



Heroes Act Amends Benefits For Employees Called Into Military Service

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On June 18, 2008, President Bush signed into law the Heroes Earnings Assistance and Relief Tax Act of 2008. The Act, which has been alternately referred to as the “HEART Act” or the “Heroes Act”, directs employers to make certain allowances in their employee benefit plans for employees that are called into active military service. The act also has a few important provisions that don’t apply directly to members of the military.

The Act includes the following provisions that will affect employee benefit plans. Please note the effective dates of each provision, as well as the provisions that necessitate a change in written plan documents.

- **Extension of the Mental Health Parity Act**— The law reinstates and extends the federal Mental Health Parity Act, which had expired on December 31, 2007, until December 31, 2008. This law bars group health care plans from providing lower annual and lifetime dollar coverage limits on mental health care services than for other medical services.
- **FSA Distribution**— The law allows employers to amend their Flexible Spending Account (FSA) plans to permit reservists called up for at least six months of active duty to take their remaining FSA balance as a taxable cash distribution. Without this law, those reservists may have had to forfeit their unused balances under the Internal Revenue Code, Section 125 “use-or-lose” rule. This provision is effective immediately.
- **Differential Pay**—The new law directs employers who offer “differential pay” (the difference between what the reservists are paid by the military and their salary with the employer before they were called to active duty) to recognize that compensation in calculating employees’ pension benefits. Differential pay will also be treated as wages subject to income tax withholding. This section of the law applies to wages paid after December 31, 2008. Employers that offer differential pay have until the last day of the plan year beginning on or after January 1, 2010 to amend their pension plans.
- **Small Employer Wage Credit**— For small employers (employing an average of fewer than 50 employees) that provide differential pay to their employees, the law gives a 20% tax credit. This provision is effective immediately, but sunsets on December 31, 2009.
- **Retirement Plan Distribution**— The law reinstates a previously expired law that allowed reservists who are called up for at least six months of active duty to withdraw funds from their 401(k), 403(b), 457 or other defined contribution plan without paying the 10% tax penalty on distributions taken before age 59½. This provision is backdated to December 31, 2007 (the date the previous statute expired.)
- **Retirement Plan Survivor Benefits**— Any tax-qualified retirement plan must provide that if a participant dies while performing qualified military service, his survivors are entitled to any additional benefits (other than benefit accruals relating to the period of qualified military service) that would have been provided if the participant had returned to work one day before dying. For example, a plan that accelerates vesting upon the death of a participant would be required to do the same for a participant that died while performing qualified military service. This change is effective

as of January 1, 2007, but plans have until the last day of the plan year beginning on or after January 1, 2010 to amend their plan for this provision.

- **Retirement Plan Accrual**— Retirement plans can permit individuals who leave for qualified military service and cannot be reemployed due to death or disability to be treated as if they had returned to work one day before death or disability. Under this provision, an employer can credit the participant with the elective deferrals the participant would have made during the period of qualified military service. This change is not required, but is allowed by the act, and is effective as of January 1, 2007. Plans choosing to make this change have until the last day of the plan year beginning on or after January 1, 2010 to amend their plan for this provision.

If you have any questions about this *Briefing* or your employee benefits plans, please contact Innovative Care Systems for more information. ICS is not a law or accounting firm and cannot offer legal advice.