

Consumer-Driven Health Care

Table of Contents

[See also the Table of Contents behind each Appendix Tab]

About the Authors	i
How to Use This Manual	ii
Current Developments	see the Current Developments Tab
Statutes, Regulations, Sample Documents, and Other Items.....	see the Appendix Tabs

Outline Table of Contents

I. Overview of This Manual	1
A. <i>What Is Consumer-Driven Health Care?</i>	1
B. <i>What This Manual Covers</i>	1
1. Health Savings Accounts (HSAs)	1
2. Health Reimbursement Arrangements (HRAs)	2
C. <i>This Manual Is Intended to Be Used With the Cafeteria Plans Manual</i>	2
II. Consumer-Driven Health Care: The Short Course	21
A. <i>The Short Course Is for You</i>	21
B. <i>What You'll Learn in the Short Course</i>	21
C. <i>What's Consumer-Driven Health Care?</i>	21
1. Consumer-Driven Health Care Describes a Variety of Plan Designs	22
2. Consumer-Driven Health Care Involves a Corridor of Risk	22
3. Fostering Employee Use of Consumer-Driven Health Care	22
4. Employers Need to Carefully Analyze Design Consequences	22
D. <i>Ways to Cut Health Care Costs</i>	23
E. <i>How to Design a CDHC Program</i>	23
F. <i>Health Savings Accounts</i>	24
1. HSAs: Who Is Eligible?	24
2. HSAs: Required HDHP Coverage	25
3. HSAs: Other Permissible/Impermissible Types of Coverage	27
4. HSAs: Contributions	29
5. HSAs: Comparability Requirements and the Cafeteria Plan Exception	33
6. HSAs: Distributions and Rollovers	34
7. HSAs: HSA Trust/Custodial Accounts	37
8. HSAs: Reporting Requirements	39
G. <i>Health Reimbursement Arrangements</i>	40
1. HRAs Are Not Subject to Many Health FSA Rules	40
2. HRAs Are Not Subject to HSA Rules	40
3. HRA Interaction With HSAs and Other Coordination of Benefits Issues	41
4. HRAs: Employer Contributions, Reimbursements, and Other Operating Rules	41
5. HRAs: Nondiscrimination, COBRA, and Other Compliance Issues	43

H.	<i>Archer MSAs</i>	44
1.	What Individuals Are Eligible?	44
2.	What Is a Small Employer?	44
3.	Must Be Covered Under a High-Deductible Health Plan	44
4.	Coverage Under Any Non-Permissible Health Plan Makes Individual Ineligible	44
5.	What Is Permissible Coverage?	44
6.	Establishment of Archer MSAs	44
7.	Tax Treatment and Limits on Contributions	45
8.	Distributions From Archer MSAs	45
9.	Additional Matters	46
I.	<i>Conclusion</i>	46
III.	Consumer-Driven Health Care	51
A.	<i>What Is Consumer-Driven Health Care?</i>	51
1.	Consumer-Driven Health Care Describes a Variety of Plan Designs	51
2.	CDHC in the Workplace: Giving Employees a Financial Stake in Health Care Decisions	51
B.	<i>Consumer-Driven Health Care Involves a Corridor of Risk</i>	52
C.	<i>Common Types of Consumer-Driven Health Care</i>	53
1.	High-Deductible Health Insurance Coverage (HDHC)	53
2.	Medical Expense Reimbursement Plans (MERPs)	54
3.	Health Reimbursement Arrangements (HRAs)	54
4.	Health Flexible Spending Arrangements (Health FSAs)	55
5.	Archer Medical Savings Accounts (Archer MSAs)	55
6.	Health Savings Accounts (HSAs)	56
D.	<i>Fostering Employee Use of Consumer-Driven Health Care</i>	56
1.	Communication	56
2.	Health Information Systems	57
3.	Wellness and Disease-Management Programs	57
E.	<i>Employers Need to Carefully Analyze Design Consequences</i>	57
1.	Overall Design Should Be Fully Disclosed to Insurers and Service Providers	57
2.	Employers Should Consider the Potential Impact of Federal and State Laws	58
F.	<i>Basic Requirements for Tax-Advantaged Health Care in the Workplace</i>	59
1.	Health Care Coverage Provided by Employer Is Not Taxable to Employee	59
2.	Employer Gets Tax Deduction for Health Care Coverage Provided to Employees	60
3.	Employee Is Not Taxed on Payments or Reimbursements From Employer-Provided Health Care	60
IV.	Cost-Cutting Plan Designs	91
A.	<i>Overview of Cost-Cutting Plan Designs</i>	91
B.	<i>Caps on Employer Contributions</i>	91
1.	In General	91
2.	Legal Compliance and Other Considerations	92
C.	<i>Spousal Surcharges and Eligibility Restrictions</i>	92
1.	Spousal Surcharges	92
2.	Spousal Eligibility Restrictions	93
3.	Legal Compliance and Other Considerations	93

<i>D. Eligibility Audits</i>	94
1. Employers Use Eligibility Audits to Control Costs	94
2. Legal Compliance and Other Considerations	95
3. COBRA	95
4. Does HIPAA Prevent a Group Health Plan From Performing an Eligibility Audit and May Adverse Action Be Taken Against an Employee for any Misrepresentation?	97
5. Application of the HIPAA Privacy and Security Rules When Conducting an Eligibility Audit	98
6. Provision of a Certificate of Creditable Coverage for Periods During Which an Ineligible Participant Participated in the Plan	98
7. Tax Consequences When Ineligible Participant Is Not a Spouse or a Code § 105(b) Dependent.....	98
<i>E. Paying Employees Not to Take Coverage</i>	99
<i>F. Wellness and Disease-Management Programs</i>	100
<i>G. Other Cost-Cutting Measures</i>	100
1. General Strategies	100
2. Healthy Lifestyle Initiatives	101
3. “Never Events”.....	101
4. Medical Tourism.....	102
V. Designing a Consumer-Driven Health Care Program	131
<i>A. Step-By-Step Guide to CDHC Design</i>	131
1. Step 1: Decide Whether to Offer High-Deductible Health Coverage	131
2. Step 2: Decide Whether to Offer a “Floor Plan”	131
3. Step 3: Decide Which Floor Plan to Use: HSAs, HRAs, or Health FSAs.....	132
4. Step 4: Network With Other Employers	134
5. Step 5: Allow Ample Time for Implementation	134
<i>B. Case Studies: How Have Other Employers Designed Their Programs?</i>	135
1. Computech—A Hypothetical Case Study	135
2. Case & Associates—A Hypothetical Case Study	135
3. Acme Manufacturing—A Hypothetical Case Study	136
4. Dayglo Inc.—A Hypothetical Case Study	136
<i>C. Chart Comparing HSAs, HRAs, and Health FSAs</i>	141
VI. Wellness and Disease-Management Programs	201
<i>A. Introduction</i>	201
1. What Is a Wellness Program?	201
2. What Is a Disease-Management Program?	202
3. How Are Wellness and Disease-Management Programs Alike (and Different)?	202
4. Why Would an Employer Offer a Wellness or Disease-Management Program?	202
5. Legal Compliance Issues Raised by Wellness and Disease-Management Programs	202
<i>B. Designing Wellness and Disease-Management Programs</i>	203
1. Common Wellness Program Designs	203
2. Common Disease-Management Program Designs.....	203
3. Coordinating Wellness and Disease-Management Programs With Each Other	203
4. Coordinating Wellness and Disease-Management Programs With Other Employee Benefit Plans	204
<i>C. Tax, Cafeteria Plan, Health FSA, HSA, and HRA Considerations</i>	204
1. Taxation of Employer-Provided Rewards.....	204

2. Cafeteria Plan and Health FSA Issues.....	206
3. HSA and HRA Issues.....	208
D. HIPAA Considerations.....	210
1. In General	210
2. Some Wellness and Disease-Management Programs Are Exempt From Certain HIPAA Nondiscrimination Requirements	211
3. HIPAA’s Administrative Simplification Requirements (Privacy, Security, and EDI)	216
E. COBRA Considerations	217
1. Group Health Plans Are Subject to COBRA	217
2. Wellness or Disease-Management Programs That Provide Medical Care Are Group Health Plans Subject to COBRA	217
3. Overview of COBRA Requirements Applicable to COBRA-Subject Wellness and Disease- Management Programs.....	218
F. ERISA Considerations	218
1. Does ERISA Apply to Wellness and Disease-Management Programs?.....	218
2. Wellness and Disease-Management Programs Often Provide Medical Care	218
3. Overview of Applicable ERISA Compliance Requirements.....	219
4. Termination of Employment for Failure to Meet Wellness or Disease-Management Program Requirements Might Trigger an ERISA § 510 Claim	219
G. GINA Considerations	220
1. Overview	220
2. Key Terminology	220
3. GINA’s Prohibitions and Limitations	222
4. Wellness Programs Offered Outside Group Health Plan May Also Raise Issues Under GINA.....	227
5. GINA’s Proposed Modifications to HIPAA’s Privacy Regulations	227
6. Enforcement Under GINA	228
H. ADA Considerations.....	229
1. Does the ADA Apply to Wellness and Disease-Management Programs?	229
2. Wellness and Disease-Management Program Benefits Must Not Discriminate Against Qualified Individuals on the Basis of Disability	229
3. Medical Examinations and Inquiries in Connection With Wellness and Disease-Management Programs Must Be “Voluntary”	232
I. Other Compliance Considerations: ADEA, Title VII, and FLSA.....	234
1. Does the ADEA Apply to Wellness and Disease-Management Programs?	234
2. Does Title VII Apply to Wellness and Disease-Management Programs?.....	235
3. Does the FLSA Apply to Wellness and Disease-Management Programs?	236
VII. [Reserved].....	251
VIII. Health Savings Accounts (HSAs): Introduction	251
A. Overview	251
1. What Are HSAs?	251
2. HSA Topics That We Cover.....	252
3. The HSA Tax Break	252
4. HSA Governing Law	253
5. Comparison of HSAs to HRAs and Health FSAs	257

<i>B. HSA Flowchart: From Contributions to Distributions</i>	257
<i>C. What Steps Must an Individual Take to Establish an HSA?</i>	258
1. Individual Must Have HDHP Coverage and No Impermissible Non-HDHP Coverage.....	259
2. Individual Must Not Be Entitled to Medicare and Must Not Be a Tax Dependent	259
3. Individual Opens an HSA With a Qualified Trustee or Custodian.....	259
4. Individual Completes an HSA Beneficiary Designation Form	260
5. Individual Determines Amount and Timing of HSA Contributions.....	260
6. Individual Chooses Investments for HSA Funds	261
7. Individual May Choose HSA Distribution Method.....	261
8. HSA Account Holder or Other Disqualified Person Must Not Engage in a Prohibited Transaction	261
9. Individual Is Responsible for Determining and Reporting Taxable HSA Distributions.....	262
IX. HSAs: Who Is Eligible?	321
<i>A. Any Individual With HDHP Coverage Could Be an Eligible Individual</i>	321
<i>B. An Individual Who Can Be Claimed as a Tax Dependent Is Not HSA Eligible</i>	322
<i>C. An Individual Who Is Entitled to Medicare Is Not HSA Eligible</i>	323
1. Medicare Entitlement Based on Age	324
2. Medicare Entitlement Based on Disability.....	325
3. Medicare Entitlement Based on ESRD	325
4. Part A Entitlement Based on Age or Disability Generally Cannot Be Waived	325
5. Entitlement to Medicare Part B or Part D	326
<i>D. Eligible Individual Must Have HDHP Coverage and No Disqualifying Coverage</i>	326
<i>E. Eligible Individual Status Determined Monthly as of the 1st of Each Month</i>	327
<i>F. Treatment of HSA After Eligibility Ends</i>	329
1. HSA Holders May Continue to Receive Distributions After Eligibility Ends	329
2. HSA Holders May Not Continue Contributions After Eligibility Ends	330
<i>G. What If an HSA Is Established by an Ineligible Individual?</i>	332
1. Ineligible Individual May Establish an HSA to Receive a Rollover Contribution From an Existing HSA	332
2. Ineligible Individual May Establish an HSA As a Result of a Divorce.....	332
3. Ineligible Individual (a Spousal Beneficiary) May Establish an HSA After HSA Holder Dies.....	333
4. Ineligible Individual Mistakenly Establishes an HSA	333
X. HSAs: Required HDHP Coverage	431
<i>A. Introduction</i>	431
<i>B. Self-Only HDHP Coverage</i>	431
1. Minimum Annual Deductible for Self-Only HDHP Coverage	431
2. Maximum Out-of-Pocket Expense Limit for Self-Only HDHP Coverage.....	432
3. Self-Only HDHP Minimum Deductible and Maximum Out-of-Pocket Limit May Increase	432
<i>C. Family HDHP Coverage</i>	432
1. Minimum Annual Deductible for Family HDHP Coverage	433
2. Maximum Out-of-Pocket Expense Limit for Family HDHP Coverage	434
3. Family HDHP Minimum Deductible and Maximum Out-of-Pocket Limit May Increase.....	434
4. Scrutinize Family Coverage HDHP for Embedded Individual Deductibles.....	434

D.	<i>HDHPs Come in Many Shapes and Sizes</i>	435
1.	Self-Insured Medical Plan Can Be an HDHP	436
2.	State High-Risk Pool Can Be an HDHP	436
3.	Network Plan Can Be an HDHP	436
4.	HRA or Health FSA Cannot Be an HDHP	437
5.	Plan Cannot Be an HDHP If Substantially All of Its Coverage Is Permitted Coverage or Permitted Insurance	437
E.	<i>What Expenditures Count Against the HDHP Out-of-Pocket Maximum?</i>	437
1.	Lifetime Limits on Plan Benefits	438
2.	Annual or Lifetime Limits on Specific Benefits	438
3.	UCR Restrictions	439
4.	No Express Out-of-Pocket Limit	440
5.	Penalties for Failure to Precertify a Provider or Procedure	440
6.	Cumulative Embedded Individual Deductibles	440
7.	Co-Payments	441
8.	Separate Benefit Deductibles	442
F.	<i>What Expenditures Are Applied Toward the Required Minimum Deductible?</i>	442
1.	Crediting Expenses Incurred But Not Reimbursed During Prior Plan Coverage	442
2.	Carrying Over Deductible Expenses Incurred in Prior Year	445
3.	Receiving Benefit of Discounted Prices Before Deductible Is Met	446
G.	<i>HDHP Can Provide Preventive Care Benefits Without Required Deductible</i>	446
1.	The IRS Has Provided a Safe Harbor Definition of Preventive Care	446
2.	Some Incidental Treatment and Drugs Can Be Preventive Care	447
H.	<i>HDHP Can Pay No Benefits (Except Preventive Care) Until Deductible Is Met</i>	448
1.	State-Mandated Services May Not Be Preventive Care	448
2.	Discounted Prices Can Be Paid Without Regard to the Deductible	449
3.	Co-Payments Before the Deductible Can Prevent Coverage From Being an HDHP	449
XI.	HSAs: Other Permissible/Impermissible Types of Coverage	481
A.	<i>General Rule—No Health Coverage Other Than HDHP Coverage</i>	481
B.	<i>Permitted Insurance and Permitted Coverage Do Not Prevent HSA Eligibility</i>	482
1.	Permitted Insurance	482
2.	Permitted Coverage	484
3.	Permitted Coverage or Permitted Insurance Alone Cannot Be an HDHP	486
C.	<i>Non-HDHP Coverage of “Carve-Out” Benefits Will Prevent HSA Eligibility</i>	487
1.	Carve-Out Coverage Under the HSA Statute	487
2.	IRS Forecloses Non-HDHP Carve-Out Coverage in Prescription Drug Ruling	487
3.	Transition Relief for Prescription Drug Coverage Under Separate Plan or Rider	487
4.	Discount Card Coverage May Not Disqualify Otherwise Eligible Individual	488
D.	<i>General-Purpose Health FSA or HRA Coverage Will Prevent HSA Eligibility</i>	489
E.	<i>Specially Designed Health FSA or HRA Coverage Will Not Prevent HSA Eligibility</i>	492
1.	Limited-Purpose Health FSAs and HRAs	492
2.	Suspended HRAs	493
3.	HDHP Coupled With a Post-Deductible Health FSA or HRA Coverage	495
4.	Retirement HRA	497

5. Combining the Above Situations	498
6. Certain Coverage Choices Under Choice Health FSAs or Choice HRAs Will Not Prevent HSA Eligibility	498
7. Coordinating Reimbursements	499
<i>F. Many EAPs, Disease-Management Programs, and Wellness Programs Will Not Prevent HSA Eligibility</i>	<i>500</i>
<i>G. Other Coverage That May or Will Prevent HSA Eligibility</i>	<i>501</i>
1. Veterans Affairs Medical Benefits and Indian Health Service May Prevent HSA Eligibility	501
2. On-Site Clinics May Prevent HSA Eligibility	502
3. TRICARE and Medicaid Will Prevent HSA Eligibility	504
4. Mini-Med or Supplemental Health Insurance May Prevent HSA Eligibility	504
5. Employer Reimbursement of Expenses Before the Minimum HDHP Deductible Is Satisfied Will Prevent HSA Eligibility	504
<i>H. What Are the Consequences of Having Impermissible Non-HDHP Coverage?</i>	<i>504</i>
<i>I. Table: Permissible/Impermissible Types of Coverage for HSA Eligibility</i>	<i>505</i>
XII. HSAs: Contributions	531
<i>A. Limits Apply to HSA Contributions</i>	<i>531</i>
<i>B. HSA Contribution Limits Are Calculated on a Monthly Basis</i>	<i>532</i>
1. General Monthly Contribution Rule	532
2. Full-Contribution Rule for Mid-Year HDHP Enrollees	533
<i>C. HSA Contribution Limit for Self-Only HDHP Coverage</i>	<i>536</i>
<i>D. HSA Contribution Limit for Family HDHP Coverage</i>	<i>537</i>
<i>E. Prior to 2007, Some Types of Coverage Could Affect Calculation of HSA Contribution Limit</i>	<i>538</i>
1. Calculating HSA Contribution Limit for Family HDHP With Embedded Individual Deductibles	538
2. Calculating HSA Contribution Limit for HDHP With Deductible Carryover Provision	539
3. Calculating HSA Contribution Limit for Individual With Post-Deductible Health FSA or HRA Coverage	539
4. Calculating HSA Contribution Limit for HDHP With Separate Deductibles	539
<i>F. HSA Contribution Limit Under the Special Rule for Married Individuals</i>	<i>540</i>
1. Calculating the HSA Limit for Married Individuals	540
2. Calculating the HSA Limit When One Spouse Is Eligible	540
3. Calculating the HSA Limit When Spouse's Coverage Does Not Cover Other Spouse	541
<i>G. Matrix of HSA Contribution Limits</i>	<i>542</i>
<i>H. Allocating the HSA Contribution Limit Between Spouses</i>	<i>545</i>
<i>I. HSA Catch-Up Contributions</i>	<i>545</i>
<i>J. Employer HSA Contributions</i>	<i>546</i>
<i>K. HSA Contributions Are Nonforfeitable</i>	<i>548</i>
1. May Restrictions Be Placed on Employer Contributions Made to an HSA?	548
2. Mistaken Contributions	549
<i>L. Tax Treatment of HSA Contributions</i>	<i>553</i>
1. Contributions Made by the HSA Holder	553
2. Contributions Made by a Non-Employer on Behalf of the HSA Holder	553
3. Contributions Made by the Employer of the HSA Holder	554

M. When Must HSA Contributions Be Made?	555
N. What Happens If Too Much Is Contributed to an HSA?	557
1. Income Tax Consequences of Excess Contributions	557
2. 6% Excise Tax on Excess Contributions	557
3. Avoiding the 6% Excise Tax With a Curative Distribution	559
4. Determining Net Income on Contributions	560
O. Rollovers and Transfers From Other Accounts	561
1. Rollover Contributions From Other HSAs and Archer MSAs	561
2. Qualified HSA Distributions From Health FSAs and HRAs	562
3. Qualified HSA Funding Distributions From IRAs	568
4. Chart Comparing Flow of Funds, Tax Treatment, and Reporting Requirements	571
XIII. HSAs: Comparability Requirements & the Cafeteria Plan Exception	591
A. Introduction	591
1. Overview of Comparability Requirements	591
2. Summary of Guidance	593
B. Who Are Comparable Participating Employees?	595
1. Categories of Comparable Participating Employees	595
2. Some Individuals Are Not Counted as Comparable Participating Employees	597
3. Comparable Participating Employees of Related Employers Must Receive Comparable Contributions	602
4. Categories of HDHP Coverage	604
5. Employers May Restrict HSA Contributions to HSA-Eligible Individuals With Employer-Provided HDHP Coverage	607
6. What If Both Spouses Work for the Same Employer?	608
7. What If an Employee Has Both an HSA and an Archer MSA?	609
C. How to Determine If Contributions Are Comparable	609
1. Scope of Comparable Contribution Requirement	610
2. Each Category of Comparable Participating Employee Is Treated Separately	610
3. Examples From the Final Comparability Regulations	611
4. Contributions Must Actually Be Made, Not Just “Made Available”	613
D. What Contribution Methods Are Available for Employer HSA Contributions?	617
1. Pay-As-You-Go Method	617
2. Look-Back Method	619
3. Pre-Funded Method	621
4. Accelerated Contributions for Employees Whose Qualified Medical Expenses Exceed the Employer’s Year-to-Date HSA Contributions	623
5. What If an Eligible Employee Fails to Open an HSA?	623
E. Getting Organized to Perform Comparability Testing	627
1. Step One: Identify Controlled Group	627
2. Step Two: Identify Excludable Individuals	627
3. Step Three: Divide Non-Excludable Employees Into Comparable Groups	627
4. Step Four: Develop Tools	627
5. Step Five: Consider Design Choices	628
F. What Happens If the Comparability Requirements Are Not Satisfied?	628
1. Contributions That Are Not Comparable	628

2. Failure to Make Qualified HSA Distributions Available to All Employees Covered by Employer's HDHP	629
3. Waiver of the 35% Excise Tax	630
G. Cafeteria Plan Exception	633
1. When Is an Employer HSA Contribution Made "Through a Cafeteria Plan"?	634
2. Availability of Pre-Tax Salary Reduction HSA Contributions Causes Employer HSA Contributions to Be Made "Through a Cafeteria Plan"	634
3. When Pre-Tax Salary Reduction HSA Contributions Are Not Available, Can Any Employer HSA Contributions Be Made "Through a Cafeteria Plan"?	638
XIV. [Reserved]	801
XV. HSAs: Distributions and Rollovers	801
A. HSA Distributions Generally Are Available Without Restriction	801
1. HSA Account Holders Can Receive HSA Distributions at Any Time	801
2. Only Reasonable Restrictions on Frequency or Minimum Amount of HSA Distributions Are Allowed	802
3. HSA Distributions Cannot Be Mandatory	802
4. HSA Balance Carries Over to Subsequent Years	802
B. HSA Distributions Are Tax-Free If for Qualified Medical Expenses	803
C. What Is an HSA Qualified Medical Expense?	803
1. Medical Expenses Under Code § 213(d)	803
2. With Some Exceptions, Insurance Premiums and Coverage Contributions Are Not HSA-Qualified Medical Expenses	805
D. Timing Issues for Tax-Free HSA Distributions	807
1. Expenses Must Be Incurred After an HSA Is Established	807
2. Deemed HSA Establishment Dates for Rollover or Multiple HSAs	808
3. No Time Limit on When HSA Distribution Must Occur	810
4. Paid or Incurred? Only Distributions "Used Exclusively to Pay Qualified Medical Expenses" Are Tax-Free	811
5. Expenses Incurred After HSA Account Holder Is No Longer Eligible May Be Tax-Free	812
6. HSA Distributions for Family Member Medical Expenses Not Taxable Even During Year Contributions Are Made	813
E. HSA Distributions for Nonmedical Expenses	813
1. HSA Distributions for Nonmedical Expenses Are Permitted, but Taxable	813
2. Mistaken Distributions May Be Returned to HSA	814
3. Excise Tax on Nonmedical HSA Distributions Before Age 65, Death, or Disability	815
4. HSA Account Fees Withdrawn From HSA Not Subject to Income Tax or Excise Tax	816
5. Deemed HSA Distributions to Covered Expatriates	816
F. HSA Rollover Distributions and Trustee-to-Trustee Transfers	816
1. General Rules Applicable to Rollovers and Transfers From HSAs	816
2. HSA Rollovers Are Subject to Timing Restrictions	817
3. Direct Trustee-to-Trustee Transfers of HSA Funds Are Unlimited	817
G. Treatment of HSAs Upon Divorce or Death	817
1. Transfer of HSA Upon Divorce	817
2. Treatment of HSAs After Account Holder's Death	818
H. HSAs and Creditors	818
1. Creditors Accessing HSA Funds Via Liens and Other Security Interests	819

2. IRS Accessing HSA Funds Via Tax Levies	819
XVI. HSA Trust/Custodial Accounts.....	851
A. <i>Who Can Be an HSA Trustee or Custodian?</i>	851
1. Banks and Life Insurance Companies Are Authorized	851
2. Approved IRA or Archer MSA Trustees Are Authorized.....	851
3. Entities Seeking Approval Must Demonstrate Ability to Meet Requirements.....	851
4. Passive Trustees May Be Relieved of Some Requirements	853
5. There Is No Required Form for the Application.....	853
6. Notice of Approval Must Be Provided to Prospective Account Beneficiaries.....	853
7. Approval May Be Revoked for Cause	853
8. State-Law Fiduciary/Trust Requirements	854
B. <i>Trust Requirements for HSA Trustees and Custodians</i>	855
1. Must Have Adequate Written HSA Trust Agreement.....	855
2. HSA Must Only Accept Cash Contributions, Valid Rollovers, Qualified HSA Distributions, or Qualified HSA Funding Distributions	855
3. Trustee/Custodian Is Not Required to Monitor Eligibility of HSA Account Holder.....	855
4. HSA Trustee/Custodian Cannot Accept More Than General Maximum Contribution.....	856
5. HSA Trustee/Custodian Is Not Required to Determine If Distributions Are Taxable	856
6. HSA Trustee/Custodian Must Comply With Reporting Requirements.....	856
7. HSA Trustees/Custodians Are Subject to Prohibited Transaction Rules.....	856
8. HSA Trustees/Custodians Are Not Required to Allow Returns of Mistaken Distributions	856
9. Trustees/Custodians May Not Restrict Ability to Request Rollover From HSA but Can Restrict Ability to Roll Over to HSA.....	856
10. HSA Trust or Custodial Agreement May Not Contain Certain Distribution Restrictions	856
11. HSA Trustees/Custodians May Impose Reasonable Restrictions Relating to Account Administration	857
C. <i>Investment of HSA Funds</i>	857
1. HSA Funds Are Subject to Some Investment Restrictions	857
2. HSA Administration or Account Maintenance Fees	858
3. Employer-Imposed HSA Investment Restrictions May Trigger ERISA	859
D. <i>Overview of HSA Prohibited Transaction Rules</i>	860
1. Rules Prevent Certain Improper Uses of Funds.....	860
2. HSAs Subject to Rules “Similar” to IRA Prohibited Transaction Rules	861
3. Examples of Likely Prohibited Transactions Involving HSAs	861
4. Prohibited Transaction Rules Carry Significant Penalties	864
5. Prohibited Transaction Rules Also Apply to HSA Trustees and Custodians.....	864
6. Exemptions From Prohibited Transaction Rules	865
E. <i>Quick Reference Chart of Selected Banking and Securities Laws</i>	867
F. <i>Comparison of IRAs and HSAs</i>	875
XVII. HSAs: Reporting Requirements	881
A. <i>HSA Trustee/Custodian Reporting Obligations</i>	881
1. Contributions	881
2. Distributions	882
3. Distributions of Excess Contributions	885
4. No Need to File IRS-Provided HSA Trust Account and Custodial Account Forms	886

5. No Need to Report HSA Administration and Account Maintenance Fees.....	886
6. No Need to Report on HSA Eligibility During Certain Testing Periods	886
7. Reporting Concerns Related to HSA Electronic Payment Cards.....	887
B. HSA Holder Reporting Obligations	887
1. Contributions	887
2. Excess Contributions	888
3. Distributions	889
4. Reporting Requirements Following HSA Holder's Death.....	890
5. Special Reporting Rules for Beneficiaries With More Than One HSA Due to Death.....	891
6. Reporting Requirements for 2008 Economic Stimulus Payments	892
C. Employer Reporting Obligations	892
1. Contributions	892
2. Excess Contributions	893
3. Reporting the Excise Tax on Comparability Failures	894
4. No Need to Report on HSA Eligibility During Certain Testing Periods	894
5. Form 5500 May Need to Be Filed If HSA Is an ERISA Plan	894
XVIII. HSAs: Plan Design Roadmap for Employers	921
A. Introduction.....	921
B. Employer Checklist for Designing and Implementing HSAs in the Workplace.....	921
1. Choose a Core Design for HSAs in the Workplace.....	921
2. Decide When to Make Employer Contributions to HSAs.....	922
3. Determine Whether Existing Health FSAs or HRAs Should Be Redesigned or Discontinued.....	923
4. Amend Existing Plans to Coordinate With HSAs.....	923
5. Make Arrangements With One or More HSA Providers	924
6. Design Employee Communication.....	924
7. Document the Program Being Offered.....	925
8. Establish Funding and Reporting Mechanisms	925
C. Special Considerations for HSAs Offered Through Cafeteria Plans	925
1. Do the Irrevocable Election Rules Apply?.....	926
2. Do Other Code § 125 Rules That Apply to Health FSAs Apply to HSAs?.....	927
3. What Nondiscrimination Rules Apply to HSAs?	928
4. Can an Eligible Individual Also Participate in a Health FSA or HRA?	930
5. Can an HSA Under a Cafeteria Plan Be Used to Fund Long-Term Care Coverage or Other Impermissible Items?.....	931
6. How Does a Health FSA Grace Period Affect HSA Eligibility?	932
7. What Cafeteria Plan Changes Are Required in Order to Offer HSAs?	933
8. Should HSA Benefits Be Implemented Mid-Year?.....	935
9. Can Existing Health FSA or HRA Account Balances Be Used to Fund an HSA?.....	935
10. To What Extent Does ERISA Apply?.....	936
11. Can Employees Make Pre-Tax Payroll Contributions to Their HSAs If Their Employer Doesn't Have a Cafeteria Plan?.....	936
D. Is an HSA an ERISA Plan?	941
1. ERISA Overview	941
2. Under DOL Guidance, HSAs in the Workplace Generally Are Not ERISA Plans	942

3. How Do ERISA’s Claims and Reporting Requirements Apply When an HSA Is an ERISA Plan?	947
<i>E. Other Federal and State-Law Issues</i>	<i>947</i>
1. COBRA	947
2. HIPAA	947
3. Medicare Part D and Medicare Secondary Payer (MSP) Requirements.....	949
4. Family and Medical Leave Act	951
5. State Law	951
XIX-XX. [Reserved].....	1051
XXI. Health Reimbursement Arrangements (HRAs): Introduction and Design Choices	1051
<i>A. Introduction</i>	<i>1051</i>
1. What Is an HRA?	1051
2. What We Cover	1052
3. Comparison of HRAs to HSAs and Health FSAs	1053
<i>B. HRA Legal Requirements.....</i>	<i>1053</i>
1. Governing Law.....	1053
2. Basic Legal Requirements for an HRA	1055
3. What Is the Consequence of Failing to Comply With IRS Guidance on HRAs?	1056A
4. Additional Compliance Requirements	1056A
<i>C. HRAs Are Not Subject to Many Health FSA Rules</i>	<i>1057</i>
<i>D. HRAs Are Not Subject to HSA Rules.....</i>	<i>1061</i>
<i>E. HRA Interaction With HSAs and Other Coordination of Benefits Issues</i>	<i>1062</i>
1. An Individual May Not Have General-Purpose HRA Coverage and Contribute to an HSA.....	1062
2. An Individual May Have Certain Limited Types of HRA Coverage and Still Be Eligible for an HSA.....	1063
3. Other Coordination of Benefits (COB) Issues	1068
<i>F. HRA Design Choices.....</i>	<i>1069</i>
1. Should the HRA Be Integrated With the Employer’s HDHC Arrangement?	1069
2. Should the Employer Adopt a Stand-Alone HRA?	1069
3. Who Should Be Eligible to Participate in the HRA?	1071
4. How Should Employer Contributions Be Structured?	1072
5. Funded or Unfunded HRA?.....	1073
6. Interest on HRA Balances?	1073
7. May HRA Coverage Be Insured?	1074
8. What Expenses Should be Eligible for Reimbursement?	1074
9. What Is the Ordering Rule for Reimbursements When There Is an HRA and a Health FSA?.....	1074
10. Must an HRA Have a Carryover Feature?	1076
11. May a Cap Be Placed on the Carryover Amount or Restrictions Placed Upon How the Carryover Amount May Be Used?	1076
12. Forfeit Account Balances or Permit Spend-Downs?	1077
13. Only Limited HRA Designs Are Compatible With HSA Eligibility	1077
14. Should the HRA Include a Direct Rollover Feature?.....	1078
15. What Issues Arise When an Employer Terminates Its HRA?.....	1078

XXII. HRAs: Employer Contributions, Reimbursements, and Other Operating Rules	1091
A. <i>HRAs Must Be Funded Exclusively by Employer and Not With Salary Reductions or Otherwise Under a Cafeteria Plan</i>	<i>1091</i>
1. No Direct Cafeteria Plan Funding of HRA—the COBRA Rule	1093
2. No Indirect Cafeteria Plan Funding of HRA	1093
3. When May Unused Vacation and Sick Pay Be Used to Fund HRAs?	1098
B. <i>HRAs May Reimburse Only Code § 213(d) Expenses</i>	<i>1103</i>
1. Out-of-Pocket Medical Expenses May Be Reimbursed by an HRA	1103
2. Health Insurance Premiums May Be Reimbursed by an HRA, but Caution Is Advised Due to HIPAA and Other Compliance Concerns	1104
3. Administrative Costs	1105
C. <i>Tax-Free Benefits May Be Provided Only to Employees, Former Employees, and Their Eligible Spouses/Dependents</i>	<i>1105</i>
1. General Rule	1105
2. Who Is a Dependent?	1105
3. No Tax-Free Benefits for Self-Employed Individuals and Those Who Are Not Spouses or Tax Dependents	1106
4. May an HRA Provide Taxable Coverage to Self-Employed Individuals and Those Who Are Not Spouses or Tax Dependents?	1107
D. <i>Timing of Expenses and Reimbursements</i>	<i>1109</i>
1. Expense Must Be Incurred When HRA Coverage Is in Effect (Although Claims May Carry Forward to Future Coverage Periods)	1109
2. Claims Incurred After Termination of Employment May Be Reimbursed If HRA Permits Participants to Spend Down Their Accounts Until Depleted	1110
E. <i>Other Reimbursement Requirements</i>	<i>1110</i>
1. No HRA Reimbursement of Expenses Reimbursed by Another Plan or Deducted by the Participant	1110
2. No Reimbursement for Employer Coverage That Could Be Funded Pre-Tax	1110
3. Expense Substantiation Requirement	1111
F. <i>No Cash-Out of Unused Amounts</i>	<i>1114</i>
G. <i>Treatment of HRAs Upon Divorce or Death</i>	<i>1115</i>
1. Treatment of HRAs Upon a Participant’s Divorce	1115
2. Treatment of HRAs Upon a Participant’s Death	1115
H. <i>Direct Rollovers of Qualified HSA Distributions</i>	<i>1117</i>
XXIII-XXIV. [Reserved]	1201
XXV. HRAs: Nondiscrimination, COBRA, and Other Compliance Issues	1201
A. <i>HRAs and Nondiscrimination</i>	<i>1201</i>
1. HRAs Cannot Discriminate in Favor of HCEs With Respect to Eligibility or Benefits	1202
2. Test #1 of 2: The Eligibility Test	1202
3. Test #2 of 2: The Benefits Test	1206
4. Special Nondiscrimination Issues Applicable to HRAs	1209
B. <i>HRAs and COBRA</i>	<i>1213</i>
1. HRAs Rarely Qualify for the Special Limited COBRA Obligation Available to Qualifying Health FSAs	1213
2. HRAs Must Offer COBRA Coverage, Even HRAs With a Spend-Down Feature	1214

3. Each Qualified Beneficiary Has an Independent Right to Elect COBRA to Continue HRA Benefits	1215
4. What Is the Qualified Beneficiary’s HRA Coverage Amount When COBRA Is Elected?.....	1216
5. Entitlement Under COBRA to Continuing Annual HRA Accruals	1218
6. Determining and Paying the COBRA Premium for an HRA.....	1218
7. Design-Based Responses to Problems Created by COBRA Under HRAs.....	1220
8. More Guidance Is Needed.....	1221
9. Temporary COBRA Premium Assistance and Plan Enrollment Option for Involuntarily Terminated Employees.....	1221
C. HRAs and HIPAA.....	1224A
1. Does the HRA Carryover Feature Violate HIPAA’s Nondiscrimination Rule?.....	1224A
2. Application of HIPAA Nondiscrimination Requirements to HRAs Designed to Reimburse Health Insurance Premiums.....	1225
D. HRAs and ERISA	1227
1. Employee Welfare Benefit Plans Are Subject to ERISA.....	1227
2. Written Plan Requirement.....	1227
3. ERISA Form 5500	1228
4. ERISA Disclosure Requirements.....	1229
5. How Do ERISA’s Claims Procedure Requirements Apply to HRAs?.....	1230
6. Plan Assets Subject to Exclusive Benefit Rule	1230
7. Trust Requirement Might Apply	1231
8. Bonding	1231
9. Fiduciary Duty and Civil and Criminal Enforcement Rules.....	1231
10. ERISA Record Retention Requirement.....	1232
E. HRAs and Other Laws	1232
1. Medicare Part D.....	1232
2. Medicare Secondary Payer (MSP) Requirements.....	1234
3. Other Laws	1238
XXVI. HRAs: Plan Design Roadmap for Employers	1251
A. Introduction	1251
B. Employer Checklist for Designing and Implementing an HRA	1251
1. Choose Between a Stand-Alone HRA or Integrated HRA+HDHC Arrangement	1251
2. Decide Which Employees (and Dependents) Will Be Eligible to Participate.....	1252
3. Decide the Benefits That Will Be Provided Under the HRA (i.e., the Expenses That Are Reimbursable).....	1252
4. Decide the Dollar Limit on Employer Contributions.....	1252
5. Decide How and When the HRA Will Be Funded	1253
6. Decide Whether to Permit Carryovers or Spend-Downs of the HRA	1253
7. Design Rules for Processing Reimbursements (Including Ordering Rules).....	1253
8. Select a Third-Party Administrator (TPA)	1254
9. Design Employee Communication, Education, and Support Tools	1254
10. Prepare and Adopt Plan Documents and Summary Plan Description (SPD) for HRA	1254
11. Prepare to Comply With HIPAA, COBRA, Medicare Part D, and Other Federal Mandates for Group Health Plans	1255
12. Know What to Do When the HRA Is Terminated	1255

13. Consider Possible Cost-Containment Strategies for HRAs	1255
XXVII-XXX. [Reserved]	1501
XXXI. Archer MSAs	1501
<i>A. What Individuals Are Eligible?</i>	1501
<i>B. What Is a Small Employer?</i>	1502
<i>C. Pilot Program Limitations</i>	1502
<i>D. Must Be Covered Under a High-Deductible Health Plan</i>	1502
1. What Is a High-Deductible Health Plan?	1502
2. Coverage Under Any Non-Permissible Health Plan Makes Individual Ineligible	1503
3. What Is Permissible Coverage?	1503
4. Utilization of Cafeteria Plan to Fund High-Deductible Coverage	1504
5. Planning Opportunity.....	1504
<i>E. Establishment of MSAs</i>	1504
<i>F. Tax Treatment of and Limits on Contributions</i>	1505
1. Who May Contribute?.....	1505
2. How Much May Be Contributed to an MSA?.....	1505
3. Employer Contributions Are Excludable.....	1505
4. Individual Contributions Are Deductible—Above the Line (but Still Subject to Employment Taxes)	1506
5. What Is the Tax Treatment of Earnings on Amounts in an MSA?	1506
6. What Happens When MSA Contributions Exceed the Amount That May Be Deducted or Excluded From Gross Income?	1506
<i>G. Distributions From MSAs</i>	1506
1. Distributions and the Code § 213 Deduction	1506
2. How Are Distributions From an MSA Taxed?.....	1506
3. Distributions for Ineligible Individuals	1506
4. What Medical Expenses Are Eligible for Tax-Free Distributions?	1506
5. Does It Matter When MSA Distributions Are Made?.....	1507
6. MSA Distributions Are Self-Reported.....	1507
<i>H. Additional Matters</i>	1507
<i>I. Medicare Advantage MSAs</i>	1508
<i>J. Specific Laws Governing MSAs</i>	1508
1. Statutes	1509
2. Legislative History	1509
3. Miscellaneous IRS Guidance.....	1509
<i>K. Archer MSAs and ERISA</i>	1510
Index	behind the Index and Glossary Tab
Glossary of Terms	behind the Index and Glossary Tab

Flowcharts, Tables and Graphics

Corridor of Risk.....	52
Chart Comparing HSAs, HRAs, and Health FSAs.....	141
HSA Flowchart: From Contributions to Distributions.....	258
Table: Permissible/Impermissible Types of Coverage for HSA Eligibility	505
Matrix of HSA Contribution Limits.....	542
Chart Comparing Flow of Funds, Tax Treatment, and Reporting Requirements.....	571
Quick Reference Chart of Selected Banking and Securities Laws.....	868
Comparison of IRAs and HSAs	875

Appendix Tabs

Tab 1: CDHC & Medical Plans	Tab 7: [Reserved]
Tab 2: [Reserved]	Tab 8: Forms & Publications
Tab 3: HSAs: Code & Regulations	Tab 9: Legislative History
Tab 4: HSAs: Other Guidance	Tab 10: Sample Documents
Tab 5: HRAs	Tab 11: Miscellaneous
Tab 6: [Reserved]	