BUILDING & GROWING WEALTH

RIVERVIEW CAPITAL ADVISERS

RIVERVIEW INSIGHTS

September 2014 | *Health Savings Accounts*

Introduction

IRAs and 401ks are the most commonly used tax sheltered accounts. Another less commonly known savings tool is an HSA (Health Savings Account). HSAs are individual accounts offered by employers in combination with a high-deductible health plan (HDHP). The advantages of an HSA are:

- The money saved is on a pre-tax basis;
- There are no taxes due on the investment growth;
- Withdrawals for qualified medical expenses are never subject to income tax;
- After age 65, an HSA essentially transforms into an IRA.

What is an HSA?

Created as part of the Medicare reform in 2003, HSAs were designed to give adults covered by HDHPs the ability to establish tax-advantaged savings accounts to use for qualified medical expenses. HSA contributors must be covered by a qualified HDHP and must not be covered by any other health plan.

When it comes to HDHPs, you must not have an annual deductible that is less than $1,250 for self-only coverage or $2,500 for family coverage, and the annual out-of-pocket expenses (deductibles, co-payments) cannot exceed $6,350 for self only and $12,700 for family. Regardless of age, anyone can set up an HSA and contribute yearly as long as the participant has a qualified HDHP and is not enrolled in Medicare.

How much can be contributed?

Employees use pretax dollars to make contributions to HSAs. The IRS maximum annual contribution limit for HSAs in 2014 is $3,350 for people with individual health plans, and $6,650 for those with family health plans. Again, the health plan provided by the employer must be considered a high deductible plan.

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Key Points

- What is an HSA?
- Contribution limits to HSAs
- Benefits and features of HSAs

Those age 55 and older may contribute an additional $1,000 each year. All of the contributions are 100% tax-deductible from gross income.

Calendar Year 2015				
	Minimum Deductible	Maximum Out-Of-Pocket	Contribution Limit	55+ Contribution Catch up
Single	$1,300	$6,450	$3,350	$1,000
Family	$2,600	$12,900	$6,650	$1,000

What are the benefits of HSAs?

Although the HSA was designed to put money aside for health care expenses, it has become an excellent, often overlooked, general retirement funding tool. An HSA allows the investor to diversify retirement savings and maximize tax benefits.

The HSA can be used to pay for some or all qualified medical expenses each year while the remaining balance grows for use in the future. Alternatively, if funds are not immediately needed, they can continue to grow tax free for future qualified medical expenses. Some of the qualified care costs include, but are not limited to: acupuncture, blood tests, braces, dentures, hospital bills, pediatrician, etc.

Funds used for qualified medical expenses will not be subject to income tax. Funds withdrawn for other expenses are subject to income tax, and a 20% penalty.

2015	Withdrawals from HSA			
	Tax-Free		Penalty (20%)	
	Age		Age	
	< 65	> 65	< 65	> 65
Qualified Medical Expense	Yes	Yes	No	No
Non-Qualified Medical Expense	No	No	Yes	No

What happens to the HSA after retirement?

After age 65, owners of HSAs become eligible for Medicare and can use HSA funds for any purpose, medical or not. Funds used for qualified medical expenses will not be subject to income tax. Funds withdrawn for other expenses are subject to income tax, but they avoid the 20% penalty faced by younger taxpayers (source). This means that after age 65, an HSA essentially transforms into an IRA. The savings built over the years can also be used for everyday expenses without penalty.

Any contributions not spent on medical expenses in one year may be rolled over for use in future years. Unused funds continue to accumulate without tax on the growth.

Calendar Year 2015					
Age	Annual Contribution	Years of Contribution	Interest Rate	Total Contribution	Ending Balance Age 65
45	$6,650.00	20	5.00%	$143,000.00	$244,089.81
50	$6,650.00	15	5.00%	$109,750.00	$163,879.11
55	$7,650.00	10	5.00%	$76,500.00	$101,031.92
60	$7,650.00	5	5.00%	$38,250.00	$44,384.63

HSAs are portable, allowing employees to take accounts with them if they leave a company for any reason (source). When changing jobs, the employee retains ownership of the account without incurring taxes, even if the new employer offers a health plan that does not qualify as high deductible.

How do I open an HSA?

Employers may choose whether to offer an HSA to their employees and whether to help fund an HSA partially or fully. However, employers have no control over how an employee's HSA funds are spent.

Summary

HSAs clearly offer compelling tax benefits, providing an excellent complement to other retirement savings vehicles. They may also provide an incentive to make careful health care spending decisions, since it is advantageous to keep funds in the plan as long as possible.

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