Funding Options for Employees on Medicare/Tricare

Who Cannot Take Advantage of Employer HSA funding

Taxable Stipends & HRAs

April, 2017

VEHI data indicates approximately 5% (755 people) of active school employees currently enrolled in a VEHI health plan are age 65 or older and, therefore, are either enrolled in or eligible for Medicare.

VEHI has no data on the number of active employees in its health plans who are enrolled in or eligible for TRICARE or who access veterans' benefits outside of TRICARE.

Most of this document is in response to questions about what is legally permissible in respect to providing additional taxable income to assist with out-of-pocket costs (co-payments, deductibles and co-insurance charges) incurred by active employees who are excluded from receiving or making contributions to an HSA because they are enrolled in or have applied for Medicare, or because they are enrolled in TRICARE. These questions were raised in the context of concerns about federal anti-discrimination rules.

There is also information about HRAs and their applicability to employees on Medicare and TRICARE.

You will also find additional clarification about the eligibility of veterans to make or receive contributions to an HSA who receive care at the V.A. but are not enrolled in TRICARE.

Finally, this document offers new guidance on FSAs, specifically the effect of an employer funding an HSA and access to those funds by an employee who exercises COBRA rights.

Option 1: Taxable Stipends for Employees Covered by Medicare or Tricare

When providing benefits to employees, the federal government prohibits discriminating in favor of highly compensated employees and discriminating against older employees. Employers may, however, provide different benefits to employees within the same work classification, if those benefits **favor** older employees and/or those with lower compensation.

1. An employer can provide additional taxable salary/hourly wage to employees without violating federal anti-discrimination rules.

2. The additional taxable salary/hourly wage would be a stipend in lieu of an employer contribution to an HSA.

3. Stipends would be negotiated where collective bargaining agreements are in place.

4. The stipend would be available only to employees who meet the following criteria:

   - They are enrolled in an HSA-eligible plan offered by their school district;

   - Employer funding to an HSA is also offered, but the employees are ineligible to receive employer contributions to an HSA because of their enrollment in Medicare or Tricare.

5. Limiting the stipend only to those who meet these criteria is not discriminatory because this specific group of employees is ineligible to make or receive contributions to an HSA based on their entitlement to a governmental program from which they cannot reasonably withdraw.

6. The amount of the stipend must be **identical** to the amount of money the employer is contributing to an HSA. This is required to avoid any appearance of discrimination between those who receive the HSA funding and those who receive the stipend.

7. Because the stipend is taxable income, employees can determine how to use it, which might include:

   a. To obtain pre-tax benefits available in their employer's Cafeteria Plan. For example, if the Plan has an FSA, employees could contribute to it. They are currently permitted to contribute up to $2,600 (the 2017 annual federal limit) to an FSA. All FSA rules apply, including a rollover of up to $500 (if allowed in the Cafeteria Plan), a "grace" period of approximately 2.5 months after the end of a calendar year, and/or the standard "use-or-lose-it" provisions.

   b. To purchase, if enrolled in Medicare Part A, Medicare Part B coverage, which would give them secondary coverage to help with OOP costs.

   c. To spend as taxable income.

8. This stipend would not be considered a cash-in-lieu benefit because the employee is enrolled in employer health coverage. The stipend supplements the primary plan coverage offered by the employer.

9. As noted in other VEHI guidance, active employees can defer enrollment in Medicare Part A without penalty. However, active employees who are drawing Social Security benefits are automatically enrolled in Medicare Part A. There are serious and potentially costly implications for employees who **disenroll** in Medicare Part A while they are also drawing Social Security benefits; if they apply to disenroll from Part A, they must first pay back to the federal government everything they received in Social Security benefits and anything Medicare may have paid in claims on their behalf before their application to disenroll from Part A will be processed. They cannot also not receive any further

Social Security benefits until they re-enroll in Medicare Part A at some point in the future.

Active employees who, on January 1, 2018, have already applied for or are enrolled in Medicare effectively cannot change that election.

WARNING: VEHI strongly advises employers NEVER to advise or incentivize an employee to disenroll from Medicare Part A.

- Employees enrolled in Medicare Part A have this coverage to assist with OOP costs covered by Part A, notably hospitalization.
- Employees enrolled in TRICARE are veterans who have this coverage to assist with health care needs.

REMINDER: The IRS determines eligibility for an HSA on a monthly basis. If contributions to an HSA in a given month are greater than 1/12th of the applicable annual limit, a change in eligibility for any reason will likely result in the individual over contributing and the need to remove excess contributions in a timely manner to avoid federal penalties. See IRS rules at https://www.irs.gov/publications/p969/ar02.html#en_US_2017_publink1000204045.

The amount that can be contributed to an HSA depends on the tier of CDHP coverage, age, the date an employee becomes an eligible individual, and the date the employee ceases to be an eligible individual. For 2017, an individual with self-only CDHP coverage can make or receive contributions up to $3,400. For other than self-only CDHP coverage, s/he can make or receive contributions up to $6,750, in combination with his/her employer or spouse. Individuals age 55 and older are eligible for an additional $1,000 catch-up contribution.

Veterans Administration (V.A.) Coverage for Employees NOT in TRICARE

Employees eligible for V.A. coverage but not enrolled in TRICARE may or may not be eligible to make contributions to an HSA if enrolled in a qualified CDHP. It depends on the employee's circumstances. In brief…

- If the employee is eligible for V.A. coverage and has a **disability rating** through the V.A., the employee **is eligible** to establish and contribute to an HSA on the same basis as any other employee.
- Employees eligible for V.A. benefits **without** a VA disability rating **may not** be eligible to contribute to an HSA during certain intervals after receiving certain kinds of V.A. care.

IRS Guidance on V.A. Coverage & HSA Contributions

When HSAs were initially introduced, an employee's eligibility for VA coverage generally prevented the employee from contributing to an HSA. For 2016, a change in the law relaxed the prohibition on employee HSA contributions provided the treatment received through the V.A. was:

(1) disregarded coverage (dental, vision and long term care),
(2) preventive care, or
(3) hospital care or medical services under any law administered by the Secretary of Veterans Affairs for **service-connected disability.**

Subsequent IRS guidance (https://www.irs.gov/pub/irs-drop/n-13-57.pdf) acknowledged:

(1) Most care provided for veterans who have a disability rating will be "qualifying care"; and
(2) The difficulty employers and HSA trustees would experience distinguishing between services provided by the V.A. for service-connected disabilities would make the plans administratively complex and burdensome.

Veteran with a disability rating

Hospital care, medical services, or prescription drugs received from the V.A. by a veteran who has a disability rating is considered hospital care or medical services under V.A. coverage for *service-connected disabilities*. Thus, these employees receiving care from the V.A. are eligible to make HSA contributions, regardless of the nature of the benefits.

Veterans without a disability rating

Employees receiving care (including prescription drugs) from the V.A. **without** a disability rating are **ineligible** to contribute to an HSA for the **three calendar months** following the date the V.A. care was received. These individuals, however, can make or receive contributions to an HSA during other periods of the year as long as they are not otherwise ineligible.

Examples:

(1) **Meredith** is covered by her employer's CDHP and establishes an HSA effective January 1, 2017. Meredith is also eligible for V.A. benefits but does not have a disability rating.

Meredith received V.A. medical benefits during April, 2017 (her first V.A. care in over a year), but did not receive VA benefits during May, June, or July, 2017. In this scenario, Meredith may contribute to her HSA during the months of January through March, 2017. But she **cannot** make or receive contributions to an HSA for May, June and July, 2017, because she got V.A. care in April. However, she is eligible to make or receive HSA contributions at the start of August, provided she did **not** seek care through the V.A. system in any of the preceding three months (May through July).

(2) **Matthew** is covered by his employer's CDHP and establishes an HSA effective January 1, 2017. Matthew has a disability rating. He received V.A. medical benefits during July, 2017. Because Matthew has a disability rating, the care he receives during July, 2017 is disregarded for purposes of eligibility to make HSA

contributions. Thus, Matthew is eligible to make contributions for each calendar month in 2017, provided he is not otherwise ineligible.

VEHI does not know how many school employees will be affected by the contribution restrictions noted above. In any event, the restrictions on HSA contributions by or on behalf of employees eligible for V.A. benefits without a V.A. disability rating should be considered when establishing plan eligibility.

VEHI also advises employers to disclose the prohibition on contributions for employees eligible for V.A. benefits **without** a disability rating in communication materials and refer employees to or encourage them to get expert guidance. These employees should report any period of ineligibility to make or receive contributions to an HSA to their employer.

Option 2: HRA Funding

Employers can offer without triggering any discrimination issues an HRA **only** for those active employees eligible for Medicare or TRICARE. The eligibility requirements must be written into the HRA Plan document.

The employer **must** report to Medicare any HRA with a value of **$5,000 or more**. If the value of the HRA is $5,000 or greater, Medicare secondary payer rules apply and the employee may need to provide documentation that the HRA funds have been exhausted before Medicare will provide benefits.

COBRA Implications if an Employer Contributes to an FSA as an Alternative to HSA Funding

When an employer funds an employee FSA, **the FSA is no longer an excepted benefit.** As a result, an employee who elects to remain in the employer health plan under COBRA after employment ends also has the right to the employer's FSA funds for the **entire COBRA period**.

Since COBRA eligibility extends into the next school year, the now former employee is eligible for the employer's FSA contribution again the following year.

FSA funds are available in full on the first day of the year, regardless of the timing of the actual contributions.

We want to stress again that VEHI is not a source of expert or definitive guidance on HRAs, HSAs or FSAs. Our guidance is for general purposes only. Therefore, we urge the parties, if needed, to consult their TPAs and attorneys, to call or set up appointments at local Social Security offices and the Veterans Administration, or to visit the websites of the IRS and the Centers for Medicare and Medicaid Services for more comprehensive legal and regulatory guidance.