

JAN - 9 1996



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METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

[Signature]
EXECUTIVE SECRETARY

December 14, 1995

To: Board of Directors (Organization and Personnel Committee--Action)

From: *[Signature]* General Manager

Subject: Implementation of Internal Revenue Code Section 125 Flexible Spending Accounts

RECOMMENDATION

It is recommended that the Board approve the establishment of a flexible spending account program that qualifies under Section 125 of the Internal Revenue Code for employees in the management, supervisory, and confidential employee units and for unrepresented managers.

EXECUTIVE SUMMARY

Negotiated agreements between Metropolitan and the Management and Professional Employees Association, the Field Supervisors and Professional Personnel Association, and the Association of Confidential Employees require a determination of the feasibility of a "cafeteria plan" which would provide tax advantages for employees in their medical contributions, dependent care, and health insurance deductibles and copayments. Such a plan has been explored, developed, and is being recommended for implementation for the above-referenced employee groups, as well as for unrepresented managers.

DETAILED REPORT

In 1994, your Board approved Memoranda of Understanding between Metropolitan and the Management and Professional Employees Association, the Field Supervisors and Professional Personnel Association, and the Association of Confidential Employees which provided for the development of a cafeteria plan which would include pre-tax payment of employee contributions toward medical insurance premiums, establishment of dependent care reimbursement accounts and medical expenses reimbursement accounts. The negotiated agreements stated that such a cafeteria plan would be recommended to your Board with an implementation date no earlier than January 1, 1996.

The plan, which is scheduled to be implemented on January 10, 1996, will provide the above-referenced employee groups three options which will allow them to reduce their federal and state taxes pursuant to Internal Revenue Code Section 125. The first option allows the cost of certain medical insurance premiums to be paid from employees' salaries before taxes are calculated, the second option allows employees to set aside monies in a medical reimbursement account to cover allowable unreimbursed medical expenses to be paid on a pre-tax basis, and the third option allows employees to set aside monies in a dependent daycare reimbursement account to cover the cost of daycare for eligible children and other dependents on a pre-tax basis. The maximum amounts which employees can set aside will be established at \$5,000 per year for the medical reimbursement account and \$5,000 for the dependent daycare reimbursement account.

Metropolitan's insurance broker, Spectrum Benefits Group, sent a request to eleven firms which provide flexible spending accounts to determine their ability to administer such a program for Metropolitan. Nine proposals were submitted, and representatives of the affected employee associations and management selected the proposal considered to best suit Metropolitan's needs, the proposal submitted by the American Family Life Assurance Company (AFLAC). AFLAC will be administering these programs for no fee. The only expenditure which may be required from Metropolitan is the potential advance of some medical reimbursements which, under Federal tax law, must be reimbursed to the employee after medical costs have been incurred even though the employee's medical reimbursement account is not fully funded. Therefore, there is minimal, if any, cost for implementing this program.