee basis, persons having less than two months of continuous service or persons whose compensation from the State is limited to reimbursement of necessary expenses actually incurred in the discharge of their official duties, provided, however, that the term "employee" shall include persons employed on an intermittent basis to whom the State has agreed to provide coverage under P.L.1961, c.49 (*C.52:14-17.25* et seq.) in accordance with a binding collective negotiations agreement. *An employee paid on a 10-month basis, pursuant to an annual contract, will be deemed to have satisfied the two-month waiting period if the employee begins employment at the beginning of the contract year.* The term "employee" shall also not include retired persons who are otherwise eligible for benefits under this act but who, although they meet the age or disability eligibility requirement of Medicare, are not covered by Medicare Hospital Insurance, also known as Medicare Part A, and Medicare Medical Insurance, also known as Medicare Part B. A determination by the commission that a person is an eligible employee within the meaning of this act shall be final and shall be binding on all parties.