



Insurance Brokers &
Consultants

Common Questions with HSAs, FSAs and HRAs

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Presenters



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Liz Mann is EPIC's internal compliance director. Liz and her team are responsible for disseminating information to clients about changing requirements and regulations and reviewing all plan designs and programs for compliance with Federal and State regulations. Liz is embedded into our account management team to provide timely support and guidance as ERISA-related regulations or concerns emerge in the marketplace. As a client, you have the option of directly accessing Liz or accessing her traditionally through your account team. Liz graduated Magna Cum Laude from Saint Mary's College in Notre Dame, IN with Bachelor of Arts degrees in History and French. She graduated with her law degree from University of Toledo, College of Law in Toledo Ohio in 2007. She has accumulated over 12 years of experience working in employee benefits and offers expertise in ERISA, IRS, COBRA, FMLA and ACA compliance.



David Flotten, J.D. Senior Compliance Consultant – Benefit Comply David has over 24 years' experience in employee benefits and employment law. David regularly presents on employee benefits compliance and other HR topics, including for the College of Continuing & Professional Studies at the University of Minnesota. He has also taught the PHR/SPHR and SHRM-CP/SHRM-SCP exam prep courses. Prior to joining Benefit Comply, David served as Sr. Compliance and Workplace Solutions Consultant at USI Insurance Services and as Sr. Compliance Consultant for Associated Benefits & Risk consulting. Before entering the employee benefits field, David worked at a private law practice and in the Minnesota court system. David received his law degree, magna cum laude, from the University of Minnesota Law School and his Bachelor of Arts degree from Gustavus Adolphus College. He is also a member of the Society of Human Resources Managers (SHRM).

Agenda

- HSAs
 - Now what? What to do when an employee fails to open an HSA.
 - HSAs & Medicare: How to handle employees who turn age 65
 - Oops! Dealing with mistaken HSA contributions
- Health FSAs
 - Health FSA elections when employees transition to an HSA plan
 - What's this thing!?! Substantiation and pay & chase reports
 - What's the difference between a run out period and grace period and what to do with unused Health FSA funds?
- HRAs
 - Did you know that HRAs are subject to COBRA?
 - An employee or retiree with an HRA can't get a premium subsidy – really?
 - Learning to count HRA participants, the PCORI way



HSA's

My employee never opened their HSA...

Do I still owe them the employer contribution?

If HSA is under a cafeteria plan...employer has flexibility

- No specific violation if employer contribution is not made
- Employee contributions are returned as taxable income

If HSA is NOT under a cafeteria plan...employer has less flexibility

- Comparability rules apply – much more complicated to avoid employer contribution

My employee never opened their HSA...

- Considerations:
 - Set forth expectations in benefits communications
 - Set notice or grace period for opening HSA and receiving employer contributions
 - DOL model notice
 - May condition employer HSA contributions on opening an HSA
 - Does not need to be made up later
 - For generous employers – can be given as taxable income, but beware
 - Have a consistent policy in place
 - Terminated employees

HSAs & Medicare: Employees Turning Age 65

An employee who enrolls in Medicare is no longer eligible to contribute to an HSA.

So, I should just automatically stop all HSA contributions once an employee turns age 65 then?

No! That would be age discrimination.

HSAs & Medicare: Employees Turning Age 65

- Some employees are automatically enrolled in Medicare upon turning age 65, e.g. if they are drawing social security retirement benefits
 - Medicare Eligible v. Medicare Entitled
- But others must affirmatively enroll in Medicare in order to be covered at age 65
- If an employee is not automatically enrolled in Medicare and does not enroll in Medicare, they can continue to make and receive HSA contributions beyond age 65
- Employer can't assume all employees age 65+ are ineligible to make or receive HSA contributions and automatically cut off contributions

HSAs & Medicare: Employees Turning Age 65

Option 1

- Include statement in benefit communications that employer will presume employee has enrolled in Medicare upon turning age 65 and terminate all further HSA contributions unless the employee specifically informs employer they have not enrolled in Medicare

Option 2

- Include statement in benefit communications that HSA contributions will continue upon the employee reaching age 65 until employee informs employer they have enrolled in Medicare; employee is responsible for all tax consequences for any improper contributions made because the employee failed to inform employer they enrolled in Medicare

Option 3

- Reach out to each employee upon reaching age 65 to inquire whether they have enrolled in Medicare and impact on HSA contributions

HSAs & Medicare: Employees Turning Age 65

No – but it's not complete nonsense either

I've heard employees have to stop contributing to their HSA 6 months before their 65th birthday. Is this true?

- For an employee who enrolls in Medicare after they turn age 65, their Medicare effective date is 6 months retroactive from the date they enroll (but not before their 65th birthday)
- The IRS has confirmed this will retroactively disqualify the employee's HSA eligibility during that 6 month period of retroactive coverage. So for an employee who is enrolling in Medicare after age 65, they should stop HSA contributions 6 months before they plan to enroll in Medicare
- But this retroactive coverage rule does not apply to someone who enrolls in Medicare at age 65 so employees do not need to stop HSA contributions 6 months before their 65th birthday

Employer Responsibility for HSA Contributions

In general, employers are only responsible for determining:

1. Whether the employee is covered under a qualifying HDHP sponsored by the employer
2. Whether the employee is covered under any non-HDHP (e.g., general purpose FSA) sponsored by the employer
3. For any catch-up contributions, the employee's age.

Provided that the above conditions are met, and provided that an employer has a reasonable basis for believing at the time it makes its contribution that an employee is HSA eligible, an employer's HSA contributions will be excludable from an employee's gross income and will not be subject to withholding from wages or income tax, or subject to FICA, FUTA, or RRTA.

Mistaken Employer Contributions

General Rule: Employer HSA Contributions are “Nonforfeitable” (i.e., cannot be recouped/recovered)

- Some Exceptions – See Next Slide
- May also be possible to seek reimbursement directly from employees
 - Personal check or from salary on after-tax basis (subject to wage-withholding)
 - Offsetting mistaken contribution against future contributions (with employee’s authorization)

Exceptions to Nonforfeitability Rule

Employee was never eligible to establish an HSA

- May recoup contributions if trustee/custodian agrees
- If employer cannot recoup amounts by end of taxable year in which contributions were made, excess amounts should be included as gross income and wages in employee's W-2
- If employer should not have contributed, then should make payroll filing corrections

Contributions made in excess of the full, annual, statutory maximum

- May recoup contributions if trustee/custodian agrees
- If employer cannot recoup amounts by end of taxable year in which contributions were made, excess amounts should be included as gross income and wages in employee's W-2

Clear administrative/process error

- Duplicate payroll files, wrong data entry, decimal point in wrong place, mixing employee names up, etc.

Mistaken Employer HSA Contributions - Examples

Scenario 1

An employee enrolls in an employer's HDHP on January 1st and does not elect any non-HDHP coverage sponsored by the employer. The employer begins contributing to the employee's HSA and discovers midyear that the employee has been covered under a general purpose health FSA through his spouse's employer.

Did the employer meet its obligations? Yes – the employee was enrolled in an HDHP sponsored by the employer and was not enrolled in any non-HDHP sponsored by the employer, so the employer's contributions are excludable. Since the employee was never actually eligible to establish an HSA, the non-forfeitability rules wouldn't apply and the employer would have the option of requesting a return of its contributions from the HSA custodian. If it is unable or unwilling to obtain the amounts contributed, the employer should include the amounts as gross income and wages on the employee's W-2.

Scenario 2

An employee enrolls in an employer's HDHP and its general purpose health FSA. The employee also establishes an HSA. Due to an administrative error, the employer begins contributing to the employee's HSA.

Did the employer meet its obligations? No – the employer should have known that the employee had also enrolled in its non-HDHP coverage. The employer could attempt to recoup its contributions since the employee was never actually eligible to establish an HSA. If it is unable or unwilling to do so, it will need to include the excess amounts in the employee's gross income and wages on the employee's W-2. And the employer will need to make appropriate corrections to its payroll filings/reports under applicable IRS regulations.

Mistaken Employer HSA Contributions - Examples



Scenario 3

An employee enrolls in the employer's HDHP effective January 1st and does not enroll in any non-HDHP coverage sponsored by the employer. The employer begins making contributions to the employee's HSA. In April, the employee enrolls in Medicare and loses HSA eligibility. The employee does not inform the employer of their Medicare entitlement until August.

Did the employer meet its obligations? Yes – the employer is only responsible for determining that the employee enrolled in its HDHP and did not enroll in any non-HDHP sponsored by the employer. The employer should discontinue any further contributions but will not be able to recoup the contribution it has already made because the employee was eligible for an HSA at the start of the year. The employee will be responsible for determining whether any excess contributions were made and for requesting a curative distribution, if necessary, to avoid the 6% excise tax.



Health FSAs

FSAs and Transitioning to an HSA

- A general purpose Health FSA is a non-HDHP that will disqualify an employee from making or receiving HSA contributions.
 - A limited purpose Health FSA, i.e. one limited to reimbursing dental or vision expenses, or a post-deductible Health FSA is not disqualifying.
- What happens when an employee moves from a non-HSA plan to an HSA plan while they have an active general purpose Health FSA election in place?
 - Scenario 1: Employer adopts new HSA plan
 - Scenario 2: Employee has a special enrollment event and enrolls in HSA
 - Scenario 3: Employee enrolls in HSA during open enrollment and Health FSA has a grace period or carryover feature

FSAs and Transitioning to an HSA

Scenario 1

- In the middle of the Health FSA plan year the employer adopts a new HSA plan option, e.g. because health plan year is different from Health FSA plan year.

ProTip

- Avoid the problem altogether by aligning health plan and Health Plan FSA plan years up front!

Three Options

FSAs and Transitioning to an HSA

- **Scenario 1, Option 1.** Terminate the general purpose Health FSA midyear and start a new general purpose/limited purpose Health FSA with first day of health plan year
 - Old general purpose Health FSA election ends so is no longer disqualifying nonHDHP coverage
 - Employees can make a new election in appropriate general purpose/limited purpose Health FSA
 - BUT all remaining balances in any underspent accounts in the old general purpose Health FSA are forfeited and employer cannot collect additional contributions on any Health FSA accounts that were overspent at time of termination

FSAs and Transitioning to an HSA

- **Scenario 1, Option 2.** Convert the general purpose Health FSA to a limited purpose Health FSA at the start of the health plan year
 - Limited purposes Health FSA is not disqualifying nonHDHP coverage so employees with Health FSA election can contribute to HSA
 - BUT must convert the Health FSA to a limited purpose Health FSA for all participants regardless of whether they have elected HSA plan or not. Cannot convert to a limited purpose Health FSA on a participant-by-participant basis depending on whether they elected the HSA or not
- **Scenario 1, Option 3.** Leave the general purpose Health FSA as is.
 - No election changes allowed but no forfeitures or losses either
 - Participants with a Health FSA election who elect the HSA plan cannot make any HSA contributions until the end of the Health FSA plan year
 - An employee whose Health FSA balance drops to \$0 is still a participant in the Health FSA and precluded from making any HSA contributions until the end of the Health FSA plan year

FSAs and Transitioning to an HSA

Scenario 2

- Employee makes a general purpose Health FSA election but waives coverage on the health plan at the start of the year. Midway through the year the employee experiences a midyear special enrollment event and enrolls on the HSA plan.

Drop?

- In most cases, the special enrollment event will not allow the employee to drop their Health FSA election.

Convert?

- The employee can't convert the general purpose Health FSA to a limited purpose Health FSA – the IRS views these as two separate accounts and you can't move funds from one FSA to another

Result

- This employee may not make or receive any HSA contributions until the end of the Health FSA plan year.
- An employee whose Health FSA balance drops to \$0 is still a participant in the Health FSA and precluded from making any HSA contributions until the end of the Health FSA plan year.

FSAs and Transitioning to an HSA

Scenario 3

- Employee has a general purpose Health FSA election for the plan year that is just ending. The Health FSA has a grace period or carry over option. The employee elects the HSA plan for the next plan year during open enrollment.
- The grace period or carryover effectively extends the general purpose Health FSA coverage into the next plan year.
- It is therefore disqualifying nonHDHP coverage precluding HSA contributions in the next plan year for some period of time.

Grace Period.

- Employee is HSA ineligible for each calendar month the grace period is in effect as of the first day of the month –typically 3 months.
- Maximum annual HSA contribution limit is prorated to 9/12 of normal (assuming employee remains HSA eligible the remainder of the year)
- Alternatively, employer can convert general purpose Health FSA to a limited purpose Health FSA but must do so for all participants, not just those who elect the HSA plan

Carryover

- If general purpose Health FSA balance is \$0 as of the last day of the plan year so there is no carryover, then employee is not disqualified from making HSA contributions
- If there is any carryover the employee is disqualified from making HSA contributions for the entire next plan year unless:
 - Employee waives their carryover balance
 - Employee elects to convert to a limited purpose Health FSA –unlike the other two scenarios this can be done on a participant-by-participant basis.

FSA Substantiation Errors – Correction (“Pay and Chase”)



- IRS Rev. Rul. 2003-43 (<https://www.irs.gov/pub/irs-drop/rr-03-43.pdf>) outlines the proper procedures for handling improper or unsubstantiated claims made via an FSA or HRA debit card (and an FSA in general if not an FSA with an exception of the first step)
- If proper substantiation is not provided, the administrator will generally take several corrective actions, including:
 - Deactivating debit card and not reactivating until all improper claims are cleared up
 - Reach out to request additional information from the individual
 - Offsetting the improper reimbursement amounts against additional claims submitted, if possible
- In cases which the amount cannot be collected (e.g. from a former employee), the employer may write it off as bad business expense and the payment should be reported as wages on the Form W-2 for the year in which the indebtedness is forgiven and is subject to withholding for income tax, FICA, and FUTA

What do I do with unused FSA funds?

- Use-or-Lose Rule

- Unused FSA funds at the end of the plan year are forfeited
 - “Experience gains”
- Exceptions:
 - Carryover
 - **Grace period** vs. **Run-out period**

Additional time to...

INCUR vs. **SUBMIT**

...claims for reimbursement

What do I do with unused FSA funds?

- Permissible uses of experience gains:
 - Offset losses from overspent accounts
 - Defray plan administration expenses
 - Reduce salary reduction amounts the following plan year – must be provided uniformly
 - Provide to employees as cash refund – must be distributed uniformly
 - Increase annual coverage amount



HRA's

Does COBRA Apply to HRAs?


- Yes
 - Even those with a spend-down feature
 - Allows a former employee to deplete their HRA funds
- Integration with Medical
 - May require bundling with medical plan for COBRA, so long as active employees are also required to bundle

What is the COBRA Premium for an HRA?

- Additional COBRA premium charge for HRA is permitted
 - Turns into a single blended premium with other elected benefits
 - Ex. Medical premium is \$200, HRA premium is \$50 – so total COBRA premium is \$250
- Setting the HRA COBRA premium
 - Two methods: Past Cost and Actuarial

HRAs and Premium Subsidies

An individual enrolled in employer sponsored Minimum Essential Coverage (MEC) cannot receive a premium subsidy through the Exchange



An HRA is MEC, unless it is limited to excepted benefits, e.g. a dental/vision only HRA



An employee or retiree enrolled in an HRA is not eligible for a premium subsidy.

HRAs and Premium Subsidies

- Usually not a problem for active employee HRAs since those generally require the employee be enrolled in other group health coverage to participate in the HRA in the first place
 - Employee generally has no need for an individual policy and subsidy
 - Other group coverage would disqualify the employee anyway
- But this can be an issue in those situations where a stand-alone HRA is allowed
 - Retiree only HRA even if it only reimburses premiums
 - HRA with a spend down feature
- To avoid trapping an employee/retiree in an HRA when they would be better off with a premium subsidy consider a waiver or suspension feature in the HRA

HRAs – Paying the PCORI Fee

HRAs are Self-Funded health plans and subject to PCORI fees unless they are an excepted benefit

- HRAs integrated with fully-insured plans:
 - Employer responsible for paying PCORI fee on behalf of the HRA
 - May assume “one covered life per enrollee” – i.e., does not need to include spouses/dependents in count
- HRAs integrated with self-funded plans:
 - Employer responsible for paying PCORI fee on behalf of self-funded plan and HRA
 - Assuming same plan sponsor/same plan year for both plans:
 - May treat plans as a single plan and count enrollees, spouses, and dependents covered by both plans only once

HRAs – Paying the PCORI Fee - Examples

Employer sponsors HRA (CY) and Self-Funded Medical Plan (6/1 Renewal)

- Employer must pay PCORI fee for each plan
- Must count participants separately under each plan

Employer sponsors CY HRA & CY Self-Funded Medical Plan

- Employer can treat the 2 plans as a single plan and count enrollees, spouses, and dependents covered by both plans only once
- If HRA covers anyone not covered under medical plan, may assume “one covered life” for each employee (i.e., does not need to count spouses/dependents)

Employer sponsors HRA and Fully Insured Medical Plan

- Carrier will pay PCORI Fee for medical plan
- Employer must pay PCORI Fee for HRA
- May assume one covered life for each employee



Questions?
