The Unique Advantages of Health Savings Accounts
These tax-advantaged savings accounts can help you cover your health care expenses

A health savings account (HSA) is a tax-advantaged savings account that allows individuals with high-deductible health plans to set money aside for medical expenses. These accounts offer unique tax benefits and can even be savings tools for retirement.

What is a health savings account and how do you qualify?
An HSA allows you to contribute pre-tax funds and make tax-free withdrawals to pay for qualified medical expenses, like prescriptions, co-pays, or dental care. It is a way to reduce the financial burden of individuals who have health care plans with high deductibles. Using your HSA to pay for non-qualified expenses before age 65 can trigger taxes and penalties.

In 2021, contributions are limited to $3,600 a year for individuals and $7,200 a year for families. Those age 55 and older can contribute an additional $1,000 a year.

HSAs are not available to everyone. To qualify, you must have a high-deductible health plan that includes:

- A deductible of at least $1,400 and an out-of-pocket maximum of $7,000 or less for a single person.
- A deductible of at least $2,800 and an out-of-pocket maximum of $14,000 or less for a family.

You must be at least 18 years old to qualify for an HSA, and you cannot be claimed as a dependent on someone else's tax return. If you are enrolled in Medicare, you can use an existing HSA to pay for medical expenses, but you cannot contribute to one.

Many employers offer HSAs as part of a benefits package; however, as long as you meet the eligibility requirements, you can open one on your own. The funds in your account never expire and carry over from year to year. This is a unique advantage of HSAs that sets them apart from flexible spending accounts (FSAs), which require you to use the funds in the account by the end of the year or lose them.

The tax advantages of using an HSA

HSAs are not only an easy way to put money away for medical expenses; these accounts also come with unique tax benefits. If you have an HSA through your employer, contributions can be deducted from your paycheck pre-tax, effectively reducing the amount of your income being taxed. If you've opened one yourself, contributions are tax-deductible and don't require you to itemize your return.

Contributions can be invested, allowing you to take advantage of compounding growth, which can supercharge your ability to save. These returns are also tax-free as long as they are used for qualified medical expenses.

If you are offered an HSA as part of a benefits package through your employer, your employer can make contributions, as well. However, combined employee and employer contributions cannot exceed the annual limit.

Retirement benefits

HSAs may not seem like a retirement tool at first glance, but they can be beneficial as you get older. Medicare recipients cannot contribute to an HSA, but they can still use one to pay for medical expenses, such as Medicare premiums. Because funds do not expire, you can start saving early in an HSA to cover medical bills in retirement.

If you do not need your HSA savings to cover medical costs when you turn 65, you can use your savings for anything. You will owe income tax on these withdrawals, but you will not be subject to penalties. Withdrawals for qualified medical expenses will continue to be tax-free.

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