Benefits Corner

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Health Savings Account Update

Health Savings Accounts and the associated qualified High Deductible Health Plans have been around for two full years now. Over 3 million Americans are covered by this type of program, and the numbers are projected to reach almost 10 million by 2010. Almost every day, I receive a question from someone about Health Savings Account (HSA) programs. It could be from an employer or from an individual, but there is still quite a bit of curiosity and considerable confusion about this type of plan.

The federal government passed into law the provisions that enable Health Savings Account plans in December of 2003. The Tax Relief and Health Care Act of 2006 has made contributing to an HSA even easier. The big idea that led to the passage of this legislation is that if people are responsible for more of their cost of health care, maybe some market forces and competition will enter into the purchase of health care services. The hope is that this awareness and competition might dampen the ever increasing cost of health care and health insurance. As with any federal government enabled plan, there are several rules and regulations that need to be complied with before you will be able to confidently open your HSA account.

The first requirement is that you must have a health insurance plan that passes the test as a “Qualified High Deductible Health Plan” or HDHP. The basic requirements are that an individual deductible must be at least $1,100, or if you have family coverage, the annual deductible must be at least $2,200. The most common individual deductibles range from $2,000 to $2,850, while the most common family deductibles range from $4,000 to $5,600. Most plans will pay 100 percent of covered in-network expenses after the deductible has been met.

The two biggest things that you will have to give up to have a qualified HDHP are the convenience features that may be the things you like most about your current plan—the office visit copay and the prescription drug copay. These items would still be covered under a qualified HDHP but would go toward your deductible. Further, most plans have a preferred provider list that would allow you to pay a discounted rate for all in-network services. Please note that under most HSA qualified plans, preventive care visits are not subject to the deductible! There are other plan design features that must be included in a qualified High Deductible Plan, but perhaps the best way to make sure that your health insurance plan is qualified is to ask your agent or your insurance company. Almost every health insurance company has set up plans specifically for use in conjunction with an HSA due to the popularity of this type of plan.

Another common question is, “Can I save on my premium by moving to an HSA qualified plan?” The answer is usually yes! By giving up the copay features in the plan design, there are usually good cost savings to be found. Oftentimes, the savings range from a low of 10 percent to a high of 50 percent over your current health insurance premiums. The biggest factor in getting any cost savings is the type of coverage you currently have.

So at this point, you have implemented and/or determined that your health insurance plan is qualified. Now, it is time to look at setting up the Health Savings Account. The first step will be finding a financial institution that can open this type of account for you. The HSA is a special type of account, similar to an IRA, and the financial institution must be willing to act as a trustee or custodian for it. Many of the health insurance companies offering the health coverage have partnered with banks and other entities to facilitate this. Another option would be to find a trustee/custodian independent of the carrier’s chosen option. Many people have chosen to use their current bank for their HSA for the convenience of transferring funds.

The HSA can be funded as you need to, or you can even set up automatic deposits from your checking account or payroll. The HSA can be funded by the individual who owns the account, by your employer, or from both sources. Please note that there is a prohibition on the employer funding the HSA directly for the owners of S-Corps, LLCs, and partners in a partnership. Once the HSA has been funded, the individual owns the account—there is no vesting schedule if your employer has made a contribution. The money going into the account is considered a tax-deductible expense, and it can earn interest or gains on a tax-free basis.

Recently passed federal legislation has made the contribution rules for HSAs easier and better than before. Individuals and families may now contribute the maximum amount allowed by the IRS regardless of the HDHP deductible: $2,850 for individuals and $5,650 for families in 2007. Account holders starting their HSA mid-year can now contribute up to the full annual limit. Previously, the contribution amounts were prorated based on the HDHP start date. IRA and unused dollars in a Flexible Spending Account may even be used, on a limited basis, to fund an HSA. There are other changes as well, but these seem to be the most important for most people.

Money in your HSA can be taken out to pay for “qualified medical expenses” on a tax-free basis. Items that are considered qualified include medical expenses covered under your health plan but subject to the deductible. Other items include dental expenses, chiropractic services, vision services, and many more. For a complete list of qualified medical expenses, you can refer to IRS publication 502 titled, “Medical and Dental Expenses,” Catalog Number 15002Q. The publication is available at the IRS Web site: www.irs.gov.

If you don’t use all of your contribution to HSA in a given year, that money stays in the account and is available for use in subsequent years. An HSA does not have a “use it or lose it” provision. The money can even be used as an additional source of retirement income, very similar to a traditional IRA, once you hit normal retirement age. If you withdraw funds prior to retirement for non-qualified expenses, you will be subject to additional taxes and penalties.

So what’s the downside to an HSA plan? For most people, there are very few. An HSA qualified plan allows you to save on your monthly premium expense and to save money for use with qualified medical expenses. However, if you know that you have ongoing medical expenses, a thorough cost versus benefit comparison needs to be completed. It may turn out that your current plan with office visit copays and prescription copays may work best for you. This can be the case if you are taking maintenance prescriptions or if your family is blessed with small children that tend to go to the doctor more frequently.

Hopefully, this has given you some useful information regarding HSAs. If you would like to discuss the feasibility of this type of program for you or your business, I would love to hear from you!

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