HSA BENEFITS

insights

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HSAs: Health Savings Accounts

Health savings accounts (HSAs) are a growing trend in health care. An HSA is a tax-exempt savings account established for the purpose of paying for the qualified medical expenses of an individual and/or his or her spouse and tax dependents. HSAs are designed to provide eligible individuals with triple federal tax benefits: (1) HSA contributions are tax-free, (2) interest and other earnings on HSA contributions accumulate tax-free, and (3) amounts distributed from an HSA for qualified medical expenses are tax-free as well.

In addition to tax benefits, HSA plans have grown in popularity because they offer potential health care cost savings to both employers and employees. For example, individuals covered under an HSA are more likely to seek preventive care, choose generic drugs, not misuse the emergency room and use online tools to research health care and providers.

HSAs are offered in combination with high deductible health plans (HDHPs). To be HSA-eligible, an individual must be covered under a qualified HDHP and not also covered by another health plan that is not an HDHP (with a few exceptions, including disability, dental care, vision care and long-term care insurance). HDHPs generally have lower monthly premiums and higher deductibles than traditional health plans. HSAs can cover medical expenses until the HDHP deductible is reached. The idea of this design is that the HSA pays for routine, smaller health expenses, while the HDHP offers protection in the event of a catastrophic medical expense, such as an unexpected illness, injury or hospitalization.

Because HSA amounts are non-forfeitable, amounts contributed to an HSA can increase savings for future health care needs, even into retirement.

In general, money placed into an HSA can be withdrawn at any time. Any HSA withdrawal used for a purpose other than to pay for qualified medical expenses is taxable as income and subject to an additional 20 percent penalty. After an individual reaches age 65, the additional penalty tax does not apply to HSA withdrawals.

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Additional HSA basics are as follows:

- HSAs are controlled and owned by the individual or employee. HSA owners are responsible for annually reporting HSA contributions and distributions to the Internal Revenue Service (IRS) as an attachment to their IRS Form 1040 (U.S. Individual Income Tax Return).
- HSA contributions are non-taxable, and can be made by the HSA owner, an employer, a family member or any other person for months during which the owner is HSA-eligible.
- Annual limits apply to HSA contributions. The amount of the annual limit is federally mandated, and depends on whether the HSA owner has individual or family HDHP coverage.
- HSA funds, including interest and earnings, accumulate tax-free from year to year. HSAs are not subject to the “use it or lose it” rule applicable to health flexible spending accounts (FSAs). HSAs are portable, meaning individuals keep their HSAs even if they change jobs, change medical coverage or make other life changes.
- Even if an HSA owner is no longer HSA-eligible (for example, because the owner is no longer covered under an HDHP), he or she can still use accumulated HSA funds to pay for qualified medical expenses on a tax-free basis.
- HSAs are an inheritable asset. If a surviving spouse is the beneficiary, the spouse becomes the owner of the account and can use it as if it were his or her own HSA. For other beneficiaries, the account will no longer be treated as an HSA, and will

pass to a beneficiary or become part of the deceased individual's estate.

- HSAs can help individuals become better health care consumers by giving them more of a stake in controlling their health care costs. Since they are responsible for more out-of-pocket costs due to the higher deductible, many employees become more conscious of the health care dollars they are spending.
- HSAs are not for everyone. The decision of whether to choose HSA/HDHP coverage is different for each individual, and may depend on the predictability of health care costs. If an individual is generally healthy and/or has a reasonable idea of health care costs, then HSA/HDHP coverage may make more financial sense than traditional health plan coverage.

HSA Annual Limits (2015/2016)

<u>Single Coverage</u>
HDHP minimum deductible:
$1,300/$1,300

HDHP maximum out-of-pocket:
$6,450/$6,550

HSA maximum contribution:
$3,350/$3,350

<u>Family Coverage</u>
HDHP minimum deductible:
$2,600/$2,600*

HDHP maximum out-of-pocket:
$12,900/$13,100

HSA maximum contribution:
$6,650/$6,750

* For family plans that have deductibles both for the family as a whole and for individual members: If either the family deductible or the deductible for an individual member is less than the minimum required deductible, then the plan is not an HDHP.

Example: A family plan has a family annual deductible of $3,500 and an individual deductible of $1,500 per family member. This plan is not a qualified HDHP.

<u>Catch-Up Contributions</u>
Individuals who are 55 years old and older are allowed to contribute an extra $1,000 per year to their HSA, to help them save for retirement.