



## Comparison of health care accounts\* — June 2012

FEATURE	HEALTH SAVINGS ACCOUNT (HSA)	HEALTH REIMBURSEMENT ACCOUNT (HRA)	FLEXIBLE SPENDING ACCOUNT (FSA) & DEPENDENT CARE ACCOUNT (DCA)
<b>Overview</b>	A tax-exempt trust or custodial account that can be used to pay current qualified medical expenses of the account holder and his or her spouse or dependents and to save for future medical expenses.	An employer funded arrangement that reimburses employees for qualified medical care expenses incurred by the employee, his spouse, or his dependents. HRAs are typically combined with a high-deductible health plan.	An employer-sponsored account established to pay qualified medical expenses incurred by the employee, his spouse, or his dependents. These accounts are typically funded with pre-tax contributions made through a cafeteria plan under Section 125 of the Internal Revenue Code. <sup>1</sup>
<b>Who is eligible to set up an account?</b>	Individuals and families covered by a qualified high-deductible health plan (HDHP). Generally, individuals and families cannot have other coverage which is not an HDHP except for certain types of coverage, including dental, vision, disability, a specific illness, long-term care, or coverage that pays a fixed amount for hospitalization.	An employee whose employer offers an HRA.	An employee whose employer offers an FSA option or DCA option, as applicable.
<b>What are the requirements for the corresponding health plan?</b>	Must be covered by an HDHP and not have certain other kinds of coverage. HDHPs can provide first-dollar coverage for preventive care and still be qualified. For 2012, the HDHP must have the following deductibles and out-of-pocket limits (i.e., deductibles, copayments, and coinsurance, not premiums): <ul style="list-style-type: none"> <li>• For self-only coverage, deductible must be at least \$1,200, with an out-of-pocket maximum of \$6,050.</li> <li>• For family coverage, deductible must be at least \$2,400, with an out-of-pocket maximum of \$12,100.</li> </ul>	No health plan requirements. HRAs may be used with any type of health plan or as a stand-alone account.	No health plan requirements.
<b>Who may contribute to the account?</b>	The account holder, the employer, or any other person.	Solely the employer.	The employee, employer, or both. Typically funded by employees on a pre-tax basis under a cafeteria plan.

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<b>What are the limits on contributions?</b>	<p>In 2012, for individuals with self-only coverage the annual contribution limit is \$3,100. Individuals with family coverage may contribute up to \$6,250 on an annual basis.</p> <p>Catch-up contribution for individuals age 55 or older is increased to \$1,000 beginning in 2009 and all years going forward.</p> <p>These amounts are adjusted each year based on a cost-of-living adjustment.<sup>2</sup></p>	<p>No federal income tax law limits. Employers typically set limits, usually equal to or less than the amount of the deductible of employees' health plan.</p>	<p>FSA No limits under federal income tax law. Employers typically set limits.</p> <p>DCA No maximum contribution limit by law, but maximum contribution that can be excluded from the employee's income is \$5,000, therefore, this is generally the contribution limit. Note, however, that the income exclusion limit is \$2,500 for married taxpayers filing a separate federal income tax return. Also, the exclusion limit cannot exceed the employee's or spouse's earned income.</p>
<b>What are qualified medical expenses?</b>	<p>Unreimbursed qualified medical expenses are defined in Section 213(d) of the Internal Revenue Code. Examples of such expenses include amounts paid for doctors' fees, prescription medicines, and necessary medical services not paid for by insurance (including many over-the-counter medications).</p> <p>HSA funds cannot be used to pay health insurance premiums; subject to certain exceptions.</p> <p>(See below "When can funds be used to pay health insurance premiums?").</p>	<p>Same as HSA, but employers have discretion, to limit use of HRAs to only certain qualified medical expenses, such as those covered by the employer plan.</p>	<p>In general, it is the same FSA as it is for HSA, but cannot be used to pay health insurance premiums and certain long-term care expenses. Also, employers have discretion to further limit the scope of eligible expenses.</p> <p>Medical expenses cannot be paid from a DCA. Eligible DCA expenses include day care, nursery school, babysitting, or the care of a handicapped dependent or elderly parent residing with the employee; provided such expenses enable the employee (and spouse) to work or look for work. Special rules apply in the case of a spouse who is a full time student or who is disabled.</p>
<b>When can funds be used to pay health insurance premiums?</b>	<ol style="list-style-type: none"> <li>1. While receiving unemployment benefits.</li> <li>2. While receiving COBRA continuation benefits.</li> <li>3. When age 65 or older for any health insurance except Medicare supplemental policies.</li> </ol>	<p>In general, funds can be used to pay for premiums under:</p> <ol style="list-style-type: none"> <li>1. the employee's health plan;</li> <li>2. the spouse's health plan;</li> <li>3. the employer's retiree health plan;</li> <li>4. COBRA continuation coverage.</li> </ol> <p>However, premiums that may be paid by salary reduction may not be funded from an HRA.</p>	<p>Insurance premiums cannot be paid from an FSA or DCA. However, premiums can be paid on a pre-tax basis under a cafeteria plan.</p>
<b>Can funds be used to pay for long-term care coverage?</b>	<p>Yes, premiums for long-term care insurance are reimburseable.</p>	<p>Same as HSA.</p>	<p>No. The Internal Revenue Code specifically excludes long-term care insurance as a qualified benefit under a cafeteria plan. As a result, long-term care insurance premiums are not reimbursable under an FSA or a DCA.</p>
<b>Are withdrawals for non-medical expenses allowed?</b>	<p>Yes, but distributions for expenses other than "qualified medical expenses" are subject to income tax as well as an additional 10% tax penalty. The additional tax does not apply if the individual is age 65 or older, disabled, or has died during the year.</p>	<p>No.</p>	<p>No.</p>

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<b>What is the federal tax treatment of contributions?</b>	Employee contributions are tax deductible. Employer contributions are excludable from gross income and not subject to FICA.	Employer contributions are generally excludable from employee's gross income and not subject to FICA. However, an arrangement that distributes the unused HRA amount at termination either as a death benefit or as a severance payment will not qualify as an HRA. Employers receive expense deductions for payments.	Employee pre-tax contributions are not subject to federal taxes (including FICA) or state taxes (other than New Jersey), but may be subject to local taxes (such as Philadelphia).  Employer contributions, if any, are excludable from gross income and are not subject to FICA.
<b>Can funds be carried over from one year to the next?</b>	Yes, HSA funds may be carried over indefinitely during a participant's life-time.  Upon a participant's death, an HSA may be passed on to a surviving spouse without federal tax liability.	Yes. Unused amounts in an HRA may be carried over, subject to any limits set by the employer.	No. Unused FSA/DCA balances are forfeited at the end of the plan year (or at the end of the grace period (see below), if offered by the employer).  Employers may permit employees participating in the employer's FSA or DCA to use unused funds for qualified medical or dependent care expenses (as applicable) incurred during a "grace period" of up to 2 ½ months after the end of the FSA's or DCA's plan year.
<b>Are accounts portable?</b>	Yes. Employees may take funds with them when they leave or change jobs.	No. However, employers can set up HRAs so that they continue to reimburse former employees or retirees for medical care after termination or retirement. COBRA applies to HRAs and the opportunity to continue coverage must be offered if coverage is lost due to a COBRA qualifying event.	No. Unused FSA/DCA balances are forfeited if the employee leaves, changes jobs, or otherwise becomes ineligible to participate. COBRA applies to FSAs (but not DCAs) and the opportunity to continue coverage must be offered if coverage is lost due to a COBRA qualifying event, subject to certain exceptions.
<b>Does interest accrue on funds deposited in the account?</b>	Yes. Interest accrues tax-free.	There is no requirement that interest accrue but employers have discretion to credit interest to the HRA accounts.	No. Interest is not typically credited.
<b>Can reimbursement be limited to the contributions made through the date of request for reimbursement?</b>	Only amounts actually contributed are available for reimbursement.	Yes, although not required. Typically, reimbursement is limited to amounts actually contributed.	FSA No. The total amount the employee elects to contribute for the year (less prior reimbursements) must be available for reimbursement at all times during the year.  DCA Yes. Only the actual amount the participant has contributed is available for reimbursement.

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<b>Is the arrangement subject to ERISA?</b>	Only if the HSA is an employer-sponsored plan subject to Employee Retirement Income Security Act (ERISA). By limiting its involvement with and control over the HSA, employers can typically meet the exception.	Same as FSAs.	<p><b>FSA</b> Yes. In general, this means the arrangement must be in writing, described in a summary plan description, and filed on Form 5500 (unless an exception applies). Other ERISA requirements apply as well.</p> <p><b>DCA</b> There are Department of Labor (DOL) Opinions to the effect that a DCA providing solely for payment of day care expenses is not subject to ERISA. In practice, a DCA may reimburse expenses in addition to traditional “day care” expenses (such as the care for a disabled individuals) that may cause the Department of Labor Opinions not to apply. Many DCAs are drafted as ERISA plans to be safe.</p>
<b>What is the principle guidance governing this account?</b>	Section 223 of the Code, Notice 2004-2, and Notice 2004-50.	Revenue Ruling 2002-41 and Notice 2002-45.	Sections 105 and 106 of the Code, Prop. Treas. Reg. section 1.125-1, Q&A-17 and Prop. Treas. Reg. section 1.125-2, Q&A-7 Sections 129 of the Code, Prop. Treas. Reg. section 1.125-1, Q&A-18, and Prop. Treas. Reg. section 1.21-1.

<sup>1</sup> Cafeteria plans are plans under which participants may choose amount of two or more benefits consisting of cash and qualified benefits.

<sup>2</sup> The annual COLA adjustments for health savings accounts must be published no later than June 1 of each year for the following year.

\*These are general guidelines. Features may vary based on group size.