Helping Employees Manage Out-of-Pocket Medical Expenses

The rising cost of health care, including prescription drugs, has made it increasingly difficult for employees to afford medical care. Employees may forgo medical care to avoid out-of-pocket costs, even when such care is recommended or necessary. Employees who do receive medical care may struggle to pay their health care bills. High deductible health plans (HDHPs) can help employees by keeping premium costs manageable, but they can also create more financial risk for employees until the deductible is met.

There are a variety of strategies available to employers to help employees manage their out-of-pocket medical expenses. These strategies include:

- Offering a health plan option with a low deductible;
- Contributing to a health savings account (HSA), health flexible spending account (FSA) or health reimbursement arrangement (HRA);
- Allowing for hardship distributions from 401(k) accounts to pay for medical expenses;
- Educating employees about their health coverage; and
- Offering an employee assistance plan (EAP) that provides resources for financial advising.

Offer a Low Deductible Health Plan

Health plans with high deductibles have become increasingly popular because they have lower premiums than health plans with low deductibles. HDHPs can also be paired with HSAs, which allow individuals to save for and pay their out-of-pocket expenses on a tax-free basis. However, if employees are struggling with their pre-deductible medical bills, an employer might consider switching to a low deductible health plan or adding a low deductible health plan option to its benefit offerings.

Low deductible health plans make it easier for employees to predict and manage their health care spending. Although these health plans tend to have higher premiums, they minimize the risk of substantial out-of-pocket expenses because of their lower deductibles. A downside to a low deductible plan is that if an employee (or family member) ultimately does not need much medical care during the year, they will have paid higher premiums without obtaining the benefit of the low deductible. These plans tend to work best for employees with more health care needs, such as employees who take expensive medications or have chronic conditions requiring regular doctor visits and prefer predictable health care costs.

Type	Advantages	Disadvantages	Works Best For
High deductible	Lower premiums Compatible with HSAs (if certain cost-sharing limits are met)	Potential for more out-of-pocket medical expenses (until deductible is met)	Individuals who anticipate minimal health care expenses and can afford to pay out-of-pocket until the deductible is met (or want to use an HSA)
Low deductible	Fewer out-of-pocket medical expenses (due to low deductible)	Higher premiums	Individuals with more health care needs who prefer predictable health care costs

Instead of offering one health plan option, some employers offer multiple health plan options for employees to choose from. Offering health plans with different deductibles allows individuals to choose a plan that best suits their health needs and financial situation. While offering multiple health plans can make an employer's benefit package more attractive to existing and prospective employees, it may not be the right approach for all organizations. In general, it is most advantageous for organizations with a diverse workforce with a wide variety of employee ages, medical needs, and resources.

Contribute to an HSA, Health FSA or HRA

A popular way for employers to help employees pay their out-of-pocket medical expenses is to make tax-free contributions to an employee medical savings account. When an employer pairs its group health plan with a tax-advantaged medical savings account, employees can use funds in their accounts for medical expenses that are not paid by the health plan (for example, pre-deductible medical expenses). There are three basic types of medical savings accounts: HSAs, health FSAs and HRAs. Although these accounts all provide a tax-advantaged way for employees to pay out-of-pocket medical expenses, each type of account is subject to different legal requirements and has its own set of advantages and disadvantages. The following is a quick summary of the key features of each type of account, followed by a more in-depth comparison chart:

- **HSAs:** HSAs require the least amount of employer involvement because they are individually owned accounts managed by a bank or custodian. They also provide the most flexibility for employees, as they are nonforfeitable and portable, meaning employees keep their HSAs when they switch jobs and unused funds are never forfeited. Anyone can contribute to an employee's HSA, including their employer, subject to annual limits. However, employees must be covered by an HDHP to be HSA-eligible.
- **Health FSAs:** Health FSAs allow both employers and employees to make tax-free contributions to pay for unreimbursed medical expenses. As employer-sponsored health plans, health FSAs require more employer involvement than HSAs. Unused funds are forfeited at the end of the plan year, although a health FSA may incorporate a grace period or carry-over feature. While employees must be covered by a group health plan to participate, the health plan is not required to be an HDHP.
- **HRAs:** HRAs are employer-funded accounts (employees cannot make their own contributions). Like health FSAs, HRAs are employer-sponsored health plans that require more involvement than HSAs. Unused funds can carry over from year to year, depending on the plan's design. While employees must be covered by a group health plan to participate, the health plan is not required to be an HDHP.

	HSA	Health FSA	HRA
What type of account is it?	An individually owned account is set up with an HSA trustee or custodian.	Employer-sponsored, self-funded health plan.	Employer-sponsored, self-funded health plan.
What type of group health plan must be offered with it?	An HDHP that satisfies minimum annual deductible and maximum out-of-pocket limits.	Any group health plan.	Any group health plan.
Who can fund the account?	Anyone can make contributions to an individual's HSA, including their employer. Employers may allow employees to make pre-tax contributions through a Section 125 cafeteria plan.	Typically funded with employee pre-tax contributions through a Section 125 cafeteria plan. Employers may also contribute.	Only employers may contribute. Employee contributions are not allowed.
What happens when an employee terminates employment?	HSAs are nonforfeitable, which means the employee keeps their HSA upon termination of employment.	The account is forfeited unless COBRA applies.	The account is forfeited unless it includes a spend-down feature. COBRA may also apply.
Can unused funds roll over to the next year?	Yes, there is no deadline for using HSA funds.	No, with two limited exceptions. A health FSA may include a grace period of 2.5 months after the end of the plan year, or it may allow employees to carry over up to $500 (as adjusted for inflation) in unused funds into the next plan year.	Yes, as a plan design option, HRAs may permit unused amounts to be carried over to subsequent years. However, this is not required.
Is there a contribution limit?	Yes. For 2025, the overall contribution limit is $4,300 for individuals with self-only coverage and $8,550 for	Yes. For plan years beginning in 2025, an employee's pre-tax contributions may not exceed $3,300 for the year. Employer contributions are limited to two times the	No. There is no limit required by law. Employers can decide

	HSA	Health FSA	HRA
	individuals with family coverage. Individuals aged 55 or older can increase their contribution limit up to $1,000 per year.	employee's health FSA contribution election for the year (or, if greater, the amount of the employee's health FSA contribution election for the year, plus $500).	how much to contribute each year.
Must claims be substantiated by a third party?	No, the HSA owner is solely responsible for maintaining records that substantiate the medical expense.	Yes	Yes
Does the uniform coverage rule apply?	No	Yes. Once the plan year begins, an employee's maximum amount of reimbursement must be available at any time (reduced only for any prior reimbursements during the same year).	No

Allow Hardship Distributions From Retirement Accounts

Employers may want to consider allowing hardship distributions from their retirement plans to help employees with their medical expenses. As an optional feature, certain tax-qualified retirement plans, including 401(k) and 403(b) plans, may be designed to allow employees to withdraw money from their accounts if they are facing financial hardships. Unlike plan loans, hardship distributions are not paid back to the employee's account.

Hardship distributions can only be made when an employee has an immediate and heavy financial need, and the distribution is limited to the amount necessary to satisfy that financial need. Many retirement plans use an IRS safe harbor to more easily determine if an employee is eligible for a hardship distribution. Under this safe harbor, an employee is considered to have an immediate and heavy financial need if the distribution is for specific reasons, one of which is **medical care expenses of the employee, the employee's spouse, dependents or beneficiary**.

In addition, for an employee to qualify for a hardship distribution, the employee must lack other resources to meet their financial need. To meet this standard, employees must obtain any other currently available distributions under the retirement plan and provide a written statement that they have insufficient cash or other liquid assets reasonably available to satisfy the financial need. Retirement plans can impose additional requirements for establishing that a hardship distribution is necessary, such as a requirement to take all nontaxable loans available under the plan.

Hardship distributions are subject to income taxes unless they consist of Roth contributions. Also, for employees who are under age 59.5, the hardship distribution is generally subject to the 10% early distribution penalty unless an exception applies.

Educate Employees About Health Coverage

Another way employers can help employees manage their medical bills is to help employees understand how their health coverage works and identify ways to reduce their out-of-pocket spending. Employers should review their current educational strategy to identify and address any knowledge gaps. Important topics to cover include basic insurance terms, such as deductible and copay; differences between in-network and out-of-network coverage; and how to make the most of the employer's specific benefit offerings. Often, providing information using various channels (including email updates, printable materials, and in-person or virtual sessions) can be most effective at reaching a diverse workforce.

As part of this process, employers should consider providing employees with these practical tips to become more savvy health care consumers:

- Contribute to an HSA or health FSA, if either of these options are available, as a tax-advantaged way to save for medical expenses;
- Utilize in-network health care providers whenever possible to avoid balance billing and higher cost-sharing limits;
- Make the most of the health plan's free preventive care benefits, such as well-child visits, routine vaccines and cancer screenings;
- Use telehealth services, which can be less costly than in-person visits, when available and practical;
- See a primary care physician for nonemergency care instead of an urgent care center or hospital emergency department;
- Ask if there is a generic version available when a doctor prescribes a brand-name drug;
- Shop around for the best prescription drug pricing; and
- Search for manufacturer coupons before filling a prescription.

Offer an EAP

Employers can also consider offering an EAP to provide individualized support for employees who are struggling with medical bills. EAPs are work-based intervention programs that connect employees with resources to identify and address personal problems. The overall goal of an EAP is to offer employees assistance with their personal issues to improve their overall health and job performance. EAPs typically include a variety of services to help employees remain healthy and productive, such as mental health counseling, substance use disorder counseling, financial advising, legal services, and resources to address family issues and other personal challenges. They are usually provided through a third-party vendor and offered at no cost to employees.

LINKS AND RESOURCES

- IRS Revenue Procedure 2024-25, which includes the inflation-adjusted HSA limits for 2025
- IRS Revenue Procedure 2024-40, which includes the inflation- adjusted health FSA contribution limit for 2025
- IRS webpage on hardship distributions from retirement accounts

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