

# The CPA Journal

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## EMPLOYEE BENEFIT PLANS

September 2003

### Benefits of Forming a Voluntary Employees Beneficiary Association

By *Lance Wallach*

Although they have been in existence since 1928, Voluntary Employees Beneficiary Associations (VEBA) are not well known or understood. VEBAs allow an employer that joins to receive a current tax deduction while putting away funds that are not currently needed. A VEBA allows the employer a great deal of latitude in choosing plan benefits. Contributions are tax-deductible and funds grow tax-deferred. VEBAs have no penalties for early distributions, and life benefits can pass to the employee's family free of income, estate, and gift taxes. A VEBA can be designed so that the benefits paid are not subject to estate taxes because participants have no "incidents of ownership" in the assets, including life insurance contracts held under the VEBA.

VEBA assets are protected from the claims of creditors, the amounts in which contributions are made can be flexible, and benefits are highly favorable to the business owner, with no vesting for employees. Additionally, a VEBA can supplement or enhance buy/sell and stock-redemption agreements, or solve retained earnings problems.

Almost any business can establish a VEBA for its employees, including owner-employees. An employer with one employee (including a spouse) can establish a VEBA. A VEBA is a tax-exempt organization, as described under IRC section 501(c)(9), and would receive a tax-exemption letter from the IRS. An employer can maintain both a retirement plan and a VEBA. VEBAs typically provide for the payment of life insurance, accident insurance, sickness, and other benefits to the members of the VEBA or their dependents and beneficiaries.

VEBA trust earnings are tax-exempt while the trust is accumulating funds. An employer can join an existing multiemployer VEBA.

In most cases, a VEBA is set up as a trust with a bank as the trustee. Some trusts look like VEBAs but are not because the trust sponsor has not taken the additional, costly, step of filing the trust with the IRS under IRC section 501(c)(9).

The IRS has recently taken decisive action against abusive plans claiming to be in conformance with IRC section 419A(f)(6) plans. Under *Treasury Decision 9000*, the disclosure requirement was extended to include participants. All employers and participants in an IRC section 419(f)(6) arrangement will be required to attach a notification to their tax returns disclosing their participation in a "listed transaction." In addition to the potentially devastating financial ramifications, failure to disclose such participation to

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the IRS carries criminal penalties.

VEBAs are subject to some Employee Retirement Income Security Act of 1974 (ERISA) rules but are not subject to the rules governing qualified plans. Therefore, VEBA termination can be made prior to age 59½ without subjecting the distributee to the 10% early distribution penalty. In addition, VEBA distributions are not required to begin by the time the participant reaches age 70½. VEBAs permit employers to deduct contributions to the trust much greater than those available for qualified plans.

Another advantage of the VEBA to the employer-owner is that upon termination all plan assets are distributed to the active participants as of the date of the termination. As a result, there is no vesting to employees that have left the service of the employer.



A VEBA allows more tax-deductible contributions than a 401(k) plan because it is not subject to strict pension plan guidelines. Contribution limits are based on "reasonableness." In 1992 the Tax Court allowed a \$1.1 million VEBA tax deduction that covered two people.

A VEBA is well suited to a business that—

- is highly profitable;
- can no longer fund its retirement plan because it is overfunded or because there is no benefit to the owner-employees;
- has owners that would like to protect assets from their creditors; and
- has owner-employees that would like to reduce their estate tax exposure.

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# VEBA/DBT

## ACCOUNT INFORMATION/ FUND ALLOCATION CHANGE FORM

THIS CHANGE IS A (CHECK ALL THAT APPLY):  FUND ALLOCATION CHANGE  NAME CHANGE  ADDRESS CHANGE

### NAME & ACCOUNT NUMBER

_____	_____
VEBA Participant Name (Please print clearly)	VEBA Acct. No. or Soc. Sec. No.

### FUND ALLOCATION CHANGE

Please change my current balances and any future contributions (if applicable) of my VEBA account(s) to one or more of the following three funds:

_____ % STABLE VALUE FUND	The Balanced Fund and the Growth Fund contain stock market investments and are not guaranteed. These funds will fluctuate up and down in value. Past performance does not guarantee future results.
_____ % BALANCED FUND	
_____ % GROWTH FUND	

= 0 (TOTAL MUST EQUAL 100%)

*This form must be received in the Plan Administrator's office (in Spokane) by the 25<sup>th</sup> of the month in order for the transfer to be effective on the 1<sup>st</sup> business day of the following month. This form must contain an original signature.*

### NAME CHANGE

_____
New Name
Reason For Change of Name (Please attach supporting legal documentation)
<input type="checkbox"/> MARRIAGE <input type="checkbox"/> COURT ORDER <input type="checkbox"/> ASSUMPTION OF A NEW NAME
<input type="checkbox"/> DIVORCE <input type="checkbox"/> DEATH <input type="checkbox"/> NAME GIVEN PREVIOUSLY INCORRECT

### ADDRESS CHANGE

PREVIOUS ADDRESS	NEW ADDRESS
_____	_____
Street Address	Street Address
_____	_____
City, State, Zip Code	City, State, Zip Code

### AUTHORIZATION (REQUIRED)

<b>X</b> _____	_____
Signature of Participant	Date

Keep a Copy For Your Records

# Direct Deposit Enrollment Form For Claims

Direct deposit is faster and more secure than mailing you a check. We encourage you to take advantage of this convenient service. If you want to make direct deposit effective on your account, please complete this form and mail or fax to the Plan Administrator's office listed below.

**PARTICIPANT INFORMATION**

_____		_____	
Participant's Name		Plan Account No. or SSN	
_____		_____	
Street Address	City	State	Zip
_____		_____	
E-mail Address	Telephone Number		

**BANK INFORMATION**

**A voided check must be included for direct deposit. (Deposit slips are not acceptable.) If a voided check is not available, please contact your bank or credit union for your account number and routing number.**

_____		_____	
Name of Financial Institution (Bank or Credit Union)		Phone Number	
_____		_____	
Account Number	Routing Number		
Account type:	Checking <input type="checkbox"/>	Savings <input type="checkbox"/>	
This direct deposit request is:    New Request <input type="checkbox"/> Updated Information <input type="checkbox"/>			
You will be notified by mail when a direct deposit reimbursement has been made.			

**AUTHORIZATION & SIGNATURE**

I understand that I must promptly provide updated information to the Plan Administrator if any of the above account information changes. I acknowledge if a deposit is returned from my financial institution, the Plan Administrator will mail a reimbursement check to the most current address they have on file. I understand this arrangement will remain in effect until changed by me. If I need to be contacted, you may contact me at the e-mail address or telephone number listed above.

\_\_\_\_\_

Signature of Participant (required)

\_\_\_\_\_

Date

Plan Administrator  
c/o Diversified Employee Benefit Services, Inc.  
P.O. Box 781889  
San Antonio, TX 78278  
Fax: (210) 558-3332

If you have any questions, please contact Melissa Boone via e-mail at [mboone@dibsinsurance.com](mailto:mboone@dibsinsurance.com), or at (210) 558-3377 in San Antonio or 1-866-320-3327

**\$250,000 Growing Need**

Do you know the average community & technical college employee and spouse retiring today will probably spend well over \$250,000 in post-employment health care costs and premiums? Health care expenses for active employees are increasing as well. *Are you doing what is necessary to begin preparing for this growing need?*

**Is there a solution?**

Yes. The VEBA DBT plan is a **tax-free** health reimbursement arrangement (HRA) that can be used anytime to pay or reimburse qualified out-of-pocket health care costs and premiums for yourself, your spouse and your IRS qualified dependents.

**What does “tax-free” really mean?**

Unlike your *tax-deferred* investments (TSAs, IRAs, 457s, etc.) which are subject to Social Security and Medicare taxes and only postpone the payment of federal income tax, your VEBA DBT account is **exempt** from all of these taxes. **All contributions, earnings and withdrawals are 100% tax-free!** You could save up to \$300 or more in taxes for every \$1,000 contributed to the VEBA DBT plan.

**Tax-free Contributions**

Tax-free funding of a VEBA DBT account through your employer could come from a variety of sources:

1. Sick leave cash-out at retirement;
2. Vacation leave cash-out (for employees not covered by state-wide collective bargaining agreements); and
3. Monthly payroll contributions (group salary reduction).

Example A: Leave Cash Out				
	Cash Out Amount	25% Income Tax	7.65% FICA Taxes	Net Amount
Taxable Wages	\$10,000	<\$2,500>	<\$765>	\$6,735
VEBA DBT Benefit	\$10,000	n/a	n/a	\$10,000
<b>VEBA DBT saves \$3,265 in taxes!</b>				

Example B: Monthly Payroll Contributions			
VEBA DBT Contribution	Tax Savings	Take-Home-Pay Difference	Annualized Tax Savings
\$30	\$10	\$20	\$120
\$75	\$25	\$50	\$300
\$100	\$30	\$70	\$360

1 Tax Savings are approximate  
 2 Based on average annualizes earning of 5.00%

**Tax-free Investments**

The VEBA DBT plan offers three tax-free investment funds:

1. Stable Value;
2. Balanced; and
3. Growth.

You can self-direct the investment of your VEBA DBT account among any one or all of these funds. Also, you can change your investment fund allocation as often as once a month.

Example C: Growth		
Starting Age	Monthly CEBA DBT Contribution	Account Value at Age 65 <sup>2</sup>
25	\$100	\$148,856
35	\$100	\$81,870
45	\$100	\$40,746
55	\$100	\$15,499

**Tax-free Withdrawals Anytime**

You don't have to wait until you retire to use your VEBA DBT account. You can file claims to pay or reimburse qualified out-of-pocket health care expenses and premiums at any time. It's easy to file a claim and payments are processed daily from DEBS, Inc.

**Death Benefit**

If you pass away, remaining funds in your VEBA DBT account may continue to be used by your surviving spouse, qualified dependents or heirs to reimburse eligible health care expenses.

**Enrollment**

When your employee group adopts the VEBA DBT plan and you become eligible to participate, you will be asked to complete a Membership Enrollment Form and submit it to your employee benefits office. All employee group members defined as eligible must participate per IRS rules.

**More Information**

The VEBA DBT plan allows you the opportunity to begin saving for out-of-pocket health care costs while putting the taxes you save where they belong—*back in your wallet!*

To learn more, visit the VEBA DBT website at [www.debsinsurance.com](http://www.debsinsurance.com) or contact the Melissa Boone at 1-866-320-3327 or email [mboone@dibsinsurance.com](mailto:mboone@dibsinsurance.com).