BENEFIT
Plan Developments

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FSAs Can Be Used For OTC Medical Purposes

In recognition of the increasing number of former prescription drugs now being made available in the over-the-counter (OTC) market, the U.S. Treasury Department and the Internal Revenue Service (IRS) are now allowing the use of health care **flexible spending accounts (FSAs)** for nonprescription drugs.

In Revenue Ruling 2003-102, the government agencies clarified that pre-tax FSA dollars can be used for such purchases. The types of drugs specifically mentioned by the IRS are antacids, allergy medicines, pain relievers, and cold medicines purchased without a physician's prescription. Reimbursements are allowed for purchases made by the employee, the employee's spouse, or the employee's dependents. One exception specified in the ruling are dietary supplements. The IRS characterized such purchases as "merely beneficial to the general health of the individual" and not an expense for medical care.

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"Many health plans no longer cover the cost of these drugs as over-the-counter," an IRS news release noted. "While an over-the-counter drug is less expensive than the prescription drug, the cost to many consumers increases because the price paid by the consumer for the over-the-counter drugs is greater than the co-payment by the consumer when the drug was covered by insurance."

The government action "makes paying for [OTC drugs] a little bit easier to swallow," said Treasury Secretary John Snow. Meanwhile, IRS Commissioner Mark W. Everson noted: "Flexible spending accounts were established under the Tax Code to provide incentives for better health care. This action is a sensible expansion and simplification of the program consistent with existing law."

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As a result of the ruling, depending on existing language, **summary plan descriptions (SPDs)** and administrative forms may need to be modified. In addition, some administrative issues may have to be addressed. For example, some dietary supplements are marketed similar to medicines, but would not fall under the FSA ruling. Furthermore, documentation can present challenges. The receipts from the purchase of OTC medicines, for example, may not necessarily show the names of the items purchased, or the name of the person making the purchase.

HRA Monies Can Be Excluded From Gross Income

In a Private Letter Ruling (#29014), the Internal Revenue Service (IRS) has stated that coverage of medical reimbursements under **health reimbursement arrangements (HRAs)** "is excludable from a participating employee's gross income under IRS Sec. 106 and that reimbursements of medical care expenses. . .are excludable. . . under IRC Sec. 105(b)."

The letter means plan sponsors can request rulings on HRAs.

Although the Private Letter only applies to the plan that requested the ruling, it reveals to plan sponsors that they can request rulings on HRAs from the IRS.

The plan reviewed by the IRS allows lower paid employees to elect a higher HRA amount than more highly paid employees without violating the **discrimination rules** of IRC Sec. 105(h). In addition, because there is no uniform coverage rule for HRAs as there is for **Section 125 flexible spending accounts,** this specific plan provides only a pro-rata portion of an HRA amount to be available for reimbursement on each payday. Finally, because the Tax Code does not prohibit it, this particular plan is made available only to employees who have elected to purchase employer-sponsored health insurance through salary reduction.

The Private Letter Ruling essentially supports HRAs that comply with IRS Notice 2002-45. Toward that end, the IRS said it defines HRAs, in part, as those that: (1) are paid for solely by an employer and not subject to salary reductions; (2) reimburse employees for expenses in accordance with IRC Sec. 213(d); and (3) carryforward any unused portion of the maximum dollar amount to subsequent periods.

HHS, OCR Do Not Provide HIPAA Endorsements

Neither the U.S. Department of Health and Human Services (HHS) nor the Office for Civil Rights (OCR) endorse any private consultants' or education providers' training materials regarding the Health Insurance Portability and Accountability Act (HIPAA) privacy rule.

The OCR said it has received reports that some enterprises are claiming their products are endorsed by the HHS or OCR. As a result, the OCR announced "HHS and OCR do not endorse any private consultants' or education providers' seminars, materials or systems, and do not certify any persons or products as 'HIPAA compliant.'"

In addition, the OCR noted that all materials on its Educational Materials page (http://www.hhs.gov/ocr/hipaa/assist.html) "have either been produced directly by OCR or have been reviewed by OCR prior to their publication. OCR also provides links to other useful sites, but does not review or endorse the materials found on those sites."

CDHPs Require Balance, Strategy To Control Expenses

Without the right implementation strategy, **consumer-driven health plans (CDHPs)** may not be particularly effective in controlling escalating health care costs, according to a speaker at the Consumer-Directed Health 2003 conference in Chicago.

Consultant Dan Plante of PricewaterhouseCoopers told those in attendance that CDHPs would be most effective in controlling costs only if the right deductibles were established and potential loopholes were closed.

For example, Plante suggested that CDHP deductibles be set at a reasonable high level. He said if deductibles are set too low—$1,000 or lower for single coverage—then they may not persuade individuals to change any of their high-spending habits. On the other hand, Plante noted, too high of a deductible could prevent employees from enrolling in a CDHP. Plante said a "happy medium" would generally be $2,000–$2,500 for single coverage and twice that amount for family coverage.

Similarly, Plante said that employee contributions to **health reimbursement arrangements (HRAs)** should be not too high or too low. He suggested setting HRA contributions at 40%–60% of the deductible.

Finally, the consultant noted that Internal Revenue Service guidance on HRAs allows plan sponsors to cover health expenses from past years—creating the possibility of a "look-back loophole." Plante explained that an employee with a $2,000 medical bill and a $1,000 HRA could use 100% of his funds in year one, wait one year, and then apply the new year's funds to pay off the remaining balance. Plante suggested that plan documents be written to prohibit such loopholes.

Another Reason LTC Could Be A Valuable Benefit

A report about the increasing prevalence of Alzheimer's disease—in the August 2003 issue of *Archives of Neurology*—provides a reason why individuals may want to consider the need for **long-term care (LTC) insurance**.

The report states that in 2000, there were 4.5 million persons with Alzheimer's disease in the United States, a number that could increase by nearly three times to 13.2 million by 2050—unless new medical discoveries are made during the interim.

That projected 300% increase could have overwhelming economic consequences, based on a study commissioned last year by the Alzheimer's Association. That study showed that American businesses were spending $61 billion a year on Alzheimer's disease in 2002, or twice as much as they did only four years earlier. That total included $10 billion in absenteeism costs, $18 billion in productivity losses, $6 billion in worker replacement costs, $2 billion for continuing insurance for workers on leave, as well as temporary worker replacement fees, and $64 million in Employee Assistance Program costs.

13.2 million people could have Alzheimer's by 2050.

An increasing number of employers are apparently cognizant of the increasing need for LTC insurance. The Society for Human Resource Management reports that 47% of employers currently offer LTC insurance to their employees, compared to 36% just three years ago.

FMLA Provides No Defense For Tardy Employee

An employee who showed up late for work and then sued her employer for violating the **Family and Medical Leave Act (FMLA),** did not provide sufficient notice prescribed by the Act. Furthermore, by signing a resignation letter and agreement, the employee waived any claims offered under the FMLA.

That was the ruling of the United States Court of Appeals for the Tenth Circuit in *Gwendolyn Bryant v. American Airlines, Inc.* (No. 02-5106) which upheld a decision by the U.S. District Court for the Northern District of Oklahoma.

After being fired for reporting late for work on November 19, 1998, Bryant was terminated pursuant to a letter of resignation and an accompanying agreement. She subsequently filed a complaint in district court. She alleged interference with her attempts to exercise her rights under the FMLA, refusal to grant FMLA leave, and retaliation in connection with her state workers compensation claim.

The district court, however, concluded that summary judgment was warranted because the plaintiff: (1) failed to give defendant sufficient notice under the FMLA; (2) waived her claims by signing the resignation letter and agreement; and (3) failed to make out a **prima facie** case of retaliation under the applicable state law.

On appeal to the circuit court, Bryant argued that the FMLA allows employees to give notice as soon as practical, rather than in advance of the requested leave, and that she need not have mentioned the FMLA expressly to give her employer adequate notice. However, the court found that there was no admissible evidence in the record showing Bryant asked for leave on November 19, 1998, or even indicated she could not work her shift.

"Without some indication to her supervisor that she needed leave in connection with her alleged back pain, defendant could not be put on notice such that its duties under the FMLA were triggered," the court's order and judgment stated.

Moreover, the court noted that the form Bryant submitted to the company's medical department earlier that same day indicated she was not currently incapacitated for work. "The FMLA provides for medical leave only when the applicant suffers from 'a serious health condition that makes the employee unable to perform the functions of the position of such employee,' " the court noted.

On appeal, Bryant had argued that the resignation letter and agreement she signed had not been done voluntarily. The circuit court rejected that point and noted that Bryant's employment records showed repeated warnings concerning tardiness and numerous instances of absences.

The form submitted by the plaintiff indicated she was not incapacitated.