

Benefits Insights

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Comparing HSAs, HRAs and FSAs: Which Approach Is Best?

Employers are increasingly looking to consumer driven health plans to help soften the blow of continually rising health care costs. Depending on the model, consumer driven health plans typically include health reimbursement arrangements (HRAs), flexible spending accounts (FSAs) or health savings accounts (HSAs).

Consumer driven health plans generally increase employees' stake in their own health care costs. In most cases, a consumer driven health plan covers a wide range of medical expenses, but also includes more cost-sharing for participants (for example, higher deductibles). Some plans incorporate an HRA, health FSA or HSA to help employees pay for their out-of-pocket medical expenses on a tax-free basis. This article provides some basic information about the similarities and differences between HRAs, FSAs and HSAs.

HSAs

The Medicare Prescription Drug, Improvement and Modernization Act of 2003 established tax-favored HSAs. Due to their tax-favored status, HSAs have strict rules regarding eligibility and contributions. In order to make or receive HSA contributions, individuals must meet the following qualifications:

- Be covered by a high deductible health plan (HDHP)
- Not have any other health coverage (with some exceptions)
- Not be claimed as a dependent on another person's tax return
- Not be covered by Medicare

The employer and employee can contribute to the HSA in the same year, subject to annual limits. Employers may allow

employees to make pre-tax salary reduction contributions to fund their HSAs. Individuals may roll over unspent funds in the HSA from year to year. Since the HSA is a tax-exempt account owned by the employee, he or she may keep the account upon termination of employment or retirement.

Health FSAs

Health FSAs provide a means for employees to reduce their income tax liability through salary reduction. Employees can contribute a portion of their own salary to an account designated to pay for health care expenses. These pre-tax contributions are exempt from income and payroll taxes. Effective for plan years beginning on or after Jan. 1, 2014, the Affordable Care Act (ACA) limits employee's pre-tax contributions to their health FSAs to \$2,500 (adjusted for inflation for future plan years). The limit for 2019 is \$2,700.

There are some strict design requirements for health FSAs that have negatively impacted their popularity. While any individual who satisfies the HSA eligibility criteria can make HSA contributions, only employees can participate in a health FSA. This means that, while self-employed individuals can establish health FSAs for their employees, they cannot set up their own accounts.

In addition, FSAs have a "use-it-or-lose-it" provision. In general, employees are required to elect a specific amount of salary reduction at the beginning of the year, and then must use every dollar in the account by the end of that year. Because annual medical expenses are hard to predict, employees often overfund the accounts and then spend unnecessarily at the end of the year to avoid forfeiting the money in their accounts.



To help avoid this problem, the IRS allows health FSAs to incorporate either a grace period or carry-over feature. Health FSAs with a grace period allow participants to access unused amounts remaining in an FSA at the end of the plan year to pay for expenses incurred during a grace period of up to two and a half months after the end of the plan year. Alternatively, health FSAs may allow participants to carry over up to \$500 of unused funds remaining at the end of a plan year to be used for qualified medical expenses incurred during the following plan year.

Health FSAs are group health plans that are subject to laws such as the ACA, the Health Insurance Portability and Accountability Act (HIPAA) and the Consolidated Omnibus Budget Reconciliation Act (COBRA).

HRAs

HRAs allow employees to use employer contributions to pay for (or reimburse) eligible medical care expenses. HRAs can only be funded with employer money; employees cannot make contributions to their HRAs. Unlike health FSAs, unused HRA balances may accumulate from year to year.

Like health FSAs, HRAs are group health plans that are subject to laws such as HIPAA and COBRA. Under the ACA, most HRAs must be “integrated” with another group health plan to satisfy certain market reforms. However, effective for plan years beginning on or after Jan. 1, 2017, small employers (those with fewer than 50 full-time employees, including equivalents) that do not offer a group health plan can offer a special type of stand-alone HRA, called a qualified small employer HRA (or QSEHRA). QSEHRAs can reimburse employees’ eligible medical expenses, including premiums for individual health insurance.

Deciding on the Right Approach

Introducing consumerism into your health plan requires an evaluation of the benefits and disadvantages of HSAs, FSAs and HRAs. No one solution is right for every employer. If your organization is considering implementing a consumer driven health plan, your JP Griffin Group representative can help you decide which plan is best for you.

A chart comparing the tax-advantaged accounts discussed in this article follows on the next page.

Comparison of Tax-advantaged Accounts

	HSA	HRA	QSEHRA	FSA
Type of account	Health Savings Account	Health Reimbursement Arrangement	Qualified Small Employer HRA	Health Flexible Spending Account
Who owns the account?	Individual/employee	Employer	Employer	Employer
Who may fund the account?	Anyone can make contributions to an individual's HSA, including employer and/or employee.	Employer	Employer	Employer and/or employee
What plans must be offered with the account?	A high deductible health plan (HDHP) that satisfies minimum annual deductible and maximum annual out-of-pocket expense requirements.	An employer must offer a health plan and the HRA must be considered integrated with group health plan coverage. Stand-alone HRAs are not permitted unless they are limited to excepted benefits or fall under an exemption to the ACA.	Employer cannot offer any group health plan.	Most Health FSAs must qualify as excepted benefits to satisfy ACA reforms. To qualify as an excepted benefit, the FSA must meet a maximum benefit requirement and other group health plan coverage must be offered by the employer.
Is there an annual contribution limit?	\$3,500 Self-Only \$7,000 Family (2019) Catch-up contributions: \$1,000/year— age 55 by end of tax year	No, there is no IRS prescribed limit	For 2018, the maximum benefit cannot exceed \$5,050 (or \$10,250 for QSEHRAs that also reimburse medical expenses of the employee's family members).	For 2019, employees may not elect to contribute more than \$2,700 per year.

	HSA	HRA	QSEHRA	FSA
Can unused funds be rolled over from year to year?	Yes	Yes	Yes (<i>but see maximum benefit limit above</i>)	No, with two exceptions. A health FSA may include a grace period of 2-1/2 months after end of plan year or it may allow employees to carry over up to \$500 in unused funds into the next plan year.
What expenses are eligible for reimbursement?	Section 213(d) medical expenses, including: -COBRA premiums -QLTC premiums -Health premiums while receiving unemployment benefits -If Medicare eligible due to age, health insurance premiums except medical supplement policies	Section 213(d) medical expenses Effective for 2014 plan years, cannot reimburse health insurance premiums for individual coverage Employer can define "eligible medical expenses"	Section 213(d) medical expenses, after the employee provides proof of coverage. This would include, for example, premiums for individual health insurance coverage and other out-of-pocket medical expenses. Employer can define "eligible medical expenses"	Section 213(d) medical expenses Expenses for insurance premiums are not reimbursable Employer can define "eligible medical expenses"
Must claims be substantiated?	No	Yes	Yes	Yes
May the account reimburse non-medical expenses?	Yes, but taxed as income and 20% penalty (no penalty if distributed after death, disability, or age 65)	No	No	No



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Does the uniform coverage rule apply?	No	No	No	Yes
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