

5 HSA RULES YOU NEED TO KNOW

Wednesday, April 05, 2023

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Health Savings Accounts (HSAs) are rapidly growing in both size and in number. These accounts offer deductible contributions and tax-free distributions for qualified medical expenses. An HSA can be a valuable tool not only for paying for medical expenses but also for planning for your future. Here are 5 HSA rules you need to know.

1. Contributions are always deductible. Many times, higher income individuals are shut out of tax breaks. For example, there are income limits on Roth IRA contributions and on IRA deductibility for those who participate in a retirement plan at work. This is not the case with HSAs. There are no income limits for HSA contributions. You will never make too much money to be eligible for this tax break. If you make an HSA contribution, you may deduct that contribution regardless of how high your income is.

2. High deductible health plan required. To be eligible to make an HSA contribution, you must be covered by a high deductible health plan (HDHP). Not all plans qualify. To qualify as an HDHP, the plan must have a minimum deductible and a maximum out-of-pocket expense. These amounts are indexed for inflation. Except for preventative care, an HDHP may not provide benefits until the deductible for the year is met. The easiest way to determine if your health insurance qualifies as an HDHP is to ask the insurance company.

3. Contribution limits. How much you can contribute to an HSA depends on your age and the type of health insurance that you have. Contributions are generally pro-rated for the number of months the individual is enrolled in an HDHP. Contributions can be made by the individual, the employer or anyone else, but an annual contribution limit applies. The contribution deadline is your tax-filing

deadline, not including extensions (usually, April 15).

4. Tax-free distributions from your HSA for qualified medical expenses. Not only are HSA contributions deductible, but distributions from an HSA used to pay qualified medical expenses are tax-free. This means that both your HSA contributions and the earnings on those contributions will never be taxed if used for eligible medical expenses. Eligible expenses also include those of your spouse or a dependent. This is true even if your spouse or child is not covered under your HDHP.

HSAs offer a lot of flexibility when it comes to tax-free distributions. You can take a tax-free distribution from an HSA to reimburse yourself for qualified medical expenses for prior years as long as the expenses were incurred after you established your HSA and you have proof of those expenses.

5. Saving for medical expenses in retirement. A critical part of saving for retirement is saving for medical expenses. Many experts estimate that a large percentage of many retirees' savings will go toward healthcare costs. If an HSA is funded annually now and you do not use the funds for current medical expenses, you can accumulate a significant amount that can help defray these costs in retirement.

You cannot contribute to an HSA once you are enrolled in Medicare. However, you can keep your existing HSA and you can still take tax-free distributions for qualified medical expenses. You can even take tax and penalty-free distributions for Medicare premiums and out-of-pocket expenses. If you do not use the funds in your HSA for medical expenses, when you reach age 65 you may use them for any other purpose without penalty. However, any distributions not used for medical expenses will be taxable.

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