"Fake News" About Health Savings Accounts—Top 10 Myths

By Karin Rettger
https://myfinancialadvisor.org
MY FINANCIAL ADVISOR
A Division of Principal Resource Group

A Health Savings Account (HSA) is a tax-advantaged medical savings account available to you if you are enrolled in an HSA Eligible Health Plan (HSA HP). They help you accumulate pre-tax savings to pay for healthcare expenses, plus it can be used by you to supplement your 401(k) or other savings for retirement.

I have found that most people misunderstand HSAs, and do not recognize their benefits. I want to clear up some of these misconceptions. Understanding these common "fake news" statements about HSA's will help you make the most out of this valuable savings vehicle.

HSA Myth #1: FSAs and HSAs work the same way.

The short answer is no, and while we will not go in depth about the differences between the two tax codes, we can start by focusing on the "S." An FSA is Flexible Spending Account, while the HSA is a Health Savings Account.

With an FSA, you set up your payroll deduction for anticipated spending on out-of-pocket health care expenses for the current year. Once the deduction is set, you are not allowed to adjust it for the year. If the amount is not used by the end of the year, you lose that money*.

An HSA allows you to adjust your deduction at any time and any amount not used by the end of the year rolls over as savings into your account. It is designed for individuals to accrue savings for future unexpected expenses (including Medicare and long-term care premiums). If you can afford your day-to-day medical expenses, such as co-pays and over-the-counter medicine, your balance will accrue for these future expenses. You get the savings benefit of healthcare and anything you don't use gets invested into a retirement account. [See our article on FSAs vs HSAs to learn more about the differences between the two.]

Myth #2: My employer controls my HSA.

False! Once your funds go into your account, you control your HSA. You are typically required to open your HSA and receive deposits with the provider that your employer has chosen, but you can transfer that amount, even while still employed. If you move the funds to a different vendor, they must go into another eligible HSA account. Keep in mind that a transaction fee may be imposed when transferring balances.

"Unlike many other employer plans, such as qualified retirement savings plans, HSAs are fully portable at any time."

Myth #3: HSA contributions must always be used for eligible health care expenses.

The truth is you can spend your HSA account on anything you want. I would not recommend they be used this way. However, if you use it for a non-medical expense before the age of 65, tax and a tax penalty may apply. After age 65, withdrawals for non-medical expenses are not subject to a penalty, but they are subject to tax. This is similar to 401(k) withdrawals, which helps to overcome any concern about over-funding the account.

Myth #4: HSA contributions can only be made through payroll deduction.

Not true. While HSA contributions through payroll allows for the maximum tax savings (FICA**, Federal, and State), you can make out-of-pocket contributions (without the FICA savings). This option makes sense if you have missed out on maximizing your HSA contribution the prior year. You can add money to your account up to the tax filing deadline for prior year contributions.

Myth #5: HSAs don't earn anything.

This is often true when just starting an account, as some vendors do not pay any interest on cash balances (others do). Once you reach a certain amount, you can invest your HSA in the market. Most vendors require a minimum balance of $1,000 be maintained before investing the savings. This makes sense as you want to have some cash available in your account in case of an emergency.

Myth #6: HSAs have high fees.

When you maintain the HSA minimum balance and strategically invest any excess (as stated in Myth #5), our experience is that this is generally false. Plus most plan sponsors pay the monthly administration fees for active employees, which are typically similar to FSA administration costs. However, there is a misconception when HSA investment options are compared to 401(k) options. Your HSA might have a higher fee than your 401(k) due to significantly lower average balances in HSAs. We are finding that many HSA vendors include access to low cost funds. As the HSA industry grows, more brokerage accounts are being made available so that you can shop around to find HSAs with more attractive fees.

Myth #7: HSAs limit portability.

Unlike many other employer plans, such as qualified retirement savings plans, HSAs are fully portable at any time. Transferring your funds to another provider does not require termination of employment or the attainment of any other event. Upon termination, you keep any funds left in your HSA account. The typical fee is $20 or less per transfer. Ask the vendor about fees.

Myth #8: HSAs are only for healthy people.

To open an HSA, you need to be enrolled in a qualified HSA Eligible Health Plan (HSA HP). These plans usually have lower monthly premiums. They used to be known as the high deductible plans but today most health plans carry high deductibles. But many people mistakenly believe that the HSA HP are only cost-effective for super healthy people. While that may be true if a high deductible would cause a financial hardship, it's not always the case, even if you have a chronic health issue.

Let's look at the total picture:

- Low deductible plans typically cost you more in monthly premiums than a HSA HP.
- HSA HP may have a higher deductible, but their total out-of-pocket cost could be less than the low deductible option.
- Many employers make a contribution into the HSA, which is free money that can help cover high costs if necessary. If you don't use it this year, it is still your money to use in the future.
- HSAs allow you to contribute significantly more than FSA plans, allowing greater tax savings.
- When we consider the premium savings and tax savings on the HSA contributions, the HSA HP may have the lowest net cost.
- HSA-eligible plans may offer access to a greater choice of in-network providers.

Every situation is different, so it's important to consider these factors when choosing a plan.

Myth #9: HSAs are just a way for employers to lower costs.

While many employers will see significant savings by offering HSA Eligible Health Plans (HSA HP), many pass along savings to their employees. Smart employers offer to match contributions in HSAs. According to Plan Sponsor Council of America (PSCA Survey, 2020), more than 80 percent of employers are making contributions to HSAs.

Myth #10: There is a time limit on when I can be reimbursed for my expenses.

False. If you use non-HSA funds to pay for eligible medical expenses, save the receipts and you can reimburse yourself years later. This makes the HSA a powerful way to save for retirement. Picture this: throughout 20 years, you accumulate a six-figure balance in your HSA by paying medical expenses out-of-pocket. You save the receipts from those expenses, which total $25,000 over the years. In your first year of retirement, you can choose to reimburse yourself for all of those expenses and effectively give yourself $25,000 of tax-free income in that one year. Now that's a triple-tax-free benefit!

Learn more about HSAs by watching our informational (and fun!) videos. [https://www.myfinancialadvisor.org/hsa-learning]. If you have questions about HSAs, please contact us at karin@myfinancialadvisor.org.

*some FSAs allow a small carryover of $500
** FICA is Social Security and Medicare Tax

800 Roosevelt Road, Building B, Suite 413, Glen Ellyn, Illinois 60137
630.858.5430 | krettger@prgresource.com | myfinancialadvisor.org