

List of Guidance Relating to Health Savings Accounts

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The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 ("Medicare Reform Act") permits employers or individuals to establish a health care savings vehicle called a health savings account ("HSA"). HSAs are designed to coordinate with an employer's high deductible health care plan. This arrangement allows contributions to be used to pay for "qualified medical expenses," defined as amounts paid for medical care as defined in Code section 213(d).

The following requirements apply to HSAs:

- Only available for individuals who have high-deductible health plans ("HDHPs")¹ (HDHPs require at least a \$1,100 deductible (in 2007) for individual coverage and at least a \$2,200 deductible (in 2007) for family coverage).
- There is no income-related eligibility requirement.
- Contribution limit is \$2,850 for individual coverage (in 2007); \$5,650 for family coverage (in 2007).
- Employers may make tax-deductible contributions; employees may make salary reduction contributions to an HSA through an FSA or deductible contributions.
- Reimbursements can be limited to amounts already contributed.
- Funds distributed from the HSA are not taxed if they are used to pay for qualified medical expenses.

The IRS and Department of Labor ("DOL") have released a significant volume of guidance with respect to HSAs since 2004. More comprehensive information on HSAs can be found at <http://www.treas.gov/offices/public-affairs/hsa/>.

The following paragraphs offer a brief overview of guidance to date:

- **Basic Information.** In IRS Notice 2004-2, the IRS published a series of questions and answers which provides basic information about what HSAs are, who can have HSAs, how to establish them, and the basic rules for making contributions to

¹ Individuals who are enrolled in Medicare are not eligible to establish an HSA.

and taking distributions from HSAs. In addition, Notice 2004-2 provides the following clarifications about HSAs:

- Employer contributions to employee HSAs are not subject to FICA taxes;
 - Employees covered by an employer self-insured HDHP may establish an HSA;
 - Trustees or custodians of HSAs are not required to determine if withdrawals are used for medical expenses;
 - Existing IRA or Archer MSA trustees or custodians are automatically approved to be HSA trustees or custodians; and
 - Otherwise eligible individuals without earnings (including self-employed and unemployed individuals) may contribute to an HSA.
- Preventive Care. In IRS Notice 2004-23, the IRS provided guidance clarifying the types of preventive care that can be provided under an HDHP. Generally an HDHP cannot provide benefits before the deductible is satisfied, but there is a limited exception for preventive care benefits. This notice indicates that preventive care generally does not include treatment of existing conditions. However, it also provides a safe harbor list of preventive care benefits that can be provided under an HDHP, including:
 - Annual physicals;
 - Immunizations;
 - Screening services;
 - Routine prenatal and well-child care;
 - Tobacco cessation programs; and
 - Obesity weight-loss programs.
 - FAQs. Notice 2004-50 includes eighty questions and answers which provide basic HSA information and outline a number of specific issues raised by employers with respect to HSAs.² This guidance also provides transition relief for health plans that would otherwise qualify as an HDHP but for an annual deductible period which is longer than 12 months. Such a plan will be treated as an HDHP if the plan was in effect or submitted for approval to state insurance regulators on or before August 16, 2004.

² See <http://www.treas.gov/press/releases/reports/hsanotice200450072304.pdf>.

- Prescription Drug Benefits. Revenue Ruling 2004-38 clarifies the interaction of HDHP benefits with prescription drug benefits. In order to establish an HSA, an eligible individual must be covered by an HDHP and generally have no other health plan coverage that is not an HDHP. In Revenue Ruling 2004-38, the IRS stated that individuals covered by a health plan that provides prescription drug benefits before the minimum annual deductible of an HDHP has been satisfied may not make contributions to an HSA. However, under Revenue Procedure 2004-22, which was issued simultaneously with Revenue Ruling 2004-38, the IRS provided transition relief so that individuals who were covered under a plan that covered prescription drug benefits before the HDHP deductible was met were able to continue to be eligible to contribute to HSAs through the end of 2005.

- Coordination with FSAs and HRAs. In Revenue Ruling 2004-45, the IRS considered the effect of an individual participating in a flexible spending account ("FSA") or a health reimbursement arrangement ("HRA") on an HSA. Generally, a person covered by a health FSA or HRA that reimburses qualified medical expenses is not eligible to contribute to an HSA. However, this revenue ruling provides that individuals may contribute to an HSA while also covered by the following types of employer-provided plans that reimburse medical expenses:
 - Limited-purpose FSAs or HRAs which provide reimbursement for only certain permitted benefits, such as vision, dental or preventive care benefits;
 - “Post-deductible” FSAs or HRAs that provide reimbursements only after the HSA minimum annual deductible has been satisfied; and
 - Retirement HRAs that provide reimbursement only after an employee retires.

- Transition Relief:
 - *Notice 2004-43.* The IRS provided transition relief for health plans that were unable to qualify as HDHPs due to state laws that require plans to offer certain mandated benefits with no deductible or a deductible that is lower than the HSA statutory minimum. Under this guidance, any such plans in effect on January 1, 2004 will be treated as an HDHP until January 1, 2006. Notice 2004-43 was amplified in Notice 2005-83, which provided additional relief through December 31, 2006 for non-calendar year health care plans that have the state-mandated benefit non-qualifying deductible problem.
 - *Notice 2004-25.* The IRS provided transitional relief for individuals establishing HSAs on or before April 15, 2005. Such individuals may use HSA accounts to reimburse qualified medical expenses incurred prior to the establishment of the HSA, as long as these expenses were incurred after the later of January 1, 2004, or the first date of the month during which the individual first became eligible to participate in an HSA.

- Model Health Savings Account Adoption Agreements. The IRS has posted model documents that can be used as trust or custodial agreements for HSAs on its website.³
- DOL Enforcement Guidance. In Field Assistance Bulletin 2004-1 (April 7, 2004), the DOL provided enforcement guidance on HSAs to its field investigators.⁴ The guidance makes clear that ERISA will not apply to an employee's HSA even when the employer contributes to the account, as long as the employee's HSA was voluntarily established and the employer's involvement in the HSA is minimal. This guidance was clarified and supplemented by FAB 2006-02 (October 27, 2006).
- FSA “Grace Period” Plans. Notice 2005-86 provides guidance on the interaction between HSA contribution eligibility rules with the rules applicable to health FSAs utilizing the special benefit payment “grace period” exception to the “use it or lose it” rule permitted by Notice 2005-42. Specifically, Notice 2005-86 provides guidance on how a cafeteria plan document can be amended to enable a health FSA participant to become HSA eligible during the grace period.
- Contributions by Spouses to HSAs. Revenue Ruling 2005-25 clarifies the contributions that spouses can make to HSA accounts where one spouse has HDHP coverage and the other has either non-HDHP coverage or no health care coverage.
- HSA Comparability Regulations. On July 31, 2006, the IRS issued final regulations on the requirement that employer contributions to HSAs be “comparable.” If employer contributions are not comparable, the employer must pay an excise tax equal to 35% of the aggregate amount contributed to the HSAs of its employees during the calendar year of the contributions.
- Rollovers from FSA or HRA into HSA. Notice 2007-22 provides guidance on how employees can rollover their health FSAs and HRAs into HSAs. Employers can amend their health FSAs or HRAs to permit a one-time rollover to an HSA by 2012. Notice 2007-22 also includes a special transition rule for transfers for 2006.

³ See <http://www.treas.gov/offices/public-affairs/hsa/forms/>

⁴ See http://www.dol.gov/ebsa/regs/fab_2004-1.html.