223 - Health Savings Accounts

What is a Health Savings Account (HSA)?

A Health Savings Account (HSA) is an individually owned tax-exempt trust account that you can put money into to pay for current and future medical expenses. There are certain advantages to depositing money into these accounts, including favorable tax treatment. HSAs were signed into law December 8, 2003. HSAs are part of the Medicare Prescription Drug Improvement and Modernization Act of 2004.

Who can have an HSA?

Any adult can contribute to an HSA if they:

- Have coverage under an HSA "qualified high deductible health plan" (HDHP).
- Have no other first-dollar medical coverage.
  - This includes but is not limited to other non-HDHP coverage, general purpose Health Care Flexible Spending Accounts or Health Reimbursement Arrangements. (Other types of insurance like specific injury insurance or accident, disability, dental care, vision care, or long-term care insurance are permitted).
- Are not enrolled in Medicare or Tricare.
- Cannot be claimed as a dependent on someone else's tax return.

High Deductible Health Plans (HDHPs)

You must have coverage under an HSA qualified HDHP to open and contribute to an HSA. Generally, this is health insurance that does not cover first dollar medical expenses. The HDHP cannot pay any benefits until a person has incurred minimum deductible amounts. Federal law requires the health insurance deductible amounts to be at least:

- $1,400 – Self-only coverage (for calendar year 2022)
- $2,800 – Family coverage (for calendar year 2022)

In addition, annual out-of-pocket expenses under the plan (including deductibles, co-pays and co-insurance) cannot exceed:

- $7,050 – Self-only coverage (for calendar year 2022)
- $14,100 – Family coverage (for calendar year 2022)

The deductible must apply to all medical expenses (including prescriptions) covered by the plan. However, plans can pay for "preventive care" services on a first-dollar basis (with or without a co-pay). "Preventive care" can include routine pre-natal and well-child care, child and adult immunizations, annual physicals, mammograms, etc.

HSA Contributions

Contributions to your HSA can be made by you, your employer or both. The total contributions are limited annually. If you make a contribution, you can deduct the contribution (even if you do not itemize deductions) when completing your federal income tax return. Contributions to the account must stop once you are enrolled in Medicare. However, you can keep the money in your account and use it to pay for medical expenses tax-free.

You can make contributions to your HSA every year that you are eligible. The contributions cannot exceed:

- $3,650 – Self-only coverage (for calendar year 2022)
- $7,300 – Family coverage (for calendar year 2022)

Banks, credit unions, insurance companies and other financial institutions are permitted to be trustees of these accounts.

Catch-Up Contributions

Individuals age 55 and older can also make additional "catch-up" contributions. The maximum annual catch-up contribution is $1,000

Determining the Maximum Contribution

Your eligibility to contribute to an HSA for each month is generally determined by whether you have HDHP coverage on the first day of the month. Your maximum contribution for the year is the greater of: (1) *the full contribution*, or (2) *the prorated amount*. The full contribution is the maximum annual contribution for the type of coverage you have on December 1. The prorated amount is 1/12 of the maximum annual contribution for the type of HDHP coverage you have times the number of months you have that type of coverage. If your contribution is greater than the prorated amount, and you fail to remain covered by a HDHP for the entire following year, the extra contribution above the prorated amount is included as income and subject to an additional 10 percent tax.

Contributions can be made as late as April 15 of the following year.

Qualified HSA Expenses

You can use the money in the account to pay for any "qualified medical expense" permitted under federal tax law. This includes most medical care, dental care and vision care services and also includes certain over-the-counter items. You generally cannot use the money to pay for medical insurance premiums, except under specific circumstances, including:

- Any health plan coverage while receiving federal or state unemployment benefits.
- COBRA continuation coverage after leaving employment with a company that offers health insurance coverage.
- Qualified long-term care insurance.

Qualified HSA Expenses (continued)

- Medicare premiums and out-of-pocket expenses, including deductibles, co-pays and coinsurance, if you are age 65, for;
    - Part A (hospital and inpatient services)
    - Part B (physician and outpatient services)
    - Part C (Medicare HMO and PPO plans)
    - Part D (prescription drugs)

You can use the money in the account tax free to pay for medical expenses for yourself, your spouse, or your dependent children. You can pay for expenses for your spouse and dependent children even if they are not covered by your HDHP. Any amounts used for purposes other than to pay for "qualified medical expenses" are taxable as income and subject to an additional 20% Federal tax penalty (and possible State penalty). Examples include:

- Medical expenses that are not considered "qualified medical expenses" under federal tax law (e.g., cosmetic surgery).
- Other types of health insurance unless specifically described above.
- Medicare supplement insurance premiums.
- Expenses that are not medical or health-related (e.g., vacations, clothes, computers).

After you turn age 65, the 20% additional tax penalty no longer applies. If you become disabled and/or enroll in Medicare, the account can be used for other purposes without paying the additional 20% penalty.

Advantages of HSAs

Security – Your HDHP coverage and HSA protect you against high or unexpected medical bills.

Affordability – Premiums for HDHP coverage are generally more affordable than premiums for traditional health coverage.

Flexibility – You can use the funds in your account to pay for current medical expenses, including expenses that your insurance may not cover, or save the money in your account for future needs, such as:

- Health insurance or medical expenses if unemployed
- Medical expenses after retirement (before Medicare)
- Out-of-pocket expenses when covered by Medicare
- Long-term care expenses and insurance

Savings – You can save the money in your account for future medical expenses and grow your account through investment earnings.

Advantages of HSAs (continued)

Control – You make all the decisions about:

- How much money to put into the account
- Whether to save the account for future expenses or pay current medical expenses
- Which medical expenses to pay from the account
- Whether to invest any of the money in the account and where
- Which investments to make

Portability – Accounts are completely portable, meaning employees can keep their HSA even if they:

- Change jobs
- Change medical coverage
- Become unemployed
- Move to another state
- Change their marital status

Ownership – Funds remain in the account from year to year, just like an IRA. There are no "use or lose" rules for HSAs.

Tax Savings – An HSA provides you triple tax savings:

1. Tax deductions when you contribute to your account or pre-tax deductions via payroll
2. Tax-free earnings
3. Tax-free withdrawals for qualified medical expenses

Additional Information

The Internal Revenue Service has a web site with additional information about Health Savings Accounts, including answers to frequently asked questions, related IRS forms and publications, technical guidance, and links to other helpful web sites. The website is www.irs.gov.

[1]Investments in mutual funds, through HSA investment accounts are: Not FDIC-Insured · May Lose Value · No Bank Guarantee.

[2]All mention of taxes is made in reference to federal tax law. States can choose to follow the federal tax-treatment guidelines for HSAs or establish their own; some states tax HSA contributions. Please check with each state's tax laws to determine the tax treatment of HSA contributions, or consult your tax adviser.
Withdrawals for non-qualified expenses are subject to income taxes and a possible additional 20% penalty, if you're under age 65. This document is not intended as tax or legal advice.