

the benefits trust

Health Care Spending Accounts



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Health Care Spending Accounts (HCSA) have become a popular alternative to traditional group health and dental plans. They are practical, affordable, flexible, and a cost-effective way to meet the changing needs of many employers and diverse needs of many employees.

Many employers are considering HCSAs as an alternative when reviewing or initiating their employee benefits plan. It is important to take the time to understand the ins and outs of HCSA, to determine if they are an appropriate solution.

What Is A Health Care Spending Account?

A Health Care Spending Account is a pre-determined amount of money provided to employees at the beginning of each benefit year for coverage of their medical and dental expenses.

This amount is held in trust and claims are submitted by employees and reimbursed in a similar fashion to a traditional benefits plan. Eligible expenses are reimbursed at 100% up to the total dollar amount available in the HCSA. A Health Care Spending Account can replace or exist alongside traditional medical and dental coverage.

Health Care Spending Accounts ensure controlled benefit costs for the employer and complete claim flexibility for the employees.

How Does It Work?

At the beginning of each benefit year, the plan sponsor determines the amount of HCSA dollars available in each employee's individual account (normally by class of employee). For example, Executives could receive \$5,000 per year, and all other employees \$1,000 per year.

Employees and their families can then claim from these accounts to cover Canada Revenue Agency (CRA) approved health and dental expenses, which they encounter throughout the benefit year. This allows employees to spend the funds on expenses their families incur, rather than restricting them to the dollar limits and specific expenses set out in a traditional benefits plan.

Which Expenses Are Eligible For Coverage?

Under the Income Tax Act, any item that qualifies for the Medical Tax Credit is eligible for coverage through an HCSA (see appendix A). Often this definition of eligible expenses is broader than that of a traditional employee benefits plan, allowing for additional flexibility for employees and executives in particular.

What Are The Tax Advantages For An Employer?

Health Care Spending Accounts provide a way for plan sponsors to deliver benefits to their employees, using pre-tax dollars. As with a traditional employee benefits plan, the costs are tax deductible business expenses and the benefits are received tax-free. This can be a significant advantage for owners, executives and key employees to pay for significant medical and dental expenses with corporate dollars in the most tax-effective way possible.

To be considered a tax deductible expense to the plan sponsor, a Health Care Spending Account must be a pre-set limit, which is 100% employer funded. The funds cannot be used to purchase additional insurance (i.e. Life Insurance). The amount of reimbursement is limited to the amount allocated to the account by the employer and to the eligible expenses defined in the Income Tax Act. Unused HCSA amounts cannot be paid out at year-end as cash to the employees.

How Are Health Care Spending Accounts Funded?

Under the terms of the Income Tax Act, to qualify as a tax-deductible expense to the company, Health Care Spending Accounts must be fully funded by the employer. These amounts can be billed on a monthly basis, rather than requiring a large lump sum payment at the beginning of the benefit year or lump sums as employee claims come in. This budgeted approach is particularly attractive to small companies who require predictable expenses each month. In some instances, such as an Executive Health Care Spending Account, annual contributions may be billed at a specified date each calendar year.

Employee expenditures may not exceed the HCSA maximum set by the plan sponsor. Employer costs will not exceed the total employee HCSA amounts, plus administration costs and taxes. There is no increase in HCSA contributions annually unless the employer chooses to change the total HCSA dollar amounts available to the employees.

How Are Unspent Funds Dealt With?

If an employee has a remaining balance at the end of year one, the funds may be carried forward and added to their balance for year two. If at the end of year two they have not spent the carry-forward funds, the remaining amount would be returned to the employer. This allows the employee to plan and budget for large expenditures, like orthodontic expenses, over a two-year period. Once an employee has exhausted their full HCSA balance any additional expenses they may have remaining cannot be carried forward to the next year under the Income Tax guidelines.

Health Care Spending Accounts and Insurance

Health Care Spending Accounts provide no “insurance” coverage. HCSAs are strictly a reimbursement plan. Traditional insurance products, like group life insurance, accidental death and dismemberment insurance, critical illness insurance, and out of Canada emergency medical coverage can be added to an employer sponsored benefit plan offering. Many employers also add stop loss insurance protection to pay for medical expenses that exceed a certain pre-determined threshold. This helps plan sponsors protect employees and their families from unexpected catastrophic medical expenses that may occur in a given year, such as high cost prescription drugs.

Plan Design Considerations

Just as with traditional benefit plans, plan sponsors may assign varying levels of benefit by class within their group of employees.

HCSA plans may be structured in one of three ways. These designs are mutually exclusive and cannot be combined within a plan.

The most popular method is Balance Carry-Forward, which permits employees to roll over any remaining credits from year one to year two. Any remaining balance would revert to the employer if not spent by the end of year two.

Expense Carry Forward and No Carry Forward plans are also eligible under the Income Tax guidelines, however, these types of plans are rare.

Employers should expect that employees might claim their full Health Care Spending Account balance each year. Employees are aware of their balance on an ongoing basis which can encourage “using up” credits available to them. In some cases employees who would normally be restricted by the limits in a traditional plan (i.e. \$200 for vision care) may spend more as their entire claim would be eligible (i.e. \$400 pair of glasses). Overall, however, employees are limited to their annual Health Care Spending Account balance.

For the plan sponsor, who decides how much to spend when setting up the plan, and the employees who decided where to spend their benefit dollars when submitting claims, an HCSA allows choice on every level.

Health Care Spending Accounts provide employers with complete control over claims costs each year, because the employees can only claim up to their individual maximums. Funds that are not used for claims within the specified time period remain the property of the plan sponsor and will be returned to them. Many employers are looking for creative ways to control their health and dental expenditures; a Health Care Spending Account can be an ideal solution.

APPENDIX A

GUIDELINES FOR CLAIM EXPENSES ELIGIBILITY

Subject to change according to the CRA

Whose Claims Are Considered Eligible?

You may submit claims for eligible expenses incurred by an employee, their spouse, or any other dependent for whom the employee is claiming a tax deduction in the taxation year the expense was incurred.

What Expenses Are Considered Eligible?

Eligible expenses include:

- Unpaid portions of expenses from regular health and dental plans such as deductibles, co-insurance amounts and amounts which exceed plan maximums;
- Expenses **not** covered under any other benefit plan (group, provincial, or private);
- Expenses listed as eligible medical expenses in the Income Tax Act, its regulations and Interpretation Bulletins (see following list). This list is subject to change as the Act is amended.

Eligible Expenses under the Income Tax Act

Medical Practitioners (if registered in the province where the expenses occurred)

- Chiropodists or Podiatrists
- Chiropractors
- Christian Science Nurses
- Christian Science Practitioners
- Dentists
- Massage Therapists
- Medical Doctors
- Naturopaths
- Nurses
- Occupational Therapists
- Optometrists, Oculists, or Ophthalmologists
- Osteopaths
- Physiotherapists
- Psychologists
- Speech Therapists
- Therapists or Therapeutists

Care and Facilities

- Expenses of a full-time attendant, or of full-time care in a nursing home, for an individual who has a severe and prolonged mental or physical impairment. The condition must be certified by a medical doctor or optometrist, where applicable.
- Expenses of a full-time attendant, if an individual lives in a self-contained domestic establishment (e.g., the individual's home), provided a doctor certifies that the individual is likely to be dependent others for personal needs and care for an indefinite period because of a mental or physical infirmity.
- Expenses of full-time care in a nursing home for an individual who, due to a lack of normal mental capacity, is and will continue to be dependent upon others for personal needs and care. The certification of a doctor is required to support the need for this care.
- Expenses for the care and/or training at a school, institution or other place (e.g., nursing home) when an individual has been certified to be someone who, because of a physical or mental impairment, requires the equipment, facilities or personnel provided by such place. An appropriately qualified person must certify that the individual's condition requires such care.
- Expenses of a public or licensed private hospital, including hospitals outside Canada.

Assistance Devices, Supplies, and Equipment

- Eyeglasses or other devices for the treatment or correction of a defect in vision
- Artificial eyes and limbs
- Crutches
- Wheelchairs
- Walkers
- Spinal brace/support
- Brace for a limb
- Iron lung/portable chest respirator
- Rocking bed for poliomyelitis victims
- Ileostomy or colostomy pads
- Cloth diapers, disposable briefs, catheters, catheter trays, tubing or other products required by an individual who is incontinent by reason of illness, injury, or infliction
- Truss for a hernia
- Artificial kidney machine
- Laryngeal speaking aid
- Aids to hearing

Assistance Devices, Supplies, and Equipment (continued)

- Device or equipment, including replacement parts, designed exclusively for use by an individual suffering from a severe chronic respiratory ailment or a severe chronic immune system dysregulation, but not including an air conditioner, humidifier, dehumidifier, or air cleaner
- Air or water filter or purifier for use by an individual who is suffering from a severe chronic respiratory ailment, or a severe chronic immune system dysregulation, to cope with or overcome the ailments dysregulation
- Electric or sealed combustion furnace acquired to replace a furnace which is neither, where the replacement is necessary solely because of a severe chronic respiratory ailment or a severe chronic immune system dysregulation
- Device or equipment designed to pace or monitor the heart of an individual who suffers from heart disease
- Device that is designed to assist an individual with mobility impairment in walking
- Device designed exclusively to enable an individual with a mobility impairment to operate a motor vehicle
- Power-operated guided chair installation that is designed to be used solely in a stairway
- Mechanical device or equipment designed to assist an individual to enter or leave a bathtub or shower or to get on or off a toilet
- Power-operated lift designed exclusively for use by a disabled individual to allow access to different areas of a building or to assist the individual to gain access to a vehicle or to place the individual's wheelchair in or on a vehicle
- Electronic or computerized environmental control system designed exclusively for the use of an individual with a severe and prolonged mobility restriction
- External breast prosthesis that is required because of a mastectomy
- Hospital beds, including any necessary attachments prescribed for an individual
- Oxygen tent or equipment necessary to administer the oxygen (includes the oxygen)
- Custom made wig for an individual who has suffered abnormal hair loss as a result of disease, medical treatment or an accident
- Device designed to be attached to an infant diagnosed as being prone to Sudden Infant Death Syndrome in order to sound an alarm if the infant ceases to breathe
- Extremity pump or elastic support hose designed exclusively to relieve swelling caused by chronic lymphedema
- Inductive coupling osteogenesis stimulator for treating non-union of a fracture or aiding in bone fusion
- Infusion pump, including disposable peripherals, used in the treatment of diabetes, or a device designed to enable a diabetic to measure blood sugar levels
- Needles and syringes for injections

Assistance Devices, Supplies, and Equipment (continued)

- Orthopaedic shoe or boot, or an insert for a shoe or boot, custom made for an individual in accordance with a prescription to overcome a disability
- Device or equipment, including a synthetic speech system, Braille printer and large print-on-screen device, designed exclusively to be used by a blind individual in the operation of a computer
- Optical scanner or similar device designed to enable a blind individual to read print
- Device to decode special television signals to permit the vocal portion of the signal to be visually displayed
- A visual or vibratory signaling device, including a visual fire alarm indicator, for an individual who has a hearing impairment
- Electronic speech synthesizer that enables a mute individual to communicate by using a portable keyboard

Drugs

- Insulin
- Vitamin B12 and liver extract indictable for pernicious anaemia
- Drugs, medications or other preparations or substances prescribed by a medical practitioner or dentist and recorded by a pharmacist

Transportation, Meals, and Accommodation

- Expenses for transportation by ambulance to or from a public or licensed private hospital
- Transportation expenses paid to an individual who is in the business of providing transportation services to transport the patient and one additional person (if medically necessary, as certified by a medical practitioner) provided:
 - Substantially equivalent medical services are not available locally
 - The route taken is reasonable direct
 - The medical treatment sought is reasonable and the distance traveled is at least 40 kilometres
- If hired transportation is not readily available, reasonable expenses for private transportation will be eligible.
- Reasonable expenses for meals and accommodation for a patient and, if medically required, an accompanying person, provided the conditions for transportation expenses (specified above) are satisfied and the distance traveled is at least 80 kilometres

Dental

- Preventive, diagnostic, restorative, orthodontic, and therapeutic care
- Making or repairing of dentures by a licensed dental mechanic

Other Expenses

- Diagnostic, laboratory, and radiological procedures or services for maintaining health and preventing disease, or assisting in the diagnosis or treatment of an injury, illness or disability of an individual, when prescribed by a doctor or dentist
- Acupuncture treatment when performed by a qualified medical doctor
- Reasonable expenses for rehabilitative therapy, including training in lip reading and sign language, incurred to adjust for an individual's loss of hearing or speech
- Reasonable expenses for modifications to a home for an individual who lacks normal physical development, or who has severe and prolonged mobility impairment, so as to enable the individual to gain access and move around the home
- On behalf of an individual who requires a bone marrow or organ transplant:
- Reasonable expenses to locate a compatible donor and arrange for the transplant
- Reasonable traveling, board and lodging expenses of the donor and the individual with respect to the transplant
- The cost of acquisition, care and maintenance (including food and veterinarian care) of an animal if the animal is specifically trained to assist an individual who is blind, profoundly deaf or has a severe and prolonged impairment that markedly restricts the use of the arms or legs. In addition, reasonable traveling, board, and lodging expenses incurred while in full-time attendance at a facility that trains individuals in the handling of such animals are eligible.

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