



Legal Alert: IRS Provides Guidance On HSA Contributions

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The IRS recently issued two notices affecting Health Savings Accounts (HSAs): Notice 2008-51 provides procedures for carrying out a qualified HSA funding distribution from certain types of IRA accounts; Notice 2008-52 replaces the old HSA maximum contribution limit rules with new rules.

Procedures for Making a Qualified HSA Funding Distribution

Section 307 of the Health Opportunity Patient Empowerment Act of 2006 (the Act) added § 408(d)(9) to the Internal Revenue Code. Generally, Code § 408(d)(9) provides that a qualified HSA funding distribution from an IRA to an HSA is not included in gross income if the individual is qualified under Section 223(c)(1).

Notice 2008-51 provides guidance on making a qualified HSA funding distribution from an IRA to an HSA. The key points of Notice 2008-51 are summarized below:

- A qualified HSA funding distribution is a one-time transfer from an individual's IRA to his or her HSA. Transfers made to an HSA owned by another individual (such as a spouse) do not qualify.
- A qualified HSA funding distribution generally is excluded from gross income and not subject to an additional 10% tax under Code § 72(t).
- A qualified HSA funding distribution may be made from a traditional IRA or a Roth IRA, but not from an ongoing SIMPLE IRA or an ongoing SEP IRA.
- The amount contributed to the HSA through a qualified HSA funding distribution is not allowed as a deduction and counts against the individual's maximum annual HSA contribution for the taxable year of the distribution.
- The amount of a qualified HSA funding distribution from an IRA must be less than or equal to the IRA account owner's maximum annual HSA contribution. The maximum HSA contribution is determined based on the individual's age and type of high deductible health plan (HDHP) coverage (either self-only or family).
- A qualified HSA funding distribution relates to the taxable year in which the distribution is actually made. The rules permitting certain contributions made before the deadline for filing an individual's federal income tax return to be deemed made in the preceding taxable year do not apply to qualified HSA funding distributions.

- The individual must be an eligible individual under § 223(c)(1) at the time of the qualified HSA funding distribution.
- The distribution must be a direct transfer from an IRA to an HSA.

Notice 2008-51 provides for a “testing period” for determining whether the individual is an eligible individual under § 223(c)(1). This period begins with the month in which the qualified HSA funding distribution is contributed to the HSA and ends on the last day of the 12th month following that month. If at any time during the testing period the individual ceases to meet all of the requirements to be an eligible individual, the amount of the qualified HSA funding distribution is included in the individual’s gross income and is subject to 10% additional tax (unless an exception applies).

Guidance on Contributions to HSAs

Notice 2008-52 provides guidance on contributions to HSAs under amendments to the Internal Revenue Code made by the Tax Relief and Health Care Act of 2006. One such amendment was the repeal of the annual limit on HSA contributions based on the deductible under the high deductible health plan (HDHP). According to the guidance, for 2007 and later, the annual HSA contribution limit will be determined by the indexed maximum HSA contribution for self-only HDHP coverage set forth in § 223(b)(2)(A), and for family HDHP coverage set forth in § 223(b)(2)(B).

Notice 2008-52 also provides guidance on determining an individual’s annual HSA contribution limits for 2007 and later. If an individual was an eligible individual on the first day of the last month of the individual’s taxable year (the first day of December for those using a calendar year as the taxable year), the individual’s maximum HSA contribution for the year is the greater of the following:

- The sum of the limits determined separately for each month under § 223(b)(2), based on eligibility and HDHP coverage on the first day of each month, plus catch-up contributions for each month, if applicable; or
- The maximum annual HSA contribution under § 223(b)(2)(A) or § 223(b)(2)(B) based on the individual’s HDHP coverage (self-only or family) on the first day of the last month of the individual’s taxable year, plus catch-up contributions if applicable. For 2008 the maximum contribution for an individual with self-only HDHP coverage is \$2,900, plus a \$900 “catch-up” amount if the individual is over age 55 and not enrolled in Medicare. The 2008 maximum contribution for an individual with family HDHP coverage is \$5,800, plus the \$900 catch-up amount if applicable. In 2009, the maximum contribution for individuals with self-only coverage will increase to \$3,000, plus any catch-up amount; the maximum contribution for individuals with family HDHP coverage will increase to \$5,950, plus any catch-up amount.

If the individual was not an eligible individual on the first day of the last month of the individual’s taxable year, the maximum HSA contribution for the year is determined by the sum of the monthly contribution limits rule under § 223(b)(2).

The full contribution rule, created by the Act and found in Code § 223(b)(8), treats an individual who is an eligible individual on the first day of the last month of the taxable year as having been an eligible individual for the entire

year. Thus, Notice 2008-52 explains that the full contribution rule applies without regard to whether the individual was an eligible individual for the entire year, had HDHP coverage for the entire year, or had disqualifying non-HDHP coverage for part of the year. However, a testing period applies to the full contribution rule. The testing period begins on the first day of the last month of the taxable year and ends on the last day of the 12th month following that month. Thus, for a calendar-year taxpayer, the testing period is from December 1 of the current year to December 31 of the following year. This provision is effective for taxable years beginning after December 31, 2006.

If the full contribution limit rules are not met, prohibited amounts are includible in gross income and are subject to the 10% additional tax imposed by Code § 72(t).

If you have any questions regarding the recent IRS Notices or other benefits related issues, please contact Penny Wofford, pwofford@fordharrison.com, 864-699-1131 or Beth Ward, bward@fordharrison.com, 312-960-6134 or the Ford & Harrison attorney with whom you usually work.