Understanding an HRA

A health reimbursement arrangement (HRA) is an employer-funded account that is designed to reimburse employees for qualified medical expenses that are paid for out-of-pocket. There are no annual contribution limits on HRAs. However, the employer usually sets the contribution below the annual deductible. HRAs are often designed to operate with a high deductible health plan (HDHP), thereby reducing premium costs while encouraging employees to spend wisely.

Your employer sets up the HRA, determines the amount of money available in each employee's HRA for the coverage period, and establishes the types of expenses the funds can be used for.

What are the benefits of an HRA?

You may enjoy several benefits from having an HRA:

- Contributions made by your employer can be excluded from your gross income.
- Reimbursements may be tax-free if used to pay for qualified medical expenses.
- Any unused amounts in the HRA can be carried forward for reimbursements in later years.

Who is eligible for an HRA?

HRAs are employer-established benefit plans. These may be offered in conjunction with other employer-provided health benefits. Employers have complete flexibility to offer various combinations of benefits in designing their plan. You do not have to be covered under any other health care plan to participate. Self-employed persons are not eligible for an HRA. Certain limitations may apply if you are a highly compensated participant.

An HRA may reimburse medical care expenses only if they are incurred by employees or former employees (including retirees) and their spouses and tax dependents. HRA coverage must be in effect at the time the expense is incurred.

Are HRAs really best only for the young and healthy?

No. HRAs and other HDHPs are well-suited for a very wide demographic of people. According to Aetna, the average age of its HRA plan members is 42, the same average age as those who opted for more traditional plans.

What is an HDHP?

An HDHP has:

- A higher annual deductible than typical health plans; and
- A maximum limit on the sum of the annual deductible and out-of-pocket medical expenses that you must pay for covered

expenses. Out-of-pocket expenses include copayments and other amounts, but do not include premiums.

An HDHP may provide preventive care benefits without a deductible or with a deductible below the minimum annual deductible. Preventive care includes, but is not limited to, the following:

1. Periodic health evaluations
2. Routine prenatal and well-child care
3. Child and adult immunizations
4. Tobacco cessation programs
5. Obesity weight-loss programs
6. Screening services (e.g., cancer, heart and vascular diseases, infectious diseases)

Contributions to an HRA

Your employer funds the account, so it costs you nothing out-of-pocket. There is no limit on the amount of money your employer can contribute to the accounts. Additionally, the maximum reimbursement amount credited to the HRA in the future may be increased or decreased at your employer's discretion. The maximum annual contribution is determined by your employer's plan document. There may also be a cap amount for the HRA. Your employer can choose to fund your HRA with an annual contribution or on a monthly basis.

Distributions from an HRA

Distributions from an HRA must be paid to reimburse you for qualified medical expenses you have incurred. The expense must have been incurred on or after the date you are enrolled in the HRA.

Debit cards, credit cards and stored value cards given to you by your employer can be used to reimburse participants in an HRA. If the use of these cards meets certain substantiation methods, you may not have to provide additional information to the HRA.

If any distribution is, or can be, made for other than the reimbursement of qualified medical expenses, any distribution (including reimbursement of qualified medical expenses) made in the current tax year is included in gross income. For example, if an unused reimbursement is payable to you in cash at the end of the year, or upon termination of your employment, any distribution from the HRA is included in your income. This also applies if any unused amount upon your death is payable in cash to your beneficiary or estate, or if the HRA provides an option for you to transfer any unused reimbursement at the end of the year to a retirement plan.

If the plan permits amounts to be paid as medical benefits to a designated beneficiary (other than the employee's spouse or dependents), any distribution from the HRA is included in income.

Reimbursements under an HRA can be made to the following persons:

1. Current and former employees
2. Spouses and dependents of those employees
3. Employees' covered tax dependents
4. Spouses and dependents of deceased employees

Qualified Medical Expenses

Qualified medical expenses are those specified in the plan that would generally qualify for the medical and dental expenses deduction. Examples include amounts paid for doctors' fees, prescription medicines* and necessary hospital services not paid for by insurance. You can use your HRA funds for deductibles, copayments and coinsurance. An extensive list can be found in the IRS document, Publication 502 at www.irs.gov.

Balance in an HRA

Amounts that remain at the end of the year may be carried over to the next year depending on your employer's plan design. Your employer is not permitted to refund any part of the balance to you. These amounts may never be used for anything but

reimbursements for qualified medical expenses.

What if I terminate my employment during the plan year?

If you cease to be an Eligible Employee (i.e., you die, retire or terminate employment), your participation in the HRA Plan will end unless you elect COBRA continuation coverage. You will be reimbursed for any medical care expenses incurred prior to your termination date, up to your account balance in the HRA, provided that you comply with the plan reimbursement request procedures required under the plan. Any unused portions will be unavailable after termination of employment. The rules regarding COBRA are contained within your Summary Plan Description.

Will I have any administrative costs under the HRA plan?

Generally, no. Your employer bears the entire cost of administering the HRA plan while you are an employee.

How long will the HRA plan remain in effect?

Although your employer expects to maintain the HRA plan indefinitely, it has the right to terminate the HRA plan at any time. Your employer also has the right to amend the HRA plan at any time and in any manner that it deems reasonable, in its sole discretion.

Are my benefits taxable?

The HRA plan is intended to meet certain requirements of existing federal tax laws, under which the benefits that you receive under the HRA Plan generally are not taxable to you. Your employer cannot guarantee the tax treatment to any given participant, since individual circumstances may produce differing results.

What is the difference between an HRA and FSA?

HRAs are employer-funded, which means your employer determines the amount that goes into the HRA account. FSAs can be funded by employee and employer contributions. FSA contributions are deducted from your salary, usually on a pre-tax basis. You determine how much to contribute to your FSA account.

What does the IRS require me to report on my taxes concerning my HRA?

Nothing. Your HRA is a health benefit.

*Over-the-counter medications are considered to be qualified expenses only if purchased with a prescription (except for insulin, which is considered to be a qualified expense even without a prescription).

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