AMI Investment Management
Registered Investment Advisor

View from the Portfolio Manager's Desk

Health Savings Accounts – Frequently Asked Questions

January 2019

Michael D. Axel, CFA

Jacob D. Benedict, CFA

Ryan A. Kay, CFP®

What is a Health Savings Account?

- Health Savings Accounts (HSAs) were established by Congress in 2003 to help individuals save for medical expenses.
- While not often thought of as a common vehicle for retirement planning, an HSA has significant benefits and can be a very efficient investment tool if used properly.
- HSAs can be opened at a variety of financial institutions, including banks, credit unions, and insurance companies.
- HSAs are not to be confused with FSAs (Flexible Spending Accounts). FSAs have a "use it or lose it" provision requiring the owner to use the money during the same year they contribute it, with the exception of some plans that allow up to $500 to be rolled over to the following year

What are the rules?

- An HSA is intended to be an account used to save money for medical expenses. When used as such, these accounts are completely tax-free.
- There are no income limits for HSA eligibility.
- To open an HSA, you must be covered by a high-deductible health plan. This is a health insurance plan that only covers you *after* you pay a deductible out of pocket.
- For 2019, a high-deductible health plan is one that requires you to pay a minimum deductible of $1,350 for individual coverage or $2,700 for family coverage.
- If your plan has individual coverage, there is a limit of $3,500 for contributions to an HSA in 2019, or $7,000 for a plan with family coverage.
- For those over age 55, a catch-up provision increases those limits by $1,000.
- Some employers might offer contributions to your HSA as a benefit; these employer contributions still count toward the aforementioned limits. If you leave the employer, the account will remain under your control, even if the employer made contributions.
- Of course, HSA withdrawals must be used for medical expenses to avoid penalty
    - For non-qualified withdrawals, there is a 20% penalty, in addition to being taxed at your ordinary rate.
    - At age 65, the 20% penalty goes away, and withdrawals are simply taxed at your ordinary rate (like a Traditional IRA).
    - Most healthcare services, medication, and equipment is qualified, although health insurance premiums are not.

What investments are available?

- Money contributed to a Health Savings Account may often be placed in FDIC-insured savings accounts, but that is not the only way to invest the funds.
- Many companies that offer HSAs also offer other investment vehicles (such as mutual funds) that may enable you to have exposure to stocks and bonds.

Why are HSAs attractive investment accounts?

- The efficiency of HSAs lies in the tax treatment of the funds:
    - HSAs are funded with pre-tax dollars.
    - Income and gains are not taxed when used for medical expenses.
    - Funds are not taxed upon withdrawal so long as they are used for medical expenses for you, your spouse, or your dependents.

Reproduction or distribution of this material is prohibited and all rights are reserved.

- When HSAs are used for medical expenses, they are more advantageous than other retirement accounts, such as Traditional or Roth IRAs
    - Traditional IRAs are taxed when money is withdrawn.
    - Roth IRAs are funded with after-tax dollars.
    - When HSAs are not used to pay for qualified medical expenses, the account essentially becomes the same as a Traditional IRA at age 65.
- Another advantage of HSAs is that you are allowed to reimburse yourself for medical expenses from previous years
    - For example, if you paid $1,000 out of pocket ten years ago in medical expenses, you could withdraw that amount from your HSA today, tax-free.
    - You may reimburse yourself if the medical expense:
        - Was originally paid out of pocket.
        - Was not reimbursed from another source.
        - Was not claimed as an itemized deduction.
        - Occurred after the HSA was established.
        - Can be documented.
    - Depending on your situation, this may enable you to pay medical expenses out of pocket, and leave money growing in your HSA account to be withdrawn later.
- HSAs can provide an additional retirement savings strategy for high-income earners who already max out their IRAs and/or 401(k)s.

How can I make these advantages work for me?

- Contributing to an HSA and allowing it to grow as much as possible during the course of your life can provide you with several options in the future
    - Withdrawing the funds tax-free to pay for Medicare premiums and additional out of pocket expenses once you reach age 65.
    - Withdrawing the funds tax-free to pay for other medical expenses that may arise, which commonly increase over time.
    - Withdrawing the funds tax-free to reimburse yourself for prior medical expenses you previously paid out of your own pocket.
    - If need be, you can withdraw funds from your HSA at your ordinary tax rate once you reach age 65. Since the penalty no longer exists at that age, this is just like a Traditional IRA withdrawal.
- These are just a few ways to use an HSA to your advantage. There are plenty of strategies that can fit into your financial plan and, most importantly, minimize the taxes you pay.

How can AMI help me with an HSA?

- The investment professionals at AMI have experience dealing with HSAs and do so as a service to our clients.
- We can walk you through the basics of HSAs, whether it be opening an account, picking an investment strategy, or withdrawing funds.
- We can also help you determine how an HSA might fit into your personal financial plan as a whole.
- If you are part of a high-deductible health plan and want to see if your HSA might be a useful retirement planning tool, please call us to discuss.

Past performance is no guarantee of future performance. All investments contain risk and may lose value. Any views expressed within this document are the views of AMI Investment Management and/or the authors. They are subject to change at any time without notice. Any graphs, charts or formulas included within this document that depict historical relationships may not be valid during future periods and should not be relied upon to make investment decisions. This material is distributed for informational purposes only and should not be considered as investment advice or as a recommendation of any particular investment security, strategy or investment product.