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Brown & Brown

HSA Compliance: A Deep Dive into the Rules Surrounding HSAs

Presented By:
Regulatory & Legislative Strategy Group

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Health Savings Account (HSA)

What is an HSA?

Tax-exempt trust or custodial account owned by the individual

What is it for?

May be used for eligible medical expenses of the individual, and the individual’s spouse and dependents

Are there any special requirements?

Must be covered by a high deductible health plan (HDHP) as defined by law, and not be enrolled in any disqualifying coverage

HSA Eligibility

WHO IS ELIGIBLE TO ESTABLISH AND CONTRIBUTE TO AN HSA?

Anyone who is:

- Covered by an HDHP
- Not ***enrolled*** in Medicare
  - » Watch out for retroactive enrollment (which can be up to 6 months) due to events like the start of Social Security distributions
- Not covered under other non-HDHP insurance or health plan
  - » Examples:
    - – General-purpose Health FSA
    - – General-purpose HRA
    - – Medicare/Medicaid
    - – TRICARE
- Not a tax dependent of another individual

Disqualifying coverage does not include separate dental plans, separate vision plans, specific disease or illness insurance, accident and disability insurance and long-term care insurance.

Other Coverage Issues

On-site Medical Clinics

If an individual receives medical benefits (or has the ability to receive medical benefits) at no-cost (or below fair-market value cost) to the employee, this coverage disqualifies the individual from contributing to an HSA

EAPs

If an individual can receive significant medical benefits at no cost (or below fair-market value cost), the availability of the EAP will disqualify the individual from contributing to an HSA

Telemedicine and HSA Eligibility

FIRST DOLLAR COVERAGE FOR TELEMEDICINE

Background

- Availability of telehealth benefits typically makes an employee ineligible to make or receive HSA contributions

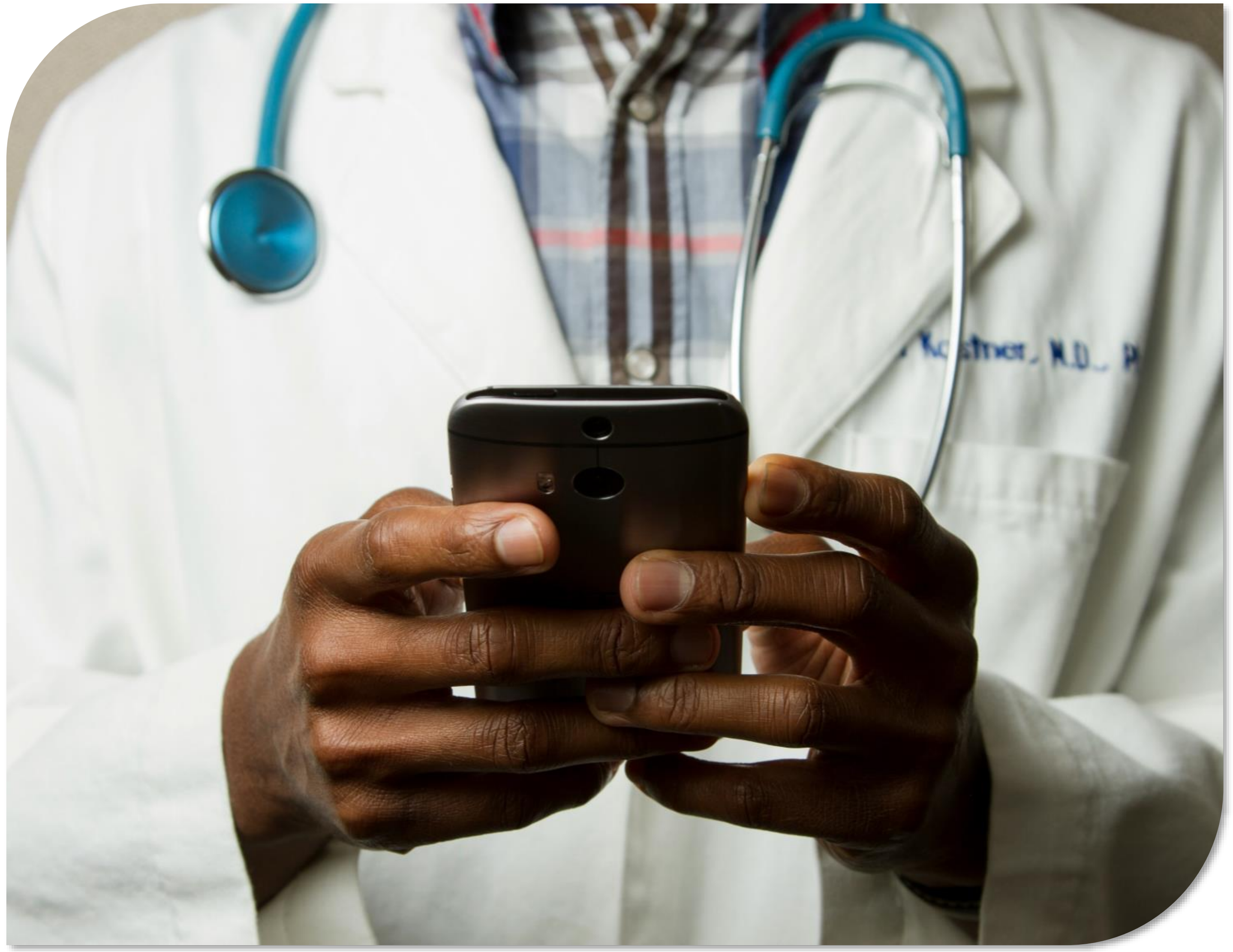
- Employers with HSA programs that also offer telehealth benefits previously (whether through the HDHP or through a stand-alone telehealth benefit) needed to either:

    1. Limit the telehealth benefits available to HDHP enrollees to preventive care until the deductible is satisfied; or

    2. Charge HDHP enrollees who use telehealth services (other than for preventive care) a fee equal to the fair market value of the care until the deductible is satisfied.

Telemedicine and HSA Eligibility

FIRST DOLLAR COVERAGE FOR TELEMEDICINE



CARES Act Amendment

- CARES Act amendment to Section 223 (March 2020)
  - » Applicable for plan years beginning before 1/1/22
  - » Coverage for "telehealth and other remote care" is disregarded when determining whether someone is eligible for HSA contributions
  - » A group health plan will not fail to be an HDHP solely because it provides coverage for "telehealth and other remote care" before the satisfaction of the minimum deductible
  - » No limit in legislation on types of care that may be received as part of "telehealth and other remote care"

First Dollar Coverage for Telemedicine

CAA of 2022

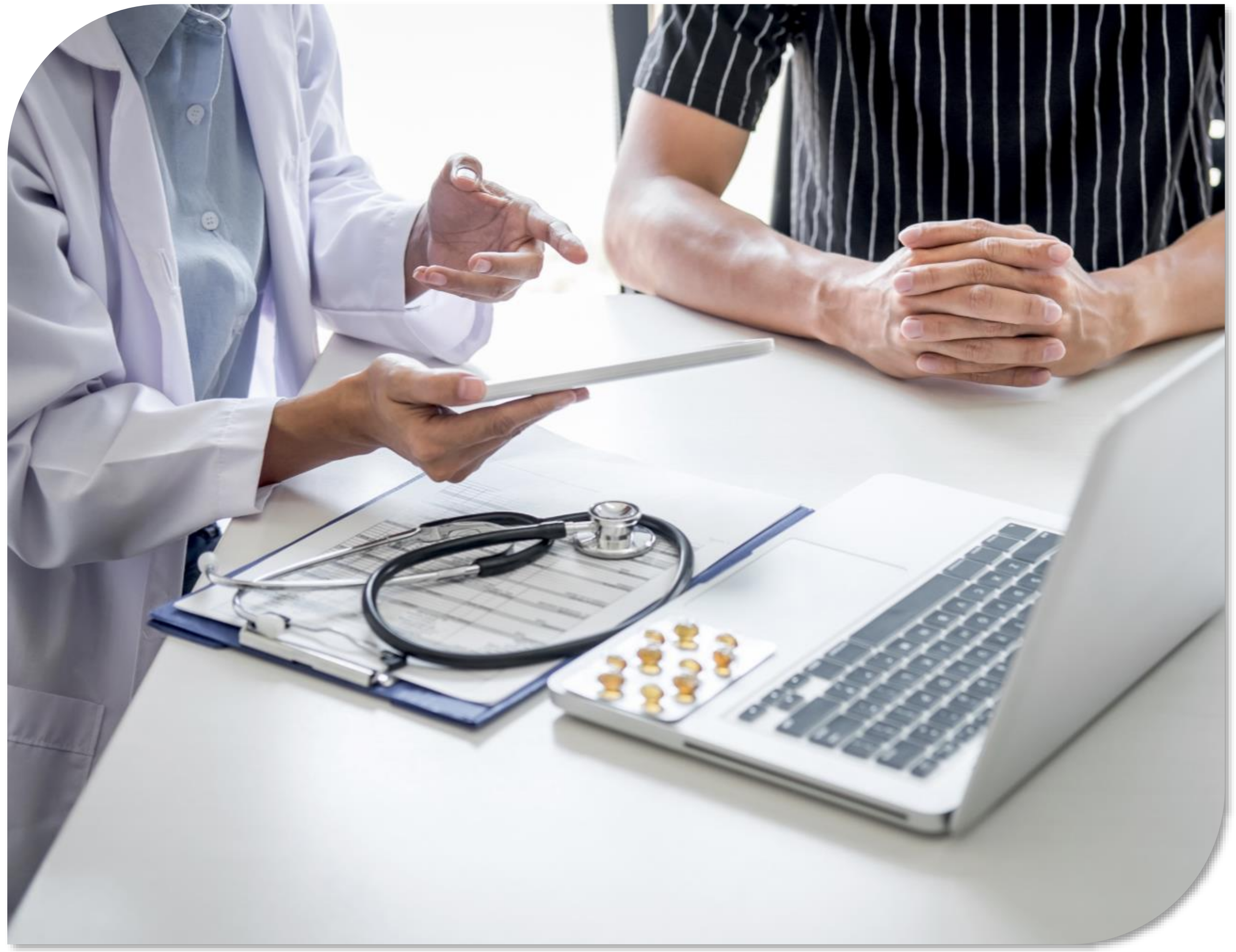
- Extended CARES Act relief
- Applies during the period of April 1 through December 31, 2022
  - » Note: Potential gap between 12/31/21 and 4/1/22

CAA of 2023

- Enacted on December 23, 2022
- Extends CARES Act and CAA of 2022 relief
- **Applies during plan years starting on or after January 1, 2023, and before January 1, 2025**
  - » Note: Potential gap between 12/31/22 and first day of 2023 plan year
- Relief is permissive: employers adopting relief must amend applicable plan documents to incorporate changes along with plan years(s) to which the relief will apply

Telehealth Expansion Act of 2023

- Proposal to permanently extend relief
- Introduced in the House and Senate 3/28/23



High Deductible Health Plan (HDHP)

Self-Only Coverage

For 2024, self-only HDHP coverage must have an annual deductible of $1,600 and an out-of-pocket maximum of no more than $8,050

Family Coverage

For 2024, family HDHP coverage must have an annual deductible of $3,200 and an out-of-pocket maximum of no more than $16,100

ACA Impact on HSAs

HSA QUALIFIED HDHP OUT-OF-POCKET MAXIMUM INTERACTION WITH THE ACA'S OUT-OF-POCKET MAXIMUM

HSA qualified HDHP out-of-pocket maximums for 2024

- Self-Only Coverage = $8,050
- Family Coverage = $16,100

ACA out-of-pocket maximums for 2024

- Self-Only Coverage = $9,450
- Family Coverage = $18,900

HHS final rule states that the annual limitation on cost-sharing for essential health benefits for self-only coverage applies to all individuals regardless of whether the individual is **covered by a self-only plan** or is covered by a plan that other than self-only

HDHP's must embed self-only ACA maximum out-of-pocket (MOOP) for family HDHP coverage even if the family HDHP maximum out-of-pocket is greater

Under a Family HDHP, no single individual can incur a MOOP greater than $9,450 because of the ACA limits

Example: Employee A elects family HDHP coverage in 2024 and incurs $10,000 in hospital expenses. Cost-sharing for Employee A will be limited to $9,450 (the ACA limit on cost-sharing for self-only coverage). The plan must cover the difference between the incurred expense and the ACA limit.

HSA Contributions

High Deductible Health Plan

MAXIMUM ANNUAL HSA CONTRIBUTION

Self-Only Coverage

2024 Maximum contribution = $4,150

Family Coverage

2024 Maximum contribution = $8,300

“Catch-Up” Contributions

Age 55 and older
by the end of the tax year = $1,000

Source of Contributions

Employer, or employee, or both
(or anyone else)

Determining Maximum HSA Contribution Limit

TWO METHODS

Prorated (Monthly) Maximum Contribution Method

- Will depend on number of months individual is HSA-eligible
- Individual eligible to contribute up to 1/12th of applicable annual maximum for each month they are HSA-eligible
- Example: Employee A enrolled in self-only HDHP for 5 months of the year and is only HSA-eligible for those 5 months.
  - » $4,150 (2024 self-only maximum) / 12 months = $345.83 a month
  - » $345.83 a month x 5 months = $1,729.15 annual maximum contribution
- Individual may make contributions until 4/15 of the following year up to the prorated limit even if not eligible during the particular month.

Special Contribution Rule

LAST "MONTH" RULE

"

An individual may contribute the entire annual limit when first eligible for an HSA as long as they are eligible on the first day of the last month of the tax year (December 1 for most individuals) and they remain HSA eligible for the next 12 months of the following tax year.

- This also applies when an employee switches from individual to family coverage
- If the employee is enrolled in the family tier as of December 1 of the applicable year and remains HSA eligible until December 31 of the following year, the individual is eligible to contribute up to the family maximum for the applicable year
- However, if an individual joins mid-year and contributes the maximum amount to their HSA, they must remain eligible for at least 12 months after the last day of the last month of that tax year (December 31 for most taxpayers), or they will be subject to taxes and penalties on the excess contribution.

Mid-Year Change from Family to Single HDHP

WHAT IS THE MAXIMUM ANNUAL CONTRIBUTION?

Employee that enrolls in family coverage as of January, but later changes to single coverage in September (2024 amounts):*

9/12 x $8,300 = $6,225
(rounded to nearest dollar)

3/12 x $4,150 = $1,038
(rounded to nearest dollar)

Maximum Contribution Limit
$6,225 + $1,038 = $7,263

*Don't forget the full contribution rule for changes from single coverage to family coverage

Multiple HSAs in the Family: Spouses

- If both spouses of a married couple are HSA eligible, and either spouse is covered by family HDHP coverage (other than self-only coverage), then both are treated as having family HDHP coverage and must divide the total family maximum annual contribution amount among the spouses
  - » They may allocate contributions between them per the spouse’s agreement
  - » Catch-up contributions are allocated separately to each spouse that is age 55 or older. Therefore, a spouse that is not age 55 or older cannot make a catch-up contribution amount into their own HSA even though they may be married to a spouse who is age 55 or older.

HSAs: Adult Dependents and Domestic Partners

- The division of the annual maximum contribution amount between married spouses does not apply to adult dependents (that are not claimed as a tax dependent on the employee's tax returns) or domestic partners of an employee
  - An adult dependent or domestic partner that is participating in a family HDHP can generally contribute the full amount allowed for family coverage into their own HSA

HSA Corrections

MISTAKES HAPPEN

What happens when ineligible contributions are made to an HSA?

- The IRS appears to differentiate between contributions that were never eligible and those that later lose eligibility

For those that were never eligible:

- No tax deductions for individual contributions
- No tax exclusions for employer contributions
- Corrections required for income reporting and tax withholding
- Employer contributions can be recovered

For those that lose eligibility:

- Curative distributions can be used if excess contribution and net income attributable to an excess contribution are distributed before the account holder’s federal income tax return filing deadline
  - » One issue: Employers generally must rely on employees to refund an employer’s excess contribution because the contributions are considered non-forfeitable

HSA Corrections

MISTAKES HAPPEN

What about contributions in excess of the statutory maximum or contributions made due to an administrative error?

- Curative distribution can be used if excess contribution and net income attributable to an excess contribution are distributed before the account holder’s federal income tax return filing deadline

- If the employer made the excess contribution or a contribution as a result of an administrative error, the employer may seek to recoup the erroneous contributions directly from the HSA administrator

Qualified Medical Expenses

HSA Funds

HSA funds may be invested and can grow on a “tax-qualified” basis

- Funds can roll over from year-to-year and an individual can keep the money even if they change jobs
- Investment options often include a minimum amount

Claims are “Self-adjudicated”

- Individuals should save receipts in case of an IRS audit

HSA funds may be used for “qualified” out-of-pocket medical expenses (generally not medical premiums)

- Code 213(d) – medical expenses incurred by the employee, spouse and/or dependents
- Dependent is a child to age 19, or age 23 if they are a full-time student
  Note: This is different from the medical plan coverage definition of dependent that health FSAs are subject to

Qualified Medical Expenses

EXAMPLES

- Most medical care that is subject to a deductible
  - Copays
  - Coinsurance
  - Doctor visits
  - Inpatient or outpatient treatment
- Prescription and OTC drugs
- Insulin (with or without a prescription)
- Dental and vision care
- Select insurance premiums:
  - COBRA
  - Qualified long-term care insurance
  - Health insurance premiums paid while receiving unemployment benefits
  - Health insurance after an individual turns 65 except for a Medicare supplemental policy

Non-Qualified Medical Expenses

EXAMPLES

- Insurance premiums (other than the exceptions listed on the previous slide)
- Surgery purely for cosmetic reasons
- Expenses covered by another insurance plan
- General health items such as tissues, toiletries and hand sanitizer

HSA Distribution Rules

TAX QUALIFIED

- HSA distributions may only be taken for qualified medical expenses
  - Non-qualified expenses will be subject to ordinary income taxes and be subject to an additional 20% penalty
- HSA distributions can only be applied to expenses incurred on or after the date the HSA was established
- May use HSA funds for expenses incurred in a prior year if the HSA was established on or after the date the expense was incurred

Distributions for non-qualified expenses for **age 65 or older**: ordinary income taxes will apply but the 20% penalty would not apply.

Interaction with Health FSAs and HRAs

Interaction of Health FSAs with HSAs

HEALTH FLEXIBLE SPENDING ARRANGEMENT (HEALTH FSA)

- A general-purpose health FSA will reimburse all otherwise unreimbursed, out-of-pocket 213(d) (medical) expenses (except for individual premiums)
- Generally, a health FSA provides for reimbursement of medical expenses prior to an individual satisfying their IRS minimum deductible for an HDHP. Therefore, the health FSA is generally considered disqualifying coverage for HSA purposes
- Typically, a health FSA will also provide reimbursement for the medical expenses of a spouse and dependent child
  - This means an employee’s enrollment in a health FSA could also cause a spouse to be ineligible to contribute to their HSA

Health FSA Grace Period Impact on HSAs

HEALTH FLEXIBLE SPENDING ARRANGEMENT (HEALTH FSA)

- The health FSA may a have grace period of up to 75 days (2.5 months) following the end of the plan year
- Claims incurred during the grace period may be reimbursed from the prior plan year funds (if available)
- For a calendar-year health FSA: If it is a “general purpose” health FSA, the covered individual will not be HSA-eligible until April 1 (assuming the grace period is the full 75 days) if there are any funds remaining in the FSA as of the last day of the plan year, as determined on a cash accounting basis
    - If there’s a $0 balance on the last day of the plan year, an individual would be eligible to contribute to an HSA during the grace period

The individual could contribute 9/12ths of the annual maximum – unless the individual follows the “last month” rule.

Health FSA Grace Period Impact on HSAs

DESIGNING AN HSA COMPLIANT GRACE PERIOD

- The plan may be amended (before the end of the plan year) to provide that during the health FSA grace period, employees may only seek reimbursement of limited purpose healthcare expenses (e.g., dental and vision care expenses) incurred during the grace period
    - » This must apply to all health FSA participants, not only those enrolling into the HDHP

- Other options could include automatic termination of health FSA participation after the end of the plan year

Interaction of Health FSAs with HSAs

DESIGNING AN HSA COMPATIBLE HEALTH FSA

Limited Purpose Health FSA

A health FSA that only provides reimbursement for dental and vision expenses

Post-Deductible Health FSA

A health FSA that only provides reimbursement of health care expenses after the employee satisfies their HDHP minimum annual deductible

- The health FSA could track an employee's cumulative satisfaction of the HDHP minimum deductible or could be designed to pay after the minimum statutory deductible is satisfied

Health FSA Carryover Impact on HSAs

HEALTH FLEXIBLE SPENDING ARRANGEMENT (HEALTH FSA)

The health FSA may include a carryover of up to $640 (indexed for inflation) into the following plan year

- The carryover amount is available to the individual for the entire following plan year

If the health FSA is "general purpose" (will reimburse all otherwise unreimbursed out-of-pocket-medical expenses), the covered individual will not be HSA-eligible for the entire plan year

- Because the health FSA provides coverage before the minimum HDHP deductible has been satisfied

Some employers allow participants to waive their carryover to avoid this issue

The health FSA may also be amended (before the end of the plan year) to provide conversion of carryover funds into a limited purpose health FSA

- Unlike the health FSA grace period, the carryover provision can provide the participant a choice of whether to carryover into a limited purpose health FSA or a general-purpose health FSA
- Also, the plan may provide that the carryover is automatically credited to a limited purpose health FSA if the individual elects the HDHP
  - » The health FSA may be amended (before the end of the plan year) to permit participants to suspend or waive carryover

Interaction of HRAs with HSAs

HEALTH REIMBURSEMENT ARRANGEMENT (HRA)

A health reimbursement arrangement (HRA) provides for reimbursement of 213(d) medical expenses

- 100% employer dollars
- Claims are typically paid from the employer's general assets

If the HRA is "general purpose" (will reimburse all otherwise unreimbursed out-of-pocket-medical expenses), the covered individual will not be HSA-eligible for the entire plan year

- Generally, the HRA provides coverage before the minimum HDHP deductible has been satisfied

Interaction between HRAs and HSAs

DESIGNING AN HSA COMPATIBLE HRA

Limited Purpose HRA

Provides reimbursement for dental and vision expenses only

Post-Deductible Health HRA

Provides reimbursement after the minimum annual deductible has been satisfied

- The HRA could track with the HDHP deductible or could be designed to pay after the minimum statutory deductible is satisfied

Retirement HRA

Provides reimbursement after the individual has retired and is no longer eligible to contribute to an HSA

HSAs and Cafeteria Plans

HSAs and Cafeteria Plans

PRE-TAX HSA CONTRIBUTIONS

- Employers may permit employees to make pre-tax contributions to their HSA accounts through an employer’s Section 125 cafeteria plan
  - » Employers are also permitted to make contributions to employee HSA accounts which may be excluded from income tax and FICA withholding if amounts are within the annual maximum contribution limit when combined with all other contributions to the account

Pre-Tax Election Changes

- Employers must allow employees to prospectively start, stop or otherwise change their pre-tax HSA elections at least once per month during the plan year

Nondiscrimination Rules

- Employer HSA contributions through the cafeteria plan will be subject to the Section 125 cafeteria plan nondiscrimination rules
- Rules prohibit discrimination in favor of highly compensated or key employees
  - » Contribution strategies that include contributing different amounts to different categories of employees should be closely monitored
- If a Section 125 plan fails nondiscrimination testing all benefits provided to highly compensated or key employees will be considered taxable income to those employees

HSAs and Ineligible Individuals

HSA-ELIGIBLE VS. CAFETERIA PLAN ELIGIBLE

Are owners, partners, and other self-employed individuals eligible to contribute to an HSA?

- HSA eligibility is distinct from cafeteria plan eligibility
  - An individual who is not eligible to participate in a cafeteria plan may otherwise be eligible to contribute to their HSA on a post-tax basis

HSA-eligible:

- Covered by an HDHP
- Not ***enrolled*** in Medicare
- Not covered under other non-HDHP insurance or health plan
- Not a tax dependent of another individual

Cafeteria plan: ineligible individuals

- Self-employed individuals
- Sole proprietor
- Partner in a partnership (general partners and in some cases limited partners)
- More-than-2% shareholder in S corporation
- Outside directors
- Members of LLCs and partners in LLPs generally cannot participate

HSA Contributions Outside the Cafeteria Plan

COMPARABLE CONTRIBUTION RULE

- Applies when employer does not permit employees to make pre-tax contributions to their HSA account through the employer's Section 125 cafeteria plan and the employer makes contributions to the HSA.
- Rules require employer contributions to be the same for all comparable participating employees
- May differentiate based on the following classifications only:
  - Based on HDHP coverage tier
    - Employer contributes $500 to all participants with single-only coverage and $1,000 to all participants with other than single-only coverage
  - Current active employees vs. former employees
  - Non-union employees vs. employees in collective bargaining unit
  - Full-time vs. part-time employees
- Prevents the employer from making matching contributions based on the employee's elections
- As previously noted, allowing employees to make their contributions through operation of the cafeteria plan will avoid the comparable contribution rules

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