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HEALTH SAVINGS ACCOUNTS: THE TRIPLE TAX BENEFIT

As an increasing number of taxpayers are looking for ways to cut their tax bill, many seem to overlook a valuable tax savings tool known as the HSA. Health Savings Accounts (HSAs) are savings accounts established for the primary



purpose of saving money for healthcare expenses. Similar to an IRA, the goal is to put money aside so that it is available to

pay your out-of-pocket medical expenses. This is especially important since healthcare costs historically have risen at a pace greater than the annual inflation rate. In fact, PwC's Health Research Institute projects a 7.5 percent growth rate in healthcare costs in 2013 alone.

HSAs not only provide a great way for us to save for healthcare expenses, but they can also provide tremendous tax benefits. The HSA is unique in that it offers a triple tax benefit to taxpayers. First, contributions to the HSA are generally tax-deductible on your tax return. Second, the earnings inside your HSA enjoy tax-deferred status, which means you do not have to pay investment taxes on your dividends, interest, and capital gains inside your HSA. Finally, when you withdraw the money from your account, the distribution is tax-free as long as the funds withdrawn are used to pay for qualified medical expenses. As a result, if used correctly, the HSA can be one of the most valuable personal tax breaks found in the entire Internal Revenue Code.

There are some important things to consider when evaluating whether an HSA is right for you. First, in order to qualify for an HSA, one must have what the IRS considers a high-deductible health plan (HDHP) and you must not be covered by another non-HDHP or Medicare. For 2013, a HDHP must have a minimum deductible of \$1,250 for self-coverage or \$2,500 for family coverage. Additionally, there are out-of-pocket maximum limits established by the IRS

for these plans. It is essential that your health insurance plan qualifies under the rules in order to participate in an HSA.

Also, when you withdraw the money from your HSA, the funds must be used to pay for qualified medical expenses in order to be tax-free. Qualified medical expenses can include doctors' visits, dental treatments, prescription medications, lab fees, etc. Over-the-counter (OTC) medications are no longer covered as qualified medical expenses under the 2010 Affordable Care Act and currently require a doctor's prescription in order to qualify. If distributions are not used to pay for qualified medical expenses, there is normally a 20 percent penalty that is assessed on top of normal income taxation on the distribution.

The maximum HSA contribution allowed for 2013 is \$3,250 for individuals and \$6,450 for families. The IRS does allow an additional catch-up contribution of \$1,000 in 2013 for those age 55 or older. The HSA can provide the best of both worlds by providing a means to save for healthcare costs and at the same time providing valuable tax benefits. The rules regarding HSA participation, contributions, and distributions do require special attention. Talk to your CPA to learn more about the tax benefits associated with HSAs.

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