

Health savings accounts

Employees taking more responsibility for protecting themselves and their families **By Janine Iacobelli**

You survived the recession, you've increased revenue, you've cut costs wherever possible and suddenly find that the profit you were expecting has been gobbled up by a 20 percent to 30 percent increase in health care costs. Year after year, employers look for ways to control these costs using strategies such as changing carriers, assuming more risk or shifting more cost to their employees.

Perhaps it is time to consider a health savings account (HSA). Although fairly new, created as part of the Medicare Modernization Act of 2003, HSAs are gaining attention. Why? Potential benefits for both employers and employees!

Let's review the basics.

HSAs are IRA-type accounts designed to help individuals save for future medical and retiree health expenses on a tax-free basis.

High deductible health plans

To be eligible, an individual must be covered under an HSA-qualified high deductible health plan (HDHP) and not covered by any other health plan. The HDHP minimum deductible must be at least \$1,000 for self-only coverage and \$2,000 for family, while the maximum annual out-of-pocket costs are limited to \$5,100 and \$10,200, respectively, for 2005.

HSA contributions

If eligible, an individual establishes an HSA with a qualified trustee or custodian such as a bank, credit union or insurance company. Every year an individual is eligible, the employer, the employee or both can make a contribution into the account. In 2005, annual contributions are limited to the lesser of the deductible or \$2,650 for self-only coverage or \$5,250 for family coverage. Similar to IRAs, an individual age 55 or older can make an additional catch-up contribution of \$600 in 2005. Contributions can be made as late as April 15 of the following year. Employer contributions are not subject to nondiscrimination rules of §105(h); however, the employer must make comparable contributions (same amount or same percentage of HDHP deductible) to comparable employees (eligible employees with comparable coverage). The individual owns the HSA and controls whether and how the account is invested in vehicles such as



CDs, annuities, stocks, bonds or mutual funds.

HSA distributions

An individual can use the money in the account to pay for qualified medical expenses such as medical care, dental and vision care, or over-the-counter drugs incurred after the HSA was established for self, spouse or dependent children. Generally, the money cannot be used to pay for health insurance premiums, except for COBRA, qualified long-term care insurance, health insurance while receiving unemployment and certain Medicare premiums. If distributions are made for non-medical expenses, amounts are included in income and subject to income tax as well as an additional 10 percent tax penalty.

Benefits

Benefits of an HSA for an employer include:

- Lower premiums for an HDHP.
- Less third party administrator expense as the employee controls which medical expenses to pay.

- Contributions are excludable from wages for employment tax purposes (FICA and FUTA).

Benefits of an HSA for an employee include:

- Portability despite change in job, medical coverage or marital status.
- Roll-over of unused balances from year to year.
- Above-the-line tax deduction when a contribution is made, tax-free earnings on the investment and tax-free withdrawals for qualified medical expenses.

HSAs allow employers to empower employees to control their own health care plan. Everybody wins!



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