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Coordinating HSAs With FSAs And HRAs

My recent articles have focused on consumer-directed health plans and the discussion of the different types of accounts that can be offered instead of or with a health savings account (HSA). Depending on an employer's goals and objectives, either a flexible spending account (FSA) plan or a health reimbursement arrangement (HRA) can be offered. This article will describe how an employer can offer an HSA, a health FSA, and an HRA program while still complying with every law surrounding these benefits.

As just a little background, HSAs are individually owned health care payment accounts that allow the participant to contribute untaxed dollars. Interest or dividends accumulate tax-free; and when an individual pays for qualified medical expenses, there will be no additional tax consequences.

In order to have an HSA, individuals must be covered by a qualified, high-deductible health plan (HDHP). The HDHP must satisfy minimum deductible amounts with certain out-of-pocket maximums. Account holders may not be covered by any other insurance plan that is not an HDHP or that covers benefits provided by the HDHP, but they may obtain narrowly defined "permitted insurance" or "permitted coverage" products (dental, vision, accident, disability and long term care benefits). The HDHP may also provide "preventive care" reimbursement that is below the minimum deductible amount or without a deductible.

This is a discussion of "other" insurance coverage. Specifically, health coverage provided through a Section 125 health flexible spending account (HFSA) or an HRA as well as limited-purpose HFSAs and HRAs, suspended HRAs, post-deductible HFSAs and HRAs, and retirement HRAs.

Limited-Purpose Health FSA or HRA

In this program an HFSA or HRA is limited to payment of only permitted coverage items such as vision and dental expenses, whether or not the minimum annual deductible of the HDHP has been met. The limited-purpose HRA could also compensate for permitted insurance plans that cover a specific disease or illness, or that provide a fixed amount per day of hospitalization.

This range of benefits does not breach the "no other insurance" rule of HSAs. It should also be noted that the limited-purpose programs could pay for preventive care. Preventive care was defined in IRS Notice 2004-23.

Suspended HRA

A suspended HRA is an employer-funded HRA that pays all qualified health care expenses for eligible employees. For an otherwise HSA-eligible employee, an election is made before the beginning of the

HRA coverage period to forgo, or suspend, all payments from the plan that are not for permitted coverage, permitted insurance or preventive care expenses. Thus, barring reimbursement then, or at any time, of otherwise eligible expenses and retaining entitlement to make tax-free contributions to the HSA.

In this case, an employer would continue to "fund" the employee's HRA account although the employee has elected to suspend full usage of the arrangement. When the employee ends the suspension period, he would no longer be eligible to make HSA contributions, because he is free to receive reimbursement of all health care expenses from the HRA.

Post-Deductible HFSA or HRA

With these benefits, the HFSA and HRA are also considered to be high-deductible insurance products. Remember the rule about no other insurance coverage? These HFSA/HRA plans won't kick off until after the minimum deductible is met. Participant reimbursement from the HFSA or HRA doesn't have to wait until the HDHP's deductible amount is met, but the "minimum" deductible standard must be met.

In addition, although the deductibles of the HDHP and the other coverage may be satisfied independently by separate expenses, no benefits may be paid before the minimum annual deductible is met, which is $1,100 for single coverage and $2,200 for family coverage in 2007 and 2008.

Are HFSAs and HRAs "Family" Coverage?

Most HFSA and HRA plans are written to allow for payment of suitable health care expenses for employees and their spouses and dependents. That means they provide family coverage. This begs the question, *If an employee has a qualifying single-coverage health plan with a deductible of $1,100, would the HFSA and the HRA have to maintain deductible amounts of $2,200 or more?* We will undoubtedly see more clarification on this issue from the IRS.

Other questions that come to mind include: If a participant elects to enroll in a "single coverage" HRA one year, and not the next, how can this be reconciled when payments are made out of the HSA? No one else sees these receipts, except the IRS—upon audit. Is the IRS going to contact the employer to see what other coverage this employee had? Will they contact the spouse's employer to check on coverage there? What if the investigation goes back several years? How long and complicated should this trail be?

Retirement HRAs

Retirement HRAs can accumulate funds during an employee's working years and make those dollars available to the individual upon retirement. It may not reimburse health care expenses except for permitted coverage, permitted insurance, and preventive care expenses during an individual's period of employment—only after retirement. When the retirement HRA begins, the participant is ineligible to make further contributions to his HSA.

Mix and Match

Combinations of the above plans can also work. For instance, an employee could be covered by a limited-purpose HFSA and a retirement HRA and still be eligible to make contributions to an individual HSA arrangement.

Contributions Versus Disbursements

Don't confuse being "eligible to make contributions" to an HSA with "eligible to receive payments" from the HSA. An HSA can pay for the qualified medical expenses of the account holder as well as his dependents, even though the account holder is no longer eligible to make contributions to his HSA. Another note, the spouse and dependents do not need to be covered by the underlying HDHP, HFSA or HRA in order to have their health care expenses reimbursed from the HSA.

A Duty to Educate

Employee education is a must when blending benefits with so many special rules. Start with the employer's offering and try to keep educational materials simple and to the point.

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