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Health Reimbursement Accounts or Health Savings Accounts: Which One is Right for Your Employees?

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In today's competitive marketplace, where budgets are stretched thin, employers want cost effective alternatives to a traditional medical plan. Companies understand that employees have historically enjoyed relatively robust medical plans that offer coverage with little to no out of pocket cost. However, with the rising costs for coverage under a traditional medical plan employers are increasingly modifying medical plan coverage to achieve greater cost savings by implementing High Deductible Health Plan ("HDHP") designs where employees pay less in premiums, but have higher deductibles and out of pocket costs.

HDHP Plans are growing in popularity amongst employers looking to maximize their employee benefit dollars; however, employees generally see HDHP plans as a benefit take away, since they do have to shoulder more of their own medical expenses. To combat this negative perception employers often elect to offset the cost-shift by funding all or a part of the deductible back to the employee through either a Health Reimbursement Arrangement ("HRA") or a Health Savings Account ("HSA"). When deciding which of these options to implement, the employer must consider a wide variety of factors, particularly when contemplating an HSA.

Health Reimbursement Arrangements ("HRA")

The basic concept of a HRA is that the employer provides funds which are used to reimburse the employee for qualified medical expenses incurred by them or their tax dependents. No employee funds are involved, and the money that is not used to pay eligible expenses remains property of the employer.

HRAs offer maximum flexibility to the employer to design and structure the amount per employee available for reimbursement, along with what expenses are eligible for reimbursement. Additionally, the employer can decide if they wish to allow a carryover right for any un-used funds or not.

The employer also has significant flexibility in designing and structuring the underlying HDHP plan. First dollar benefit designs are permitted and a full Flexible Spending Account (FSA) can be offered alongside the HRA, which is not the case with an HDHP/HSA paring.

HRA's are attractive not only for their design flexibility, but also because they appeal to diverse economic and age demographics within the employer's workforce. Employees like HRA's since the employer is essentially paying for some or all of the deductible. HRAs are a great addition when the employee compensation level is such that disposable income might not be sufficient to absorb the full HDHP deductible costs. HDHP/HRA's easily coordinate with other insurance coverage that employees or their dependents might carry, including Medicare, so regardless of the age of the participant population everyone can benefit from the HRA.

Drawbacks to HRAs are that the employer must ensure that sufficient funds are available to cover the amounts allocated to the HRA, even though the money might not actually be reimbursed, which does require additional accounting involvement and reconciliation. Additionally, since it is employer funds employees don't have as much incentive to spend those dollars wisely as they do when it is their money on the line.

In comparison with HSAs, HRAs are generally regarded as offering the best opportunity for control, flexibility, and work well with both younger and older employees.

Health Savings Accounts

Unlike HRAs which are legally considered medical plans, a Health Savings Account (HSA) is a tax-favored bank account, that is in the name of the employee and all funds deposited into it by Employer and/or Employee are immediately property of the employee. Due to the fact that the all monies deposited into the HSA are non-taxable, the government has strict regulations surrounding the amount of funds per year that may be deposited, and how the money is used. To ensure that the account is not used as a end-run around paying taxes, the underlying HDHP plan must follow strict design parameters in order to deemed qualified for bundling with an HSA.

Since the HSA is a bank account, once funds are deposited into the account the employer's obligation is complete and the responsibility resides solely with the employee on the use of the funds. Employees like the fact that the money is theirs to either spend or save depending on their given situation. A relatively healthy person with low claim experience can effectively allow funds to build up in that account and then can utilize it as another source of retirement income. Due to some of the tax complexities involved with funding and utilizing HSAs, these type of arrangements work best in workplaces with highly educated, well compensated, white collar employees who generally have the sufficient levels of disposable income to fund their deductibles.

One of the nuances to HDHP/HSA plan design requirements is that in order for the employee to be eligible to make contributions or receive funds in their HSA, the employee and their covered dependents cannot have any other form of insurance coverage in effect other than another qualified HDHP plan. This requirement means that HDHP/HSA plans may work best in companies who have relatively younger workers who are less likely to have other coverage in effect. Workforces that tend to have older workers who are nearing retirement or Medicare entitlement, or whose employees have other impermissible coverage in effect will either have to drop their other coverage, or they will be prohibited from utilizing the HSA. This can have a very negative impact on employees and their dependents, so careful analysis of workforce demographics must be considered prior to implementing an HSA.

In comparison with HRAs, HSAs are generally regarded as having the best opportunity for consumer engagement, cost control, and works well in environments that have a young healthy workforce that has higher compensation levels.

When done right the implementation of either a HRA or an HSA can be a wonderful complement to a HDHP medical plan and can be viewed as a positive benefit for both the employee and the employer. However, when implemented without a thorough analysis of the demographics of the employee population, the fundamental requirements and regulations involved, and the level of administrative involvement required by the employer; the outcome can have a negative impact on both the employer and their employees. HRA and HSA both are great options to enhance a HDHP medical plan, but it is critical that employers carefully consider the pros and the cons to each option and select the one that best fits their organization.

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Healthcare Management Administrators (HMA), is a third party benefits administrator based in Bellevue, WA. HMA currently administers over 600 benefits plans and

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