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Health Savings Accounts

What is an HSA?

A *Health Savings Account* (HSA) is a tax-advantaged personal savings or investment account that an individual can use to save and pay for qualified health expenses, now or in the future. An HSA must be used in conjunction with a “High Deductible Health Plan” (HDHP).

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Who can participate?

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Any individual who meets the following requirements, with respect to any month, can open an HSA.

(1) Is covered under a high-deductible health plan (HDHP) on the first day of such month;

(2) Is not also covered by any other health plan that is not a HDHP (with certain exceptions for plans providing certain limited types of coverage);

(3) Is not enrolled for benefits under Medicare (can be eligible for Medicare just not enrolled)

(4) May not be claimed as a dependent on another person's tax return.

What is a HDHP (High Deductible Health Plan)?

A health plan that meets certain requirements (adjusted annually for inflation) regarding deductibles and out-of-pocket expenses.

- **COVERED BENEFITS**

One key difference between traditional health insurance plans and High Deductible Health Plans is that the deductible must apply to all covered benefits. What this means is there are no Doctor office co-pays or Prescription co-pays in High Deductible Health Plans.

- **LIMITS ON OUT-OF-POCKET EXPENSES**

Annual out-of-pocket maximums (including deductibles and co-pays) do not exceed the maximum out of pocket limit set yearly by the IRS.

Contribution Rules

- Employees must have an HSA-qualified HDHP to open or contribute to an HSA.
- If an employee no longer has an HSA-qualified HDHP, that employee can no longer contribute to the HSA, but can still spend the already deposited funds as stipulated by law.
- Contributions to HSAs can be made by the employer, the individual, or other individuals (including family members):
  - If made by the individual, it is an “above-the-line” deduction.
  - If made by the employer, it is not taxable to the employee (excluded from income).
  - Can be made by others on behalf of the individual and deducted by the individual.
  - The maximum amount that can be contributed to an HSA is set yearly by the IRS.
- All contributions are aggregated.
- For individuals age 55 and older, additional “catch-up” contributions to an HSA are allowed but limited based on the maximum which is set yearly by the IRS.
- Contributions must stop once an individual is eligible and enrolled in Medicare.
- You will not be able to make the full contribution to your HSA for any year that you drop or lose your HSA-qualified coverage before the end of the year. You will need to pro-rate your contribution for that year.

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Distribution Rules

- Distribution is tax-free if taken for "qualified medical expenses" (listed in future slide).
- Cannot be used to pay for other health insurance premiums except:
  - COBRA coverage.
  - Health plan coverage while receiving unemployment compensation.
- Your HSA funds can be used to pay not only your qualified medical expenses, but also the qualified medical expenses incurred by your spouse and dependents. Your spouse and dependents do not need to be covered by your HSA-qualified plan to use the funds for qualified medical expenses.
- 20% additional tax on distributions if used for non-medical expenses, except when taken after:
  - Individual dies or becomes disabled.
  - Individual is eligible for Medicare.
- HSA custodian must report all distributions
  - Not required to check them for eligibility.

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How does this all work?

High Deductible Health Insurance Plans and Health Savings Accounts work very similar to traditional insurance plans

PRESCRIPTION DRUGS

▶When the pharmacy fills a prescription, be sure to provide them a copy of your health insurance card and they will apply the appropriate discount.

▶Pay for the prescription using your debit card or checks, similar to how you would pay a medical provider above. The amount will be counted towards your deductible by the insurance carrier. If you have met your health insurance deductible for the year, the pharmacy may not register that and charge you for the prescription. However, the insurance company will reimburse you when the prescription is submitted to be applied toward the deductible.

Keep track of all your EOBs and receipts. This is the only proof you have that your expenses were "qualified medical expenses." If your tax return is audited by the IRS, you will need to prove that your medical expenses were "qualified."

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Advantages of HSA's

- **HSA accounts encourage savings for future medical expenses**
  - When employer-sponsored coverage is lost during periods of unemployment
  - Insurance coverage or medical expenses after retirement (before Medicare enrollment)
  - Long-term care expenses
  - Out-of-pocket expenses for Medicare
  - Non-covered services under future coverage
- **Accounts are owned by the individual (not an employer)**
  - Individual decides
    - How much to contribute
    - How much to use for medical expenses
    - Which medical expenses to pay from the account
    - Whether to pay for medical expenses from the account or save the account for the future
    - Which company will hold the account
    - What type of investments to grow account
- **Accounts are completely portable, regardless of:**
  - Whether the individual is employed or not
  - Which employer the individual works for
  - Which state an individual moves to
  - Age or marital status changes
  - Future medical coverage
- **No "use it or lose it rules" like Flexible Spending Arrangements (FSAs)**
  - Unspent balances in accounts remain in the account and can grow through investment earnings
  - Encourages account holders to spend their funds more wisely on their medical care
  - Encourages account holders to shop around for the best value for their health care dollars
- **Accounts can grow through investment earnings**
  - Many different investment options could be pursued
- **HDHP premiums should be less expensive than health insurance with traditional deductibles**

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Disadvantages of HSA's

Employee knowledge and changing habits

Cash flow and money management

- Takes employees a while to build up their accounts
- Employees must learn to manage their money better

Recordkeeping

Fees on Accounts

Changes Every Year

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"Qualified Medical Expenses"

- Acupuncture
- Alcoholism Treatment
- Ambulance
- Annual Physical Examination
- Artificial Limb
- Artificial Teeth
- Bandages
- Birth Control Pills (by prescription)
- Body Scan
- Braille Books and Magazines
- Breast Pumps and Supplies
- Breast Reconstruction Surgery
- Car Special Hand Controls (for disability)
- Certain Capital Expenses (e.g., for the disabled)
- Chiropractors
- Christian Science Practitioners
- COBRA Premiums
- Contact Lenses
- Cosmetic Surgery (if due to trauma or disease)
- Crutches
- Dental Treatment
- Dermatologist
- Diagnostic Devices
- Disabled Dependent Care Expenses
- Drug Addiction Treatment (inpatient)
- Drugs (prescription)
- Eye Exam and Eyeglasses
- Eye Surgery
- Fertility Enhancement
- Founder's Fee
- Guide Dog or other Service Animal
- Gynecologist
- Health Institute (if prescribed by physician)
- H.M.O. (certain expenses)
- Hearing Aids
- Home Care
- Home Improvements
- Hospital Services
- Insurance Premiums
- Intellectually and Developmentally Disabled Home
- Laboratory Fees
- Lactation Expenses
- Lead-Based Paint Removal
- Learning Disability Fees (prescription)
- Legal Fees (if for mental illness)
- Lifetime Care Fees
- Lodging (for out-patient treatment)
- Long-Term Care (medical expenses)
- Long-Term Care Insurance (up to allowable limits)
- Meals (associated with receiving treatments)
- Medical Conferences (for ill spouse/dependent)
- Medical Information Plan
- Medicines
- Menstrual care products, defined as tampons, pads, liners, cups, sponges or other similar products
- Neurologist
- Nursing Home
- Nursing Services
- Obstetrical Expenses
- Ophthalmologist
- Operations
- Optometrist
- Organ Transplant (including donor's expenses)
- Orthodontia Expenses
- Orthopedic Shoes
- Orthopedist
- Osteopath
- Out-of-pocket expenditures and deductibles for your spouse or dependent even if insured under a non-HSA
- Out-of-pocket expenditures while enrolled in Medicare
- Over-the-counter products and medications*
- Oxygen and Equipment
- Physical Examination
- Pregnancy Test Kit
- Premium Tax Credit
- Prenatal Care
- Prescription Medicines
- Prosthesis
- Psychiatric Care
- Psychoanalysis
- Psychologist
- Special Education
- Sterilization
- Smoking Cessation Programs
- Surgery
- Telephones and Television for the Hearing Impaired
- Therapy
- Transplants
- Transportation Expenses for Health Care
- Tuition
- Vaccinations
- Vasectomy
- Vision Correction Surgery
- Vitamins (if prescribed)
- Weight Loss Programs
- Wheelchair
- Wig (hair loss from disease)
- X-Rays

*Over-the-counter product coverage is not all inclusive.

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Frequently Asked Questions

Do my HSA contributions have to be made in equal amounts each month?

- No, you can contribute in a lump sum or in any amounts or frequency you wish. However, your account trustee/custodian (bank, credit union, insurer, etc.) can impose minimum deposit and balance requirements.

Does my contribution depend on when I establish my HSA account or when my HDHP coverage begins?

- Your eligibility to contribute to an HSA is determined by the effective date of your HDHP coverage. Your annual contribution depends on your HDHP coverage. The amount you can contribute is not determined by the date you establish your account. However, medical expenses incurred before the date your HSA is established cannot be reimbursed from the account.

I'm on Medicare, can I have an HSA?

- You are not eligible for an HSA after you have enrolled in Medicare. If you had an HSA before you enrolled in Medicare, you can keep it. However, you cannot continue to make contributions to an HSA after you enroll in Medicare. If you still have an HSA balance after reaching Medicare eligibility age, you can empty the account for any reason without a tax penalty. If you don't use the withdrawal to cover qualified medical expenses, you'll owe federal income tax and possibly state income tax. But the 20% tax penalty that generally applies to withdrawals not used for medical expenses won't apply.

For an employee, spouse and child coverage, does each individual open their own HSA or is there one account for all? If there is one for all on the plan, what happens to the account if the spouses divorce?

- Each spouse can have their own account, and need to if you are making catch up contributions. Either spouse can use their account for any medical expenses for any member of the family, even if they are not covered by the HSA-qualified plan. If the couple divorce, the divorce settlement will decide the fate of the funds.

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What's the difference between the new HSAs and the flexible-spending accounts? It seems they are for the same purpose.

- The tax benefits of both plans are quite similar, but there are several differences. The biggest and most important difference is that your HSA balances can roll over from year to year and continue to grow tax-deferred.
- Money in your flex plan must be spent by the end of the plan year or you lose it. Also, you can open a flexible-spending account only if the plan is offered by your employer, and you do not need to have a high-deductible health insurance policy.
- Legislation passed by Congress December 9, 2006; will let you make a one-time transfer of funds tax free from a flexible-spending account to an HSA. Changes to the law also will allow individuals to make a one-time tax-free direct transfer of funds from an IRA to an HSA (up to the HSA annual contribution limit).

If I set up an HSA through my employer, what happens if I switch jobs?

- You can keep the money in an HSA account even after you leave that job, similar to a retirement account and use it for eligible expenses.

Who decides if expenses incurred are qualified?

- You are solely responsible for determining if expenses are qualified or not and therefore should keep all your receipts in case you need to defend your expenditures during an audit.

Frequently Asked Questions

Can an HSA be used to pay for nonqualified expenses, such as new furniture or a plasma screen TV?

- Yes. However, these would be subject to regular income taxes (plus a 20% tax penalty if you are younger than 65) because they are not considered "qualified medical expenses".

Are dental and vision care qualified medical expenses under a Health Savings Account?

- Yes, as long as these are deductible under the current rules. For example, cosmetic procedures, like cosmetic dentistry, would not be considered qualified medical expenses.

Can I use the money in my HSA to pay for medical care for a family member?

- Yes, you may withdraw funds to pay for the qualified medical expenses of yourself, your spouse or a dependent without tax penalty. This is one of the great advantages of HSAs.

I have an HSA but no longer have HDHP coverage. Can I still use the money that is already in the HSA for medical expenses tax-free?

- Once funds are deposited into the HSA, the account can be used to pay for qualified medical expenses tax-free, even if you no longer have HDHP coverage. The funds in your account roll over automatically each year and remain indefinitely until used. There is no time limit on using the funds.

What happens to the money in my HSA if I lose my HDHP coverage?

- Funds deposited into your HSA remain in your account and automatically roll over from one year to the next. You may continue to use the HSA funds for qualified medical expenses. You are no longer eligible to contribute to an HSA for months that you are not an eligible individual because you are not covered by an HDHP. If you have coverage by a HDHP for less than a year, the annual maximum contribution is reduced; if you made a contribution to your HSA for the year based on a full year's coverage by the HDHP, you will need to withdraw some of the contribution to avoid the tax on excess HSA contributions. If you regain HDHP coverage at a later date, you can begin making contributions to your HSA again.

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Frequently Asked Questions

How do I use my HSA to pay my physician when I'm at the physician's office?

- If you are still covered by your HDHP and have not met your policy deductible, you will be responsible for 100% of the amount agreed to be paid by your insurance policy to the physician. Your physician may ask you to pay for the services provided before you leave the office. If your HSA custodian has provided you with a checkbook or debit card, you can pay your physician directly from the account. If the custodian does not offer these features, you can pay the physician with your own money and reimburse yourself for the expense from the account after your visit.

- If your physician does not ask for payment at the time of service, the physician will probably submit a claim to your insurance company, and the insurance company will apply any discounts based on their contract with the physician. You should then receive an "Explanation of Benefits" from your insurance plan stating how much the negotiated payment amount is, and that you are responsible for 100% of this negotiated amount. If you have not already made any payment to the physician for the services provided, the physician may then send you a bill for payment.

In accordance with IRS requirements, you are advised that any tax advice contained in this communication is not a formal legal opinion any may not be used by any person for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.

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