

HR & Benefits News

Confirming what you already know

Direct-to-consumer advertising accounts for 12% of the annual increase in spending on prescription drugs, according to a new study. Each 10% increase in direct-to-consumer advertising for specific drugs within a therapeutic class resulted in an aggregate 1% increase in sales for drugs within that class. The study was done by the Menlo Park, Calif.-based Henry J. Kaiser Family Foundation, is based on data from 2000.

IRS on debit & credit cards for health FSAs AND HRAs

[Rev. Rul. 2003-43 (May 6, 2003)] <http://www.irs.gov/pub/irs-drop/rr-03-43.pdf>

The IRS has issued guidance on the use of debit and credit cards for health FSAs and HRAs, but only if claims substantiation requirements are satisfied for each claim (*no sampling permitted*). These cards allow participants to access health FSA or HRA funds to pay providers at the point of service, thereby streamlining claims administration and avoiding cash-flow hardships for participants.

Under existing claims substantiation requirements, “a health FSA may reimburse a medical expense only if the participant provides a written statement from an independent third party stating that the medical expense has been incurred and the amount of such expense and the participant provides a written statement that the medical expense has not been reimbursed or is not reimbursable under any other health plan coverage.”

Bad news: “Under the facts described, payments made to medical service providers through the use of debit, credit, and stored-value cards are reportable by the employer on **Form 1099-MISC** under [Code Section] 6041.” Form 1099-MISC reporting isn’t an issue under traditional health FSAs or HRAs that require participants to complete a reimbursement request form and where, days or weeks after the medical services are provided, reimbursements are made to participants rather than payments to providers.

Every Claim Must Be Substantiated And Adjudicated. The tax code excludes from an employee’s gross income employer-provided accident or health plan coverage or amounts received through accident or health insurance for personal injuries or sickness if such amounts are paid specifically to reimburse for expenses incurred for medical care. However, the regulations require, among other things, **substantiation. (2003-43)**, provides that medical expense reimbursements made through a debit or credit card will be excludable from employees’ gross income **only** in cases where the employer has adopted a substantiation methodology. *The sampling approach was rejected by the IRS.* Debit, credit, and stored-value cards are reportable by the employer on Form 1099-MISC under [Code Section] 6041. Section 6041 provides for information reporting by persons engaged in a trade or business who make payments of fixed or determinable income to another person in the course of such trade or business of **\$600 or more** in a taxable year. Service providers’ taxpayer identification numbers (TINs) have to be collected.

IRS Approves HRA Linking Reimbursements, W-4 Reporting

In a private letter ruling issued July 18, the IRS approved a health reimbursement arrangement (HRA) that links employees' reimbursement amounts to their wages and personal exemptions reported on Form W-4. According to the IRS, this plan design meets the requirements for an HRA under Revenue Ruling 2002-41 and Notice 2002-45. Therefore, the value of both the employer-provided coverage and the HRA reimbursements are excludable from a participating employee's gross income under Code Sections 105(b) and 106. *The plan is available only to employees who have elected, through salary reduction, to purchase employer-provided health insurance.* At the beginning of the plan year, the employer designates a specific annual aggregate amount of reimbursements or payments based on each employee's wages and personal exemptions reported on Form W-4. Thus, employees with a higher withholding rate have a lower aggregate amount; those with a lower withholding rate have a higher aggregate amount. However, only a pro-rata portion of that amount is available for reimbursing substantiated medical expenses on each payday. The ruling expresses no opinion on whether the plan discriminates under Code Section 105(h). The ruling is applicable only to the employer requesting it and may not be used or cited as precedent. See: www.irs.gov/pub/irs-wd/0329014.pdf

Harry Beker (IRS's Chief of Health and Welfare) Says Health FSA Substantiation Is a Must

Employees seeking reimbursement of medical expenses through a health flexible spending account (FSA) must follow acceptable means of substantiating that the expenses are legitimate, said Mr. Beker on Aug. 15 at a flexible benefits symposium in Chicago. Harry Beker, Chief of the Health and Welfare Branch in the Office of Associate Chief Counsel, explained that *the only acceptable means of substantiation are either a statement from an independent third party stating that the expense has been incurred (for paper transactions), or by using the procedures for paying by debit or credit card under Revenue Ruling 2003-43.* Under either form of processing, the participant cannot rely solely on his or her own word that the medical expense was incurred. In addition, Beker said, *the debit or credit card should be swiped each time an expense is incurred,* even if, for example, all family members have the same co-pay or more than one family member is going to the doctor at the same time.

Opinion: Ten Keys Listed to Compliant Debit Card Reimbursement System

The IRS did flex plan administrators and participants a favor by approving the use of debit cards for reimbursing qualified medical expenses, but before instituting a debit card reimbursement system, the administrator or sponsor should consider **10 questions** to help spot critical compliance-related issues, a leading benefits attorney told a June 24 meeting of the Employers Council on Flexible Compensation. Facilitating electronic claims processing makes sense, explained **John Hickman**, a partner in the Employee Benefits Practice Group of **Alston & Bird, LLP**. However, the IRS also imposed a Form 1099 reporting requirement on payments directly to medical providers by the plan, employer or debit card vendor. Therefore, the **10 issues to consider**, according to Hickman, are:

1. Does the system provide for adequate participant certification?
2. Is the card limited by merchant category code to eligible health care providers?
3. Does the system adjudicate every claim?
4. Does the system provide adequate flagging of claims that cannot be adjudicated automatically?
5. Can the system de-activate cards for terminated employees or individuals who submit ineligible claims?
6. Are claims paid from a participant-owned credit or debit account?
7. If not, can the system obtain taxpayer identification number information from the provider?
8. Is the system compliant with HIPAA electronic data interchange requirements?
9. Is the system compliant with ERISA's trust and plan asset rules?
10. Is the vendor willing to provide contractual representations and warranties, and agree to indemnify for all compliance issues?

HR 2351

The House Ways and Means Committee on June 19 approved the Health Savings Account Availability Act (H.R. 2351), which would replace Archer medical savings accounts with a new, more generous system of health savings accounts (HSAs) providing for tax-free reimbursements of qualified medical expenses.

Eligible individuals - persons currently covered under a health plan meeting minimum deductible requirements (\$500 for employee-only coverage, \$1,000 for family coverage), or uninsured persons - could contribute up to \$2,000 or \$4,000 respectively each year to an HSA established for their benefit. Neither the contributions to such an account, nor distributions from the account to pay for qualified medical expenses, would be includible in taxable income.

In addition, **participants could roll over up to \$500 of unused benefits in a health flexible spending account (FSA) to the next year's account or to an HSA. An individual not eligible to contribute to an HSA for the taxable year could transfer up to \$500 of unused benefits to a tax qualified retirement plan.**

The proposal also provides an exception from the generally applicable information reporting provisions (Form 1099) for payments for medical care under either an FSA or a health reimbursement arrangement that is treated as employer-provided coverage. The House is expected to approve H.R. 2351, possibly as early as July 1.

401(K) Online Learning Center

The NASD releases a new 401(k) online learning center: www.nasd.com/Investor/Smart/401k

Smart 401(k) Investing pulls together a plethora of information on 401(k) plans and outlines the different options and special features that should be considered when investing in 401(k) plans. The tool provides a number of interactive tools, including a Minimum Required Distribution Calculator and:

enrollment process guides *PLUS* suggestions on managing a 401(k) account questions and answers on topics such as 401(k) investment options; asset allocation and diversification; moving a 401(k) when changing jobs; handling withdrawals after retirement.

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