



RINA *accountancy corporation*

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May 24, 2004
Volume 3 Issue 1

RINA ALERT!

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The purpose of **RINA ALERT!** is to provide information of a general nature. It is not designed to take the place of or to be

Health Savings Accounts Are (Almost) Here!

If you have been looking for a way to reduce your health benefit costs, the new Health Savings Account (HSA) legislation, IRC Code Section 223, may soon prove to be an answer. The new plans are not for everyone but you should become familiar with them in order to determine if they might work for you or your company.

By enrolling in a High Deductible Health Plan (HDHP) and, at the same time, depositing tax deductible dollars in a Health Savings Account (HSA) you may find that you can reduce the after tax cost of health care while improving your retirement savings.

A High Deductible Health Plan is defined as one whose annual deductibles are at least \$1,000 for individual coverage or a total of \$2,000 for family coverage. Annual maximum permissible out of pocket expenses for each type of coverage is \$5,000 and \$10,000, respectively.

Eligible individuals under the age of 55 can annually contribute as much as \$2,600 to an HSA account. Eligible families can contribute as much as \$5,150. All contributions must be made in cash. Individuals between the ages of 55 and 64 can make catch up contributions to their accounts. In 2004 and subsequent years, an additional \$500 can be added to the HSA by these older individuals, bringing the total that can be set aside, tax free, to \$3,100 for individual coverage. The excess increases periodically so that, in 2009, an additional \$1,000 can be added to the normal annual HSA contribution. Payment of these contributions is treated as a tax deduction on the tax return of eligible individuals. Employer paid contributions will not be considered to be taxable income to employees. Contribution limits are computed on a monthly basis for plans which do not commence at the beginning of a calendar year.

In addition, to be eligible, you must be enrolled in a HDHP and neither you nor your spouse can have any other health plan. Some coordination with Flexible Spending Accounts (Section 125) is permissible so long as the certain conventions are followed.

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Your comments on specific articles as well as suggestions for future articles are always welcome and may be directed to alert!@rina.com

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Contributions accumulate in the HSA account until used. The amounts are invested as you see fit. Amounts contributed to the HSA can accumulate until needed to pay eligible expenses including co-pays, annual deductibles and other co-insurance charges that are not covered under the High Deductible Health Plan policy and which were previously paid out of pocket.

What happens if you don't use all of the accumulated contributions to your HSA account? The unused balance and accumulated earnings can be used to pay for long-term care insurance, medical expenses during a period of unemployment or after retirement, and even to pay medical expenses of a surviving spouse. Distributions used to make these payments will not be considered to be taxable income. Withdrawal of amounts which are not used for qualified medical costs or expenses are subject to income tax (and also a federal penalty of 10% of the amount withdrawn if the owner is under age 65).

HSAs are portable and are not tied to any employer. An HSA moves with the individual and can be used for qualified medical purposes regardless of employment status, even if you are unemployed or retired. In fact, an eligible individual may set up his or her own HSA regardless of if the individual is self employed, unemployed, retired or an employee of another company. The only qualifications are that the individual must be age eligible and must have a HDHP insurance policy and may not be covered under any other health policy.

Most larger health care providers are now offering HDHP policies which are HSA eligible. Unfortunately, we are not aware of many custodians who offer HSA plan options. None of the traditional low cost IRA custodians and trustees such as national banks, savings and loans or major brokerage houses is currently offering HSA accounts. We expect this to change momentarily but it remains a consideration for the time being.

While the IRS has not yet issued regulations with respect to the new legislation, IRS Notice 2004-2 provides some guidance on establishing and operating Health Savings Accounts. This notice can be found at <http://www.irs.gov/pub/irs-drop/n-04-2.pdf> and is in PDF format for easy downloading.

Now may be a good time to explore the advantages and disadvantages of an HSA. However, RINA recommends caution until some significant details become clearer. Until larger, well established custodians and trustees can be

found and until the state of California conforms to the HSA legislation and IRS regulations are in place, we think that HSA implementation for companies should be postponed. It is highly likely that complete implementation packages will be available for companies who would like to start offering this option as of January 1, 2005.