

IRS Announces PPE Is Medical Expense

WRITTEN BY

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Who Needs to Know

U.S. employers, particularly HR personnel.

Why It Matters

On March 26, the IRS announced that personal protective equipment (PPE) — such as masks, hand sanitizer, and sanitizing wipes for the primary purpose of preventing the spread of COVID-19 — are treated as medical care under Section 213(d) of the Internal Revenue Code (IRC). While deemed worthy of the weekend news, the announcement comes with wrinkles that make the relief seem better on paper than it is in reality. For employers, the announcement means that individuals can seek reimbursement from employer-sponsored Health Flexible Spending Accounts (FSAs) and Health Reimbursement Accounts (HRAs) for periods beginning on or after January 1, 2020. As a practical matter though, this raises timing and substantiation questions.

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For individuals, the announcement means that they can include PPE expenses in determining their itemized deductions on their 2020 individual tax return. Medical expenses, including expenditures for PPE, that exceed 7.5% of adjusted gross income may be claimed as an itemized deduction. However, relatively few individuals still itemize deductions now that the standard deduction exceeds \$12,000 for a single individual, \$18,000 for a head of household, and \$24,000 for a married couple filing jointly.

In addition, individuals may be able to obtain tax-free distributions from their Health Savings Accounts (HSAs) and Archer Medical Savings Accounts (MSAs) for PPE expenses.

Employer Considerations

Timing of Claim. Ordinarily, most Health FSAs and HRAs have already reached or are very close to reaching the last day for filing requests for reimbursement of expenses incurred during 2020. Employers and their FSA/HRA administrators will need to consider whether to extend the deadline for submitting 2020 claims in order to reimburse PPE expenses incurred in 2020. The purchase of the bulk of PPE occurred early in 2020 when there

was a rush to acquire masks and stock up on hand sanitizer and sanitizing wipes. Because of the timing of these expenditures, for the IRS announcement to have much of an impact, this extension may be needed.

However, in spite of their stated deadlines, when determining how to administer the deadline for submitting 2020 claims, employers and their FSA/HRA administrators also will need to factor in the individualized extended deadlines to submit ERISA claims and appeals, which were recently clarified in Notice 2021-01 (*i.e.*, beginning on March 1, 2020, the deadline to submit claims and appeals under ERISA plans ends on the earlier of one year from the ordinarily applicable deadline or 60 days from the end of the national emergency, which is ongoing). Health FSAs and HRAs are ERISA group health plans, and the submission of a reimbursement request from such accounts constitutes the filing of an ERISA claim for benefits. Thus employers may very well need to accept reimbursement requests for expenses incurred in 2020, even after the normal claims submission deadline, in accordance with this most recent federal agency guidance that provides for such deadline extensions during the current COVID-19 national emergency.

Substantiation Requirements. In addition, employers and their FSA/ HRA administrators will need to address what will be acceptable substantiation of a PPE expense in determining whether to reimburse such expenses. Health FSAs and HRAs typically require a written statement from an independent third party stating that a qualified health care expense has been incurred and the amount of such expense. Thus, receipts or other statements documenting the expenditures are needed to obtain reimbursement. Given the time that has passed and the likely inattention by employees to retain such expenditure receipts, it is not anticipated that this IRS announcement will significantly impact 2020 Health FSAs or HRAs due to lack of substantiation.

It is unclear whether employers and their FSA/HRA administrators will need to make difficult determinations in processing claims for reimbursement. Is the purchase of a mask to match every outfit actually made for the primary purpose of preventing the spread of COVID-19? Does the purchase of fabric and other supplies necessary to make PPE satisfy the expanded definition? And finally, is an employer required to discern the reasonableness of a \$125 versus a \$10 mask, or \$50 bottle versus a \$3 bottle of hand sanitizer?

For future purchases, qualifying pharmacies and merchants will update their inventory information approval systems to reflect that PPE products are eligible expenses for purchase on Health FSA debit cards. However, the timing of these updates may vary. Until the updates have been implemented, Health FSA debit cards will not approve these expenses, and claims must be submitted manually with appropriate substantiation specifying the items purchased.

Plan Amendment. Many Health FSAs and HRAs already define qualifying medical expenses as any expense incurred for medical care as defined in IRC Section 213(d). For a plan with that broad definition, no plan amendment will be needed to implement the IRS announcement. If the plan language is more limiting, the plan may reimburse such expenditures if properly substantiated and within the applicable claim period, but it will need to be amended no later than the last day of the first calendar year beginning after the effective date. Thus, for calendar year plans, the amendment would be required by December 31, 2021 in order to have an effective date of January 1, 2020.

Health Savings Accounts

Distributions from HSAs and MSAs are not taxable if used to pay qualifying medical expenses. An individual covered by an HSA reports such a distribution on a Form 8889 (or a Form 8853 in the case of an MSA) when filing his/her individual income tax return. The individual makes the determination of whether a withdrawal is for a qualifying medical expense and reports it as such. Distributions not taken for a qualifying medical expense will be subject to income tax and possibly an additional 20% tax. On audit, the IRS may request documentation substantiating the purpose of the withdrawals and thus require the receipts or other written statements to be provided. In the HSA and MSA context, this substantiation burden will rest with the individual account owner.

If you have any questions or require assistance, please contact any member of the Troutman Pepper Employee Benefits and Executive Compensation Practice Group. We are here to help you in any way that we can. This alert reflects guidance as of March 26, 2021.

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