Benefits Insights

Provided by:
Brady, Chapman, Holland & Associates

Health Savings Accounts

In an effort to respond to the rising costs of health care, many employers are offering tax-favored accounts, such as health flexible spending accounts (health FSAs), health reimbursement arrangements (HRAs) and health savings accounts (HSAs).

WHAT IS A HEALTH SAVINGS ACCOUNT?

An HSA is a tax-exempt trust or custodial account established for the purpose of paying qualified medical expenses. An HSA accompanies a high deductible health plan (HDHP).

HSAs can be a powerful tax savings tool. In general, HSA contributions made by an eligible individual are tax-deductible, and employer HSA contributions made on behalf of an eligible employee are excluded from the employee's gross income. Interest and other earnings on HSA contributions accumulate tax-free. Amounts distributed from an HSA for qualified medical expenses are generally tax-free as well.

Keep in mind that some states define income differently than the IRS. As a result, HSAs that are tax-exempt at the federal level may not be tax-exempt at the state level.

WHO CAN ESTABLISH AN HSA?

An individual may contribute to an HSA in any month in which he or she is covered under an HDHP on the first day of the month. The individual cannot be covered by another health plan that is not an HDHP (with certain exceptions), and he or she cannot be entitled to Medicare benefits or be claimed on another person's tax return. Self-employed individuals are eligible to establish an HSA.

WHAT EXPENSES ARE ELIGIBLE FOR TAX-FREE REIMBURSEMENT FROM AN HSA?

An HSA may reimburse qualified medical expenses incurred by the account beneficiary and his or her spouse and dependents. In addition to qualified medical expenses, COBRA premiums and qualified long-term care (QLTC) premiums may be reimbursed from an HSA. A full list of qualified medical expenses can be found here.

WHAT EXPENSES ARE NOT ELIGIBLE FOR TAX-FREE REIMBURSEMENT FROM AN HSA?

The following expenses may not be reimbursed from an HSA: Establish a high standard for product quality control at your organization.

- Premiums for Medicare supplemental policies;
- Expenses covered by another insurance plan;
- Expenses incurred prior to the date the HSA was established; or
- Any expenses other than qualified medical expenses and the HSA reimbursable premiums described above.

The amount withdrawn from an HSA for a non-qualifying medical expense is added to the account beneficiary's income and subject to a 20% penalty. If funds are distributed as a result of the account beneficiary's death, disability or after he or she becomes eligible for Medicare, the 20% penalty does not apply.

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HOW MUCH CAN AN INDIVIDUAL CONTRIBUTE TO AN HSA?

In 2024, eligible individuals may contribute up to $4,150 for single coverage and $8,300 for family coverage. In 2025, it increases to $4,300 for individual coverage and $8,550 for family coverage. Individuals who are age 55 or older by the end of the tax year are permitted to make “catch-up contributions” and can contribute up to an additional $1,000 annually.

HSA contributions do not have to be made in equal amounts each month. An eligible individual can contribute in a lump sum or in any amounts or frequency he or she wishes.

Also, the HSA contribution limit is reduced by any contributions made to a medical savings account (MSA) in the same year. Rollover contributions from another HSA or MSA can be accepted. These rollover contributions are not subject to the annual contribution limit.

WHAT ARE THE DIFFERENCES BETWEEN HSAS, HRAS, FSAS AND MSAS?

The chart below provides a comparison among these tax-favored accounts.

WHERE CAN I FIND MORE INFORMATION ON HSAS?

To find more information about HSAs, visit: [www.irs.gov/publications/p969/ar02.html.](www.irs.gov/publications/p969/ar02.html)

HSAs may not be right for all employers or individuals. Please contact Brady, Chapman, Holland & Associates for assistance in determining what tax-advantaged account will best meet your goals.

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Comparison of Tax-advantaged Accounts

	HSA	HRA	FSA
Type of account	Health Savings Account	Health Reimbursement Arrangement*	Health Flexible Spending Account
Who owns the account?	Individual/employee	Employer	Employer
Who may fund the account?	Anyone can make contributions to an individual's HSA, including employer and/or employee.	Employer	Employer and/or employee
What plans must be offered with the account?	A high deductible health plan (HDHP) that satisfies minimum annual deductible and maximum annual out-of-pocket expense requirements.	An employer must offer a health plan and the HRA must be considered integrated with group health plan coverage. Stand-alone HRAs are not permitted unless they are limited to excepted benefits or fall under an exemption to the ACA.	Most Health FSAs must qualify as excepted benefits to satisfy ACA reforms. To qualify as an excepted benefit, the FSA must meet a maximum benefit requirement and other group health plan coverage must be offered by the employer.
Is there an annual contribution limit?	$3,850 Ind. $7,750 Family (2023) $4,150 Ind. $8,300 Family (2024) Catch-up contributions $1,000/year– age 55 by end of tax year	No, there is no IRS prescribed limit	For plan years beginning in 2023, employees may not elect to contribute more than $3,050. For 2024, the limit is $3,200.
Can unused funds be rolled over from year to year?	Yes	Yes	No, with two exceptions. A health FSA may include a grace period of 2-1/2 months after end of plan year or it may allow employees to carry over up to $640 (as adjusted for inflation) in unused funds into the next plan year.
What expenses are eligible for reimbursement?	Section 213(d) medical expenses, including: • COBRA premiums • QLTC premiums • Health premiums while receiving unemployment benefits • If Medicare eligible due to age, health insurance premiums except medical supplement policies	Section 213(d) medical expenses Effective for 2014 plan years, cannot reimburse health insurance premiums for individual coverage Employer can define "eligible medical expenses"	Section 213(d) medical expenses Expenses for insurance premiums are not reimbursable Employer can define "eligible medical expenses"
Must claims be substantiated?	No	Yes	Yes
May the account reimburse non-medical expenses?	Yes, but taxed as income and 20% penalty (no penalty if distributed after death, disability, or age 65)	No	No
Does the uniform coverage rule apply?	No	No	Yes

*For purposes of this comparison chart, an HRA refers to a traditional HRA that is properly integrated with a group health plan. It does not include retiree-only HRAs, qualified small employer HRAs, individual coverage HRAs or excepted benefit HRAs.