

Compliance Briefing: Debit Card Use at Pharmacies, Drug Stores and Mail Order Pharmacies after July 1, 2009



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This Compliance Briefing is provided to assist clients in understanding the application of IRS guidance for use of debit cards with Health Care Flexible Spending Accounts and Health Reimbursement Arrangements.

Background

In the spring of 2003, the IRS released their first debit card guidance. This publication gave direction on exactly how an electronic reimbursement arrangement should be established by an employer that sponsors a Section 125 health Flexible Spending Account (FSA) plan or a Health Reimbursement Arrangement (HRA).

IRS Revenue Ruling 2003-43 limited the use of debit cards to specified Merchant Category Codes (MCCs) relating to healthcare and explained the accepted methods of auto substantiation such as, copayment match, recurring expenses and real-time third party verification.

Notice 2006-69 introduced additional methods of auto substantiation. These include the matchup of copayment multiples, insurance carrier submitting claims using an explanation of benefit (EOB) and the inventory information approval system (IIAS).

Particular emphasis was placed on the fact that these type of debit cards could only be used at healthcare related vendors. This left drug dispensing vendors like grocery and discount stores in a pinch. Compliance with this notice was to begin on or after January 1, 2007 which meant vendors had very little time to program and institute the IIAS.

IRS Notice 2007-2 was released December 14, 2006. It provided a one year period of transition relief with respect to the use of debit cards at retailers with non-healthcare related MCCs. That meant that grocery and discount stores had until January 1, 2008 to set up an IIAS if they wanted to be a part of the healthcare debit card business.

In a startling twist, however, Notice 2007-2 also provided that healthcare debit cards could not be used at merchants with the drug store or pharmacy Merchant Category Code (MCC) beginning January 1, 2009 unless: 1) The store participates in the IIAS, or 2) On a store location by store location basis, 90 percent of the store's gross receipts generated during the prior taxable year consisted of items which qualify as medical care expenses, including over-the-counter medications. Later guidance delayed the effective date of the application of Notice 2007-02 to July 1, 2009. That date is fast approaching.

While the provision requiring that drugstores and pharmacies adopt IIAS is rather straight forward, the 90% rule adds an extra level of complexity to the equation. Today, there are many merchants and mail order pharmacies that believe they are covered by the 90% exemption. While this may technically be true, they may still have difficulties as the healthcare debit card is typically set up to only work with the SIGIS Associations standards for IIAS compliance or the Walgreen's solution. This is because the SIGIS Association is a voluntary standards association comprised of retailers, card vendors, card associations, third party administrators and others who worked together to develop an industry solution.

Fortunately, SIGIS has stepped up to the challenge by providing a means for merchants who believe they meet the terms of the 90% exemption to register their exemption and their card acceptor identification information to enable the card to continue to be used at such merchants. Additionally, many of the Point of Sale software vendors that work with independent merchants have developed a solution enabling these vendors to be IIAS compliant.

While being able to accept the card is important, having IAS is a key differentiator that is important to the card users' overall experience. An IAS compliant vendor will be able to accept the health care card AND create a superior experience for the cardholder—because no further documentation will be required on that transaction as it is adjudicated at the point of sale. Those merchants who have identified themselves as a “90 percent” vendor, and have registered themselves as a “90 percent” vendor with SIGIS will still require their customers to provide third-party documentation for the expense*.

It is important to note that this also applies to any mail order pharmacy that the client may have contracted with. In this case, even though it is likely that the merchant ONLY sells eligible items, they will need to register as a 90% merchant, and participants will be required to submit documentation -- the only exception being merchants that have received the IAS certification.

But there is one more option: WageWorks has developed a process whereby mail order pharmacies can provide documentation attesting to their compliance with IAS rules, which enables us to treat them as a “trusted vendor” and auto-adjudicate transactions without need for further substantiation.

In order for WageWorks to allow a merchant to accept its Card, the merchant must comply with the following IRS IAS regulations:

- The merchant must ONLY allow the use of the card for eligible health care items eligible under section 213(d) (including nonprescription medications).
- The merchant must retain specific transaction data that will be available to the participant and/or the plan Sponsor and/or WageWorks, in the event of an audit by a government agency (DOL or IRS).

WageWorks will work with clients and their mail order pharmacies to help them coordinate their registration with SIGIS as a 90% merchant or for certification as an IAS merchant and/or will work to treat them as a trusted vendor for purposes of WageWorks' Health Care Cards.

** In limited cases, the transaction may not need substantiation if it matches a copayment amount, is a multiple of a copayment amount, a recurring expense or has real-time verification by a third party. In every other case, a receipt must be requested from the participant in order to authenticate the expense.*