

Is a Health Savings Account For You?

Health Savings Accounts first became available in 2004, but they are just now beginning to generate a buzz. They can be a valuable tool for some people, but others will probably want to take a pass. You should consider an HSA if you have significant medical expenses that you can't deduct because of the 7.5% of adjusted gross income threshold for deducting medical expenses or if you are looking for a tax favored vehicle for saving. If you are an employer, an HSA can be a device you can use to limit your medical insurance premiums while offering your employees tax benefits. If you already receive good medical insurance through your or your spouse's employer, an HSA may not be for you.

An HSA consists of two parts: 1) a high deductible health insurance policy and 2) a savings/security account. The idea behind HSAs is that people will make more careful medical decisions if they are spending some of their own money. Therefore, to be eligible to open an HSA, you must be covered by a qualified high-deductible health insurance policy and you cannot be covered by other health insurance. Thus, you will bear the expense of the first few thousand dollars of medical care per year, but the insurance will protect you against catastrophic medical expenses.

Purchasers of qualified high deductible health insurance can open up health savings accounts. Contributions you make to the account are immediately deductible by you and may be invested. Income earned in the account is tax free or tax deferred depending on how the money is eventually used. As medical expenses are incurred, you can withdraw funds from the account tax free to pay the uninsured portion. Withdrawals for nonqualified medical expenses before age 65 are subject to a 10% penalty as well as income tax. After age 65 the 10% penalty disappears.

Because contributions to an HSA are deductible, HSAs offer a means around the usual 7.5% of AGI limit on the deduction of medical expenses. HSAs also aren't subject to the phase-out of the deduction for itemized deductions. For people who don't incur significant medical expenses, the money contributed to the account can be invested and grows tax free/deferred. There is no requirement that one use funds in an HSA to pay for medical expenses. Therefore, persons who are looking for another tax favored savings vehicle can use it simply for that. There are no income limits on who can use an HSA.

There are limits on the amount you can annually contribute to an HSA as well as numerous other details. If you want additional information on HSAs, give us a call.