

ACA COMPLIANCE OVERVIEW



Reimbursement of Over-the-Counter Drugs

The Affordable Care Act (ACA) placed restrictions on tax-free reimbursements for over-the-counter (OTC) drugs from health flexible spending arrangements (health FSAs), health reimbursement arrangements (HRAs), health savings accounts (HSAs) and Archer medical savings accounts (Archer MSAs). In most cases, individuals using these accounts must have had a prescription to reimburse the costs of OTC drugs purchased after Dec. 31, 2010.

However, on March 27, 2020, President Trump signed the [Coronavirus Aid, Relief and Economic Security Act](#) (CARES Act) into law to provide \$2.2 trillion in federal funding to address the COVID-19 crisis. **Effective Jan. 1, 2020, the CARES Act allows OTC drugs, along with menstrual care products, to be treated as qualified medical expenses that may be paid for using these tax-advantaged arrangements.**

This ACA Compliance Overview describes the ACA's requirements with respect to OTC drugs, including changes made by the CARES Act.

LINKS AND RESOURCES

- The Internal Revenue Service (IRS) issued [Notice 2010-59](#) on Sept. 3, 2010, to provide more information on this requirement.
- The IRS subsequently released [Notice 2011-5](#) to modify the guidance in Notice 2010-59 regarding debit card usage.
- IRS [Q&As](#) provide additional guidance on the ACA's changes for OTC medicines and drugs.
- The [CARES Act](#) allows OTC drugs and menstrual care products to be treated as qualified medical expenses.

Affordable Care Act Rules

The ACA limited reimbursements for the cost of OTC drugs or medicines from certain health accounts to only those purchased with a prescription.

This requirement did not apply to:

- Insulin, even if purchased without a prescription; and
- OTC items that are not medicines or drugs, such as medical supplies or devices.

The CARES Act

- Effective Jan. 1, 2020, the CARES Act treats all OTC drugs and menstrual care products as qualifying medical expenses that may be paid for (or reimbursed) on a tax-free basis by an HSA, health FSA, HRA or Archer MSA.
- This change eliminates an ACA provision that required individuals to have a prescription for an OTC drug (except insulin) to pay for it on a tax-free basis with their HSA, health FSA, HRA or Archer MSA.

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Overview

Effective Jan. 1, 2011, the ACA placed restrictions on tax-free payment or reimbursement of OTC medicines and drugs from health FSAs, HSAs, Archer MSAs and HRAs. Under these rules, after Dec. 31, 2010, tax-free payment or reimbursement was available for expenses incurred for a medicine or drug only if the medicine or drug was a **prescribed drug** (regardless of whether the drug was available without a prescription) or was **insulin**.

Expenses incurred for OTC medicines or drugs purchased without a prescription before Jan. 1, 2011, could be reimbursed tax-free at any time, under the terms of the plan and any applicable rules.

Changes Made by the CARES Act

Effective Jan. 1, 2020, the CARES Act treats all OTC medicines as qualifying medical expenses that may be paid for (or reimbursed) on a tax-free basis by an HSA, health FSA, HRA or Archer MSA. **This change eliminates the ACA provision that required individuals to have a prescription for an OTC medication (except insulin) to pay for it on a tax-free basis with their HSA, health FSA, HRA or Archer MSA.**

In addition, effective Jan. 1, 2020, menstrual care products are qualifying medical expenses that can be paid for (or reimbursed) on a tax-free basis by an HSA, health FSA, HRA or Archer MSA. Menstrual care products include tampons, pads, liners, cups, sponges or similar products used by individuals with respect to menstruation.

These changes are discretionary for employers that sponsor health FSAs and HRAs. However, because HSAs are individual accounts, and not employer plans, employers do not control how HSA funds are used.

Definition of Prescription

For purposes of these rules, a “**prescription**” is a written or electronic order for a medicine or drug that:

- Meets the legal requirements of a prescription in the state in which the medical expense is incurred; and
- Is issued by an individual who is legally authorized to issue a prescription in that state.

Rules for Other OTC Items

The ACA’s requirement to get a prescription did not apply to OTC items that are not medicines or drugs, including equipment (such as crutches), supplies (such as bandages) and diagnostic devices (such as blood sugar test kits). These items can qualify as medical care if they otherwise meet the Code’s definition of medical care, which includes expenses for the diagnosis, cure, mitigation, treatment or prevention of disease, or for the purpose of affecting any structure or function of the body. However, expense for items that are merely beneficial to the general health of an individual (such as an expenditure for a vacation) are not expenses for medical care.

Effective Dates

The requirement to obtain a prescription applied for expenses incurred after Dec. 31, 2010, regardless of whether the plan year for the employer’s plan is a fiscal or calendar year, or whether there is no plan year (or other coverage period, in the case of an HRA), and regardless of any applicable grace period for a health FSA.

The changes made by the CARES Act with respect to OTC medicines and menstrual products applies beginning Jan. 1, 2020.