

# HSA Road Rules

*for Consumers, Employers, Insurers,  
Banks, Credit Unions and Administrators*

## The HSA Insider

---

*By Dan Perrin*

January 1, 2006

Fourth Edition

# Table of Contents

Universal HSA Principles .....	Page 2
Health Savings Account Eligibility Road Rules .....	Page 3
Health Savings Account Deposit Road Rules .....	Page 5
Health Savings Account Spending Road Rules .....	Page 7
Health Savings Account Road Rules for Trustees or Custodians .....	Page 8
Health Savings Account Road Rules for Employers .....	Page 11
Health Savings Account Road Rules for Health Insurers .....	Page 13
Table A: Allowable Health Savings Account Investments .....	Page 14
Table B: Allowable “Catch Up” Contributions for Americans 55 Years and Older .....	Page 15
Table C: Allowable Expenditures on Long-Term Care Insurance from Your Health Savings Account .....	Page 16
Table D: Allowable Expenditures from Your Health Savings Account .....	Page 17
Table E: Non-Allowable Expenditures from Your Health Savings Account .....	Page 19
Why Were Health Savings Accounts Designed this Way? .....	Page 20
Author’s Note .....	Page 23

# Universal HSA Principles

1. You must have an HSA qualified high deductible health plan to open or contribute to a Health Savings Account in your own name.
2. Switching to a high deductible health plan from a traditional low deductible health plan will cut the cost of your health plan substantially. You deposit the savings gained into your Health Savings Account. The whole point of a health savings account is to allow you to use that money on a tax-free basis to pay for your health expenses below your new, higher deductible.
3. The money in your Health Savings Account is your own. This means your employer cannot tell you what to do with your own money or restrict what you can spend it on. Since it is your money, it goes with you when you change jobs.
4. You are in charge of your Health Savings Account funds, making you and your doctor the decision makers, not some third-party. Spending your own money also means that you will/should ask about the cost of health care expenditures, which will bring marketplace competition to the world of health care.
5. There is no time limit for when you can reimburse yourself for your health care expenses; you just need to keep legible receipts and records in case you do reimburse yourself, or in case you are audited.
6. You decide whether to spend from the account for your medical expenses and how much to spend, or whether to spend out-of-pocket and to save the HSA money for the future.
7. Anyone can contribute to another person's Health Savings Account. The tax benefit from such a contribution is gained by the person receiving the contribution, not to the person giving the contribution.
8. You decide which company will hold the account, and what type of investments you make with your account. Any investment allowed for IRAs is allowed for HSAs (please see [Table A](#)).
9. IRS Publication 502 provides a list of allowable expenditures from your Health Savings Account. (Please see [Table D](#) and [E](#) of this document for a partial and summary list of allowable (tax-free) and non allowable (not tax-free) expenditures from your HSA.)

# Health Savings Account Eligibility Road Rules

1. You must have an HSA qualified high deductible health insurance plan.
2. A HSA qualified high deductible health plan has the following characteristics:
  - i) a minimum deductible\* of \$1,050 for self-only coverage (2006);
  - ii) a minimum deductible\* of \$2,100 for family coverage (2006);
  - iii) a maximum out-of-pocket limit\* (including deductibles and co-pays) of \$5,250 for self-only coverage, and \$10,500 for family coverage (2006);
  - iv) preventive care can have first dollar coverage;
  - v) prescription drugs taken to prevent the onset of a condition for which a person has developed risk factors for can be considered preventive care, like cholesterol-lowering medication;
  - vi) preventive care examples include: periodic health evaluations like annual physicals, screening services like mammograms, routine prenatal and well-child care, child and adult immunizations, tobacco cessation programs, and obesity weight loss programs;
  - vii) As a general rule of thumb, if you are treating an existing illness or condition with either a drug or procedure, that drug or procedure is not considered to be preventive care (because the condition already exists, and therefore you cannot be preventing it.) If you are trying to prevent an illness or condition from occurring by taking a drug or with a procedure, that is considered to be preventive. Some drugs, like cholesterol lowering ones, can be both preventive and non-preventive under HSA Rules, depending on your own health situation;
  - viii) co-pays are allowed to apply to preventive care;
  - ix) higher out-of-pocket (co-pays and co-insurance) is allowed for out-of-network care;
  - x) until January 1, 2006, you can have an HSA qualified plan that pays for prescription drugs below the deductible, as long as the prescription drug benefit is a separate plan or rider; and,
  - xi) after January 1, 2006, prescription drug coverage before the deductible is met is not allowed.
3. You cannot be covered by any other health insurance that reimburses you for health expenses you incur, unless it is another HSA qualified high deductible health plan. For example, if a family has all members covered under two HSA qualified high deductible health plans, or some family members on one plan and the other family members under another HSA qualified high deductible health plan, the maximum annual contribution to the account remains in force. Just

because you have coverage under two HSA qualified high deductible health plans, you cannot double your HSA contribution. It remains at a maximum of \$5,450\* for a family (2006) regardless of whether or not you are covered by one or two HSA qualified high deductible health plans.

4. For those covered by two HSA qualified high deductible health plans, it is a violation of the coordination of benefit rules to be paid by each plan for the same expense.
5. Flexible Spending Accounts (FSAs) and Health Reimbursement Arrangements (HRAs) may make you ineligible for an HSA unless they are: (1) "limited purpose" (limited to dental, vision, child care, or preventive care) or (2) "post-deductible" (pay for medical expenses after the plan deductible is met). HRAs that set aside money only for retiree health expenses are also acceptable.
6. An employer can restrict the type of expenditures an employee can make from their FSA during the new two and a half month grace period that some employers may grant to employees, for relief from the FSA "use-it-or-lose-it" rule. If an employer restricts the FSA expenditures to non-health items (such as is the case with a limited-purpose FSA) during this grace period, then such employee is eligible for HSA, provided they have the proper high deductible health plan.
7. If you are enrolled in Medicare or Medicaid, you cannot have an HSA.
8. Tricare does not currently offer an HSA qualified high deductible health plan. Therefore, if you are on Tricare, you cannot have an HSA. Once Tricare offers an HSA qualified high deductible health plan, and you select it, you can have an HSA.
9. If you have received any Veterans Administration health benefits in the last three months, you cannot have an HSA.
10. If you are Medicare eligible, and you are not enrolled in Medicare, you can open or contribute to an HSA, if you have an HSA qualified health insurance plan. [Please see the note below [Table B.](#)]
11. You cannot establish separate HSA accounts for your minor dependent children.
12. You do not have to have earned income from employment to have an HSA.
13. There are no income limits to have an HSA.
14. You do not have to itemize your deductions on your federal income taxes to deduct your contributions to an HSA.
15. State mandates for first dollar coverage that adversely impact HSA qualified high deductible health plan design are allowed until January 1, 2006, in order to give certain states time to make changes to their own state laws before that date. The two states with mandates that prevent any qualified HSA health plan from being sold to individuals or to small groups as of 1/1/06 are New York and New Jersey.

\*NOTE: These amounts are indexed annually for inflation.

# Health Savings Account Deposit Road Rules

1. You must have an HSA qualified high deductible health plan to open or contribute to an HSA.
2. If you no longer have HSA qualified high deductible health plan, you cannot contribute to your Health Savings Account, but you can continue to spend or save the funds already deposited, as you see fit.
3. Your annual HSA deposit can never exceed your insurance plan's deductible, unless you are 55 or older and are making "catch up" contributions.
4. The higher your deductible, the more you can deposit into your HSA. However, the maximum amount you can contribute per year is \$5,450\* for family coverage (2006) and \$2,700\* for self-only (2006), excluding catch up contributions for those 55 years and older.
5. Individuals 55 and older can make additional catch-up contributions until they enroll in Medicare. For a schedule of the increasing catch up deposit amounts allowed, please see [Table B](#).
6. Catch up contributions are not pro-rated, unless you did not have HSA qualified high deductible health plan coverage for the entire year.
7. If you are covered by your HSA qualified high deductible health plan for the entire year, you may deposit the entire catch-up amount starting with the year you turn 55.
8. In the year you enroll in Medicare, you must pro-rate your catch-up contribution for the number of months you had HSA qualified high deductible health plan coverage, prior to the month your Medicare enrollment is effective.
9. If you have a family plan with a per-person deductible below the overall family deductible, you can deposit into the account the maximum allowed, if you have enough people in the family so that the sum of their per-person deductibles exceeds the maximum allowable family deposit. However, you cannot deposit more into the HSA than the overall or total family deductible. For example, a family of two with a \$2,000 per-person deductible, and an overall deductible, or total family deductible of \$5,000, can only deposit \$4,000 into the HSA. If a family of three has a \$2,000 per-person deductible, and a \$5,000 overall or total family deductible, then the maximum deposit to the HSA is \$5,000.
10. Trustees and custodians may open an account with a nominal deposit before the HSA qualified high deductible health plan is in effect. For example, if an individual's or an employer's HSA qualified high deductible health plan becomes effective January 1 – the trustee or custodian could open the account with a nominal deposit, say \$1, in December of the preceding year. The account will not officially be established as an HSA until the first day of the first full month the health plan is in effect. In this example, that date is January 1. The trustee does not report this account as an HSA until the health insurance is in effect, and the account is, in fact, an HSA.
11. A trustee or custodian can use the date the account application was signed as the start date for the Health Savings Account provided, as of that date, the high deductible health plan is in effect.

12. There is no tax code rule preventing a custodian, trustee, HSA administrator or insurer from making your Health Saving Account effective date back to the date you are first eligible (i.e., the first day of the first full month the HSA high deductible health plan is in effect). This is the date from which the maximum allowable contribution is calculated, and is the date when allowable withdrawals can begin.
13. You can “front load” or fully fund your HSA account on day one of your health savings account being in effect, provided you do not exceed the annual maximum amount (or the pro-rated amount if your account is open on a date other than January 1st.) You can make the deposit anytime after your HSA is open. If you lose your high deductible health plan later in the year, you will have to withdraw some of the contribution from the account.
14. If your high deductible coverage is effective after January 1st, then the total contributions to the account must be pro-rated based on the number of full months your qualified high deductible insurance is in effect. Count only those months for which your high deductible coverage is in effect on the first day of the month. For example, if your high deductible coverage starts on January 3, the maximum number of months for which you can make a contribution to your HSA is 11.
15. You can deposit funds into your HSA in a lump sum or in any amounts or frequency you wish. However, your account trustee/custodian can impose minimum deposit and balance requirements.
16. Deposits to an HSA must be made in cash. Funds in an IRA, 401(k), or other retirement/pension account cannot be directly deposited or “rolled over” into an HSA. But you can take a distribution from one of these accounts, pay applicable taxes (and penalties if withdrawn early) and use the remaining funds to make deposits into your HSA.
17. Rollovers from an Archer Medical Savings Account into a Health Savings Account are allowed if completed within 60 days of withdrawing the funds from your Archer Medical Savings Account.
18. The term “rollover” has several meanings. Rollover of HSA funds from year to year of unspent balances is well understood. However, IRA and HSA rollovers has another meaning to the IRS: you are allowed to take any amount of your HSA funds out of your account out once a year, and there is no limitation on what those funds can be spent on. If the funds are returned to the HSA within 60 days, there is no tax or penalty. However, if those funds are not returned to the HSA within 60 days, then you must pay the taxes due on those funds, and the 10% penalty. Unofficially, this “rollover” rule is known as the “playing with fire” rule.
19. Unlimited HSA trustee to HSA trustee transfers are allowed, meaning, you can move your HSA account any number of times you want in a given year.
20. If you have contributed an amount into your HSA which exceeds your maximum allowable deposit, you may withdraw the excess amount and any earnings on the excess amount prior to April 15th of the following year. However, you must pay income tax on your excess contributions and income tax on any earnings of the excess contribution. There is no 10% penalty on excess contributions.
21. If you do not withdraw the excess contribution to your HSA prior to April 15th of the following year, you must pay a 6% excise tax on the excess contribution, and on any earnings of the excess contribution. If in the next year you decreased your maximum contribution by the amount of your excess contribution made the year before, you do not have to pay the 6% excise tax again. If, however, you leave the excess contribution in, and do not decrease your maximum contribution by the amount of your excess contribution made the year before, you will have to pay the 6% excise tax each year the excess contributions and earnings are in the HSA.

\*NOTE: These amounts are indexed annually for inflation.

# Health Savings Account Spending Road Rules

1. There are a wide range of allowable tax-free HSA expenditures, including vision and dental expenses, and for example, braces for your children. A description of qualified Health Savings Account expenditures can be found in IRS Publication 502, and is located at the web at: [\[Click here\]](#). Publication 502 has great examples, but it is not the definitive list. (Please see [Table D](#) for a partial list of allowable tax-free expenditures and [Table E](#) for non allowable expenditures.)
2. If an expenditure from your Health Savings Account is used for purposes other than a qualified health care expense as defined in IRS Publication 502, then the amount withdrawn is subject to both income tax and a 10% penalty, unless the person who makes such a withdrawal from their HSA is over the age of 65. If 65 years old or older, the amount withdrawn for non-medical purposes is treated as retirement income, and is subject to normal income tax, but is not subject to the 10% penalty.
3. Withdrawals that were made for what the HSA owner thought were qualified medical expenditures, but turned out not to be qualified medical expenditures, can be returned to the Health Savings Account if there is clear and convincing evidence that the expenditure was a mistake of fact. Such repayment to the Health Savings Account must be made on or before April 15th of the year following when the individual knew, or should have known, the expenditure was a mistake.
4. Other qualified medical expenses from a Health Savings Account include out-of-pocket expenditures while enrolled in Medicare, including Medicare premiums, deductibles, coinsurance and copays, but not Medigap premiums.
5. Everyone with a Health Savings Account must keep all their receipts showing their expenditures from their account. There are two key reasons you must do this: (1) if you exceed your deductible, you may need the receipts to send to your insurer, and (2) in case you are audited by the IRS, you need to explain your HSA expenditures.
6. April 15, 2006 is the last date that you can open your Health Savings Account to fund and reimburse yourself for expenses incurred in 2005 while covered by a high deductible health plan.
7. You may use funds from your Health Savings Account to reimburse for expenses from a previous year, only if you had an HSA at the time the expenses were incurred.
8. Your spouse will inherit your Health Savings Account upon your death, unless your will provides otherwise.
9. Should the Health Savings Account holder have no spouse, the funds in the account shall no longer be treated as a Health Savings Account but part of the individual's estate and will be subject to estate taxes.
10. HSA funds cannot be used to pay for health insurance premiums unless the individual is receiving federal or state unemployment benefits.
11. HSA funds can also be used to pay premiums for COBRA continuation health insurance coverage from a former employer.
12. An employer paying COBRA for an employee with an HSA does not have to continue deposits into the account. The employer does have to pay the premium for the qualified high deductible health plan.
13. HSA funds can be used to pay premiums for qualified long-term care insurance coverage, subject to the age limits in the Internal Revenue Code. (Please see [Table C](#).)

# Health Savings Account Road Rules for Trustees or Custodians

*(Banks, Credit Unions, Insurers and others)*

1. Banks, Credit Unions or any other entity that currently meets the IRS standards for being an IRA trustee or custodian can be a HSA trustee or custodian. Insurers can also be HSA Trustees or Custodians.
2. Any entity already approved by the IRS to be a Archer MSA trustee or custodian is automatically approved to be a HSA custodian.
3. Trustees and custodians can modify existing IRA custodial account or trust account documents for HSAs.
4. The IRS has issued a model HSA Trustee Account document, which can be found on the web at: [\[Click here\]](#).
5. The IRS has issued a model HSA Custodian Account document, which can be found on the web at: [\[Click here\]](#).
6. Deposits to the Health Savings Account can be accepted by the custodian or the trustee at any time preceding the filing date of the account owner's tax return for that year (without extensions.)
7. Deposits to the Health Savings Account can be made by any person or entity, or by the account holder, to their Health Savings Account.
8. No deposit that exceeds the maximum allowable amount (including catch up contributions) should be accepted by a custodian or trustee.
9. It is the final responsibility of the account holder, not the trustee or the custodian, to determine if deposits have exceeded the maximum allowable amount.
10. It is the responsibility of the account owner to notify the custodian or trustee if there has been excess deposits made, and it is the responsibility of the account owner to request the withdrawal of those funds, and the payment of income tax on those funds and the pro-rata share of the earnings, and the payment of the 6% excise tax.
11. Rollover contributions from a Health Savings Account or Archer MSA into another HSA are not subject to the maximum deposit rules.
12. The account owner's interest in the balance of the custodial or trust account is non-forfeitable.

13. Health Savings Account funds in either a trust or custodial account may not be invested in life insurance contracts or in collectibles as defined in section 408(m)(3) of the Internal Revenue Code.
14. Assets of Health Savings Accounts may not be commingled with other property, except in a common trust fund or common investment fund (like a mutual fund.)
15. Prohibited transactions include borrowing against or pledging the funds in the Health Savings Account, or any other such prohibited transactions as described in Section 4975 of the Internal Revenue Code.
16. Withdrawals or other distributions from Health Savings Accounts are made at the direction of the owner. However, HSA custodians or trustees can put reasonable limitations on access to the HSA funds, such as the number of withdrawals or size of the withdrawals.
17. The trustee or the custodian is not required to determine whether the distribution is for the payment or reimbursement of qualified medical expenses.
18. Only the account owner is responsible for substantiating that any distribution is for qualified medical expenses and must retain records sufficient to show, if required, that the distribution is for a qualified medical expense.
19. Withdrawals to pay for qualified medical expenses for the account owner, or their spouse, or dependents are tax free.
20. Withdrawals to pay for non-medical expenses are subject to income tax and a 10% penalty. The 10% penalty does not apply if the withdrawal is made after the account owner's death, disability or the account holder is 65 years or older.
21. Upon the account owner's death, the HSA becomes the spouse's HSA, unless there is another beneficiary.
22. If the beneficiary is the account owner's estate, the fair market value of the account as of the owner's date of death is taxable on the account owner's final return.
23. If the beneficiary is someone other than the spouse, the HSA ceases to be an HSA on the date of the owner's death and the fair market value of the account is taxable to that person in the tax year that includes such date.
24. Account owners must give trustees or custodians the necessary information for the preparation of any report required by the IRS.
25. Trustees and custodians agree to submit any such reports required by the IRS.
26. Trustees and custodians may have restrictions of investment powers, voting rights, amendments and termination, removal of custodian, withdrawal procedures, including minimum allowable amounts and frequency, use of credit cards, debit cards, or stored-value cards, return of

mistaken distributions and can provide for descriptions of prohibited transactions, definitions of account terms, and can conform the account to state law requirements and include exculpatory provisions.

27. Multiple trustee to trustee or custodial account to custodial account transfers are allowed in a single year. Such transfers are not subject to the rollover rules.
28. The same self-dealing restrictions on IRAs apply to HSAs.
29. Reporting requirements for financial entities holding HSA funds are relatively simple. Trustees, custodians and health savings account administrators need to file two IRS forms, one for distributions from the HSA, and one for contributions to the HSA.
30. These forms cannot be printed out on your desktop computer because of the special machine readable red ink used on the IRS forms.
31. The two IRS Forms are 5498-SA for contributions, and IRS Form 1099-SA for distributions. Instructions for these forms can be found at: [\[Click here\]](#). Form 5498-SA can be found at: [\[Click here\]](#). Form 1099-SA can be found at: [\[Click here\]](#).
32. The contribution Form 5498-SA is due to both the account owner and the IRS by May 31st.
33. The distribution Form 1099-SA is due to the account owner by January 31, 2005 and are due to the IRS on February 28th, unless you are filing electronically with the IRS, and if so, the due date is March 31st.

# Health Savings Account Road Rules for Employers

1. The employee owns your contributions to their account as soon as the funds are deposited.
2. The employer can no more restrict the use of the funds in the employee's Health Savings Account than they can restrict the employee's funds in the employee's personal checking account.
3. Employee contributions to their Health Savings Account can be made on an after-tax basis and taken as an above-the-line deduction on their tax return (making such contributions tax-free) or the employee can make pre-tax contributions to their Health Savings Account through a Section 125 (aka "salary reduction" or "cafeteria") plan.
4. Employee contributions to their Health Savings Account through a cafeteria plan can change on a month-by-month basis. However, the employer can put reasonable limits on how often those contribution amounts can change.
5. Employer contributions to an employees Health Savings Account are always excluded from any employees' income (such contributions are made pre-tax).
6. Employers must make comparable contributions to all employees' Health Savings Accounts (unless made through a Section 125 plan).
7. Such comparable contribution to an employee's Health Savings Account means all employer contributions must be of the same amount for all family HSAs and the same amount for all single HSAs; or are the same percentage of the annual deductible.
8. Comparability rules are likely being violated if "extra contributions" to any employee's Health Savings Account are being made. For example, additional contributions to an employee's Health Savings Account being made based on the employee's seniority, length of service or giving catch up contributions to those employees 55 years and older violate the comparability rules.
9. The comparability rule can be applied separately to part-time employees. The rule can also be applied separately for employees with self-only vs. family coverage.
10. Matching contributions by an employer through a Section 125 plan are not subject to the comparability rule, but are subject to the non-discrimination rules of 125 plans.
11. The non-discrimination rule for Section 125 plans, in general, is that contributions cannot be higher for higher-paid employees than they are for lower-paid employees. Contributions that favor lower-paid employees are allowed.
12. There are no cases in which the Health Savings Account comparability rule or the 125 non-discrimination rules do not apply.

13. Without violating the comparability rule, employers may make their contribution to an employee's Health Savings Account conditional on the employee's participation in a Wellness program. However, the employer must offer an equal cash amount to all HSA eligible employees (those who have an HSA qualified high deductible health plan) who participates in the Wellness program, through a cafeteria plan.
14. For employers who do not provide their employees with health insurance but whose employee may purchase a Health Savings Account on their own, such employer may make pre-tax contributions to such employees' Health Savings Account through a Section 125 plan, as long as the offer is open to all such employees, and the contribution amount follows the Section 125 plan's non-discrimination rule.
15. For employers who do not provide their employees with health insurance but whose employee may purchase a Health Savings Account on their own, such employer may make pre-tax contributions to such employees' to reimburse their monthly health insurance premium, provided the employee brings their monthly health insurance bill to the employer each month.
16. Self-employed, partners and S-Corporation shareholders are not generally considered employees and cannot receive pre-tax employer contributions to their Health Savings Accounts. Self-employed can only take an above-the-line deduction for their premium and Health Savings Account contribution.
17. Regardless of how your S-Corporation or your LLC is structured, the company cannot make pre-tax contributions to owners, shareholders, or partners.
18. It is prohibited to transfer the employee's balance of a Flexible Spending Account (FSA) into a Health Savings Account.
19. It is prohibited to transfer the employer's notional balance of a Health Reimbursement Account (HRA) into any Health Savings Account.
20. A limited purpose FSA or a limited purpose HRA is allowed for expenditures like dental, vision or preventive care.
21. Post deductible HRAs or post deductible FSAs are allowed to pay for expenses above the minimum HSA deductible.
22. COBRA rules apply to the high deductible health insurance plan portion of an HSA, but not to the account.

# Health Savings Account Road Rules for Health Insurers

1. The minimum deductibles for HSA qualified high deductible health plans are \$1,050\* for self-only (2006), and \$2,100\* for families (2006). These deductible minimums are indexed annually for inflation during the preceding year and rounded to the nearest \$50 increment. New deductible limits, if any, will be announced annually by the IRS (likely in November of this year).
2. The maximum deductibles for HSA qualified high deductible health plans are \$5,250\* for self-only (2006), and \$10,500\* for families (2006). However, all policies with the maximum allowable deductible must cover all costs 100% thereafter to meet the maximum out-of-pocket spending limits.
3. The maximum out-of-pocket limits are \$5,250\* for self-only (2006) and \$10,500\* for families (2006).
4. Imbedded (per-person) deductibles for family plans are not allowed unless they meet the minimum deductible for families of \$2,100\* (2006). The maximum out-of-pocket limit of \$10,500\* (2006) still applies.
5. Insurers may allow, but are not required, preventive care services to be covered by the insurance on a first-dollar basis (co-pays permitted) below the deductible.
6. As of January 1, 2006, if prescription drugs are covered by an HSA qualified high deductible health plan, such prescription drug expenses must be subject to the plan deductible.
7. State mandates which currently prohibit HSA qualified plans from being sold in a certain states will not disqualify you from contributing to an HSA, up until January 1, 2006. This deadline will be not extended for health plan contracts that expire after January 1, 2006. States that do not modify their state law to make them HSA friendly by January 1, 2006, will prevent insurers from offering HSA qualified health plans in those states. The two states with mandates that prevent any qualified HSA health plan from being sold to individuals or to small groups as of 1/1/06 are New York and New Jersey.
8. Insurers themselves determine whether their high deductible plan meets the requirements of federal law. There is no federal government entity, agency or officer who reviews and approves HSA qualified plans. State insurance departments also will not determine whether plans are HSA-qualified.
9. Insurers are expected to inform their customers which high deductible health plans are HSA-qualified.
10. States will continue to regulate high deductible health plans, whether or not they are HSA-qualified.

\*NOTE: These amounts are indexed annually for inflation.

# Table A: Allowable Health Savings Account Investments

- Bank Accounts
- Annuities
- Certificates of Deposits
- Stocks
- Bonds
- Mutual Funds
- Certain types of Bullion or Coins - see Section 408(m)(3) of the Internal Revenue Code
- Your HSA custodian or trustee may restrict certain types of investments

## Not Allowable HSA Investments

- Collectables: including any work of art, antique, metal, gem, stamp, coin, alcoholic beverage or other personal property as described in Section 408(m)(3)
- Life Insurance Contracts

# Table B: Allowable “Catch Up” Contributions for Americans 55 Years and Older

2005:	\$600
2006:	\$700
2007:	\$800
2008:	\$900
2009 and after:	\$1,000

Each spouse age 55 or older can contribute up to the maximum catch up amount. Catch up contributions are not pro-rated, unless you did not have HSA qualified high deductible health plan coverage for the entire year. If you had HSA qualified high deductible health plan coverage for the entire year, you can deposit the entire catch-up amount starting with the year you turn 55. If both spouses want to make catch-up contributions, each spouse must have a separate health savings account.

In the year you enroll in Medicare, you must pro-rate your catch-up contribution for the number of months you had HSA qualified high deductible health plan coverage, prior to the month your Medicare enrollment is effective. You can delay enrollment in Medicare Part A only if you delay taking Social Security. You can delay taking Social Security up until age 70 and one half years old.

Once either spouse enrolls in Medicare, that spouse can no longer contribute any funds, including catch up amounts, to their Health Savings Account. If you are not enrolled in Medicare, you can contribute to your HSA and continue to make catch-up contributions. Note: If you enroll in Social Security you will be automatically enrolled in Medicare Part A, which will disqualify you from contributing to an HSA.

# Table C: Allowable Expenditures on Long-Term Care Insurance from Your Health Savings Account

In order to spend money from your HSA on long-term care, your long-term care insurance contract must:

1. Be guaranteed renewable,
2. Not provide for a cash surrender value or other money that can be paid, assigned, pledged, or borrowed,
3. Provide that refunds, other than refunds on the death of the insured or complete surrender or cancellation of the contract, and dividends under the contract, must be used only to reduce future premiums or increase future benefits, and
4. Generally not pay or reimburse expenses incurred for services or items that would be reimbursed under Medicare, except where Medicare is a secondary payer, or the contract makes per diem or other periodic payments without regard to expenses.

The amount of qualified long-term care premiums you can pay from an HSA is limited. You can include the following amounts as a qualified medical expense in 2006 (adjusted annually for inflation):

Age 40 or under - \$280.

Age 41 to 50 - \$530.

Age 51 to 60 - \$1060.

Age 61 to 70 - \$2,830.

Age 71 or over - \$3,530.

# Table D: Allowable (tax-free) Expenditures from Your Health Savings Account

There have been thousands of cases involving the many nuances of what constitutes “medical care” for purposes of section 213(d) of the Internal Revenue Code. A determination of whether an expense is for “medical care” is based on all the relevant facts and circumstances. To be an expense for medical care, the expense has to be primarily for the prevention or alleviation of a physical or mental defect or illness. The determination often hangs on the word “primarily.”

Note: If you are receiving federal or state unemployment insurance, you may pay for your health insurance premiums out of your HSA.

Examples of Allowable Expenditures from Your Health Savings Account:

Acupuncture	Drugs (prescription)
Alcoholism Treatment	Eyeglasses
Ambulance	Fertility Enhancement
Artificial Limb	Guide Dog
Artificial Teeth	Gynecologist
Bandages	Health Institute (if prescribed by physician)
Birth Control Pills (by prescription)	H.M.O. (certain expenses)
Breast Reconstruction Surgery (mastectomy)	Hearing Aids
Car Special Hand Controls (for disability)	Home Care
Certain Capital Expenses (e.g., for the disabled)	Hospital Services
Chiropractors	Laboratory Fees
Christian Science Practitioners	Lasik Surgery
COBRA premiums	Lead-Based Paint Removal
Contact Lenses	Learning Disability Fees (prescription)
Cosmetic Surgery (if due to trauma or disease)	Legal Fees (if for mental illness)
Crutches	Life-Care Fees
Dental Treatment	Lodging (for out-patient treatment)
Dermatologist	Long-Term Care (medical expenses)
Diagnostic Devices	Long-Term Care Insurance (up to allowable limits)
Disabled Dependent Care Expenses	Meals (associated with receiving treatments)
Drug Addiction Treatment (inpatient)	Medical Conferences (for ill spouse/dependent)

Medicare Deductibles	Prescription Medicines
Medicare Premiums	Prosthesis
Mentally Retarded (specialized homes)	PSA Test
Nursing Care	Psychiatric Care
Nursing Homes	Psychiatrist
Obstetrician	Psychoanalysis
Operating Room Costs	Psychoanalyst
Operations - Surgical	Psychologist
Ophthalmologist	Qualified Long-Term Care Services
Optician	Radium Treatment
Optometrist	Smoking Cessation Programs
Organ Transplant (including donor's expenses)	Special Education for Children (ill or disabled)
Orthodonture	Specialists
Orthopedic Shoes	Spinal Tests
Orthopedist	Splints
Osteopath	Sterilization
Out-of-pocket expenditures and deductibles for your spouse or dependent even if insured under a non-HSA health plan	Surgeon
Out-of-pocket expenditures while enrolled in Medicare	Telephones and Television for the Hearing Impaired
Over-the-Counter Medicines	Therapy
Oxygen and Equipment	Transportation Expenses for Health Care Treatment
Pediatrician	Vaccines
Personal Care Services (for chronically ill)	Vitamins (if prescribed)
Podiatrist	Weight Loss Programs
Post-Nasal Treatments	Wheelchair
Prenatal Care	Wig (hair loss from disease)
	X-Rays

# Table E: Non-Allowable (not tax-free) Expenditures from Your Health Savings Account

## Examples of Non-Allowable Expenses:

Advance Payment for Future Medical Expenses

Athletic Club Membership

Automobile Insurance Premium

Babysitting (for healthy children)

Boarding School Fees

Bottled Water

Commuting Expenses for the Disabled

Controlled Substances

Cosmetics and Hygiene Products

Dancing Lessons

Diaper Service

Domestic Help

Electrolysis or Hair Removal

Funeral Expenses

Hair Transplant

Health Programs at Resorts, Health Clubs, & Gyms

Household Help

Illegal Operations and Treatments

Illegally Procured Drugs

Maternity Clothes

Medigap premiums

Nutritional Supplements

Premiums for Life, Disability, Other

Accident Insurance

Premiums for your HSA Qualified High

Deductible Health Plan, unless you are receiving Federal or State unemployment benefits, or you are on COBRA

Scientology Counseling

Social Activities

Special Feeds/Beverages

Swimming Lessons

Teeth Whitening

Travel for General Health Improvement

Tuition in a Particular School for Problem Children

# Why Were Health Savings Accounts Designed this Way?

1. Why are there limits on the maximum deductible for a HSA qualified health insurance plan?

Some critics of Health Savings Accounts want the limits on the maximum deductible amount removed. The maximum deductible amounts in the HSA law were picked because there are diminishing reductions in premiums at deductibles above the deductibles prescribed in the HSA legislation. Further, since the deductibles and maximum contributions are tied to the rate of inflation, these amounts will grow over time. This limitation on the maximum deductibles also attracted support from moderate Members of Congress, and we needed their votes to pass the law.

2. Why can't the out-of-pocket amount be tied to the maximum contribution, instead of the deductible?

While the maximum contribution amount was originally tied to the deductible, the HSA allows for a deductible roughly double the size of the maximum contribution. Tying the maximum contribution rate to the out-of-pocket maximum is a viable policy, but the cost to the Federal government in lost taxable income made that idea politically unviable.

3. Why not carve out prescription drugs and allow tiered co-pays?

Including prescription drugs as a benefit below the deductible will drive up the now affordable cost of HSA qualified health plans, and, as a result, reduce the amount of savings derived from switching to a HSA qualified health plan. This means that less money can be deposited each year into the Health Savings Account, which will diminish their appeal and reduce the ability to build up funds in an HSA.

Tiered co-pays, or any other benefit that is paid below the deductible, seriously compromises the effect of a consumer spending their own money. When you spend your own money, you spend it differently than if you are spending someone else's money. Think of going out for an all expenses paid meal, versus going to a restaurant where you are paying: you order differently.

4. Why can't early retirees pay their HSA qualified health insurance premium from their Health Savings Account?

This change in the law was suggested and the response was: given that there are millions of uninsured Americans, and millions more in the individual market who have health insurance but receive no tax break for their purchase, why should insured early retirees get special treatment?

5. Why can't seniors use their HSA to pay for Medigap coverage?

The guiding principle of HSAs is for people to use their own money to meet a substantial deductible, thereby providing a financial incentive to spend the funds wisely and not to over consume. The main purpose of a Medigap policy is to insure the Medicare deductible.

Allowing HSA funds to pay for Medigap insurance would be akin to allowing HSA funds to buy insurance to cover the HSA deductible. In other words, it would be using HSA funds to defeat the entire purpose of an HSA. Here is an example of the difference it makes when the Medicare deductible is paid by the consumer: the Bipartisan Medicare Commission found that seniors without a Medigap policy spend \$1,400 less per year in Medicare benefits than seniors with a Medigap policy.

6. Why are the long-term care premium amounts that can be paid out of an HSA limited?

In crafting legislation, there is a fine line between asking for what you want and getting what you need. There were other issues being negotiated that needed the political capital more than allowing for unlimited amounts to be spent on long-term care premiums.

7. Why aren't IRAs and 401(k)s allowed to be rolled into an HSA?

While Health Savings Accounts have an investment component, the main purpose of an HSA is to fund health care expenditures and to put the patient in charge of those expenditures, not to have a principle role as a retirement savings vehicle.

8. Why can't HSA distributions be tax free upon your death?

The revenue loss to the Federal government made the price tag for that suggestion too high.

9. What is the status of Medicare Savings Accounts, and why aren't they being promoted more?

Medicare Savings Accounts have gone through their second revision in law, the most recent of which was included in the Medicare Prescription Drug bill that contained the Health Savings Account provision. Unfortunately, due to a drafting error and other needed changes that were not made, further legislative changes will need to be made for Medicare Savings Accounts to become widely offered by insurers. Finally, the health insurance market is moving to offer Health Savings Accounts, and as a practical matter, in most cases, even if the Medicare Savings Account provisions were picture perfect, it is likely Medicare Savings Account product offerings would not begin until the under-65 market has been squared away.

10. Why can't we have one joint HSA Account and still make catch up contributions?

There can be only one primary account holder of the HSA. Both spouses may contribute. The practical effect of this restriction is not significant.

11. Can we use our HSA to pay for medical services provided in other countries, like Mexico and Canada?

Yes.

12. Are catch up contributions pro-rated when you turn 55 and 65?

Please see the language below [Table C](#).

13. If I am self-employed, can I contribute on a pre-tax basis? How about for partnerships or for S-Corporation owners who own more than 2% or for LLC owners?

Self-employed can only take an above-the-line deduction for their premium and Health Savings Account contribution. Regardless of how your S-Corporation or LCC is structured, the only way you can structure your HSA contributions is as an above-the-line deduction. The HSA legislation simply cited current law in this regard. It was a political impossibility in the HSA legislation to make the necessary change in law to allow pre-tax contributions for LLC owners, S-Corp. owners or the self-employed. For further guidance for partnerships and S-Corporations, see IRS Guidance 2005-8 at [\[Click here\]](#).

14. What is an “above-the-line” deduction?

An above-the-line deduction reduces your Federal taxable income dollar for dollar by the amount you contribute. You do not have to itemize to claim this deduction. For example, if you contribute \$1,000 to your HSA, you reduce your Federal taxable income by \$1,000.

15. Why can't I pay my health insurance premiums with my HSA?

The money in your HSA is to meet your health care expenses below your deductible, not to meet your health insurance premiums. What if people spent their entire HSA deposit on their insurance premiums, and found no funds left to meet their health care costs to meet their deductible? The only time you are allowed to pay the health insurance premium with your HSA funds is if you are collecting Federal or State unemployment benefits, or you are on COBRA.

16. Can you provide a list of qualified medical expenses?

See Tables D and E, for a list of allowable and non allowable medical expenses. Please also see IRS Publication 502, which can be found in the U.S. Treasury section of this website, or at [\[Click here\]](#).

17. Can I be my own trustee?

No, the account portion of the HSA legislation cites existing IRA law. You cannot open your own IRA, can you? The same rule applies for HSAs.

---

# Author's Note

HSA Road Rules is designed to be as simple and comprehensive as possible. However, as events warrant, the online version of HSA Road Rules will be updated, so check back at [www.hsainsider.com](http://www.hsainsider.com) periodically to make sure you have the most recent edition.

This document is copyrighted by HSA Insider Corporation.

Dan Perrin is the President of HSA Insider Corporation and is the Publisher of HSA Insider, which can be found at [www.hsainsider.com](http://www.hsainsider.com). All errors and omissions contained herein are mine.