

Pretax Benefits: Access to Section 125 Cafeteria Benefits and Health Savings Accounts in the United States, Private Industry

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In an effort to attract and retain employees, employers provide compensation packages that include wages and benefits. Benefits that are paid for by the employer generally are not taxable to the employee. If benefits, such as group life insurance, are paid for by the employee, generally the money used to pay for the benefits is taxable. In recent years, tax laws have been created that permit certain benefits--such as defined contribution (401(k)) retirement benefits, [section 125 cafeteria benefits](#), and health savings accounts--to be paid for with pretax money. Pretax benefits enable both employers and employees to set aside money on a tax-free, salary-reduction basis for retirement expenses as well as for qualified dependent care and healthcare expenses. As employers seek to keep the costs of employee benefits under control, and employees seek to maximize their take-home pay, pretax benefits have become more prevalent.¹

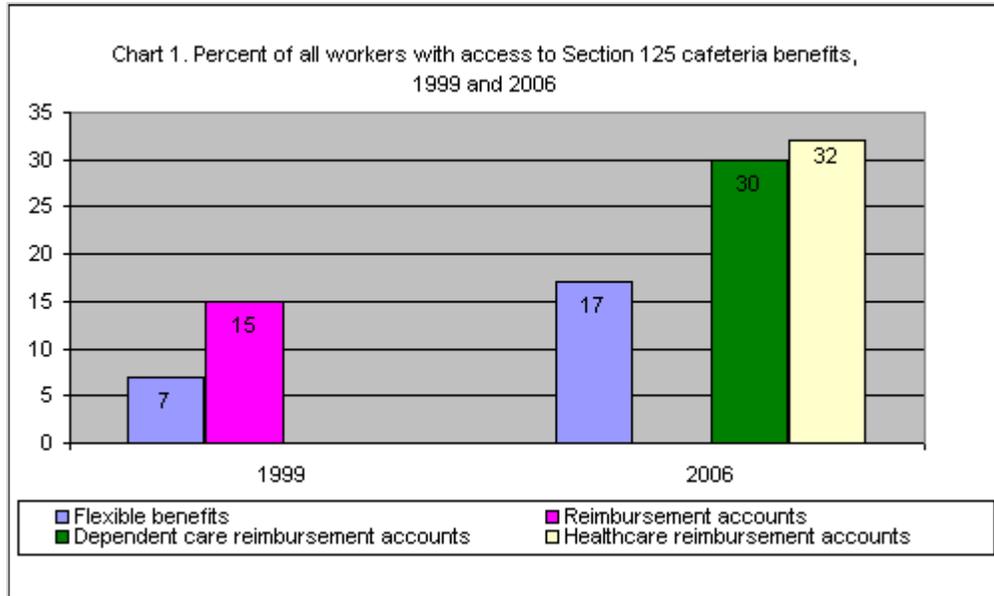
The [National Compensation Survey \(NCS\)](#) collects and publishes data on employee access² to a number of pretax benefits, including three types of section 125 cafeteria benefits: flexible benefits plans and two types of reimbursement accounts (also called flexible spending accounts)--*dependent care reimbursement accounts* and *healthcare reimbursement accounts*. The NCS also collects and publishes data on employee access to health savings accounts.³

[Flexible benefits](#) enable employers to offer benefit plans that allow employees to select from different plan options according to their needs. Employees can select benefits that are of most value to them and forgo those benefits that are less important to them. For example, an employee who already is covered by a spouse's health benefit plan might choose only vision or dental coverage from her employer; or a dual-earner family in which both the husband and wife are employed might require funds to pay for childcare, which may not be covered by a one-size-fits-all benefits package.⁴

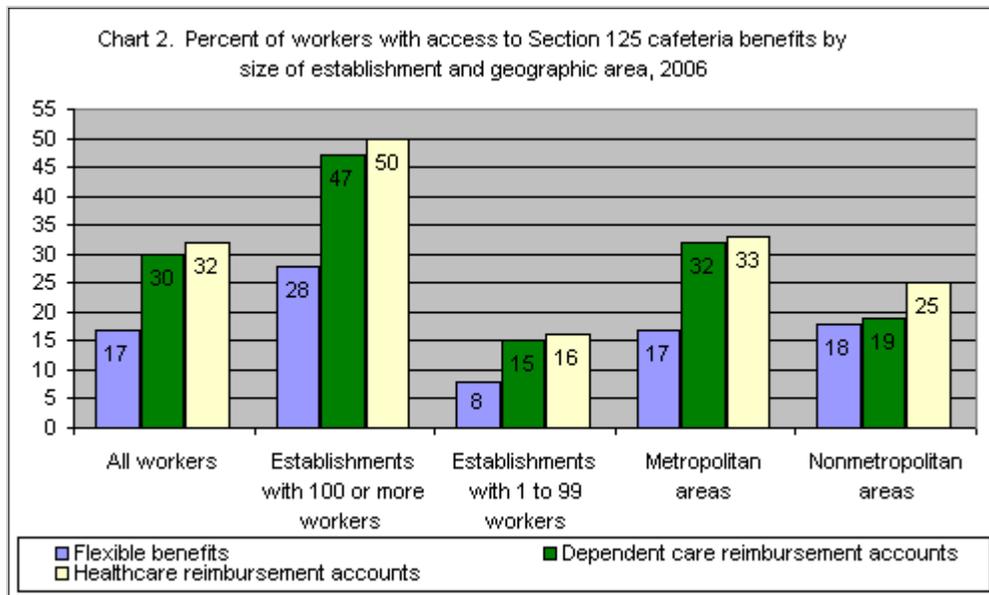
Dependent care reimbursement accounts set aside money to be used to pay for expenses including childcare, eldercare, or services to a disabled dependent. *Healthcare reimbursement accounts* set aside money to be used to pay for out-of-pocket medical expenses including deductibles, co-payments, and other healthcare costs not covered by health insurance. Reimbursement account benefits can be part of a flexible benefits package, or they can stand alone.

Health savings accounts allow employees to set aside money to pay for future medical expenses. Health savings accounts must be offered along with a high-deductible health insurance plan. Other features of health savings accounts include the rollover of unused contributions, the portability of accounts, and tax-free interest.

The charts below show the percent of all workers with access to employer-provided section 125 cafeteria benefits as follows: flexible benefits and reimbursement accounts as a whole in 1999; and flexible benefits, dependent care reimbursement accounts, and healthcare reimbursement accounts in 2006. The charts also show the percent of all workers with access to health savings accounts in 2005 and in 2006. Furthermore, the charts show the 2006 access rates for selected groups of employees for section 125 cafeteria benefits and for health savings accounts.

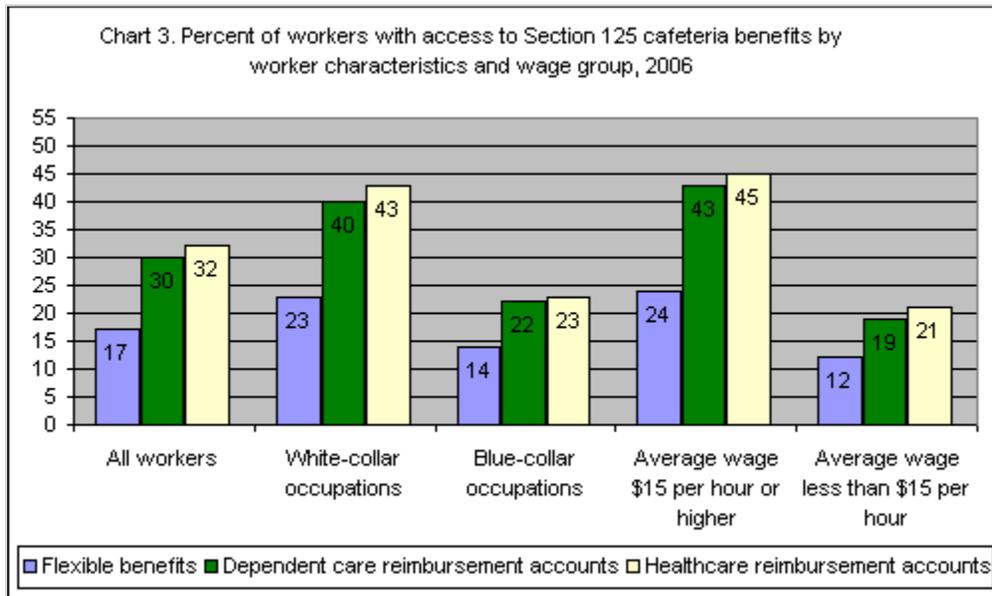


- Chart 1 shows that in 1999 employee access to section 125 cafeteria benefits for all workers was 7 percent for flexible benefits and 15 percent for reimbursement accounts as a whole; and in 2006 employee access was 17 percent for flexible benefits, 30 percent for dependent care reimbursement accounts, and 32 percent for healthcare reimbursement accounts.
- In 2006, the least prevalent section 125 cafeteria benefit was flexible benefits. Dependent care and healthcare reimbursement accounts were more prevalent. This pattern holds true for all worker groups. As can be seen in charts 2 and 3, however, among different worker groups the rates of access varied widely.

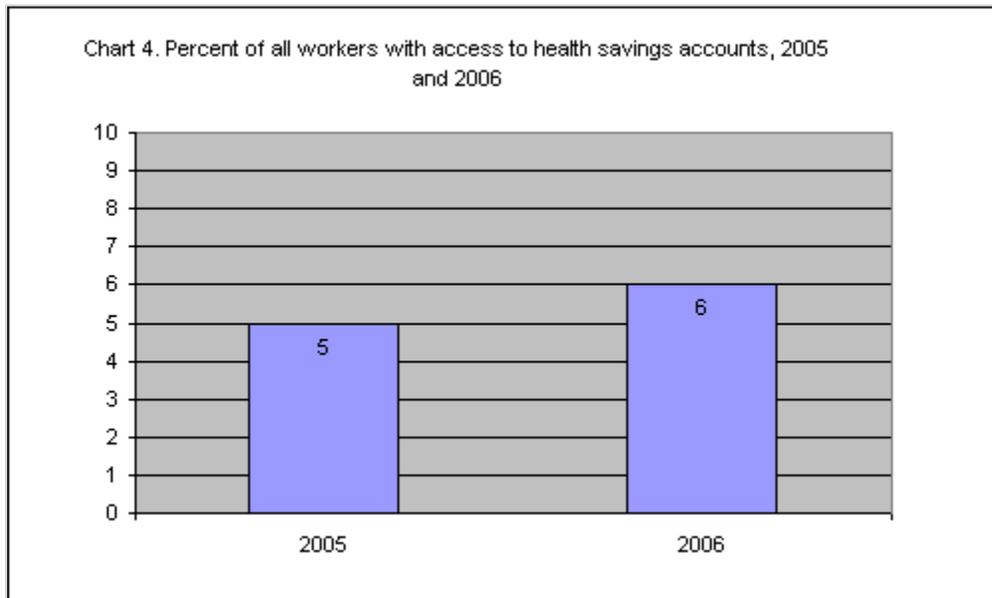


- Chart 2 shows that employees who worked in establishments with 100 or more employees had relatively high rates of access to each of the three section 125 cafeteria benefits--flexible benefits, dependent care reimbursement accounts, and healthcare reimbursement accounts--while employees who worked in establishments with fewer than 100 employees had relatively low rates of access.
- Chart 2 also shows that workers who were employed in metropolitan areas had access to flexible benefits at about the same rates as those employed in nonmetropolitan areas; however, workers in metropolitan areas had higher rates of

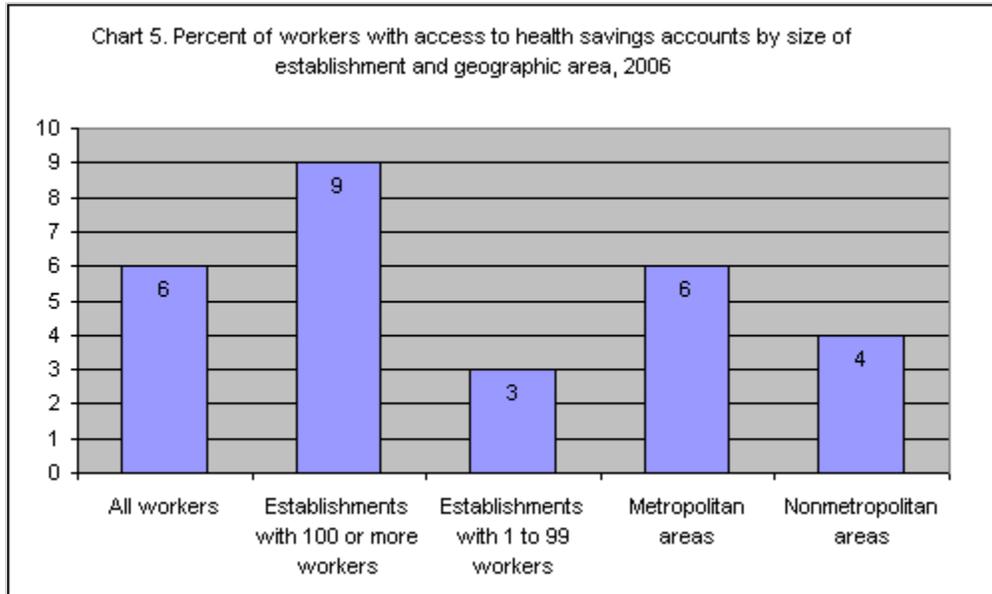
access to dependent care reimbursement accounts and to healthcare reimbursement accounts than did workers in nonmetropolitan areas.



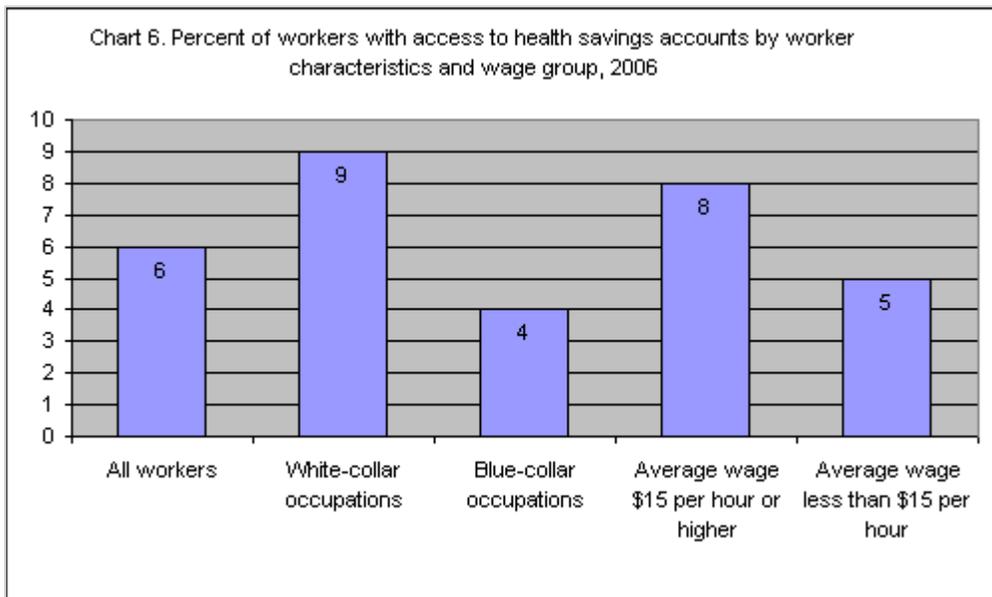
- Chart 3 shows that white-collar workers had access to section 125 cafeteria benefits at about the same rates as workers earning \$15 or more per hour, and that blue-collar workers had access at about the same rates as workers earning less than \$15 per hour.



- Chart 4 shows that employee access to health savings accounts for all workers was 5 percent in 2005 and 6 percent in 2006.



- Chart 5 shows that, in 2006, 9 percent of employees who worked in establishments with 100 or more employees had access to health savings accounts, while 3 percent of employees who worked in establishments with 1 to 99 workers had access to such accounts.
- Chart 5 also shows that 6 percent of workers who worked in metropolitan areas had access to health savings accounts and that 4 percent of workers in nonmetropolitan areas had access to such accounts.



- Chart 6 shows that 9 percent of white-collar workers and 4 percent of blue-collar workers had access to health savings accounts; and 8 percent of workers earning \$15 or more per hour and 5 percent of workers earning less than \$15 per hour had access to health savings accounts.

NOTE: Standard errors have not been calculated for NCS benefits estimates. Consequently, none of the statistical inferences made in this report could be verified by a statistical test.

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Notes

1 Ron Polaniecki, "Big Savings," *Credit Union Management*, August 2005, pp. 54-56.

2 As defined by the National Compensation Survey, an employee has access to a benefit plan if the employee is in an occupation that is offered the plan. By definition, either all employees in an occupation have access to a benefit or none has access.

3 The advent of section 125 cafeteria benefits dates to the Tax Reform Act of 1978. Section 125 cafeteria benefits are subject to section 125 of the Internal Revenue Code. For more information, see Title 26 of the Internal Revenue Code, on the Internet at http://www.gpo.gov/uscode/title26/subtitlea_chapter1_subchapterb_partiii_.html. The advent of health savings accounts dates to The Medicare Prescription Drug, Improvement, and Modernization Act of 2003. The Tax Relief and Health Care Act of 2006 provided additional health savings account benefits. At the time of this writing, health savings accounts are subject to Revenue Procedure 2006-53. See 26 CFR 601.602: Tax forms and instructions; on the Internet at <http://www.ustreas.gov/offices/public-affairs/hsa/pdf/rp-2006-53.pdf>.

4 Joseph R. Meisenheimer II and William J. Wiatrowski, "Flexible Benefit Plans: Employees Who Have a Choice," *Monthly Labor Review*, December 1989, pp. 17-22; on the Internet at <http://www.bls.gov/opub/mlr/1989/12/art3abs.htm>.

Data for Chart 1. Percent of all workers with access to Section 125 cafeteria benefits, 1999 and 2006

| | 1999 | 2006 |
|---------------------------------------|------|------|
| Flexible benefits | 7 | 17 |
| Reimbursement accounts | 15 | |
| Dependent care reimbursement accounts | | 30 |
| Healthcare reimbursement accounts | | 32 |

Data for Chart 2. Percent of workers with access to Section 125 cafeteria benefits by size of establishment and geographic area, 2006

| | Flexible benefits | Dependent care reimbursement accounts | Healthcare reimbursement accounts |
|---|-------------------|---------------------------------------|-----------------------------------|
| All workers | 17 | 30 | 32 |
| Establishments with 100 or more workers | 28 | 47 | 50 |
| Establishments with 1 to 99 workers | 8 | 15 | 16 |
| Metropolitan areas | 17 | 32 | 33 |
| Nonmetropolitan areas | 18 | 19 | 25 |

Data for Chart 3. Percent of workers with access to Section 125 cafeteria benefits by worker characteristics and wage group, 2006

| | Flexible benefits | Dependent care reimbursement accounts | Healthcare reimbursement accounts |
|--------------------------------------|-------------------|---------------------------------------|-----------------------------------|
| All workers | 17 | 30 | 32 |
| White-collar occupations | 23 | 40 | 43 |
| Blue-collar occupations | 14 | 22 | 23 |
| Average wage \$15 per hour or higher | 24 | 43 | 45 |
| Average wage less than \$15 per hour | 12 | 19 | 21 |

Data for Chart 4. Percent of all workers with access to health savings accounts, 2005 and 2006

| | 2005 | 2006 |
|-------------------------|------|------|
| Health savings accounts | 5 | 6 |

Data for Chart 5. Percent of workers with access to health savings accounts by size of establishment and geographic area, 2006

| | Health savings accounts |
|---|-------------------------|
| All workers | 6 |
| Establishments with 100 or more workers | 9 |
| Establishments with 1 to 99 workers | 3 |
| Metropolitan areas | 6 |
| Nonmetropolitan areas | 4 |

Data for Chart 6. Percent of workers with access to health savings accounts by worker characteristics and wage group, 2006

| | Health savings accounts |
|--------------------------------------|-------------------------|
| All workers | 6 |
| White-collar occupations | 9 |
| Blue-collar occupations | 4 |
| Average wage \$15 per hour or higher | 8 |
| Average wage less than \$15 per hour | 5 |