



***Retirement and Insurance Service
Benefits Administration Letter***

Number: 00-215

Date: August 24, 2000

Subject: *Pre-Tax Payment of FEHB Insurance Premiums (Premium Conversion)*

Starting with the first pay period that begins on or after October 1, 2000, most Federal employees in the Executive Branch will see an increase in their take-home pay. That's because the U.S. Office of Personnel Management (OPM), in cooperation with Departments and Agencies, has implemented premium conversion for Federal employees. This Benefits Administration Letter (BAL) provides you with the information and guidance you need to implement and administer this new pre-tax benefit.

Payroll Office Letter P-00-13 dated July 13, 2000 includes information and instructions needed by payroll offices as they adapt their systems for premium conversion by October 1. Benefits Officers should focus their attention on the few minor changes in Federal Employees Health Benefits Program rules that are explained under "What's Different?" below.

We have received questions about the effect of premium conversion on Social Security. This Letter and the information on our web site will allow you and your employees to see the effects of premium conversion. Nonetheless, employees have a right to waive the benefits of premium conversion. This is a personal decision. We can tell you in advance, however, that the vast majority will not waive, because premium conversion will be a "no-brainer."

We have created a series of questions and answers on our website: www.opm.gov/insure/health/pretaxfehb. This site is the first and best source for up-to-date information on premium conversion. We encourage you and your employees to check it for updates periodically. If you do not find the answer to your question, please email us at fehb@opm.gov. We will respond to all your questions, as well as update the web site as needed.

*Civil Service
Retirement
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*Federal Employees
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*Federal Employees
Health Benefits
Program*

*Federal Employees
Retirement
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Enclosures to this document include:

- "Good News!", a sample handout with information for employees;
- a " Premium Conversion Financial Worksheet," with instructions for employees on how to compute their tax savings and to estimate the effect of premium conversion on Social Security benefits; and
- a sample "Premium Conversion Waiver/Election Form" template. The actual template is available on our web site. You should modify the waiver form template (for example, putting your agency logo in the upper left corner, etc.) and locally reproduce the document.

What's Different?

For the most part, it's business as usual. We have received a number of questions from payroll and personnel offices that are under the false impression that premium conversion has changed many of the rules affecting the FEHB and premium deductions. Only a few situations change under premium conversion:

Beginning with the first pay period that begins on or after October 1, the deduction for FEHB premium will be the amount converted to pre-tax. This includes deductions for retroactive coverage, payback of premiums from a prior period of LWOP and other adjustments.

Except during open season, an employee participating in premium conversion will not be allowed to cancel coverage or change from self and family to self only unless the cancellation or change is due to a "qualifying life event" and the request is filed timely.

An agency may, but is not required to, offer an employee the option to pre-pay FEHB premiums prior to beginning a period of Leave Without Pay (LWOP). We expect that few agencies will be able to offer this option right away.

While annuitants are not eligible for premium conversion, reemployed annuitants employed in positions that normally convey FEHB eligibility may participate in premium conversion, and each of them has an election to make (see below).

Except for these situations, the FEHB rules have not changed. You will find that you arrive at the correct answer if you apply two simple rules:

Process the action in question exactly as you would have before (except for a cancellation or change to self only, which now require a "qualifying life event"); and

If premium conversion is in effect for an individual, then any deduction for FEHB premiums is subject to conversion (including retroactive and other adjustments).

What is Premium Conversion?

Premium conversion is a tax benefit. It allows an employee to allot a portion of salary back to the employer, which the employer then uses to pay the employee's contribution for Federal Employees Health Benefits (FEHB) coverage. This allotment is made on a pre-tax basis, which means that the money is not subject to Federal income, Medicare, or Social Security taxes. In most States and many localities that impose an income tax, the allotment will not be subject to those taxes as well. The allotment reduces the employee's taxable income, so less tax is withheld, and paychecks are larger.

The Government will still pay the Government share of premiums as provided in the Federal Employees Health Benefits Act. Premiums are not affected; however paying health insurance premiums on a pre-tax basis will make FEHB coverage more affordable for Federal employees.

Who's Eligible?

All employees in the Executive Branch of the Federal Government who are participating in the FEHB Program and whose pay is issued by an Executive Branch agency are eligible to have their FEHB premiums paid under the premium conversion plan. Individuals enrolled in the FEHB Program who are employed outside the Executive Branch, or whose pay is not issued by an agency of the Executive Branch, may be eligible if their employer agrees to adopt our plan and offer participation in premium conversion.

We have contacted all non-Executive Branch agencies that employ individuals covered under FEHB to offer participation in the premium conversion plan. A listing of those agencies can be found on our website. If you are not sure if your agency/organization is automatically covered under our plan, please contact OPM's Insurance Policy and Information Division at (202) 606-0191.

Reemployed Annuitants

Reemployed annuitants enrolled in the FEHB Program are eligible to automatically participate in premium conversion, provided they are employed:

- in a position that normally conveys eligibility for FEHB coverage, such as a career or career-conditional appointment; and
- by an agency covered by OPM's premium conversion plan.

In order for eligible reemployed annuitants to participate in premium conversion, their FEHB enrollment must be transferred from their retirement system to the employing agency. Each agency was asked to submit information on their reemployed annuitants whose annuity is paid under the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS) to OPM so we can transfer FEHB enrollment back to your agency. We ask that you coordinate with your payroll office to make sure that these enrollments are transferred in no later than the day before the first pay period that begins on or after October 1.

A number of other Federal retirement systems maintain FEHB enrollment information and deduct FEHB premiums from annuity checks. Some annuitants who have retired under one of these systems are currently reemployed by another Federal agency. OPM has communicated

with these retirement systems and suggested that they adopt the same procedures as OPM to allow all eligible reemployed annuitants the opportunity to participate in premium conversion.

Currently, the employer share of the FEHB premium for reemployed annuitants under CSRS/FERS is paid from an OPM appropriation. Effective with these new rules, you must contribute the employer share of the FEHB premium for all reemployed annuitants that are enrolled in the FEHB as employees. The agency contribution for reemployed annuitants will be remitted to OPM in the same manner as that for other employees.

How much will Federal employees save?

Based on information from the Department of the Treasury, the *average* Federal employee who participates in the FEHB Program will pay \$434 less per year in Federal income, Social Security and Medicare taxes. In many jurisdictions, state and local income taxes will also be reduced. The website includes a formula for employees to calculate their own savings, as well as some examples.

How much will Agencies save?

Agencies will save the employer share of the Medicare tax and the employer share of Social Security contributions when applicable for each employee who participates in premium conversion.

How do Federal employees enroll?

Participation in premium conversion is automatic. Employees need to complete a form only if they wish to opt-out or waive participation in premium conversion.

Can an employee choose not to participate in premium conversion?

Yes, but the employee needs to opt-out, or waive participation in premium conversion. We are attaching a sample waiver form for your agency to make available to employees. A form will also be available on Employee Express. Employees who want to opt-out must file a waiver form with you by the date you set, but not later than the day before the effective date of coverage.

Why would anyone not want the tax-savings?

There are two potential reasons: Flexibility and Social Security.

Flexibility: An employee participating in premium conversion generally has all the same flexibility as a person who chooses not to participate. Because of the tax laws, there are exceptions. Employees who choose to waive premium conversion retain the flexibility, *without giving any reason whatsoever*, either to drop FEHB coverage altogether or change from a self and family enrollment to self only at any time. Employees who are participating in premium conversion will be allowed to drop coverage, or change to self only, only during open season or if the decision to do so comes at the time of a “qualifying life event,” such as marriage. This flexibility is generally of little or no value compared to the tax savings of premium conversion.

Social Security. Premium conversion may result in somewhat lower Social Security benefits for those Federal employees who pay Social Security taxes on salary. Therefore, in rare situations, it

may be advantageous to pay full Social Security taxes rather than the lower Social Security taxes. These rare cases do not involve employees covered by the CSRS or the CSRS-Offset plan. Employees who are covered by the FERS and pay no Federal income taxes may wish to investigate further.

For most people, the benefit of having more take-home pay far outweighs the slightly lower Social Security retirement benefit. However, it's a personal decision that must be made by each employee.

Will premium conversion have any effect on CSRS, FERS, TSP, or FEGLI benefits?

No. Federal retirement, thrift savings and life insurance benefits are not affected by participation in premium conversion.

Is this an ongoing benefit?

Yes, once an employee participates in premium conversion, the participation continues automatically unless an employee elects not to participate. Each year during FEHB Open Season Federal employees may decide whether or not to participate for the following year.

Can employees change their premium conversion participation status?

Employees may change their participation in premium conversion during the annual FEHB open enrollment period, or during the calendar year if they experience a qualifying life event. Qualifying life events include marriage, or a change in a spouse's employment, and are explained in more detail on the web site.



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Attachments