

COMPLIANCE OVERVIEW



Using HSAs, Health FSAs and HRAs for Over-the-Counter Items



Health savings accounts (HSAs), health flexible spending accounts (FSAs) and health reimbursement arrangements (HRAs) **may provide tax-free reimbursements of certain over-the-counter (OTC) items**. OTC items are generally available to consumers without a prescription.

To be reimbursable, an OTC item must be for “medical care,” as defined under Internal Revenue Code (Code) Section 213(d). Medical care expenses are amounts paid for the diagnosis, cure, mitigation, treatment or prevention of disease, or for the purpose of affecting a structure or function of the body.

Prior to 2020, the Affordable Care Act (ACA) generally prohibited health FSAs, HRAs and HSAs from reimbursing the costs of OTC medicine or drugs on a tax-free basis, unless they were prescribed. However, effective Jan. 1, 2020, the [Coronavirus Aid, Relief and Economic Security Act](#) (CARES Act) eliminated the ACA’s prescription requirement and allowed OTC drugs, along with menstrual care products, to be treated as qualified medical expenses that may be paid for using these tax-advantaged arrangements.

Medical Care Expenses

To be reimbursable, an OTC item must be for “medical care,” as defined under Code Section 213(d). Medical care expenses are amounts paid for the diagnosis, cure, mitigation, treatment or prevention of disease, or for the purpose of affecting a structure or function of the body.

Payments for medicine and drugs qualify as medical care expenses, regardless of whether the item is available without a prescription (that is, an OTC item) or requires a prescription. However, only items that are legally procured and are generally accepted as being medicine and drugs qualify as reimbursable medical care expenses.

Expenses for OTC items (other than medicines or drugs) may qualify as medical care only if they are “**primarily for**” the prevention or alleviation of a physical or mental defect or illness. **Expenses that merely benefit general health, on the other hand, are considered personal expenses and will not qualify as medical care expenses.**

Plan Design Tip: Employers that sponsor health FSAs or HRAs may design their plans to define the medical care expenses that are eligible for reimbursement more narrowly than what is permitted under Code Section 213(d) and the CARES Act. For example, some employers may exclude certain expenses that are difficult to administer, such as specific OTC items, even when those items may qualify as “medical care expenses” under IRS guidelines.

Medical Care Factors

Whether an otherwise personal expense is primarily for medical care is a question of fact. Several objective factors may be considered in making this determination, including:

- The motive or purpose for making the expenditure;
- Whether a physician has diagnosed a medical condition and recommended the item as treatment;
- The link between the treatment and the illness;
- Treatment effectiveness; and

- The proximity in time to the onset or recurrence of a disease.

The “But For” Test

For the expense to be deemed medical care, it must be established that the expense would not have been paid “but for” the disease or illness. That is, the item is not for medical care if the individual would have paid for it even without a medical condition.

Personal and Medical OTC Items

An IRS [information letter](#) from 2009 specifically addresses several items (other than medicine or drugs) that may be both personal and medical in nature, as well as items that are generally used only for medical care. In addition, the IRS has provided a [set of frequently asked questions](#) (FAQs) addressing whether certain costs related to general health, nutrition and wellness are medical expenses that can be paid or reimbursed by an HSA, health FSA or HRA.

Personal Items as Medical Care

Certain items may qualify as medical care or may be personal items, depending on how they are used. For example, a person may use these items to maintain general health, or as toiletries or cosmetics (such as face creams, deodorants, perfumes, shampoos or toothpaste). These are personal uses. However, if it can be shown that the item is used to treat or alleviate a disease or injury, and satisfies the “but for” test, the item may qualify as a medical care expense.

Medical Care Only Items

Items that have no purpose other than to treat a disease, illness, or mental or physical defect may qualify as medical care. Treatments for the following conditions will most likely qualify as medical care: acne, incontinence, arthritis, constipation, colds and sinus problems, dehydration and indigestion.

The following items will probably qualify as medical care:

- Support braces and shoe inserts for injured or weakened body parts;
- Products that have no purpose but to treat existing skin conditions such as eczema (as opposed to products that are designed to prevent the development of the condition); and
- Wheelchair cushions that are a necessary accessory to a wheelchair.

OTC Contraceptives

Group health plans and health insurance issuers must cover OTC preventive products, including contraceptives, without cost sharing only when they are prescribed for an individual by their health care provider. However, federal agencies have [confirmed](#) that individuals can use their HSAs to pay for the costs of OTC contraception on a tax-free basis. Also, health FSAs and HRAs can be designed to reimburse OTC contraceptives.

Excess Cost of Personal Items

The excess cost of an otherwise personal item that is specially designed to treat or alleviate a medical condition, over the cost of the item without the special features, may be considered an expense for medical care. For example, the cost of specially designed clothing that is used to treat a specific disease, such as diabetic socks, compression hose or orthopedic shoes that exceed regular clothing, may be a medical care expense. However, these items may also be used for personal or preventive reasons. Whether they are eligible for reimbursement will depend on the facts of each specific case.

Special Foods and Nutritional Supplements

According to the IRS' [FAQs](#), the cost of food or beverages purchased for weight loss or other health reasons is a medical care expense that can be paid or reimbursed by a health FSA, HRA or HSA only if:

- The food or beverage does not satisfy normal nutritional needs;
- The food or beverage alleviates or treats an illness; and
- The need for the food or beverage is substantiated by a physician.

The medical expense is limited to the amount by which the cost of the food or beverage exceeds the cost of a product that satisfies normal nutritional needs. If any of the three requirements above are not met, the cost of food or beverages is not a medical expense. Also, the cost of nutritional supplements is a medical care expense if the supplements are recommended by a medical practitioner as treatment for a specific medical condition diagnosed by a physician. Otherwise, the cost of nutritional supplements is not a medical expense.

LINKS AND RESOURCES

- [Code Section 213\(d\)](#) contains the federal definition of "medical care."
 - [IRS information letter from 2009](#) addresses whether certain OTC items qualify as medical care expenses.
 - The [CARES Act](#) allowed OTC drugs and menstrual care products to be treated as qualified medical expenses.
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