



More Guidance Issued on HSAs

Health Savings Accounts have been getting accolades from many quarters lately. Enacted in December 2003 as part of Medicare reform legislation, HSAs have been drawing special praise from Treasury Secretary John W. Snow.

“Health Savings Accounts... are a product that is designed to help individuals take more control over how their healthcare dollars are spent and save for future medical and retiree health expenses on a tax-free basis,” stated Treasury Secretary Snow at an HSA conference in March 2004. Snow continued with “... HSAs are a terrific option that I think every American ought to consider.”

To ensure Americans understand the advantages of HSAs, more guidance on HSAs was issued on July 29, 2004. It came in the form of 88 questions and answers that range from lifetime limits on benefits to HSAs set up in Puerto Rico, American Samoa, Guam, and the U.S. Virgin Islands.

This article hits the highlights of this newest quest for HSA insight. Click here to read the entire IRS Administrative, Procedural, and Miscellaneous Notice 2004-50.

Eligible Health Plan

- “Permitted insurance” includes insurance coverage for specified diseases or illnesses, such as cancer, diabetes, asthma, or congestive heart failure, and generally must be provided under insurance contracts.
- Discount cards or prices for healthcare services or products and coverage under an Employee Assistance Program (EAP) are “permitted insurance” coverage.
- Eligible health plans can include a state high-risk health insurance plan and can impose a reasonable lifetime limit on benefits. Out-of-pocket maximums apply only to covered benefits.
- Payments for expenses that have exhausted the lifetime limit, are in excess of “usual, customary, and reasonable,” or impose a penalty for failure to obtain pre-certification, would not be counted toward the out-of-pocket maximum.
- Cumulative embedded deductibles would be counted toward the out-of-pocket maximum.
- Health plan deductibles may be credited from one policy to another policy during a calendar year.
- Any treatment or drug that is incidental or ancillary to a preventive care service or screening falls within the safe harbor for preventive care. Drugs include those taken to prevent the reoccurrence of a disease from which the person has recovered, including drugs for obesity weight loss and tobacco cessation programs.
- An eligible high-deductible health plan (HDHP) must satisfy the deductible and out-of-pocket limits on the first day of the HDHP plan year.

Eligible Individual

- Eligibility for a low-deductible health plan or for Medicare does not make an individual ineligible to contribute to an HSA.
- An otherwise HSA-eligible individual who participates in TRICARE (the healthcare program for active duty and retired members of the uniformed services, their families, and survivors) cannot contribute to an HSA.
- Eligibility to contribute to an HSA starts on the first day of the month the employee is covered by the HDHP.

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- Bona fide residents of the U.S. Virgin Islands, Guam, and the Commonwealth of the Northern Mariana Islands may establish HSAs.

Contributions

- An employer, a family member, state government, or any other person may make contributions to an eligible person's HSA.
- The maximum annual election includes the embedded individual deductible for family coverage.
- The comparability rules for HSAs do not apply to employer contributions made through a Section 125 cafeteria plan. This includes employer "matching" contributions and wellness incentives offered through a cafeteria plan.
- Comparability may be calculated on a month-to-month basis for part-time employees, but not on the age of employees.
- Employers do not have to "pre-fund" HSAs.
- Account beneficiaries may start or stop their contributions to their HSA through a cafeteria plan at any time as long as the change is effective prospectively, including a mid-year election if the HSA is offered as a new benefit.
- Employers may provide negative elections for an HSA if offered through a cafeteria plan.
- Trustees or custodians need not determine HSA eligibility of each account beneficiary, but must know the individual's age and limit any contribution to the family dollar amount allowed for a calendar year plus any catch-up contributions.
- Employers must determine an employee's eligibility to contribute to an HSA by verifying coverage under an HDHP and knowing the employee's age for catch-up contributions.
- Employers may not recoup any portion of the employer's contribution to the employee's HSA.
- Employer contributions are not considered earned income for the Earned Income Credit.

Investments

- An HSA may not invest in life insurance contracts, collectables, alcoholic beverages, or other tangible personal property.
- HSA account beneficiaries, trustees, or custodians may not enter into "prohibited transactions."

Disbursements

- Disbursements from an HSA may be for the account beneficiary, the individual's spouse, or dependents even though the spouse or dependents may not be covered by the HDHP.
- Clear and convincing evidence may allow an account holder to repay a mistaken distribution to the HSA and not be subject to income or additional tax consequences.
- Reimbursement may be delayed to later tax years for expenses that were incurred in a previous year.
- A retiree's Medicare premium, long-term care premiums, and expenses for services may be paid from an HSA that has been funded with salary redirection from a Section 125 cafeteria plan, but must adhere to the premium limits established under Section 213(d)(10).

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- There is no limit on the number of trustee-to-trustee transfers allowed during a year.
- Employers may “pre-fund” an individual’s HSA account, in the same manner and amount for all eligibles, and recoup these accelerated contributions from the participant at the end of the plan year.
- Amount fees withdrawn from an HSA are not considered a taxable distribution, nor do these fees count toward the annual maximum contribution limit.
- Custodians must allow for rollovers out of an HSA, but do not have to accept rollovers from other HSAs.
- A trust or custodial agreement may not limit disbursements to only qualified medical expenses, but may limit disbursement opportunities for amounts of less than \$50 or allow a certain number of distributions per month. ■

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