COMPLIANCE ALERT

Insurance Brokers & Consultants

HEALTH SAVINGS ACCOUNTS: *DISQUALIFYING HEALTH COVERAGE*

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QUICK FACTS

- In order to make or receive tax-free contributions to a Health Savings Account (HSA), an individual may not have "disqualifying health coverage."
- Disqualifying coverage is coverage that pays for or reimburses medical expenses before an individual meets the minimum deductible for coverage under a High Deductible Health Plan (HDHP).
- Examples of coverage that may disqualify an individual from making or receiving HSA contributions are general-purpose Health Flexible Spending Accounts (HFSA), Medicare, certain on-site health clinics, and certain telemedicine programs.
- Employers providing HSA contributions are responsible for determining that employees are not covered by any HSA-disqualifying coverage sponsored by the employer.
- Clear communications about HSA qualifications and safeguards for preventing enrollment in HSA-disqualifying coverage are essential for avoiding HSA eligibility issues.

BACKGROUND

In order to make or receive tax-free contributions to a Health Savings Account (HSA), an individual must meet certain qualifications. Two key requirements are having coverage under a high-deductible health plan (HDHP) and having no other coverage that is "disqualifying health coverage." Some types of disqualifying health coverage are obvious, while other types may come as a surprise to employer plan sponsors and HDHP/HSA participants.

WHAT IS DISQUALIFYING HEALTH COVERAGE?

Disqualifying coverage, for purposes of HSA eligibility, is coverage that pays for or reimburses medical expenses before the individual's HDHP minimum deductible has been met. Common examples are described below.

- ***Non-HDHP Health insurance***. Non-HDHP coverage that provides significant benefits for medical care or treatment benefits is disqualifying for HSA contribution purposes. Certain coverage that provides limited health benefits such as disability, limited-scope dental and/orvision, long-term care, and limited purpose health care flexible spending account (HFSA) are not disqualifying coverage.

- ***General-Purpose Health Flexible Spending Account (HFSA) or Health Reimbursement Arrangement (HRA).*** Enrollment in or eligibility for reimbursement from a general-purpose HFSA (which provides reimbursement for all eligible health care expenses) or an HRA generally prevents HSA eligibility. This includes a general-purpose HFSA or HRA of a spouse or dependent that covers the expenses of the individual.

  Individuals with a general-purpose HFSA that provides a grace period during which it will reimburse claims are ineligible to contribute to an HSA until the first day of the first month after the end of the grace period. Thus, for individuals enrolled in general-purpose HFSA that is based on the calendar year, these individuals will generally remain ineligible to make or receive HSA contributions until April 1st (first day of the first month following the end of a 2½ month grace period).

  Also, if a general-purpose HFSA allows for a carryover of up to $500 from previous plan year, the carryover constitutes disqualifying coverage for HSA contribution purposes. However, a cafeteria plan may provide that any employee who enrolls in HDHP will be automatically enrolled in a limited-purpose HFSA (e.g., used only for vision and dental expenses). Thus, any unused amounts from the general-purpose HFSA may be rolled over to a limited-purpose HFSA which would not prevent HSA contributions.

- ***Medicare***. Enrollment in Medicare, including Parts A, B, and D, prevents eligibility for HSA contributions. As an added complication, Medicare Part A may provide retroactive coverage of up to six months prior to the date an individual enrolls in Medicare. Therefore, individuals intending to enroll in Medicare Part A should discontinue making or received HSA contributions at least six months before enrolling in Medicare.

- ***Employee Assistance Plans (EAPs) and other limited benefits.*** EAPs that provide significant benefits in the nature of medical care or treatment may disqualify individuals from being eligible to contribute or receive contributions to an HSA. Whether an EAP provides significant medical benefits is determined under the specific facts and circumstances under which it is offered. Luckily for employers, most employee assistance, disease management, or wellness programs are not HSA-disqualifying because they do not generally provide significant benefits in the nature of medical care or treatment.

- ***On-site clinics***. On-site health clinics that provide significant medical benefits for free or at reduced cost may disqualify employees from making or receiving HSA contributions. Clinical services that are limited to first aid, treatment of workplace illnesses or injuries, preventive care or other types of permitted coverage are not disqualifying coverages. However, if structured carefully, even more significant on-site clinical services that coordinate with HDHP coverage will not prevent HSA eligibility. For example, if HDHP participants pay the fair market value (FMV) of the services before the deductible has been paid, they would not be prevented from receiving or making HSA contributions.

- ***Telemedicine.*** Telemedicine benefits allow employees to access medical care via electronic means (e.g., telephone or video conferencing). Telemedicine benefits will not prevent HSA eligibility when the telemedicine services are structured to provide only preventive services or otherwise do not provide significant benefits for medical care or treatment. However, if the benefit *does* provide significant medical care – such as diagnosis, treatment plans or prescriptions – at no cost or at a reduced- cost before the HDHP deductible is satisfied, the benefit is disqualifying coverage for purposes of HSA contributions. One method to preserve employee HSA eligibility entails charging participants the FMV of the services until the HDHP deductible is satisfied. After the deductible is paid, employees can access the benefit at low or no cost without jeopardizing HSA contributions.

EMPLOYER RESPONSIBILITY REGARDING DISQUALIFYING HEALTH COVERAGE

Employers that make HSA contributions (both employer and employee contributions from salary reductions) are responsible for determining that employees are not covered by any HSA-disqualifying coverage sponsored by the employer (such as a general purpose HFSA). This requires clear, concise and effective communications prior to enrollment.

As another protective measure, some employers ask employees to certify that they meet the criteria for HSA-eligibility. This practice helps an employer avoid contributing on behalf of an ineligible individual. It is also a way to explain HSA eligibility criteria and the factors that might affect the ability to make or receive contributions. In addition, administrative or technical safeguards should be set up to prevent enrollment in HSA-disqualifying coverage for those that wish to enroll in an HDHP that features an HSA.

SUMMARY

Employers should understand the requirements that apply to their HDHPs and HSAs in order to maintain compliance with federal laws and avoid penalties and excise taxes. Employers should establish administrative safeguards to ensure HDHP/HSA eligibility. Finally, clear and thorough employee communications about HDHP features and HSAs qualifications is essential for successful HDHP enrollment and prevention of erroneous HSA contributions.

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