

Great News For Employees

Over-the-Counter Drugs are now eligible

On September 3rd, 2003 the IRS issued Revenue Ruling 2003-102. This Revenue Ruling changes the IRS position regarding the reimbursement of over-the-counter (OTC) drugs from health care Flexible Spending Accounts (health FSAs) and Health Reimbursement Arrangements (HRAs). In the past, the IRS had stated that OTC drugs could not be reimbursed by such plans because reimbursements are limited to expenses that would qualify as deductible medical expenses. IRC §213(d) only permits a deduction for drugs that are “prescribed drugs” or insulin. A “prescribed drug” is a drug that is not available in any form without a prescription. Thus, if a drug can be obtained in any form OTC, then it is not a deductible medical expense.

The change in the IRS position is the result of a strict interpretation of IRC §105. IRC §105 permits an individual to exclude from income any amounts paid by a health plan that are reimbursements of expenses for “medical care.” The key to the IRS interpretation is that the statute only refers to “medical care” as defined in IRC §213(d). Under that statutory scheme of IRC §213, amounts spent for OTC drugs are “medical care” expenses, they just aren’t deductible. Because IRC §105 allows the reimbursement of any medical care expense, not just those that would be deductible, it is permissible for health FSAs and HRAs to reimburse OTC drugs. The response to this IRS change in position has generally been

favorable. While all claims must be substantiated, presumably the substantiation of an expense for OTC drugs would be handled in the same manner as any other expense.

Some practitioners have questioned whether a change in benefit elections can be made due to the new IRS position. Regulations provide that participants in a health FSA offered through a cafeteria plan cannot change elections for the health FSA due to cost of coverage changes. Therefore, mid-year election changes for health FSAs are not permitted as a result of the Revenue Ruling.

Plan Amendments

The provisions of existing health FSAs and HRAs need to be reviewed in order to determine whether a plan amendment is needed in order to permit the reimbursement of OTC drugs. For example, the health FSA language in the documents provided to you by Vantage Flex does not need to be amended. The relevant provision in the document refers to medical care as defined in code section 213, and therefore could be interpreted in the same manner as described above.

In the case of an HRA however, unless a plan design allows for Section 213 eligible expenses, the new ruling will have no effect.

The Revenue Ruling that was released still emphasizes that the over the counter drug must still be for the purpose of providing medical care. Medical care is defined as diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body.

The IRS specifically addressed antacid, allergy medicine, pain reliever, and cold medicine as eligible expenses. Listed below are categories of medicines that are eligible as well as some that are ineligible.

Eligible Items

Allergy medicines

Antihistamines
Decongestants
Nasal Sprays
Sinus Medications

Anti-itch

Antihistamines
Athletes foot creams, powders

Cold medications

Cough drops
Cough syrups
Decongestants
Flu and cold medications
Sore throat sprays
Vapor rubs

Digestive tract relief

Antacids
Anti-diarrhea medications

Anti-nausea medications
Heartburn medications

Miscellaneous

Cold sore remedies
Eye drops
Lice treatments
Nicotine patch/gum
Wart removers
Yeast infection treatments

Pain relievers

Acetaminophen (Tylenol)
Anti-inflammatory drugs
Disinfecting creams, ointments
Ibuprofen (Motrin)
Fever Reducers
Naproxen Sodium (Aleve)

Ineligible Items

General health items *

Appetite suppressants
Herbal remedies

- Chondroitin Sulfate
- Echinacea
- Gingko Biloba
- Ginseng
- Glucosamine

- St John’s Wart Supplements
- Vitamins
- Weight loss

*These items may be eligible with a doctor’s letter stating a specific medical diagnosis.

Ineligible items

Cosmetic items
Cosmetics including face creams
Shampoo

Soaps and cleansers
Sundry items
Toiletries such as toothpaste