



IRS ISSUES Q & A's ON HSAs

The IRS has just released Notice 2004-50, the final installment of guidance on the new health savings accounts (HSAs) authorized under the new Medicare law. The guidance consists of 88 questions and answers on a host of issues that may arise in connection with these accounts. Although it will take some time to sift through and evaluate the whole of the guidance, the following points are of interest.

- Employers may not exercise any control over contributions made to an HSA. This was apparently a contentious issue that employer representatives and the IRS could not agree on. The only guidance on employer contributions is that employers may not recoup any portion of their contributions to an HSA (e.g., there can be no recovery if the employee terminates employment soon after a contribution for the entire year was made). In addition, the IRS specifically states that an HSA trust or custodial agreement may not contain a provision that restricts HSA distributions to pay or reimburse the account beneficiary's qualified medical expenses – only the account beneficiary may determine how the HSA distributions will be used.
- Individuals may be covered under an EAP, disease management program or wellness program without jeopardizing their eligibility to participate in an HSA as long as the program does not provide significant benefits in the nature of medical care or treatment.
- Drugs or medications can be considered for preventive care when they are taken by a person who has developed risk factors for a disease that has not yet manifested itself or become clinically apparent, or to prevent the reoccurrence of a disease from which a person has recovered.
- There is no time limit on when a distribution must occur, other than the expense must have been incurred after the HSA was established. Thus, accountholders may wait until retirement to use their accounts. In order to be excludable from income, however, the beneficiary must be able to show that the distribution is exclusively for medical care that was not otherwise reimbursed or deducted as a medical expense.
- Employers may make matching contributions to an HSA through a cafeteria plan (i.e., the employee is given a choice between cash and the employer contribution) because they are not subject to the comparability requirements. However, in this case, the contributions, including matching contributions to the HSA, are subject to the Section 125 nondiscrimination rules.

- HSAs are generally not subject to the rules applicable to health FSAs under Section 125. Thus, for example, an HSA may be established at any time during a plan year.
- For purposes of the deductible for an HDHP created mid-year, amounts applied to the deductible in the previous health plan's short plan year may be taken into account.
- Long-term care insurance may be purchased through an HSA offered under a cafeteria plan.
- Fees for account maintenance paid from the account are not taxable distributions. If these fees are paid directly to trustees, they are not subject to the contribution limits.
- Permissible account investments include those permissible for IRAs (e.g., bank accounts, annuities, certificates of deposit, stocks, mutual funds, or bonds.)
- A Medicare-eligible individual that is not *enrolled* in Medicare may contribute to an HSA.

There are of course many more issues discussed in the IRS guidance. For example, there are extensive explanations of how high-deductible health plans can be designed to fall within the permissible range and the acceptable role of trustees and employers. We will be issuing a more comprehensive analysis of the guidance in a forthcoming *For Your Information*.

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