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Health Savings Accounts
and
High Deductible Health Plans

by
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I. WHAT IS A HEALTH SAVINGS ACCOUNT ("HSA")?

A. A tax favored savings vehicle (similar to an IRA) used to fund the payment of medical expenses.

B. They are available to individuals who are covered by a high deductible health plan ("HDHP").

C. Contributions are tax deductible, or not includible in income.

D. Earnings are tax free.

E. Distributions are tax free if used for qualifying medical expenses.

F. Unlike a cafeteria plan, there is no "use it or lose it" requirement.

II. MUST BE COVERED BY A HIGH DEDUCTIBLE HEALTH PLAN ("HDHP")

A. What is an HDHP?

1. Health plan that has $1,100 minimum deductible for self-only coverage and $2,200 minimum deductible for family coverage.

a. These minimums are indexed for cost of living, and are subject to change each calendar year.

b. The numbers above are for 2007.

2. The health plan must limit annual out-of-pocket costs to $5,250 for self-only coverage and $10,500 for family coverage.

a. These maximums are indexed for cost of living just like the minimum deductibles above.

b. The numbers above are for 2007.

3. The maximums do not apply to deductibles and expenses for out-of-network services.

B. Exceptions to Minimum Deductibles.

1. Plan may pay "first dollar" expenses for preventative health care.

2. An HDHP may provide preventive care benefits without a deductible or with a deductible below the minimum annual deductible.

3. Preventative care includes, but is not limited to, the following:

a. Periodic health evaluations, including tests and diagnostic procedures ordered in connection with routine examinations, such as annual physicals.

b. Routine prenatal and well-child care.

c. Child and adult immunizations.

d. Tobacco cessation programs.

e. Obesity weight-loss programs.

f. Screening services. This includes screening services for the following:

i. Cancer.

ii. Heart and vascular diseases.

iii. Infectious diseases.

iv. Mental health conditions.

v. Substance abuse.

vi. Metabolic, nutritional and endocrine conditions.

vii. Musculoskeletal disorders.

viii. Obstetric and gynecological conditions.

ix. Pediatric conditions.

x. Vision and hearing disorders.

4. Participant may be covered by other “permitted insurance” in addition to the HDHP.

   a. Worker’s compensation.

   b. Casualty insurance.

   c. Disability insurance.

   d. Vision and dental insurance.

   e. Specified disease insurance (e.g., cancer insurance).

   f. Per diem hospitalization coverage.

C. Medical reimbursement plans and cafeteria plans.

1. They <u>are</u> “other insurance,” so beware of having them with an HDHP.

2. Must carefully coordinate a medical reimbursement plan and cafeteria plan so that you do not violate the “first dollar” rules.

III. <u>WHO IS AN “ELIGIBLE INDIVIDUAL” FOR AN HSA?</u>

A. Must be covered by an HDHP.

1. The determination is made monthly on the first day of the month.

B. Must not have other coverage except permitted insurance.

1. That includes coverage from a spouse’s plan.

2. Cannot be enrolled in Medicare.

3. Cannot be claimed as a dependent by another.

IV. <u>WHAT CAN BE CONTRIBUTED TO HSA IF ELIGIBLE?</u>

A. The determination is made monthly.

B. For self-only coverage, the limit is $1/12^{th}$ of the <u>lesser</u> of:

1. The HDHP deductible, or

2. $2,850

   a. The amount is indexed for cost of living.

b. The number above is for 2007.

C. For family coverage, the limit is 1/12th of the lesser of:

1. The HDHP deductible, or

2. $5,650

a. The amount is indexed for cost of living.

b. The number above is for 2007.

D. Need not be an "eligible individual" when the contribution is made.

1. Actual contributions can be made up to due date of return, without extension (April 15).

2. Can make for eligible months, even after no longer eligible for an HDHP.

3. Can make up front, but take a refund (including earnings) if cease to be eligible.

E. Catch-up contributions if age 55 or older.

1. $800 additional contribution for 2007.

2. Increases $100 a year through 2009.

V. WHO MAY CONTRIBUTE?

A. The HSA owner.

1. The account owner can contribute and take an adjustment to income deduction.

a. See Form 1040 - Line 25.

b. See also IRS Form 8889.

2. Other persons may contribute, but it is deductible by the HSA owner.

3. The account owner can make contributions through a salary reduction, Section 125 cafeteria plan.

B. The employer.

1. The amount is deductible by employer.

2. Treated as an employee fringe benefit, not compensation.

3. Not subject to FICA.

4. Employer must make "comparable contributions" to comparable participant employees.

   a. Must contribute same amount or same percentage of annual deductible limit.

   b. Must be comparable <u>within each category</u> of participating employees:

      i. Full-time (30+ hours) self-only.

      ii. Full-time family.

      iii. Part-time (under 30 hours) self-only.

      iv. Part-time family only.

   c. You can have differing amounts between the categories, and can limit contribution to employer sponsored HDHPs.

   d. Comparability rules do <u>not</u> apply to cafeteria plan contributions.

   e. 35% excise tax on employer for failure to make comparable contributions. Can cure with additional contributions.

   f. Nothing in tax law or ERISA mandates who is covered by HDHP.

5. Employer reports its deductible contribution in Box 12 of Form W-2 using Code "W."