

CONSUMER DRIVEN HEALTH PLANS

The goal of consumer driven health plans is to give an employee greater control over how their health care dollars are spent. These types of programs shift an employee's expense from the presumption of claims through guaranteed premium dollars to the payment of claims once they have actually been incurred.

This concept originated in 1996 with the introduction of **Medical Savings Accounts (MSA)**. Simply stated, an MSA allowed an individual to make tax-deferred deposits into an account which was designated to pay for qualified medical expenses. However, MSAs had many limitations which inhibited growth and they soon became obsolete. At this time there are no financial institutions opening new MSAs.

MSAs have since been superseded by **Health Savings Accounts (HSA)** which are available to **almost** everyone who participates in a qualifying **High Deductible Health Plan (HDHP)**. An HDHP applies a deductible to all eligible network and non-network medical expenses, including prescriptions. Only "preventive care" may be covered on a first-dollar basis (with or without a copay). Deductibles and out-of-pocket expense maximums may be adjusted annually for inflation. Following are individuals who are **not** eligible to contribute to an HSA:

- Anyone enrolled in a second plan which covers first-dollar expenses e.g., a husband and wife working for two different employers who offer plans with coordination of benefits;
- Anyone enrolled in Medicare;
- Anyone who can be claimed as a dependent on someone else's tax return.

Participation in a Flexible Spending Account (FSA) or a Health Reimbursement Arrangement (HRA) **may** also make an individual ineligible to contribute to an HSA.

Contributions to an HSA can be made by an employee, their employer or a combination of both. However, total contributions are limited and, as with the deductibles and out-of-pocket expenses of an HDHP, may be adjusted annually. All parties should consult with their accountant/tax advisor regarding the deductibility criteria of their contributions as well as contributions made on their behalf. In addition, employers must ensure that their contributions comply with the IRS comparability rules. If not, a 35% excise tax will be assessed.

Money may be withdrawn from an HSA to cover qualified medical expenses as well as certain health care premiums as defined by IRC 213d. Non-qualified use results in a taxable withdrawal plus a 10% penalty. After you turn age 65, become disabled and/or enrolled in Medicare, the 10% tax penalty no longer applies. Note that the account is wholly owned by the employee and completely portable. In addition, any unused funds remain in the account from year to year. Transactions are administered and recorded by the individual. Contributions, distributions and interest must be listed on Form 8889 and included with an individual's annual tax return.

Health Reimbursement Arrangements (HRA) would be another method of reimbursing employees for qualified medical expenses. HRAs are considered a “virtual account” since they do not require funding up front. Cash would only need to be made available once a claim has been approved. In addition, an employer may choose to roll over the “virtual balances” to the next year or start fresh each year by implementing a “use it or lose it” provision. When setting up the plan, an employer may choose whether to have terminated employees forfeit any unused funds when they leave or to allow them access to the unused amounts for a period of time. Unlike HSAs, an HRA may be paired with any medical plan. An HRA can be as limited or broad as the employer deems appropriate. Claim reimbursement transactions can be administered by the employer (not recommended) or managed by a Third Party Administrator (fees may apply). Again, employers should consult with their accountant/tax advisor regarding deductibility criteria of contributions as well as if officers can receive reimbursements e.g., 2% owners, partners, sole proprietors, etc.

Ideally, the savings associated with purchasing a consumer driven health plan would be used to fund an HSA or HRA. Under an HDHP (paired with an HSA or HRA) or cost sharing plan (paired with an HRA), costs would be more transparent making individuals knowledgeable about the actual expense of their health care. Consequently, individuals will be better equipped to make decisions such as using a Tier 1 drug versus a Tier 2 or 3 drug, shopping for the most reasonably priced provider or trying therapy before having surgery performed. However, it is also foreseeable that an individual may forgo treatment if a large sum of money needs to be output. Furthermore, HSA participants may simply allow their account to grow in lieu of using funds for needed care.

Lastly, are the most familiar tax-advantaged financial accounts – **Flexible Savings Accounts (FSA)**. This type of account is funded by the employee and includes a “use it or lose it” feature. In addition to qualified medical expenses, FSAs may also include provisions for dependent care.

Some of the accounts represented may be offered simultaneously, however they cannot reimburse an individual for the same medical expense. Regulations have been created to determine the order in which payments will be made.

As mentioned previously, an accountant/tax advisor should always be consulted before implemented an alternate funding vehicle.