# ST20-14 Health Savings Accounts (HSA)

## Tax Law

### Overview

A health savings account (HSA) is a tax-favored medical savings account available to taxpayers. HSAs enable taxpayers to pay for current medical expenses and save for future qualified medical expenses on a tax-free basis.

Contributions are reported on Form 5498-SA issued by HSA trustee.

- Employer contributions are also shown on the employees W-2 in box 12 with code W.

Distributions are reported on Form 1099-SA issued by HSA trustee

An HSA is created by:

- Enrolling in a High-Deductible Health Plan (HDHP) and then
- Opening a tax-exempt trust or custodial account, with a qualified HSA trustee, to pay for qualified medical expenses

### References

- IRS Publication 969 Health Savings Accounts and Other Tax-Favored Health Plans
- IRS Instructions for Forms 1099-SA and 5498-SA
- IRS Instructions for Form 8889, Health Savings Accounts (HSAs)
- IRS Publication 4491 NTTC modified
- IRS Publication 4412 as modified by NTTC version 2a pages E6-E8.1
- NTTC Slide Deck 44 Health Savings Account
- NTTC HAS video series: AARP portal>search “online training guide”

### HSA Benefits

There are several benefits from having an HSA including the following:

- Amounts contributed to an HSA, except for employer contributions, can be used as an adjustment to income.
- Contributions to an HSA by an employer may be excluded from gross income; this includes contributions made through a Section 125 cafeteria plan.
- The contributions remain in the account and are carried over, without limit, from year to year until the taxpayer uses them.
- The interest and other earnings on the assets in the account are tax-free.
- Distributions will be tax-free if used to pay unreimbursed qualified medical expenses.
- An HSA is portable, so it stays with taxpayers even if they change employers or leave the work force.
- There is no deadline by which qualifying expenses must be reimbursed by HSA

### Individuals Who Qualify for an HSA

To be an eligible individual and qualify for an HSA, the taxpayer must meet the following requirements:

- Be covered by a high-deductible health plan (HDHP) on the first day of the month
- Not be covered by other health insurance (see Publication 969 for exceptions)
- Not be enrolled in Medicare (the individual can be HSA-eligible for the months before being covered by Medicare)
- Not be eligible to be claimed as a dependent on someone else’s tax return (applies even if the person can claim the individual but does not)

## Rules for Married Individuals

- In the case of married individuals, each spouse who is an eligible individual who wants to have an HSA must open a separate HSA. Married couples cannot have a joint HSA, even if they are covered by the same HDHP; however, distributions can be used to cover the qualified expenses of the other spouse.
- In the event of the death of one of the married individuals, the HSA will be treated as the surviving spouse's HSA if the spouse is the designated beneficiary of the HSA
- If either spouse has family HDHP coverage, the family contribution limit applies; both spouses are treated as having family HDHP coverage.
- If **both** spouses are 55 or older and not enrolled in Medicare:
  - Each spouse is entitled to increase his or her contribution limit with an additional contribution.
  - Their maximum total contributions under family HDHP coverage would include a catch-up contribution for each spouse
  - The contribution limit is divided between the spouses by agreement. If there is no agreement, the contribution limit is split equally between the spouses
  - Any additional contribution for age 55 or over must be made by each spouse to his or her own HSA.

Examples:

- Both spouses have single only coverage – Contribution limit /spouse = $3,550
- One spouse has single coverage
  Other spouse has family coverage – Total contribution limit = $7,100 split as agreed
- Same as above but one spouse over 55 – Total contribution =$7,100 + spouse over 55 can contribute an additional $1,000 to their plan.

## Contributions to HSA

- Any eligible individual can contribute to an HSA. For an employee's HSA, the employee, employer, or both may contribute to the employee's HSA in the same year. For an HSA established by a self-employed (or unemployed) individual, the individual can contribute.
- Family members or any other person may also contribute on behalf of an eligible individual. Contributions to an HSA must be made in cash. Contributions of stock or property are not allowed.
- Amounts contributed to an HSA, except for employer contributions and qualified HSA funding distributions from IRAs, can be used as an adjustment to income for the account owner

## Employer Contributions

- Employer contributions (including an employee's contribution through a cafeteria plan) can be made to an employee's HSA. Generally, employer contributions are excludable from an employee's income.
- Employer contributions are reported on Form W-2, Box 12 using code W
- Taxpayers must reduce the amount they, or any other person, can contribute to their HSA by the amount of any contributions made by the taxpayer's employer that are excludable from income. This includes amounts contributed to the taxpayer's account by the employer through a cafeteria plan. For example, in 2020, if the employer contributed $1,000 to a under 55 year old taxpayer's HSA who had a self-only HDHP, the remaining contribution limit would be $2,550.

## Health Savings Account (HSA) Contribution Limits for TY2020

The annual limit on deductions for HSAs is:

- $3,550 for self-only coverage younger than 55 at the end of the year
- $4,550 for self-only coverage older than 55 at the end of the year

- $7,100 for family coverage younger than 55 at the end of the year
- $8,100 for family coverage older than 55 at the end of the year
- If the taxpayer is an eligible individual on the first day of every month with the same coverage for the entire year, the full contribution amount is allowed.
- If the taxpayer was not an eligible individual for the entire year or changed his or her coverage during the year, the contribution limit is:
    - Last-month rule allows eligible individuals to make a full contribution for the year even if they were not an eligible individual for the entire year. They can make the full contribution for the year if:
        - They are eligible individuals on the first day of last month of their taxable year. For most people, this would be December 1, and — They remain eligible individuals during the testing period. The testing period runs from December 1 of the current year through December 31 of the following year (for calendar taxpayers).
        - TP will have to determine if they think they will be eligible for the entire following year. If they say yes and become ineligible, their return for that following year will be OUT OF SCOPE.
    - OR
    - Sum of the monthly contribution limits rule (use Limitation Chart and Worksheet in Form 8889 Instructions). This is the amount determined separately for each month based on eligibility and HDHP coverage on the first day of each month plus catch-up contributions. For this purpose, the monthly limit is 1/12 of the annual contribution limit, as calculated on the Limitation Chart and worksheet. A taxpayer who cannot use the last-month rule must use the sum of the monthly contribution limits rule to determine the maximum HSA contribution.

### HSA Contribution Timeframe

Taxpayers and employers can make contributions to the taxpayer's HSA until the filing deadline without regard to extension. If taxpayers were not eligible individuals for the entire year, they can still make contributions until the filing deadline without regard for extension, for the months they were eligible individuals.

### Distributions

Qualified medical expenses are expenses that generally would qualify for the medical and dental expenses deduction. Examples include unreimbursed expenses for doctors, dentists, and hospitals. A medicine or drug will be a qualified medical expense only if the medicine or drug:

- Requires a prescription
- After Dec. 31, 2019
    - Over-the-counter products and medications are now reimbursable without a prescription.
    - The cost of menstrual care products is now reimbursable

A taxpayer cannot treat insurance premiums as qualified medical expenses unless the premiums are for:

- Long-term care insurance based on premium limits as shown in IRS Pub 510.
- Health care continuation coverage, such as coverage under COBRA
- Health care coverage while receiving unemployment compensation
- Medicare and other health care coverage if the taxpayer was 65 or older (other than premiums for a Medicare supplemental policy, such as Medigap)

Qualified medical expenses are those incurred by the following persons even if it is a self only high deductible health plan:

- The taxpayer and spouse
- A dependents at the time the expense was incurred or paid
- Any other person who could have been claimed as a dependent on the taxpayer's return except that:

- The person filed a joint return or
- The person had gross income of the exemption amount ($4,300 in 2020) or more, or
- The taxpayer or spouse (if filing jointly) could be claimed as a dependent on someone else's tax return (child of divorced parents)

Taxpayers who have taken distributions will receive Form 1099-SA from trustee and **must provide it before a return can be completed.**

### OUT OF SCOPE

Refer taxpayers with these issues to a professional tax preparer:

- Excess contributions to an HSA that are not withdrawn in a timely fashion
- Qualified HSA funding distributions from an IRA
- Death of an HSA holder (when spouse is not the designated beneficiary)
- Additional Tax for Failure to Maintain HDHP Coverage
- Deemed distributions from an HSA due to prohibited transactions, such as using an HSA as a security for a loan
- Archer Medical Saving Accounts (MSA)
- Medicare Advantage MSA
- Health Reimbursement Arrangement
- Form 8889, Part III

## Reporting

**Before completing Form 8889, interview the client using the Screening Sheet for HSAs on page E-6 of the 4012.**

### Form 5498-SA

- Form 5498-SA shows the amount contributed during the year for any HSA.
- It includes both employer and employee contributions.
- In addition to being included on Form 5498-SA, employer contributions will also be shown on Form W-2, box 12, with code W.

**<u>Excess contributions are out of scope.</u>**

### Form 1099-SA

- Form 1099-SA reports distributions to a taxpayer.
- Box 5 will indicate whether the distribution is from an HSA, Archer MSA, or a Medicare Advantage MSA.
- The code in Form 1099-SA, box 3, identifies the distribution the taxpayer received. Code 1 is a normal distribution. Refer to Form 1099-SA for an explanation of the other codes.

### Form 8889, Health Savings Accounts (SAHSA)

- A taxpayer must file Form 8889 with Form 1040 if the taxpayer (or spouse if filing a joint return) had any activity in an HSA.. This is true even if only the taxpayer's employer or the spouse's employer made contributions to the HSA.
- Taxpayers who are filing jointly and who each have separate HSAs will each complete a separate Form 8889. Married taxpayers cannot have a joint HSA.
- Ask taxpayers during the interview process if their HDHP coverage is "self-only" or "family," and check the corresponding box on Form 8889

**Part 1**

- Form 8889, Part 1, is used to report all HSA contributions and to compute the allowable HSA deduction.
- The entry of code W and the amount in box 12 of Form W-2 will automatically go to Form 8889.
- The contribution limit is automatically adjusted for age by TaxSlayer.
- After all entries have been completed on Form 8889, the HSA deduction will be carried from Form 8889 to the Adjustments section of Form 1040, Schedule 1, Line 12.

**Part 2**

- Form 8889, Part II, is used by taxpayers to report distributions from an HSA.
- Form 1099-SA reports distributions to a taxpayer. Box 5 will indicate whether the distribution is from an HSA, Archer MSA, or a Medicare Advantage MSA. The code in Form 1099-SA, box 3, identifies the distribution the taxpayer received. Code 1 is a normal distribution. Refer to Form 1099-SA for an explanation of the other codes.
- If distributions are received for reasons other than qualified medical expenses, the amount withdrawn will be included in income and reported on Form 1040, Schedule 1, line 8 (Other Income). The additional tax on distributions not used for qualified medical expenses is 20%.Exceptions are if the account beneficiary:
    a. Dies
    b. Becomes disabled
    c. Turns 65(distributions after the TP 65th birthday)

This tax is computed on Form 8889 and reported on Form 1040, Schedule 2, Line 8.

- Taxpayers do not have to take distributions from their HSA each year.
- Amounts entered on Form 8889 are automatically carried over to the applicable lines of Form 1040. The amount of HSA distributions not used for qualified medical expenses will carry over to 1040, Schedule 1, line 8.
- Taxpayer have until April 15 to return excess distribution to the HSA without tax or penalty.

**NOTE 1 HSA distributions should NOT be included on Schedule A.**
**NOTE 2 HSA distributions should be included in the NJ medical. See the NJ section at the end of this document for qualifications.**

**Part 3**

Out of Scope

### Completing Form 8889

Top of Form – Check Taxpayer or Spouse

**Part 1 Contributions**

**Step 1** – Ask the taxpayer is their HSA is Self only or Family and select from the drop-down menu.

**Step 2** – Check box if you and your spouse have separate HSAs

**Step 3** – Enter all the employee's contributions including those made from 1/1/20 to 4/15/20. that were for 2018. If the taxpayer has not yet received Form 5498-SA, they need to tell you the amount of their contribution. Do not include employer contributions, contributions through a cafeteria plan, or rollovers.

Contributions to an employee's account through a cafeteria plan are treated as employer contributions and are not included here. These contributions are already pretax and should not be included as a adjustment to income on Form 1040, Schedule 1, Line 12. Generally, contributions included on this line are those made directly to the HSA custodian and are not shown on the W-2 as pre tax contributions

**Step 4** – Number of months TP or SP were eligible individuals. Use "Last Month Rule" or "Sum of monthly contribution limits rule" for partial year. See above.

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**Step 5** – Out of scope – If the taxpayer has an Archer MSA the entire return is out of scope

**Step 6** – Employer contributions for 2020. Employer contributions (including contributions through a cafeteria plan) include any amount an employer contributes to any HSA for the employee for 2018. These contributions should be shown in box 12 of Form W-2 with the code W. **Do not include amounts entered in the W-2, Box 12, Code W.** TaxSlayer will automatically pull the amounts from your W-2.

**Step 7** – Out of Scope – If TP has qualified Funding Distributions from IRA or Roth IRA, the return is Out of Scope

**Part 2 Distributions**

**Step 8** – Total distributions received in 2020. From form 1099-SA Box 1 with the HSA box checked. If the HSA box is not checked, the return is OUT OF SCOPE.

**Step 9** – Distributions received in 2020 that were used for qualified medical expenses. Use scratch pad to document.

**Step 10** - Distributions received in 2020 that were rolled over into another HSA. Also, any excess contributions and earning that were withdrawn by the due date of the return.

**Step 11** - Check if you meet exceptions to the 20% tax. Form 8889 Instructions page 6. Exceptions are:

- Account beneficiary dies
- Account beneficiary become disabled
- Account beneficiary turns 65

**Adjustments**

**Step 12**

Use the HSA Adjustment section for MFJ returns with family coverage when both spouses have separate HSAs. It is needed for a self only plan only when the plan coverage has changed during the year (e.g. family for part of the year and self only for part of the year. See the NTTC modified 4012-page E-8 for guidance.

# ST20-14 Health Savings Accounts (HSA)

## Form 8889 - Health Savings Account

CANCEL

Form belongs to:

- (•) Taxpayer
- ( ) Spouse

Step 1 – 8889 Line 1

Coverage under high deductible health plan. If you are no longer covered under a plan, please select your previous type of coverage *

Family

Step 2

☐ Check here if you and your spouse have separate HSAs.

### HSA Contributions

HSA Contributions you made for 2020

* INCLUDE contributions made from Jan 1 to Apr 15 of this year that were for 2020.
* DO NOT INCLUDE employer contributions, contributions through a cafeteria plan, or amounts that were rolled over into your HSA(s).

$ 2500

Step 3 -8889 Line 2

Number of months during this tax year that you were an eligible individual *

12

Step 4

Amount you and your employer contributed to your **Archer MSAs** for 2020 from **Form 8853**, lines 3 and 4. If you and your spouse had family coverage under an HDHP at any time during the tax year, also include any amount contributed to your spouse's **Archer MSA**.

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Step 5 Out of Scope

Amount to Adjust Employer Contributions made to your HSA(s) for 2020

We will automatically pull your employer contributions from your W-2. DO NOT enter amounts from your W-2.

$

Step 6

Qualified HSA Funding Distributions from IRA or ROTH IRA

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Step 7 Out of Scope

### HSA Distributions

Total distributions received during 2020 from all HSAs.

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

$ 1480

Step 8 – 8889 Line 14a

Distributions used for qualified medical expenses

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

$ 1280

Step 9 – 8889 Line 15

Distributions you received in 2020 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.

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Step 10 – 8889 Line 14b

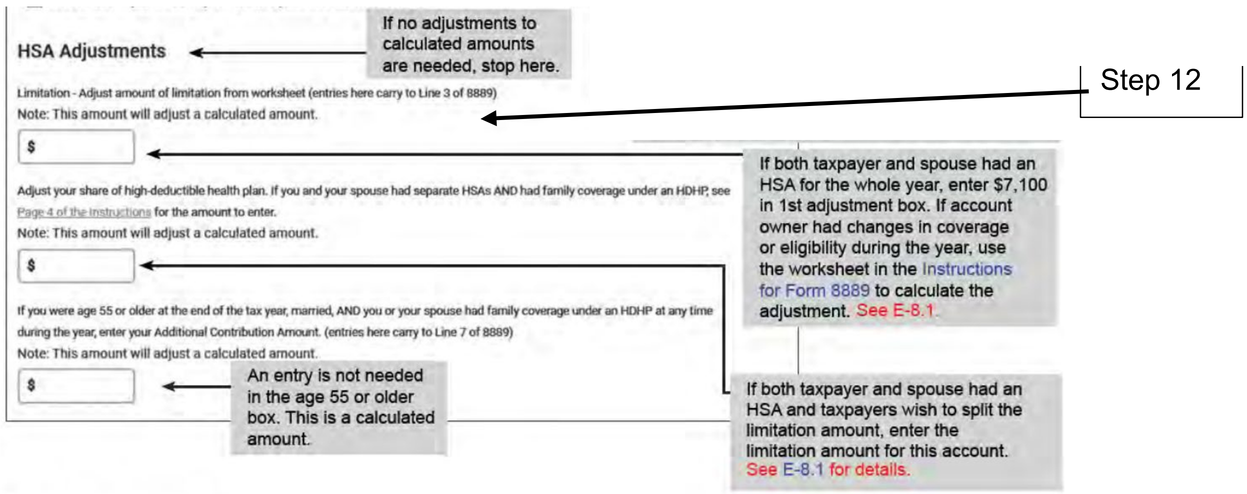
Exceptions - The additional 20% tax does not apply to distributions made after the account beneficiary dies, becomes disabled, or turns age 65.

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

Step 11 – 8889 Line 17a

# ST20-14 Health Savings Accounts (HSA)

**From Pub 4012 Page E-8**




**HSA for New Jersey**

Most of the tax benefits of an HSA do not apply to New Jersey.

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**Contributions (Form 5498-SA)**

- Contributions (Employer and Employee) are included in W-2 NJ box 16 and are taxed accordingly.

**Distributions (Form 1099-SA)**

- Because HSA distributions used for medical expenses are not reported on federal Sch A, they must be manually accounted for on NJ-1040 line 31. However, in TY 2020 allowable distributions for HSA are not the same as allowable medical expenses on Sch A or Line 31 on the NJ return. The following new HSA allowed items are not deductible medical expenses on the NJ return:
    - Over-the-counter products and medications without a prescription
    - Menstrual care products
- The amount of qualified distributions used for qualified medical expenses (8889 line 15 – Step 9 above) **less** over the counter products without prescriptions and menstrual care products are entered on the NJ checklist.
    - Enter on NJ Checklist - Subtractions from income – FSA/HSA distributions (qualified)
- Distributions from an HSA account that are not qualified distributions are entered as income on 1040, Schedule 1, line 8 (Other Income). TSO will pass the amount to NJ other Income line 26. Remove this income from the NJ return
    - Enter on NJ Checklist – Income subject to tax – Taxable Amount of Scholarships included on Federal Return – HSA distributions (NOT qualified) enter as a negative number