Dear Representative Hill:

I am responding to your inquiry, on behalf of your constituent, , about disclosure requirements for health flexible spending arrangements. Specifically inquired about the amount of information required for tax-free employer reimbursements of medical expenses under IRS rules.

Under section 105 of the Internal Revenue Code (the Code), employer reimbursements of medical expenses are excluded from an employee’s income and wages for tax purposes. These rules also apply to reimbursements of medical expenses under an employer-sponsored health flexible spending arrangement (health FSA) through a section 125 cafeteria plan.

Generally, a health flexible spending arrangement must satisfy certain substantiation requirements before paying or reimbursing medical expenses to ensure that the reimbursement qualifies for the exclusion from income and wages. In particular, the rules require information from a third party (such as the provider of the medical services) describing the medical service or product, the date the service or product was provided, and the amount of the expense. Proposed Income Tax Regulation section 1.125-6(b)(3) says:

(3) Substantiation by independent third-party. (i) In general. All expenses must be substantiated by information from a third-party that is independent of the employee and the employee’s spouse and dependents. The independent third-party must provide information describing the service or
product, the date of the service or sale, and the amount. Self-substantiation or self-certification of an expense by an employee does not satisfy the substantiation requirements of this paragraph (b). The specific requirements in sections 105(b), 129, and 137 must also be satisfied as a condition of reimbursing expenses for qualified benefits. For example, a health FSA does not satisfy the requirements of section 105(b) if it reimburses employees for expenses where the employees only submit information describing medical expenses, the amount of the expenses and the date of the expenses but fail to provide a statement from an independent third-party (either automatically or subsequent to the transaction) verifying the expenses. (emphasis added)

In addition, the employee must certify that any expense being reimbursed has not already been reimbursed and the employee will not seek reimbursement from any other health benefit plan.

Generally, the taxpayer must provide sufficient details related to the description of the service or product to allow the health FSA administrator to verify that the service or product is a qualifying medical expense. Typically, this is the same level of detail an insurance company requires from a health care provider to pay for a medical expense.

In addition, like information health care providers submit to insurance companies, information about health care submitted to health FSA administrators as part of a request for reimbursement is generally protected health information subject to the same protections against disclosure and system-security requirements as information submitted to other health insurance plans.

I hope this information is helpful. If you have any questions, please call me at or .

Sincerely,

Christine Ellison, Acting Chief, Health and Welfare Branch, Office of Associate Chief Counsel (Tax Exempt and Government Entities)