

UNDERSTANDING SECTION 125 HEALTH CARE REIMBURSEMENT ACCOUNTS

OVERVIEW

Section 125 of the IRS code allows employers to sponsor a plan that creates an account for employees to set aside pre-tax dollars from their paychecks to pay for eligible medical, dental and vision expenses such as deductibles, copays, non-covered items such as eyeglasses, and more. The account is called a “Health Care Reimbursement Account” and is also known as a Medical Spending Account or Flexible Spending Account. All three terms mean the same thing.

NO FEDERAL OR FICA TAXES FOR THE EMPLOYEE AND NO FICA MATCH FOR THE EMPLOYER

If an employee elects to defer \$100 from their pay into their Health Care Reimbursement Account, they do not pay federal or FICA taxes on that \$100, and the employer does not have the “FICA match” on the \$100. In other words, a Health Care Reimbursement Account allows the employee to reimburse themselves for eligible Health Care expenses on a tax free basis. Participation is voluntary.

HOW IT WORKS

First, the employer sets a maximum funding limit for the medical reimbursement account. Then the employee determines how much they wish to defer each year. An amount is deducted each pay period before taxes are calculated. After the employee incurs an expense, they submit a claim form and a reimbursement check are sent to them. Employees, by law, have access to their entire year’s deferral amount at any time, as long as they have incurred the actual expense that is eligible for reimbursement.

ELIGIBLE EXPENSES

Employees may submit claims for reimbursement for the following items: (this is a partial list and generally grows as the IRS issues new guidelines and clarifications):

- Out-of-pocket medical expenses such as deductibles, copays, and many items not covered by the insurance
- Dental services such as crowns, bridges, x-rays, dentures, exams, cleaning, fillings, orthodontia and more
- Medical treatment expenses (not paid by insurance) such as blood tests, lab fees, x-rays, medication such as birth control, prescribed vitamins and more
- Over the counter medications to treat a specific medical condition such as allergy medicine, antacid, pain reliever, pregnancy tests, vapor rub, throat lozenges, laxatives, first aid cream, contact lens solution, sleeping aids and more
- Obstetric Services including Lamaze class, mid-wife expenses, pre and post natal treatments
- Other Eligible Services: acupuncture, treatment for chemical dependency, treatment for infertility, In-vitro fertilization, Norplant birth control, physical therapy, rolfing, sterilization, vaccinations, well baby care and more

INELIGIBLE EXPENSES (NOT REIMBURSABLE)

Items not eligible for reimbursement include the following:

- Cosmetic procedures
- Exercise and fitness programs including health club dues
- Insurance premiums including Long Term Care insurance premiums
- Marriage counseling
- Message therapy (unless part of treatment plan for physical problem)
- Rogaine
- Teeth whitening
- Vitamins for general health and more.

IMPORTANT NOTE

There are two important IRS rules that employers and employees need to be aware of. First, if the employee does not use their entire account balance during the plan year, the employee forfeits any remaining monies in the account under the use it or lose it rule. Also, employees have access to their entire year's account balance at any point during the plan year, even if they have not yet fully funded the account through payroll deduction.

A Section 125 Health Care Reimbursement Account is a great way to save tax dollars for both the employee and the employer. Call your Section 125 Plan Administrator for more information.

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EMPLOYEE BENEFITS