Diversified Benefit Services, Inc.

Health Savings Account (HSAs)

A Beginners Guide

WISCONSIN STATE COUNCIL SHRM

DIVERSIFIED BENEFIT SERVICES, INC.
Dedicated to Excellence in Benefit Management Solutions

Introduction

- **Presenter**
  - Christopher Kramer
    - Sales Manager – DBS, Inc.
    - 19 years experience implementing HRAs/FSAs/HSAs

Purpose of Presentation

- **Educate attendees on:**
  - How HSAs work
  - Rules and regulations
  - How HSAs integrate with HRAs/FSAs
  - Incorporate into benefits package
  - Answer questions

Unlock the mystery of HSAs

Introduction to DBS

- TPA since 1987
- Located in in Hartland, WI
- Communication//Service Emphasis
- Advanced Technology
- Strong Core Business Principles
- Member of ECFC

Hartland, WI

DBS Specialized Services Offered

- Section 125 – FSA (Flexible Spending Accounts)
- Section 105 – HRA (Health Reimbursement Arrangements)
- **Section 223 – HSA (Health Saving Accounts)**
- Section 132 – TRP (Transportation Reimbursement Plans)
- Customized Employee Reimbursement Plans

Health Savings Account Background

- Health Savings Accounts (HSAs)
- Part of Medicare Prescription Drug Improvement and Modernization Act
- Regulated by Code Section 223, Section 12 of the Act
- Effective 1/1/2004
- Based on Medical Savings Accounts

Internal Revenue Service

DIVERSIFIED BENEFIT SERVICES, INC.
Dedicated to Excellence in Benefit Management Solutions

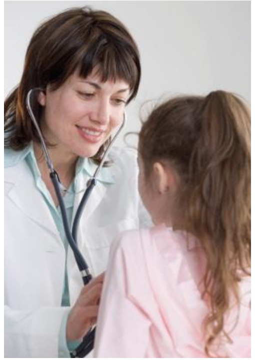
What is an HSA?

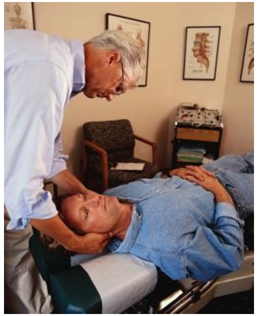
- Individually owned tax exempt trust
- Money can be contributed on a tax-free
  - Participant
  - Employer
  - Combination
- Utilize funds to pay for current & future "medical" expenses on a tax-free basis

What is an HSA?

Qualified medical expenses include:

- Deductibles
- Prescription Drugs
- Dental care
- Vision expenses
- Chiropractic care
- Acupuncture
- Medicare premiums





What is an HSA?

- Dollars rollover if unused
- Utilize for future qualified expenses tax-free
- Utilize for non-qualified expenses
  - Taxable
  - Possible penalty
- Some liken it to a health care IRA

Qualifying for an HSA

- Individual MUST have specific insurance coverage:
  - Called a qualified "High Deductible Health Plan" (HDHP)
  - Not all plans with a higher deductible are HDHPs
- Qualified HDHPs have deductibles and out of pocket limits that are established by law
- Insurance carrier should confirm plan is a qualified HDHP

HDHP Deductible

In-network deductible (2013) must be at least:

Self-only coverage:	$ 1,250
Family coverage:	$ 2,500

The HDHP cannot pay any claims until these minimum deductible amounts have been satisfied

All expenses incurred apply to the deductible

HDHP Out-of-Pocket Maximum

In-network out-of-pocket maximum cannot exceed (2013):

Self-only coverage:	$ 6,250
Family coverage:	$ 12,500

This may include the deductible, co-insurance and copays

Deductible and out-of-pocket maximums indexed by IRS.

HDHP Sample Plan Design

In-network deductible: Single: $1,500 / Family: $3,000

After the deductible is satisfied, the health plan pays 100% of claims in-network except for prescription drugs.

At this point drug copays start $10/$25/$50 until the copays and deductible total $2,500 (Single) and $5,000 (Family)

Most HSAs have an aggregate family deductible – not required

Agent/consultant or insurance company verifies health plan is HSA compatible

HDHP Deductible Example

- You go to the doctor and provide them your insurance card
- Your HDHP insurance plan is billed $200 for the office visit
- The insurance carrier applies their negotiated in-network discounts to the $200 claim
- Due to the discounts, the claim is reduced to $150
- The $150 is applied to the deductible
- You are responsible to pay the $150
- Use your HSA money to pay the $150

HDHP Deductible Example

- You go to the pharmacy and provide them your insurance card
- Your HDHP insurance plan is billed $110 for the prescription
- The insurance carrier applies their negotiated in-network discounts to the $110 claim
- Due to the discounts, the claim is reduced to $90
- The $90 is applied to the deductible
- You pay the pharmacy $90 at point of purchase
- You the HSA money to pay the $90

HDHP Exception

- HDHP exception to expenses being applied to the Deductible:
  - Preventative care
  - Per IRS Notice 2004-23
  - Health Care Reform codified that preventative care must be paid at 100% as well

Reason for HDHP design

Reason

- Make insurance more like insurance
- Promote consumerism

Concept

- Raise the deductible
- Premium more affordable
- Set aside tax-free dollars for expenses
- If not used, dollars rollover for future use

Qualifying for an HSA

You cannot be covered by other first-dollar medical coverage such as:

- Other non-HDHP health insurance
- Flexible Spending Account*
- Health Reimbursement Arrangement*

  *Including a spouse's plan

  *Unless properly designed

Qualifying for an HSA

- Cannot be enrolled in Medicare/Tricare
- Cannot be a dependent on someone else's tax return
- Eligibility is based on the coverage the potential HSA accountholder has
  - Example 1:
    - Employee A has family HDHP coverage
    - Spouse elects single coverage at her employer
    - Employee A qualifies for HSA as he is not covered by non-HDHP coverage
  - Example 2:
    - Employee A has family HDHP coverage
    - Spouse enrolls in general purpose Medical FSA
    - Employee A is not qualified for HAS as he has non-HDHP coverage

Funding an HSA

2013 Contribution limits:

Based on a calendar year

Indexed each year

Self-only coverage: $3,250

Family coverage: $6,450

(Maximum per family)

Funding an HSA

2013 Catch-up Contribution limit:

- Catch-up contribution: $1,000
  - (If you are 55 years old or older by year end)
- If husband/spouse both 55 year old, the spouse must establish an HSA for her $1,000 catch-up amount

Funding an HSA

- Individuals eligible on 12/1 of the taxable year are allowed the full annual HSA contribution regardless of the number of months covered by the HDHP
  - Example:
    - New employee enrolls into family HDHP as of 7/1/13 and maintains the coverage as of 12/1/13
    - The employee may contribute up to $6,450 for calendar year 2013

- If no longer eligible on this date, amount is pro-rated

Funding an HSA

- Full contribution test: Participants must maintain the HDHP for 12 months beyond the end of the year in which the HDHP started
- Otherwise, all or a portion of the contribution is included in income and subject to a penalty
- Can be funded as late as April 15 of the following year

How can HSAs be Funded

Payroll deducted employee contributions:

- Deducted from payroll pre-tax
  - Federal, State & FICA in Wisconsin
  - Most save 15%-25% in taxes
  - Employers save matching FICA tax
- Need form of Section 125 plan to allow
- Employer decides if they will allow payroll deductions

How can HSAs be Funded

Payroll deducted employee contributions:

- Payroll deductions typically deducted in equal amounts over year
- Unlike other Section 125 elections, participant can change amount for any reason during year
  - No status change needed
- Need to allow them to do change at least once a month

How can HSAs be Funded

Post-tax direct employee contributions:

- Contribute dollars directly to HSA with after-tax dollars
  - Set up EFT from regular bank account
  - Periodically send check to HSA
- Claim off your income taxes at year-end
- Pre-tax and after-tax contributions cannot exceed the contribution maximums

How can HSAs be Funded

Employer contributions outside a Section 125 Plan:

- Employers can contribute to employees HSA outside of a Section 125 plan
  - Need to make comparable contributions for all comparable participating employees during the year
  - Must be the same dollar amount or percentage of the HDHP deductible
- Failure to do so results in a 35% excise tax equal to all of the employers contributions for the year
  - IRS Form 8928

How can HSAs be Funded

Employer contributions outside a Section 125 Plan:

- Comparability rules
  - Permit different contributions for three tiers of family coverage (self+1, self +2, and self+3 or more)
  - Require, if differing amounts, that the amounts for the higher tiers be greater than the amounts for the lower tiers
  - Exclude collectively bargained employees from comparability testing
  - Permit employer to contribute more to non-HCEs than to HCEs
  - Based on a calendar year basis
  - Can restrict to those on the employer’s health plan

How can HSAs be Funded

Employer contributions outside a Section 125 Plan:

- Comparability rules
  - Do not permit different contributions based on:
    - Salaried/hourly, exempt/non-exempt, etc.
    - Geographic locations
    - Divisions within the company
    - Whether employee completes a wellness activity
    - Age, sex, length of service, wages, health conditions, etc.
- General Rule
  - All HSA-eligible employees in the same non-collectively bargained category with the same HDHP coverage receive the same dollar amount or percentage of deductible

How can HSAs be Funded

Employer contributions inside a Section 125 Plan:

- Comparability rules do not apply to Cafeteria Plan
- Regular Section 125 non-discrimination rules apply
  - Allows more employer flexibility with employer funding
  - Need to allow employee to make pre-tax contributions
    - Matching HSA contributions
      - Employee contributes $1 pre-tax into HSA, then employer matches $.50 into the HSA
    - Incentive based contributions
      - Complete health risk assessment
    - Non-elective seed money – regardless of whether the employee elects to contribute

HSA Distributions

- Can access HSA dollars tax free for any "qualified medical expense" permitted under federal tax law
- Expenses for spouse and legal dependents also qualify
  - Not to age 26 however
  - Old definition of dependents
  - Adult children can be covered by the health plan
    - Set up own HSA if independent
- HSA funds usually accessible via a debit card and/or checkbook

HSA Distributions

- Withdrawals for non-qualified items are subject to income tax + a 20% penalty
  - Car, vacation, cosmetic surgery, etc.
- Penalty waived if
  - Attain age 65 for accountholder
  - Accountholder dies
  - Becomes disabled
- Non-qualified expense only subject to income taxes

HSA Distributions

REMEMBER!

- Expenses must be incurred after the establishment of the HSA
  - Example:
    - Establish HSA 7/1/13
    - Have dental work 5/10/13
    - The 5/10/13 dental work is not a tax-free distribution
- You can only access dollars that have been contributed so far
- No advancement payment

HSA Distributions

- You can only access dollars that have been contributed so far
  - If an expense exceeds the funds available, participants can reimburse themselves as the monies are contributed
- You don’t have to take funds out if have an expense – can do it at any time in the future
  - Example:
    - Incur several small qualified expenses over the year
    - Pay for them from your regular checking account
    - At the end of the year, reimburse yourself from HSA for expenses

Examples of Eligible Expenses

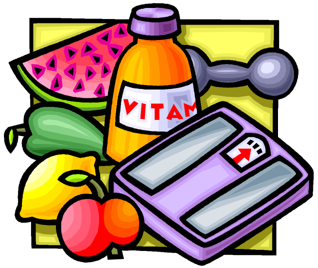
Eligible Out-of-Pocket Expenses Include:

- Medical Insurance deductibles, co-pays and co-insurance
- Dental Insurance deductibles and co-insurance
- Dental expenses such as exams, caps, crowns, bridges & filings
- Orthodontia
- Vision exams, glasses, frames, contact lenses & supplies
- Lasik eye surgery
- Hearing aids
- Chiropractor costs
- Prescription drugs
- Certain COBRA premiums
- Medicare premiums

Examples of Taxable Expenses

Expenses which are Taxable include:

- Surgery for cosmetic reasons
- Medical supplies that are not medically necessary
- Teeth bleaching/whitening/bonding
- Health club membership dues
- Over-the-counter vitamins for general health purposes
- Cosmetic drugs
- Medicare supplements
- Toothpaste



HSA Funds Rollover

- HSA funds are non-forfeitable once in the account
  - Including Employer funded amounts
  - Employer contributions are a “cost” of the health plan
- Accountholder owns the money
- Unused dollars roll forward year to year
- No “use-or-lose” provision

Consumerism

- Dollars accumulate in HSA over time
- “Shop around” for best price on prescriptions, lab work, office visits, etc. to use HSA dollars wisely
- Try to squeeze more from your HSA dollars
  - Example:
    - MRIs
    - Lab tests
- More data on costs and quality on carrier websites
- Not all participants will however HSA provides incentive

HSA and FSA

- Cannot contribute to the HSA if covered by the Medical FSA
  - Doesn’t matter if you have spent all your Medical FSA money early in the Plan Year
- Employee can have the HDHP coverage however they cannot contribute to the HSA
- Participation in the Dependent Care FSA does not affect participating in a HSA

HSA and FSA

- Employer can offer a "Limited Purpose FSA"
- Participant maintains eligibility to contribute to HSA
- Utilize dollars only for dental and vision expenses
  - Cleanings, braces, crowns, glasses, contacts, etc.
- Why use if HSA covers the same expenses?
  - Helps participants maximize tax savings
  - Preserve HSA dollars for the future
  - Aids participants with high expenses

HSA Funds

What if you drop the HDHP?

- You can utilize HSA funds on qualified medical expenses
  - At any time regardless of what type of health coverage you have in the future
- You lose your eligibility for the HSA which means:
  - You cannot contribute additional money if you are not covered under a HDHP
- Unused dollars stay in the account and rollover year to year

HSA Funds

- Money can earn interest tax-free in most States
  - Including Wisconsin
- Dollars must be held by a trustee
  - Typically a bank or insurance company
- Entity needs to be able to follow HSA trustee rules
  - General checking account not a trust account

HSA Trustee

- Generally HSA funds held in a very liquid account like a savings account
- Some allow HSA dollars to be invested once a participant accumulates a certain amount in the HAS
  - Participant could gain higher rate of return OR
  - Participant could lose value in the HSA
- Interest earned accumulates tax-free

Trustee Responsibility

- Trustee reports to the participant and IRS
  - Total dollar amounts contributed to the HSA
  - Total dollar amounts withdrawn from the HSA
- Trustee does not report or keep track of
  - The nature of the expense
  - Providers utilized
  - Name of health care user

Account Holder Responsibility

- Employee keeps track of which expenses qualify and which do not
  - Self--directed claims substantiation
  - Must keep documentation validating expense
    - Nature of expense
    - Date of service
    - Out-of-pocket cost
    - Provider
    - Recipient of services

Account Holder Responsibility

- Participant reports contributions & withdrawals on Federal taxes
- Participant Form 8889
- States the amount they claim as being eligible
- States the amount they claim as being ineligible
  - Subject a 20% penalty
  - Subject to income taxes
- Participant does not submit receipts with tax forms
  - Keep on file in case they are audited

Form **8889**

Department of the Treasury
Internal Revenue Service

Health Savings Accounts (HSAs)

► Attach to Form 1040 or Form 1040NR. ► See separate instructions.

OMB No. 1545-0074
2011
Attachment Sequence No. **53**

Name(s) shown on Form 1040 or Form 1040NR | Social security number of HSA beneficiary. If both spouses have HSAs, see instructions ►

Before you begin: Complete Form 8853, Archer MSAs and Long-Term Care Insurance Contracts, if required.

Part I **HSA Contributions and Deduction.** See the instructions before completing this part. If you are filing jointly and both you and your spouse each have separate HSAs, complete a separate Part I for each spouse.

1	Check the box to indicate your coverage under a high-deductible health plan (HDHP) during 2011 (see instructions) . . . ► ☐ Self-only ☐ Family		
2	HSA contributions you made for 2011 (or those made on your behalf), including those made from January 1, 2012, through April 17, 2012, that were for 2011. **Do not** include employer contributions, contributions through a cafeteria plan, or rollovers (see instructions)	2	
3	If you were under age 55 at the end of 2011, and on the first day of **every** month during 2011, you were, or were considered, an eligible individual with the **same** coverage, enter $3,050 ($6,150 for family coverage). **All others,** see the instructions for the amount to enter	3	
4	Enter the amount you and your employer contributed to your Archer MSAs for 2011 from Form 8853, lines 1 and 2. If you or your spouse had family coverage under an HDHP at any time during 2011, also include any amount contributed to your spouse's Archer MSAs	4	
5	Subtract line 4 from line 3. If zero or less, enter -0-	5	
6	Enter the amount from line 5. But if you and your spouse each have separate HSAs and had family coverage under an HDHP at any time during 2011, see the instructions for the amount to enter	6	
7	If you were age 55 or older at the end of 2011, married, and you or your spouse had family coverage under an HDHP at any time during 2011, enter your additional contribution amount (see instructions)	7	
8	Add lines 6 and 7	8	
9	Employer contributions made to your HSAs for 2011 . . . 9		
10	Qualified HSA funding distributions . . . 10		
11	Add lines 9 and 10	11	
12	Subtract line 11 from line 8. If zero or less, enter -0-	12	
13	**HSA deduction.** Enter the **smaller** of line 2 or line 12 here and on Form 1040, line 25, or Form 1040NR, line 25	13	
	Caution: *If line 2 is more than line 13, you may have to pay an additional tax (see instructions).*		

Part II **HSA Distributions.** If you are filing jointly and both you and your spouse each have separate HSAs, complete a separate Part II for each spouse.

14a	Total distributions you received in 2011 from all HSAs (see instructions)	14a	
b	Distributions included on line 14a that you rolled over to another HSA. Also include any excess contributions (and the earnings on those excess contributions) included on line 14a that were withdrawn by the due date of your return (see instructions)	14b	
c	Subtract line 14b from line 14a	14c	
15	Unreimbursed qualified medical expenses (see instructions)	15	
16	**Taxable HSA distributions.** Subtract line 15 from line 14c. If zero or less, enter -0-. Also, include this amount in the total on Form 1040, line 21, or Form 1040NR, line 21. On the dotted line next to line 21, enter "HSA" and the amount	16	
17a	If any of the distributions included on line 16 meet any of the **Exceptions to the Additional 20% Tax** (see instructions), check here . . . ► ☐		
b	**Additional 20% tax** (see instructions). Enter 20% (.20) of the distributions included on line 16 that are subject to the additional 20% tax. Also include this amount in the total on Form 1040, line 60, or Form 1040NR, line 59. On the dotted line next to Form 1040, line 60, or Form 1040NR, line 59, enter "HSA" and the amount	17b	

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 37621P Form **8889** (2011)

DIVERSIFIED BENEFIT SERVICES, INC.
Dedicated to Excellence in Benefit Management Solutions

Enrollment

- Technically can enroll in HSA at anytime as long as the person is eligible for the HSA
- Only expenses incurred after the establishment of the HSA qualify.
- Example:
  - Person has HDHP coverage 7/1/12
  - Completes HSA enrollment form for 10/1/12
  - Incurs $500 of deductible expense 8/1/12
  - This does not qualify to be paid from the HSA

Enrollment

- Employee can change payroll deductions throughout the year
- Most clients place some limitations on this so as to not be inundated with changes (i.e. once a month)
- Does not require a status change

Implementing an HSA

- Determine fiscal impact of switching to HDHP
- Compare cost of current plan to HDHP
- Figure in the cost of any employer contributions into cost of HDHP
- Review impact of HDHP on employees
  - Compare out-of-pocket expenses under both plans
  - Compare premium share from paycheck

Implementing an HSA

- **Communication is key**
- Thorough understanding of how the health plan works is very important
- Don't gloss over how the deductible works
  - Especially the prescription drugs
- Suggestion for employee meetings
  - Part 1: How the health plan works
  - Part 2: What is an HSA

Implementing an HSA

- **Communication is key**
  - Suggestion for employee meetings
    - Provide examples of low and higher users of health care in illustrating fiscal impact of HSA on employees
  - Don’t assume high users will not benefit from HSA
    - Many times when taking into account the employee share of premiums, employer HSA contributions and the health plan design, high users come out even or ahead.

Conclusion

Health Savings Accounts:

- Helps control health care costs
- Provides tax-free reimbursement
- Vehicle to save for retiree health expenses
- Lowers your taxes

Questions?

DIVERSIFIED BENEFIT SERVICES, INC.
Dedicated to Excellence in Benefit Management Solutions