

**EPSTEIN BECKER & GREEN, P.C.**

ATTORNEYS AT LAW

1227 25th Street, NW, Suite 700  
Washington, DC 20037-1175  
202.861.0900  
FAX: 202.296.2882  
EBGLAW.COM

**MEMORANDUM**

**To:** N.G.A.

**From:** Epstein Becker & Green<sup>1</sup>

**Date:** December 28, 2010

**Re:** FSA and HRA Debit Cards and Purchase of Prescribed Over-The-Counter Drugs

---

**Overview**

On December 23, 2010, The Internal Revenue Service (“IRS”) issued a Notice 2011-5 (“Notice”), modifying previous guidance, with regard to Section 9003 of the Patient Protection and Affordable Care Act (“PPACA”). The guidance provides a method whereby, after January 15, 2011, Health Flexible Spending Arrangement (“FSA”) and Health Reimbursement Arrangement (“HRA”) debit cards may be used to purchase over-the-counter (“OTC”) drugs when they are prescribed. The Notice provides a method to confirm prescribed status for OTC drugs for two specified groups of vendors which include N.G.A. members: 1) drug stores and pharmacies, non-health care merchants that have pharmacies, and mail order and web-based vendors; and 2) vendors (other than those mentioned above) having health care related Merchant Codes.

Section 9003 of PPACA revised the definition of medical expenses for employer-provided accident and health plans, including FSAs, HRAs, Health Savings Accounts (“HSAs”), and Archer Medical Savings Accounts (“Archer MSAs”). PPACA amended the definitions of the above plan structures, with regards to OTC drugs, to allow for reimbursement or inclusion as a medical expense, “only, if such medicine or drug is a *prescribed drug* (determined without regard to whether such drug is available without a prescription) or is insulin.”<sup>2</sup> Therefore, consumers are generally prohibited from purchasing non-prescription OTC medications using their FSA or HSA debit cards. Because OTC drugs are sometimes prescribed (i.e., aspirin therapy) the Notice provides guidance on the steps that vendors must take in order to accept FSA and HSA debit cards for the purchase of those OTC medications.

**IRS Notice 2011-5**

**I. Drug Stores and Pharmacies, Non-Health Care Merchants That Have Pharmacies, and Mail Order and Web-Based Vendors that Sell Prescription Drugs.**

---

<sup>1</sup> Mark Lutes and Adam Solander prepared this update.

<sup>2</sup> PPACA § 9003 (*emphasis added*).

ATLANTA • BOSTON • CHICAGO • HOUSTON • LOS ANGELES • MIAMI  
NEWARK • NEW YORK • SAN FRANCISCO • STAMFORD • WASHINGTON, DC

Epstein Becker Green Wickliff & Hall, P.C. in Texas only.

Notice 2011-05 provides a method whereby, after January 15, 2011, FSA and HRA debit cards may continue to be used to purchase prescribed OTC medicines or drugs at drug stores and pharmacies, at non-health care merchants that have pharmacies, and at mail order and web-based vendors that sell prescription drugs. These requirements include:

- 1) Prior to Purchase: i) the prescription for the OTC medicine or drug must be presented to the pharmacist; ii) the OTC medicine must be dispensed by the pharmacist in accordance with applicable law and regulations pertaining to the practice of pharmacy; and iii) an Rx number must be assigned;
- 2) The pharmacy or other vendor must retain a record of the Rx number, the name of the purchaser (or name of the person for whom the prescription applies), and the date and amount of the purchase in a manner that meets the IRS recordkeeping requirements;
- 3) All records must be made available to the employer or its agent upon request;
- 4) The debit card system must not accept a charge for an OTC medicine or drug unless an Rx number has been assigned;
- 5) The existing requirements for use of FSA or HSA debit cards, must be satisfied.<sup>3</sup>

## **II. Vendors (Other Than Those Mentioned Above) Having Health Care Related Merchant Codes.**

Similarly, FSA and HRA debit cards may be used to purchase OTC drugs after January 15, 2011, from vendors (other than those described in the preceding paragraph) having health-care related Merchant Codes, if a modified set of these same conditions is met.

The Notice states, “[a]fter January 15, 2011, health FSA and HRA debit cards may also continue to be used to purchase [OTC] medicines or drugs from vendors (*other than drug stores and pharmacies, non-health care merchants that have pharmacies, and mail order and web-based vendors that sell prescription drugs*) having health care related Merchant Codes... if all requirements in the preceding paragraph are satisfied, other than the requirements in clause (1) and clause (4) of the preceding paragraph and the requirement in clause (2) of the preceding paragraph that a record of the Rx number be retained. If these requirements are satisfied, these debit card transactions will be considered fully substantiated at the time and point-of-sale.”

Significantly, the Notice states, “[f]or all other providers and merchants, other than those described in this notice, health FSA and HRA debit cards may not be used to purchase [OTC] medicines or drugs after January 15, 2011.”

---

<sup>3</sup> The existing requirements are set forth in: Prop. Treas. Reg. § 1.125-6 and in Rev. Rul. 2003-43, 2003-1 C.B. 935; Notice 2006-69, 2006-2 C.B. 107; Notice 2007-2, 2007-1 C.B. 254; and Notice 2008-104, 2008-2 C.B. 1298.

### **Impact on N.G.A. Members**

*The Notice provides guidance to N.G.A. members who may be vendors within the meaning of the rule. The Notice sets forth the process those vendors must employ in order to accept FSA and HRA debit cards for prescribed OTC drugs.*

*Further, previously released guidance did not differentiate between different types of vendors.<sup>4</sup> Therefore, the Notice provides some relief to vendors, having health care related Merchant Codes, with regards to the process they must following order to accept debit cards for prescribed OTC drug purchases.*

*Please note this rule does not provide relief to consumers who wish to use their FSA or HRA debits cards to purchase non-prescription OTC medications.*

---

<sup>4</sup> *IRS Notice 2010-59 stated, on or after January 16, 2011, [OTC] medicine or drug purchases at all providers and merchants (whether they have an inventory information approval system (IIAS)) must be substantiated before reimbursement is made. Substantiation is accomplished by submitting the prescription (or a copy of the prescription or other documentation that a prescription has been issued) for the OTC medicine or drug, and other information from an independent third party that satisfies the requirements. for example, a customer receipt issued by a pharmacy which identifies the name of the purchaser (or the name of the person for whom the prescription applies), the date and amount of the purchase and an Rx number satisfies the substantiation requirements for over-the-counter medicines or drugs, as does a receipt without an Rx number accompanied by a copy of the related prescription.*