MULTNOMAH GROUP

Nuts and Bolts of HSAs

Agenda

- The landscape
- The basics
- Common misconceptions
- Selection and monitoring of HSA providers
- Question-and-answer

The Landscape

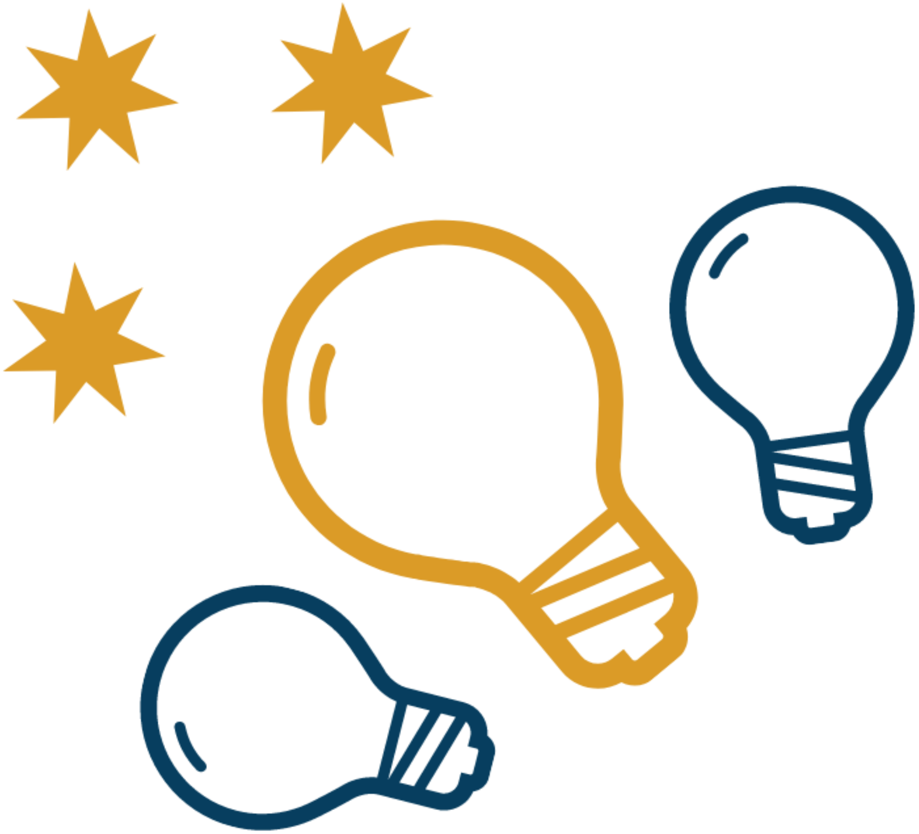
A brief history

- In 2003, under the Bush Administration, the Medicare Prescription Drug Improvement and Modernization Act of 2003 was enacted, creating:
  - Medicare Part D Prescription Drug Program
  - Health Savings Accounts (HSAs)
- High Deductible Health Plans (HDHPs) and HSAs were established to introduce consumerism into the healthcare marketplace

The Landscape

What's the big idea?

Give individuals control over their healthcare dollars, and individuals will seek more cost effective healthcare solutions.



The Landscape

A movement toward HDHPs + HSAs

- Companies moving toward HDHPs + HSAs
  - They believe that greater use of HDHPs will reduce inflationary pressure on healthcare spending, and, in turn, lower their health insurance expenses*
  - They believe that if employees have more skin in the game, they will seek preventative care and lower-cost providers*
- Legislation appears to favor HDHPs + HSAs

*Morningstar, 2017 Health Savings Account Landscape, 27 June 2017.

The Landscape

What's the cost of healthcare?

- Medical costs for a family of four (assuming employer-provided PPO insurance) has tripled since 2002, says a recent report.*

What's the correlation to retirement?

- A 2016 study showed that some workers experienced cost increases in their health plans during the past year and of those workers, 28% state they decreased their contributions to retirement plans.**
- A 65-year-old couple retiring this year will need an average of $275,000 (in today's dollars) to cover medical expenses throughout retirement, up from $260,000 in 2016.***

*Milliman Medical Index – 2016.

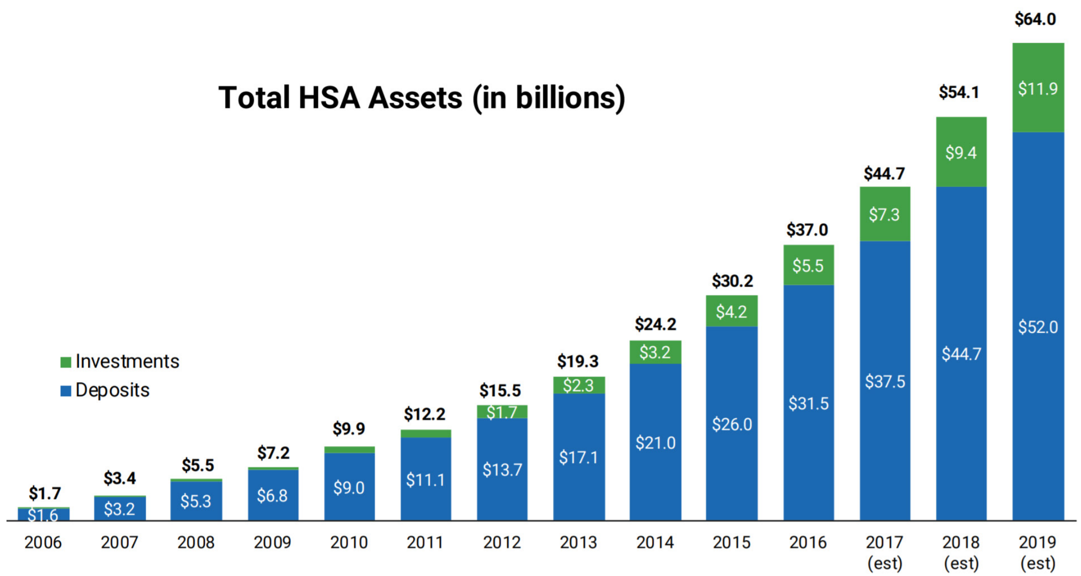
**EBRI, Workers Like Their Benefits, Are Confident of Future Availability, But Dissatisfied With the Health Care System and Pessimistic About Future Access and Affordability, available at: https://www.ebri.org/pdf/notespdf/EBRI_Notes_10-no11-Oct16-WBS.pdf.

***See Fidelity, Retiree health care costs continue to surge, available at: https://www.fidelity.com/viewpoints/retirement/retiree-health-costs-rise.

The Landscape

How many HSA assets are out there?

- Over 21 million HSA accounts (as of June 2017)*
- About $42.7 billion in HSA assets (as of June 2017)*
- About $6.8 billion in HSA assets are invested (as of June 2017)*



Source: Estimates derived from 2017 Midyear Devenir HSA Market Survey, press releases, previous market research and market growth rates.

*See Midyear HSA Market Statistics & Trends Executive Summary, available at: http://www.devenir.com/wp-content/uploads/2017-Midyear-Devenir-HSA-Market-Research-Report-Executive-Summary.pdf

The Landscape

Who are the participants?

- Millennials
  - Preference for HDHPs was strongly correlated to age whereby preference shifted away from HDHPs as the group moved toward retirement age.
- Higher earners
  - There is a greater preference for HDHPs in higher wage earners, presumably because higher wage earners will not fear the occasional out of pocket medical expenses.

*Benefitfocus, The State of Employee Benefits, 2017.

The Basics

The Basics

What is an HSA?

- A health savings account is a tax-exempt trust or custodial account you set up with a qualified HSA trustee to pay or reimburse certain medical expenses you incur, says the IRS
- HSAs are used in conjunction with HDHPs
- Typically, HSAs are in the form of a checking, savings, or other type of account used to pay for the medical expenses
- HSAs are associated with individuals and generally tied to the individual’s social security number

The Basics

What are the basic eligibility requirements?

- ✓ Individual must be covered by the HDHP
- ✓ Individual must not be covered by a spouse's non-HDHP
    - Example: Individual cannot be covered by spouse's PPO or HMO
- ✓ Individual must not be claimed as a dependent on another person's tax return
- ✓ Individual must not be covered by a spouse's or other person's general health FSA or HRA.

Assuming eligibility is met, then the individual is eligible on the first day of the first month following all requirements above being met.

The Basics

How is an HSA funded?

- Employer contributions
- Employee contributions
  - *Employer contributions drive enrollment and growth in HSAs!*
- Friends, family, anyone!

Contributions come in many forms, including:

- Pre-tax payroll contributions
- Check or cash deposit from the individual (not via payroll)
- Transfer from another HSA, rollover from another HSA, conversion of an IRA
  - Special rules apply for rollovers and conversions

When are contributions made?

- Contributions start as early as January 1
  - An individual could make the full contribution to the HSA on January 1; if eligibility changed during the year, a corrective distribution would be necessary
- Contributions can be made as late as the individual's tax filing deadline (April 15 of the next year)

The Basics

Maximum HSA Contribution	2018
Individual Plan	$3,450
Family Plan	$6,900
55+ Catch-up Contribution	$1,000

The Basics

What an HSA *can* pay for:	What an HSA *cannot* pay for:
Qualified medical expenses listed in IRS Section 213(d) & IRS Publication 502	Medigap Insurance Premiums
Medicare Expenses	Cosmetic Surgery
Long Term Care Premiums	Funeral Expenses
Prescription Drugs	Some over-the-counter drugs (e.g. dietary supplements & sunscreen)
Eye Exams & Associated Hardware	Life insurance premiums
Psychological & Psychiatric Care	
COBRA	
X-Rays	
Ambulance Services	
Chiropractic Care	

This slide is not an exhaustive list, but shall serve as an introduction to examples that are (and are not) HSA eligible expenses.

*See IRS Publication 502 and Internal Revenue Code Section 213(d).

The Basics

How does an individual take a distribution & what's the tax consequence?

- **Tax Free Option**:
  - ✓ **Distribution at any age for qualified medical expenses (see prior slide)**
  - ✓ **Distribution available for rollovers and transfers**
- Taxable Option, but with *no penalty*:
  - ✓ Distribution *after* turning age 65 for non-qualified medical expenses (see prior slide)
  - ✓ Distribution to a beneficiary (other than a spouse) upon death
  - ✓ Distribution for disability
- Taxable Option, and *with a penalty*:
  - ✓ Distribution *before* turning age 65 for non-qualified medical expenses (see prior slide)
  - ✓ Excess contributions after tax filing deadline

See Access Point HSA, Distribution Rules (2018).

The Basics

And, what happens when individuals turn 65?

- 65 is a critical age for individuals with HDHPs and HSAs
- HSAs and Medicare are mutually exclusive; once enrolled in Medicare, an individual can no longer contribute to an HSA
  - However, an individual can still take distributions from an HSA, which may be used to reimburse Medicare Premiums or pay out-of-pocket expenses
- For individuals that want to continue to contribute to an HSA after turning 65, then that's an option if the individual does not enroll in Medicare, but penalties may apply.
  - This would be an appropriate conversation for the individual to have with a tax professional, financial professional, or other third party professional.

See Access Point HSA, Distribution Rules (2018).

The Basics

Does ERISA Apply?

DOL Field Assistance Bulletin 2004-01 says that even though there are employer contributions to the HSA, it will not be considered an ERISA-covered plan if the following six conditions are met:

1. HSA is completely voluntary on the part of the employees
2. Employer does not limit the ability of eligible individuals to move their funds to another HSA
3. Employer does not impose conditions on utilization of HSA funds
4. Employer does not make or influence the investment decisions with respect to funds contributed to an HSA
5. Employer does not represent that the HSAs are an employee welfare benefit plan established or maintained by the employer
6. Employer does not receive any payment or compensation in connection with an HSA

The Basics

What if ERISA applies?

- If one of the six conditions is met, then the HSA would be subject to ERISA
- The Employer would be required to meet the ERISA requirements (similar to an ERISA-covered retirement plan)
  - File Form 5500
  - Maintain a Plan Document
  - Circulate the Summary Plan Description

- *Caution: Compliance with ERISA would be difficult because HSAs are individual accounts!*
- *Caution: Even though ERISA doesn't apply, prohibited transition rules do apply! For example, timely deposit of the contributions withheld from pay is still important.*

The Basics

Common areas that may cross the ERISA divide:

- Giving advice to employees related to whether to invest in their 401(k) versus their HSA*
  - This could violate the condition that the employer will "not make or influence the investment decisions with respect to funds contributed to an HSA"

- Making materials from vendors available that provide investment advice (versus education)**
  - Again, this could violate the condition that the employer will "not make or influence the investment decisions with respect to funds contributed to an HSA"
  - Employers need to review the materials they make available to employees as a part of the HSA

See PlanSponsor, Guidelines for Keeping HSAs Not Subject to ERISA, available at: https://www.plansponsor.com/guidelines-for-keeping-hsas-not-subject-to-erisa/.
** *See* HSA Bank, Employer Responsibilities for HSAs Under the New DOL Fiduciary Standards, available at: http://www.hsabank.com/~/media/files/whitepaper/DOL-Fiduciary-Standards-2.

The Basics

How does the DOL Fiduciary Rule apply?

- DOL Fiduciary Rule applies to HSAs (June 2017)
  - Full compliance date for the Rule was pushed back to 2019
- Employers are not the target of the DOL Fiduciary Rule
  - Financial professionals were the target
  - The purpose of the rule was to heighten the standard that applied to financial professionals providing services to retirement accounts, including HSAs
- Potential impacts of the DOL Fiduciary Rule:
  - Ensuring that fees charged to participants are reasonable and fully disclosed
  - Reviewing communication materials for participants to ensure they are not providing investment advice
  - Reviewing the investment options within the HSA

Common Misconceptions

A recap of the most common misunderstanding about HSAs

- ✓ "If I don't use it, then I will lose it," say many employees
  - Employees often confuse the HSA with the FSA and HRA (example: Emeriti plans)
  - FSAs are the "use it or lose it" model. HSAs do NOT have to be spent within the year
- ✓ "I can use my HSA for any medical expense," say many employees
  - Only qualified medical expenses are tax free
  - Other medical expenses are allowed, but will be taxable + penalty before 65 (or taxable, no penalty after 65)
- ✓ "My employer will take care of everything related to my HSA," say many employees
  - HSAs are individual custodial accounts
  - Responsibility lies with the individual to make sure they remain eligible for the HSA and do not exceed the annual limits
- ✓ "All HSA providers are the same and likely have the same investment options and services. I will go with the one that gives a discount based on my other services," say many employers
  - HSA providers vary substantially in terms of services, fees, investment options, and structure as a bank or non-bank provider
  - Receiving a discount on the HSA service may be deemed as indirect compensation to the employer, which could subject the HSA to ERISA coverage

Selection and Monitoring of HSA Providers

HSAs are generally not covered by ERISA. Regardless (and in light of the DOL Fiduciary Rule), best practices dictate that employers should:

1. Ensure fees to participants are reasonable
2. Ensure fees are fully and clearly disclosed
3. Review participant education and communication materials
4. Review investment options

This requires employers to pay particular attention to the service provider(s) selected for the HSA.

Selection and Monitoring of HSA Providers

Selecting an HSA provider is similar to selecting other benefit service providers. Things to consider include but are not limited to:

- ✓ Reputation in the marketplace
- ✓ Experience
- ✓ Account and investment fees
- ✓ Investment menu design
- ✓ Participant outreach and education
- ✓ Integration capabilities with other benefits, i.e., retirement plans

Take Action Today

How should Employers proceed?

- Review the HSA program to ensure the 6 conditions for ERISA are not met. Ensure the employer is *not*:
  - Making employees' contributions to an HSA involuntary
  - Limiting employees' ability to move funds to another HSA
  - Imposing conditions on the use of HSA funds. If employees want to use the funds for something other than medical expenses, they must be allowed to, even though the employees may have to pay penalties and taxes on the funds.
  - Influencing HSA investment decisions.
  - Representing that the HSA is subject to ERISA when it's not; doing so, makes it subject to ERISA
  - Receiving payment in connection with the HSA; this can even be indirect payment such as a discount on another service from the vendor (example, aggregate pricing with the retirement plan)
- Review educational materials the HSA program makes available to participants
- Review and monitor HSA service provider(s) to ensure that fees are reasonable
- Understand how the investment line-up was selected and monitor accordingly

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