

# PUBLICATION

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## Spotlight on Health Care Reform: The OTC Ban

September 27, 2010

Health care reform brought sweeping changes to employer-sponsored group health plans. Many plan sponsors are working diligently to ensure that their plans are compliant with the provisions of the Patient Protection and Affordable Care Act (PPACA) as they become effective. Parts of PPACA are effective as early as September 23, 2010 for some plans. In the bustle of ensuring compliance with PPACA, plan sponsors should recognize that health care flex-spending accounts, health reimbursement arrangements, health savings accounts, and Archer medical savings accounts (collectively the Reimbursement Account Plans) have their own requirements under PPACA, which include a new limit on reimbursement for over-the-counter medications (OTCs).

Generally effective January 1, 2011, PPACA limits reimbursements or distributions from Reimbursement Account Plans to (i) prescription drugs, (ii) OTCs obtained with a doctor's prescription, and (iii) insulin. Therefore, reimbursements or payments for OTCs without a prescription will not be permitted by Reimbursement Account Plans. Improper reimbursement of non-prescription OTCs will result in the amount being included in the participant's gross income and subject to an additional 20% excise tax.

On September 3, 2010, the IRS issued guidance in Notice 2010-59 regarding the implementation of the new requirements for OTCs. The Notice provides three points that are key to Reimbursement Account Plan administration:

- Definition of a Prescription. A prescription must (i) be in a written or electronic form, (ii) meet the legal requirements for a prescription in the state in which the expense is incurred, and (iii) be issued by a person legally authorized to write prescriptions where the expense is incurred.
- Exclusion of Other Medical Products. Medical equipment (e.g., crutches), supplies (e.g., bandages), and diagnostic devices (e.g., blood sugar test kits) are not subject to the prescription mandate required for OTCs and, therefore, may be reimbursed without a prescription.
- Debit Card Ban for OTC Purchases. The Notice recognizes that most store checkout systems are not capable of substantiating that a valid prescription is held for the purchase of OTCs. Therefore, effective January 16, 2011, participants may not use Reimbursement Account Plan debit cards to purchase OTCs. Instead, participants must submit the prescription, along with a receipt for the OTC, to the Reimbursement Account Plan's administrator for payment.

In light of these changes, employers that maintain any of these Reimbursement Account Plans should consider the following action steps:

- Amend any Reimbursement Account Plan to limit the reimbursements or distributions for the purchase of OTCs to those substantiated with a valid prescription. This is generally effective for any purchase made after 2010, though Reimbursement Account Plan debit card purchases as late as January 15, 2011 will not be challenged by the IRS.
- Notify participants before January 1, 2011, and preferably well before that date, that they will be unable to receive reimbursement for unprescribed OTCs. This will allow adequate time to purchase such products prior to the ban's January 1, 2011 general effective date. Note that as long as the purchase is made by December 31, 2010, the reimbursement may be made later without the adverse

tax effects described above. This ban becomes effective January 1, 2011, regardless of the plan year.

- For plans that utilize debit cards, coordinate with the administrator about the ban on the use of debit cards for OTCs. Once the substantiation procedure is established with the administrator, a notice should be distributed to participants explaining the proper procedure for reimbursement of prescribed OTCs.

If you would like to discuss any of the matters addressed in this Alert, please contact any attorney in our Tax or Health Departments.