

IRS Releases New Debit Card Guidance for FSA's

Bethesda, MD July 12, 2006 The IRS released updated regulations pertaining to the administrative and procedural use of debit cards and their interaction with health FSA's, dependent care FSA's and HRA's. These regulations update the original guidance released in May of 2003. The guidance is effective immediately except for the records retention requirement for SKU substantiation which is effective for plan years beginning after December 31, 2006. Below is a summary of the guidance. A complete text of the release is available for your review by going to www.flexamerica.com.

Allowance for Multiple Co-pays

The co-pay match substantiation has been expanded to allow for exact multiples of co-pays. The new guidance states that employees who use a debit card for multiples of co-pays, up to 5 multiples, are considered "fully substantiated without the need for submission of a receipt for further review". This means an employee who purchases 5 RX items for \$5, for a total of \$25, will not need to verify his or her purchases.

Inventory Information Approval System

Employers may adopt inventory approval systems by which all items in a pharmacy are categorized as medical or non medical expenses. Purchases which are all medically coded are considered fully substantiated, while mixed purchases of medical and non-medical items can be treated as conditional, pending confirmation of the charge. Furthermore, the transaction may be partially approved requiring the employee to tender at the point of service the ineligible portion of the purchase with funds other than the FSA debit card. All data used to verify transactions must also be available for later review which will require the debit card processors to implement record retention systems that will allow transaction verification information to be retrieved and reviewed.

Direct Third Party Substantiation

The IRS reaffirmed the use of employee responsibility or Explanation of Benefits (EOB) data files, whereby the employee's out of pocket costs are transmitted and automatically reimbursed through the health FSA. For example, if an employee incurs \$150 of expenses of which \$100 is covered by the health plan, the health plan may supply a EOB file detailing the \$50 employee responsibility and have this amount automatically reimbursed through their health FSA.

Prohibition of Self Certification

The guidance reaffirmed that self-substantiation of claims or self-certification of an expense by a participant does not meet the IRS substantiation requirements.

Use of the Debit Card for Dependent Care FSA

The IRS does allow the debit card to be used for Dependent Care FSA expenses as long as they are not prepaying for the expense.

FlexAmerica Comments

The IRS reaffirmed that all expenses not meeting one of the above criteria are "treated as conditional pending confirmation of the charge". These expenses must be documented to include (1) Service or product rendered, (2) the date of service or sale and, (3) the amount must be submitted for review and substantiation. The IRS also did not permit a de minimus amount, meaning that charges as little as \$.01 which do not meet the auto substantiation requirements must be documented. This requirement puts a substantial burden on employees and requires them to be more organized and retain all receipts. Additionally, the absence of this from the regulations will continue to increase the cost of administering debit card based

plans due to the increased number of claims requiring manual substantiation and the increased call volume resulting from a higher number of suspended cards due to a lack of substantiation.

FlexAmerica's Action Plan

FlexAmerica will begin working immediately with our employers and software development department to implement the multiple co-pay allowance. FlexAmerica is currently integrated at the SKU data level with Walgreen's, Long Drug, Drugstore.com. FlexAmerica and MBI (our debit card partner) are continuously working with other pharmacy chains on SKU level data integration. FlexAmerica currently has the capability to import EOB files. As a final note, FlexAmerica, in partnership with Mellon Bank, now has the capability to administer your HSA plan and implement limited use FSA's for employees enrolled in a HSA that permit only dental and vision items to be reimbursed.

Questions regarding this release may be directed to your dedicated FlexAmerica contact.