Webinar Title Q&A – the following questions were asked during the two- Introduction to Health Savings Accounts (HSA) webinar sessions in January 2018

Q: On slide 29, if someone over-contributes and can remove the excess funds, how do they remove it without it being considered a normal distribution or medical usage and reported by the trustee? Does this have to be worked out with the trustee?

A: The distribution of the excess contribution is not taxed, but the excess contribution must be included in the taxpayer's gross income because it is not deductible. You avoid the 6% excess contribution penalty if the withdrawal happens before the taxpayers' income tax filing deadline. The taxpayer should notify the HSA trustee/custodian of the excess contribution and request a distribution of the excess amount and it is considered attributable earnings (the earnings will be taxable). The trustee/custodian will report the distribution on Form 1099-SA coded as an excess contribution.

Q: The dependent over age 26 can also contribute up to the family max?

A: If an adult child is not an income tax dependent of the parent and they are covered under the parent's qualified HDHP, they can open their own HSA and are able to contribute the family maximum based upon the fact that they are covered under a family HDHP. What the adult contributes to their own HSA **will not** count against what the parent can contribute. So it is possible for the parent to have an HSA contribute the family limit and the adult child can have an HSA and contribute up to the family maximum.

Q: We have a current client with the Rx issue waiving the deductible and participating in an HSA. What are the best next steps now that we know it's disqualifying?

A: According to IRS §223, you cannot have any first dollar medical coverage other than preventive care or excepted benefits (restricted to dental and vision coverage). So the RX cost must go towards the deductible on the major medical plan for at least the minimum required deductible amount ($1,350 Single or $2,700 Family) to be considered an HSA qualified plan.

Q: We have employees turning 65 this year. If they waive Medicare and continue on our HDHP can we as the employer continue to contribute to their HSA? Can they as the employee continue to contribute after turning 65?

A: If the employee is not enrolled in any part of Medicare (Part A, B, C or D), they will be HSA eligible and can continue to contribute to the HSA.

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Q: Would you please re-explain adult child rule age 26 and under?

A: If an adult child is not an income tax dependent of the parent and they are covered under the parent's qualified HDHP, they can open their own HSA and are able to contribute the family maximum based upon the fact that they are covered under a family HDHP. What the adult contributes to their own HSA **will not** count against what the parent can contribute. So it is possible for the parent to have an HSA contribute the family limit and the adult child can have an HSA and contribute up to the family maximum.

Q: As long as your child (under age 26) is a dependent you can pay for their expenses out of you HSA?

A: As long as your child is your income tax dependent, you can use HSA dollars tax free to pay for their expenses without penalty.

Q: I've learned that Tricare coverage is considered disqualifying coverage - given the # of individuals that may have this coverage; it may be worthwhile to include it as an example of 'disqualifying coverage.'

A: I agree, Tricare coverage does not meet the HSA qualified plan parameters. Thank you for bringing this up.

Q: Why are Medicare supplement premiums NOT an eligible HSA expense?

A: IRS §223 does not permit the use of HSA dollars tax free for Medicare supplement premiums.

Q: There was a question from a client that has a hospital income policy and that they should consider combine this with their HSA and talk to their tax advisor about tax implications? I am confused as to what they are asking them to do. What does one have to do with the other?

A: The hospital policy might be considered disqualifying coverage for purposes of HSA eligibility. So it really depends upon how the coverage is structured as to whether or not it would be considered first dollar coverage. Typically a hospitalization policy that pays a daily benefit and does not specifically cover the deductible on the health plan like a GAP policy should be ok, but I really cannot say with certainty without knowing the details of the policy.

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Q: A husband and wife work for same employer. Husband takes health insurance and spouse is covered under his plan. Employer offers HSA and contributes to it annually. Can the spouse also have her own HSA even though she isn't the one taking the insurance? Can employer contribute to her HSA also if she has one?

A: Yes, if the employer permits and they collectively do not exceed the family maximum contribution.

Q: Can you give more information on Owners access to HSA on their own? How would that work?

A: Any taxpayer enrolled in a qualified high deductible health plan (HDHP) can open and contribute to an Health Savings Account (HSA). For sole proprietors, partners in a partnership, members of a limited liability company, 2 % or greater shareholders in a Sub S Corporation and their family members by stock attribution rules, who cannot participate in a cafeteria plan, they can make contributions directly to a HSA custodian (i.e. bank) and take the tax deduction on their personal tax return at the end of the year. These owners can sponsor a cafeteria plan for their employees'; however, owners of the business types described here cannot take pre-tax payroll deductions to fund their HSAs under the cafeteria plan. They can make post tax deductions from payroll. HSAs deductions are an above the line deduction on the IRS Form 1040 and most state income tax returns at the end of the year.

Q: Slide 16 you stated there is a maximum deductible? I can understand a minimum, but not max!

A: This slide was attempting to illustrate that the deductibles in the example exceeded the minimum required deductible. However, in the second example the maximum out of pocket was exceeded because the deductible was so large.

Q: We missed a person that had a FSA account in 2017 and had a balance in the account as of Dec. 31st. They moved to a HDHP with an HSA account for 2018 and we the employer and the employee has started contributing into the HSA - what do we need to do now to correct the situation?

A: This depends upon if you had runout, grace period or rollover on your cafeteria plan. If you just have the standard runout where someone has three months (for example) to file claims incurred in the prior year, there is no HSA impact. The employee is HSA eligible on January 1st.

If you have the grace period, where the employee can incur expenses through March 15th of the following year, the employee is not HSA eligible until April 1st (1st of the month following the end of the grace period) even if the expenses they file during the grace period are attributable to the prior plan year.

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If you have the rollover, where an employee is permitted to rollover up to $500 to the next plan year, the employee is potentially not eligible for the HSA for the entire next plan year. If they use what would be their rollover dollars for expenses incurred in the prior plan year and file claims during the runout period, they delay HSA eligibility until April 1st.

So, if you have runout only and no grace period or rollover, there are no HSA issues and you can continue to fund the HSA.

If you have the grace period and the HSA eligibility is delayed to April 1st, technically the individual was not eligible to open the HSA until April 1st.

You should talk with the HSA custodian about reversing the dollars if the individual was never HSA eligible. You will have similar consequences if you have the rollover. If you are unable to reverse the HSA, the employee will need to understand that the expenses incurred prior to their true HSA eligibility date are not qualifying expenses for purposes of withdrawals from the HSA. Under the full contribution rule, they still may take advantage of the full annual contribution, as long as they remain HSA eligible through the testing period.

Q: If a spouse goes on Medicare a few years prior to the other spouse, can the spouse still on an HDHP still have their own HSA?

A: The spouse's enrollment in Medicare does not impact the employee's HSA eligibility so long as they have the coverage in their name and will be the individual funding the HSA.

Q: Do you know, if an employee waives Medicare Part A when first eligible, can they get it back, later, without a penalty?

A: You will need to consult the Social Security Administration for help with this question.

Q: What is the dollar amount that is considered to be a "high deductible"?

A: The minimum deductible to be an HSA qualified plan is $1,350 Single or $2,700 as an aggregate for coverage other than single coverage. The deductibles can be higher than the minimum. Keep in mind that there cannot be any first dollar coverage for major medical expenses except preventive care. So there cannot be any co-pays for RX, Office Visits, ER until after the minimum required deductibles are met.

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Q: Greetings, my question is for the HSA, so if all the money is not used, it rolls over

A: Yes, if you have a balance in the HSA at the end of the year the amounts roll over from one year to the next.

Q: Our ERISA attorney is adamant that no nondiscrimination testing is required for HSA. Where is the legal substantiation that requires NDT?

A: Contributions to health savings accounts (HSAs) that are made through a cafeteria plan are subject to the Code §125 nondiscrimination rules. Consequently, such contributions must be taken into account for purposes of the Key Employee Concentration Test (as well as for the Eligibility Test and the C&B Test), creating one more bucket of benefits to consider.

Per IRS Notice 2004-50 Q/A 47

Q-47. If an employer makes contributions through a cafeteria plan to the HSA of each employee who is an eligible individual in an amount equal to the amount of the employee's HSA contribution or a percentage of the amount of the employee's HSA contribution (i.e., "matching contributions"), are the contributions subject to the section 4980G comparability rules?

A-47. No. The conference report for the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 states that the comparability rules do not apply to contributions made through a cafeteria plan. Conf. Rep. No. 391, 108th Cong., 1st Sess. 840 (2003). Notice 2004-2, Q&A 32 similarly provides that the comparability rules do not apply to HSA contributions made through a cafeteria plan. Thus, where matching contributions are made by an employer through a cafeteria plan, the contributions are not subject to the comparability rules of section 4980G. However, contributions, including "matching contributions", to an <u>HSA made under a cafeteria plan are subject to the section 125 nondiscrimination rules (eligibility rules, contributions and benefits tests and key employee concentration tests).</u> See section 125(b), (c) and (g) and Prop. Treas. Reg. § 1.125-1, Q&A 19.

Q: If an employer does not make employee contributions to HSA's, is the employer still subject to non-discrimination testing? Or is that only if there are employer contributions to employee HSAs?

A: All HSA contributions made through a cafeteria plan are subject to nondiscrimination testing. This would be true if the contributions are employee only, employer only or a combination of the two.

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Q: I have an employee who might be dropping our HSA HDHP plan mid-year and going on to her husband's plan who has a 7/1 plan year. Will she need to claim anything in excess of 6 months of prorated contributions of taxable income?

A: If she will not be enrolled in a qualified HDHP after 6/30 she is only eligible for a prorated annual maximum, she should review her contributions and make an excess contribution withdrawal to avoid the excess contribution tax if applicable.

Q: If an employee's spouse is eligible for Medicare Part A, and they have an employee +Spouse plan. What is their maximum HSA contribution?

A: If the employee continues to have an employee+ spouse plan after the spouse enrolls in Medicare, they are eligible to contribute up to the family maximum. The spouse cannot contribute to the HSA however.

Q: Do you agree that the IRS has not taken a position to consider a stand-alone telehealth product (with a $0 or $45 consultation) disqualifying coverage?

A: Agree that more guidance is needed in this area.

Q: Individuals turning 65 during the calendar year would need to prorate contributions for the year they turn 65. Correct? If so, what would be the impact if a spouse does not turn 65 during the same year?

A: The HSA accountholder will need to prorate their contributions in the year they turn 65 and enroll in Medicare. The contribution rule is based upon the accountholder. If the employee's spouse is not yet enrolled in Medicare and remains covered under a qualified HDHP, it may be possible for the spouse to open and contribute to an HSA in the spouse's name. It may be possible that they are already have an HSA open for the purposes of making the $1,000 catch up contribution that is permitted when you are over the age of 55.

Q: If employers contribute to employee HSA accounts and the employee is on FMLA leave, does the employer have to continue to make contributions, as they do with health care premiums?

A: The employer is only obligated to continue the health insurance plan during a FMLA. Technically the HSA is a bank account and not a health plan. However, the employer could choose to continue to make HSA contribution while the employee is on FMLA.

Q: Can an FSA account holder, who now wants to contribute to an HSA, be able to "change" their FSA account into a Limited Purpose FSA?

A: An individual cannot convert their regular Health Care FSA to a Limited Health Care FSA mid-cafeteria plan year because this is not a qualifying event. The employee can choose to enroll in the Limited Health Care FSA or decline enrollment in the Health Care FSA during open enrollment for the next cafeteria plan year. It is recommended that the cafeteria plan and the health insurance plan renew at the same time where possible for this reason.

Q: Post-deductible FSA - please explain what that is in more detail - when is it used and why

A: The Post-deductible FSA is structured so that it begins as a Limited Health Care FSA until the participant can show evidence that they have met the minimum required HDHP deductible (2017- $1,300 Single or $2,600 Family) and then the account switches from that point forward back to the regular Health Care FSA. This can be used in a cafeteria plan as an HSA compatible Health Care FSA.

Q: You can't contribute more to your HSA than your HDHP deductible – correct?

A: As long as your health plan has the required minimum deductible, you can contribute to full annual contribution permitted under the law. For 2018 that is $3,450 Single and $6,900 Family, plus any eligible catch up contributions. This would be true even if the deductible is $1,350 and $2,700 respectively.

Q: We know that having money in a traditional health FSA (not limited purpose) can cause issues, but I have received conflicting information on something. I have been told that you cannot open an HSA account at all until the money is spent down. However, I have also been told that you can open the account, but simply just not contribute until the FSA money is spent down, although your employer can (e.g. if the employer seeds the account with a contribution). Can you please confirm what is correct?

A: If you have a regular Health Care FSA with a traditional runout period that does not impact HSA eligibility. For example, if I have a regular Health Care FSA for the time period 1/1/18-12/31/18 and I have a claims runout period that lasts until 3/31/19, I will be HSA eligible on 1/1/19 even if I don't completely exhaust my 2018 Health Care FSA balance until 3/31/19. The claims runout is merely an administrative period to clean up paperwork for the prior plan year and all expenses must be incurred in 2018 in my example. This also assumes that I do not enroll in the regular Health Care FSA for 2019 or I opt to enroll in the Limited Health Care FSA.

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If you have the grace period, which extends the coverage period by 2 ½ months into the new plan year, whether or not you have a balance in your account on 12/31/18 will determine if the grace period is triggered and that will definitely have an impact on HSA eligibility. The grace period would delay your ability to open a HSA until after the grace period is over regardless of when you exhaust your FSA funds. That would include for purposes of the employer contributions as well as employee contributions.

Q: If you have a pre-tax payroll deduction for HSA contributions, can you change your pre-tax payroll deduction at any time during the year (and/or as many times as you want) as long as the total contribution doesn't go over the maximum?

A: The pre-tax election for the HSA contribution is not subject to the normal permitted election change rules of the cafeteria plan. The employee can change their election any time during the year, so long as the change is for a prospective payroll and does not cause them to exceed the annual limit.

Q: As an employer, we have a health FSA in place. If we put in place an HSA with a HDHP, do we need to get rid of the health FSA?

A: No. You can still offer a Health Care FSA, but any employee that elects the health FSA can't make HSA contributions. You can also add the Limited Health FSA that can be used by those that are enrolled in the HSA.

Q: Once no longer eligible for HDHP can the HSA account remain open, unused?

A: Yes. The HSA is a savings account and can be contributed to while eligible to make the contributions – just like a regular bank account gets opened and the account holder makes contributions for a period of time. Once the individual is ineligible to make HSA contributions, the account remains open, even though no contributions are being made, and can be used to pay for eligible expenses with tax free distributions.

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