

1. What is an HRA?

An HRA is an employer-funded arrangement that reimburses employees for certain medical care expenses incurred by employees (and their spouses and dependents). Typically an employer creates a notional (i.e., unfunded) HRA account for each participating employee and then reimburses the employee for substantiated medical expenses up to his or her account balance. An HRA must be paid for solely by the employer and may not be provided pursuant to a salary reduction election or otherwise under a Code 125 Cafeteria Plan. (1) Benefits that are not used to reimburse an employee during the coverage period may be carried over to subsequent coverage periods. There is no specific Code section governing HRAs, but the IRS has confirmed their tax-favored treatment under the general principles of Code 105 and 106.

2. What are the Tax advantages of an HRA?

If an HRA is designed and operated in compliance with IRS guidance, employees will not be taxed on the value of their HRA coverage or on reimbursements that they receive from the HRA, under Code 105 and 106, even though unused amounts may carry forward into future years for reimbursement of medical expenses. The employer will, subject to certain conditions and limitations, be entitled to a deduction for reimbursements made under the HRA.