

Health Savings Account (HSA) FAQs with 2022 and 2021 limits

What is an HSA?

An HSA is a tax-exempt trust or custodial account, like an Individual Retirement Account (IRA), established to pay qualified medical expenses in conjunction with a High-Deductible Health Plan.

What is a High-Deductible Health Plan (HDHP)?

An HDHP is a health plan that for 2022 or 2021:

- Has an annual deductible of at least \$1,400 and annual out-of-pocket expenses (including the deductible) of not more than \$7,050 or \$7,000, respectively for *individual* coverage, or
- Has an annual deductible of at least \$2,800 and annual out-of-pocket expenses (including the deductible) of not more than \$14,100 or \$14,000, respectively for *family* coverage.

An HDHP can be a self-insured medical reimbursement plan sponsored by an employer.

In addition to the HDHP, you can be insured for accidents, disability, dental, vision, long-term care and insurance that pays a fixed amount per day of hospitalization. You can be covered under an Employee Assistance Program provided the plan does not provide significant benefits in medical care or treatment. You **cannot** be covered by another **low**-deductible health plan (i.e., spouse's plan).

HDHPs must apply costs of prescription drugs (that are not preventive drugs) to the annual deductible or the individual **may not** contribute to an HSA.

Eligibility

An "eligible individual" can establish an HSA. An "eligible individual" means, with respect to any month, an individual who:

- Is covered by an HDHP on the first day of such month,
- Is **not** covered by any other health plan that is **not** an HDHP,
- Is **not** enrolled for benefits under Medicare, and
- May not be claimed as a dependent on another individual's tax return.

Eligibility to contribute to an HSA does **not** depend upon your income (no limits) or the amount of earned income (i.e., you don't have to be working).

An uninsured individual is not eligible to contribute to an HSA. An individual with dual coverage (i.e., spouse's plan) may not contribute unless the spouse's plan is also an HDHP.

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. If you are not covered on December 1, your contribution depends on the number of months of HDHP coverage you have during the year (i.e., the months when you have HDHP coverage on the first day of the month).

If you are covered on December 1, you are treated as an eligible individual for the entire year.

However, if you cease to be an eligible individual, the excess over the prorated contribution is included in income and subject to a 10% additional tax. 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.

What first-dollar medical benefits make someone ineligible for an HSA?

Medicare, Medicaid, Tricare (no HDHP available), “General Purpose” Flexible Spending Accounts (GPFSA) and “General Purpose” Health Reimbursement Arrangements (GPHRA) make someone ineligible. “General purpose” means reimbursement for any qualified medical expense.

Coverage under a spouse’s plan that includes low-deductible insurance coverage or GPFSA/GPHRA through the spouse’s employer also makes someone ineligible.

What FSA and HRA plans are permitted?

Permitted plans are “limited purpose” FSAs and “limited purpose” HRAs that restrict reimbursement to certain permitted benefits, such as vision, dental or preventive care benefits.

Also permitted are “post-deductible” FSAs or HRAs that provide reimbursement only after the minimum deductible has been satisfied under the HDHP.

Establishing an HSA

Any eligible individual may establish an HSA with a qualified HSA trustee or custodian (e.g., insurance company or bank) with no permission or authorization from the IRS and with or without the involvement of an employer. The HSA trustee or custodian does not need to be the same institution as the insurer for the HDHP.

The HSA trustee must report contributions and year-end account value on Form 5498-SA and distributions on Form 1099-SA.

The account is set up in the name of one individual. An HSA **cannot** be set up in the name of two individuals (joint account), but medical expenses of the spouse and dependents can still be reimbursed from the account.

Contributions to an HSA

Any individual may contribute to an HSA:

- For an HSA established by an employee, the employee, the employee’s employer or both may contribute to the HSA of the employee in any given year.

- For an HSA established by a self-employed (or unemployed) individual, the individual may contribute to the HSA.
- Family members may also contribute to an HSA on behalf of another family member as long as that family member is an eligible individual (the eligible individual gets the tax deduction).
- Contributions must be made in cash, not stock or other property.
- The employer can match employee contributions, as long as the match is nondiscriminatory.

How much can be contributed to an HSA?

For 2022 or 2021:

- For individuals with **self-only** coverage under an HDHP, the maximum contribution is \$3,650 or \$3,600, respectively.
- For eligible individuals with **family** coverage under an HDHP, the maximum contribution is \$7,300 or \$7,200, respectively.
- Catch-up contributions can also be made to an HSA if the individual is age 55 or older. (For 2022 and 2021, the catch-up contribution is \$1,000.) If each spouse is age 55 or older, **each** spouse must have an individual HSA account if both want to make “catch-up” contributions.
- Rollovers from MSAs, HSAs and IRAs (once in lifetime) are permitted.
- Tax filing status does not affect your contribution.
- If you had HDHP coverage for the full year, you may make the full catch-up contribution regardless of when your 55th birthday falls during the year. If you did not have HDHP coverage for the full year, you must prorate your “catch-up” contribution for the number of full months you were “eligible” (i.e., had HDHP coverage). However, if you are covered on December 1, you are treated as an eligible individual for the entire year and get the full contribution.
- If spouses have separate HDHP coverage and one has family coverage, they are both treated as having family coverage. If spouses have separate HDHP self-only coverage, they are treated totally separate for contribution deduction purposes.
- Your HSA contributions can be made in a lump sum or in any amounts or frequency you wish. For eligible individuals in a cafeteria plan, it is most

advantageous to contribute via cafeteria plan because of FICA payroll savings.

If an individual enters the plan midyear (does not have 12 months of HDHP coverage), the individual may still contribute the maximum annual amount, provided that the individual maintains HDHP coverage for the entire plan year following the year in which HDHP coverage began and that HDHP coverage begins on or before December 1.

If coverage is not maintained for the following plan year, an excess contribution for the partial year will result in adverse tax consequences if the maximum HSA contribution was made. To determine the allowable contribution (if HDHP coverage is not maintained for the following plan year), the individual must determine the contribution limit by pro rating the IRS statutory maximum for the number of months covered by the HDHP as of the first of the month.

Tax treatment of an HSA contribution: Employee contributions

Triple-tier tax benefits:

- Contributions to the HSA through a cafeteria plan (Section 125) are “pretax” and not subject to federal or state income tax (most states) or employment taxes (FICA, FUTA, SUTA).
- Earnings inside the HSA are not included in the eligible individual’s income.
- Distributions are not included in the eligible individual’s income if the distribution is for “qualified medical expenses” of the account beneficiary, spouse or dependent.

Employee contributions made outside a cafeteria plan qualify for a deduction in determining adjusted gross income (above-the-line deduction), regardless of whether the individual itemizes deductions. There is no FICA deduction, however.

Elections to make contributions through a cafeteria plan can change on a month-by-month basis (unlike salary reduction contributions to an FSA).

Account holders must file Form 8889 and report on Form 1040 the amount of contributions to the HSA and distributions from the HSA.

Tax treatment of an HSA account

Excess contributions to an HSA are subject to a 6% excise tax for **each** taxable year if the excess, plus earnings, is not distributed to the account owner by the due date of the tax return, including extensions.

There is no time limit to reimburse expenses from an HSA. Distributions can be taken to reimburse prior-year expenses as long as the expenses were incurred on or after the date the HSA was established.

Distributions made for non-medical reasons prior to death, disability or attainment of age 65 are subject to ordinary income taxes on the eligible individual’s tax return. A 20% penalty tax also applies unless one of the exceptions to the 20% additional tax applies (e.g., death, disability or attainment of age 65).

Two states — California and New Jersey — do not conform to federal regulation and do not recognize HSAs for deduction purposes.

Tax treatment of an HSA contribution: Employer contributions

For an employer of an eligible individual, HSA contributions are deductible by the employer as employer-provided coverage for medical expenses and excluded from employees’ income.

Employer contributions outside a cafeteria plan to an HSA must be “comparable” for all eligible employees, which means either the same dollar amount or the same percentage of each employee’s annual deductible. You may apply the rule separately to the same category of coverage (single vs. family) and part-time vs. full-time employees. There is a 35% excise tax for failure to meet the comparability rule if the cafeteria plan exception does not apply.

Employer contributions made through a cafeteria plan to an HSA are not subject to the comparability rules but are subject to the discrimination rules.

There are special rules for employer contributions to self-employed individuals, partners and S-corporation shareholders. The reporting rules on the Form W-2 are complex. Consult IRS Notice 2005-8, which addresses the tax ramifications of an employer contribution.

What are “qualified medical expenses”?

Qualified medical expenses are expenses paid for the account beneficiary, spouse or dependents for medical care as defined in IRS Code Section 213(d), including over-the-counter (OTC) drugs without a prescription or doctor’s note, but only to the extent the expenses are not covered by insurance or otherwise. The FDA defines OTC medications as a drug product marketed for use by a consumer without the need of a supervising healthcare professional to obtain the drug. Also, menstrual care products – including tampons, pads, liners, cups, sponges or other similar items used – constitute medical care.

The medical expenses must be incurred on or after the HSA has been established.

Expenses paid by an HSA cannot also be taken as itemized deductions or reimbursed by another source (no “double dipping”).

Generally, health insurance premiums are not qualified medical expenses.

However, an HSA can pay for long-term care insurance, COBRA healthcare continuation coverage and healthcare coverage while an individual is receiving unemployment compensation. In addition, for individuals over 65, premiums for Medicare Part B or D, other than Medicare supplemental policies, can be paid from the HSA.

Premiums for the employee’s share for employer-sponsored retiree health insurance may be reimbursed by the HSA provided the retiree is at least age 65. Insurance premiums paid prior to age 65, other than for COBRA or USERRA or while employed, cannot be reimbursed by the HSA.

Who determines whether the distributions from the HSA are for “qualified medical expenses”?

The eligible individual HSA account owner – not the trustee, custodian or employer – makes the

determination of whether the expense is a “qualified medical expense.” Thus, it is important to maintain sufficient records to substantiate the claim in the event of an IRS audit, which may challenge the HSA owner’s determination.

What are the tax consequences after the death of the HSA account owner?

If the HSA passes to a surviving spouse, the account becomes the HSA of the surviving spouse and remains tax-exempt provided it is exclusively used to pay qualified medical expenses.

If the account passes to a person other than a surviving spouse, the HSA ceases to be an HSA as of the date of death. The fair market value of the account, reduced by payment of any decedent qualified medical expenses within one year after death, is included in the beneficiary’s income in the year of the death of the account owner.

Miscellaneous

- An HSA and an HDHP can be offered to employees on a salary-reduction basis through an employer-sponsored cafeteria plan.
- An HSA is not subject to COBRA continuation coverage.
- HSAs are not subject to the “use it or lose it” rules.
- An HSA is **not** a welfare benefit plan of an employer subject to ERISA.
- Debit, credit and stored-value cards may be used by eligible individuals for distributions from an HSA for qualified medical expenses.
- Mistaken distributions from an HSA can be repaid without penalty or taxes.
- Account fees paid from an HSA account are nontaxable distributions.

Learn more

Contact Wipfli’s employee benefit services team at HCM@wipfli.com.