

Health Savings Accounts (HSAs)

Background

A Health Savings Account (HSA) is a tax-favored medical savings plan available to individuals and families covered by a high deductible health plan (HDHP). HDHPs appeal to employers because, in comparison with other plans, a larger portion of plan costs are paid by employees, thus allowing the employer to pay lower premiums to the insurer selling the plan. But HDHPs are unpopular with employees for the same reason. HSAs provide a tax subsidy to both parties. Employers gain the benefit of providing a financial benefit to employees which is not subject to employment taxes. Employees may effectively “itemize” medical expenses even if they use the standard deduction. Those expenses are not subject to the 10% AGI floor applicable to Schedule A medical deductions. Distributions from an HSA are nontaxable if they are used for qualified medical expenses. And employees may claim a deduction for HSA contributions in the current tax year in the expectation of using those funds for medical expenses to be incurred in future years.

Foundation Communities Policy

The IRS requires those VITA volunteer tax preparers who assist clients with HSAs complete the HSA specialty certification. VITA preparers may take the on-line Link & Learn HSA course and become certified upon passing the test. If no such certified preparer is available when an HSA client requires assistance, see your site manager for available options.

How To Assist Tax Clients

HSA clients may require proper tax reporting of four types of economic events:

Employer contributions to an HSA

These contributions may be excluded from gross income. Employer contributions to an employee’s HSA are indicated by the employee’s Form W-2. The W-2 will include a code W in box 12. As with all box 12 codes, tax preparers should enter the W code on the TaxSlayer W-2 screen. Doing so will prompt TaxSlayer to load a Health Savings Account screen (Form 8889). Employer contributions to an HSA are not deductible by the employee and should be entered only on the TaxSlayer W-2 screen. Never enter employer contributions on Form 8889.

Employee contributions to an HSA

Subject to various limitations, an employee may make optional contributions to an HSA from her own funds or funds provided by friends and family. These contributions can be used as an adjustment to income. In such circumstances, the HSA custodian may provide the employee with a Form 5498-SA, or the employee may self-report the contributions. Tax preparers should enter employee contributions on

the HSA screen. This screen can be found under: Federal Section>Deductions>Adjustments>Health Savings Account Form 8889.

Form 8889 - Health Savings Account

Form belongs to:

Taxpayer

Coverage under high deductible health plan *

Self-only

HSA Contributions

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HSA Contributions you made for 2016

* INCLUDE contributions made from Jan 1 to Apr 15 of this year that were for 2016.

* DO NOT INCLUDE employer contributions, contributions through a cafeteria plan, or amounts that were rolled over into your HSA(s).

Note: The following fields are Out of Scope: Archer MSA and Qualified HSA funding distributions.

Distribution of HSA funds to employee

An employee may request a distribution of funds from her HSA. The HSA custodian may provide the employee with a Form 1099-SA, or the employee may self-report the distributions. Tax preparers should enter HSA distributions on the HSA screen under total distributions. (see example below)

Employee use of HSA funds to pay for medical expenses

An employee may use distributed HSA funds to pay for qualified medical expenses, including the deductible portion of expenses paid for in part by an HDHP. Qualified medical expenses are those that generally qualify for a medical expense deduction on Schedule A. Distributions used for unreimbursed qualified medical expenses are tax free. Tax preparers should enter medical expenses on the HSA screen under distributions used for qualified medical expenses.

HSA Distributions

Total distributions received during 2016 from all HSAs.

(Usually shown in Box 1 of Form(s) 1099-SA)

600

Distributions used for qualified medical expenses

* If you do not enter an amount here your entire distribution will be considered taxable.

600

Distributions you received in 2016 that you rolled over into another HSA. Also include any excess contributions (and the earnings on those excess contributions) included above that were withdrawn by the due date of your return.

usual none

Exceptions - The additional 20% tax does not apply to distributions made after the account beneficiary dies, becomes disabled, or turns age 65.

Check here if you meet any of the exceptions to the 20% tax.

Note: HSA adjustments are normally out of scope.

Medical expenses in excess of those paid with HSA funds may be eligible for deduction on the client's Schedule A. HSA contributions remain in the account and are carried over from year to year until the client uses them. Any interest earned in the account is tax free. And an HSA is portable, so even if the client changes jobs or leaves the workforce, they may keep their HSA.