

Part III - Administrative, Procedural, and Miscellaneous

Health Savings Accounts

Notice 2008-52

This notice provides guidance on contributions to Health Savings Accounts (HSAs) under amendments to the Internal Revenue Code by §§ 303 and 305 of the Health Opportunity Patient Empowerment Act of 2006 (the Act) included in the Tax Relief and Health Care Act of 2006, enacted December 20, 2006, Pub. L. No. 109-432.

ANNUAL HSA CONTRIBUTION LIMIT

HDHP deductible limit on annual HSA contributions repealed

For 2004 through 2006, the maximum annual HSA contribution was the lesser of (1) the annual deductible under the high deductible health plan (HDHP) or (2) the statutory maximum under § 223(b)(2)(B). See Notice 2004-2, 2004-1 C.B. 269, Q&A-12. Section 303 of the Act repeals the limit on annual HSA contributions based on the amount of the deductible under the HDHP. For 2007 and later years, the indexed maximum HSA contribution under § 223(b)(2)(A) (for self-only HDHP coverage) and § 223(b)(2)(B) (for family HDHP coverage) determines the contribution limit, without regard to an individual's HDHP deductible. Thus, for 2008, the maximum annual HSA contribution is \$2,900 for individuals who have self-only HDHP coverage and \$5,800 for individuals who have family HDHP coverage.

Annual HSA contribution limits for 2007 and later years

Section 305 of the Act adds § 223(b)(8) which provides that if an individual is an eligible individual on the first day of the last month of the individual's taxable year

(December 1 for calendar year taxpayers), the individual's maximum HSA contribution for the year is the greater of the following:

- (1) 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 (see sum of the monthly contribution limits discussion below), or
- (2) 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 under § 223(b)(3), if applicable (see full contribution rule under § 223(b)(8) discussion below).

A testing period applies to the full contribution rule (see discussion of the testing period below). If an individual is not an eligible individual on the first day of the last month of the individual's taxable year (December 1 for calendar year taxpayers), the individual's maximum HSA contribution for the year is determined under the sum of the monthly contribution limits rule under § 223(b)(2). See Example 6 below.

Sum of the monthly contribution limits

Eligible individuals (as defined in § 223(c)(1)) may contribute to HSAs. See Notice 2004-2, Q&A-2; Notice 2004-50, 2004-2 C.B. 196, Q&A-2, 3. Under § 223(b)(1) and (2), the maximum annual contribution to an HSA is the sum of the contribution limits determined separately for each month, based on eligibility and health plan coverage on the first day of the month. For this purpose, the monthly limit is 1/12 of the indexed amount provided under § 223(b)(2)(A) for self-only coverage (\$2,900 for 2008) and

under § 223(b)(2)(B) for family coverage (\$5,800 for 2008). In addition, the maximum HSA contribution is increased by an additional contribution amount (catch-up amount) for individuals age 55 or older as of the last day of the calendar year who are not enrolled in Medicare. The catch-up contribution is also computed on a monthly basis. Section 223(b)(2).

Full contribution rule

New § 223(b)(8)(A) 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 and may increase, but not decrease, the contribution limit for such an individual. Thus, in order to make a full contribution for the year under § 223(b)(8), a taxpayer must be an eligible individual on the first day of the last month of his or her taxable year (December 1 for calendar year taxpayers). The eligible individual is also treated as enrolled in the same HDHP coverage (i.e., self-only or family coverage) as he or she has on the first day of the last month of the year. For example, if an individual first becomes HSA-eligible on December 1, 2007, and has family HDHP coverage, he or she is treated as an eligible individual and having family HDHP coverage for all twelve months in 2007. This full contribution rule also applies to catch-up contributions. 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 for purposes of the full contribution rule.

The testing period

The testing period applies to an individual who is an eligible individual on the first day of the last month of the taxable year. 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. Section 223(b)(8)(B)(iii). For 2008 HSA contributions, the testing period for calendar year taxpayers begins in December 2008 and ends on December 31, 2009.

Failure to remain an eligible individual during the testing period

If an individual who is an eligible individual on the first day of the last month of the taxable year contributes an amount to his or her HSA greater than the sum of the monthly contribution limits under § 223(b)(1) and (2), and at any time during the testing period, the individual ceases to meet all requirements to be an eligible individual, an amount is included in the individual's gross income and subject to an additional 10 percent tax, unless the failure is due to disability (as defined in § 72(m)(7)) or death.

The amount that is included in the individual's gross income is computed by subtracting the sum of the monthly contribution limits that the individual would otherwise have been entitled to under § 223(b)(1) and (2) from the amount actually contributed. Section 223(b)(8)(B). It is not necessary to distribute this amount from the HSA, and there may be additional adverse tax consequences from such a distribution. See discussion below on distributions not used for qualified medical expenses. Withdrawing this amount from the HSA will not prevent the inclusion of the amount in income or the additional 10 percent tax. However, earnings on the amount are not included in gross

income or subject to the 10 percent additional tax, so long as the earnings remain in the HSA or are used for qualified medical expenses.

Unlike the additional 10 percent tax under § 223(f)(4)(A), the additional 10 percent tax under § 223(b)(8)(B)(i)(II) applies regardless of the age of the account beneficiary (i.e., even after age 65).

To remain an eligible individual during the testing period, an individual is not required to keep the same level of HDHP coverage during the testing period. Thus, changing from family HDHP coverage to single HDHP coverage during the testing period does not result in inclusion of amounts in gross income or an additional 10 percent tax. See Examples 8 and 14 below.

Excise tax on excess contributions

Section 4973 imposes a six percent excise tax for each taxable year on HSA contributions in excess of the maximum contribution limit for the year (excess contributions). If the excess contributions for the year and the net income attributable to such excess contributions are withdrawn from the HSA before the last day (with extensions) for filing the federal income return for the taxable year, the amount is not subject to the excise tax for that year. However, an amount included in gross income under § 223(b)(8)(B) because an individual failed to remain an eligible individual during the testing period is not an excess contribution and § 4973 does not apply to this amount. For this reason, the amount cannot be withdrawn under the excess contribution rules.

HSA distributions not used for qualified medical expenses

An HSA distribution not used for qualified medical expenses (as defined in § 223(d)(2)) is included in gross income under § 223(f)(2) and is subject to the additional 10 percent tax under § 223(f)(4) (with certain exceptions), regardless of whether the amount contributed to the HSA under the full contribution limit is included in the account beneficiary's income and subject to the additional tax under § 223(b)(8)(B)(i). See Notice 2007-22, 2007-10 I.R.B. 670 regarding consequences of distributions from HSAs. See Example 9 below.

Establishing HSAs

An individual may establish an HSA at any time on or after the date the individual becomes HSA-eligible. Contributions for the taxable year can be made in one or more payments, at any time prior to the time (without extensions) for filing the individual's federal income tax return for the taxable year. An individual who becomes an eligible individual after January 1 may make the maximum contribution to an HSA on the first day he or she is an eligible individual. Notice 2004-2, Q&A-21. In that case, the individual's contribution is based on the individual's expected coverage on the first day of the last month of his or her taxable year. But see testing period rules above.

EXAMPLES

The following examples illustrate these rules. It is assumed in the examples that the taxable year of all individuals is the calendar year, and that, for purposes of § 223(b)(8)(B)(ii), no individuals are disabled within the meaning of § 72(m)(7) unless otherwise stated.

Example 1. Individual A, age 53, enrolls in family HDHP coverage on December 1, 2008 and is otherwise an eligible individual on that date. A is not an eligible individual in any other month in 2008.

A is an eligible individual with family HDHP coverage on December 1, 2008. A's full contribution limit under § 223(b)(8) for 2008 is \$5,800. The sum of the monthly contribution limits is \$483.33 ($1/12 \times \$5,800$). A's annual contribution limit for 2008 is \$5,800, the greater of \$5,800 or \$483.33

Example 2. Same facts as Example 1, except that A contributes \$5,800 to his HSA on December 1, 2008 and ceases to be an eligible individual in June 2009.

The testing period for 2008 HSA contributions ends on December 31, 2009. In 2009, A ceases to be an eligible individual during the testing period. In 2009, A must include in gross income \$5,316.67, the amount contributed to the HSA for 2008 minus the sum of the monthly contribution limits ($\$5,800.00 - \483.33). In addition, the 10 percent additional tax (\$532) in § 223(b)(8)(B)(i) applies to the amount included in gross income.

Example 3. Individual B, age 39, enrolls in self-only HDHP coverage on January 1, 2008 and is an eligible individual on that date. B's coverage changes to family HDHP coverage on November 1, 2008 and B retains family HDHP coverage through December 31, 2008. B is an eligible individual from January 1, 2008 through December 31, 2008 and remains an eligible individual through December 31, 2009.

B is an eligible individual with family HDHP coverage on December 1, 2008. B's full contribution limit under § 223(b)(8) for 2008 is \$5,800. B's sum of the monthly contribution limits is \$3,383.34 ($(2/12 \times \$5,800) + (10/12 \times \$2,900)$). B's annual contribution limit for 2008 is \$5,800, the greater of \$5,800 or \$3,383.34.

Example 4. In 2007, Individual C, age 47, is covered by a general purpose health FSA with a grace period ending March 15, 2008. C enrolls in family HDHP coverage on January 1, 2008. C becomes an eligible individual on April 1, 2008 and remains an eligible individual through December 31, 2009. On April 2, 2008, C contributes \$5,800 to his HSA for 2008.

C is an eligible individual with family HDHP coverage on December 1, 2008. C's full contribution limit under § 223(b)(8) for 2008 is \$5,800. C's sum of the monthly contribution limits is \$4,350 ($9/12 \times \$5,800$). C's annual contribution limit for 2008 is \$5,800, the greater of \$5,800 or \$4,350. The testing period for 2008 ends on December 31, 2009. Because C is an eligible individual during the testing period, no amount of the \$5,800 contribution is included in C's gross income and C is not subject to the 10 percent additional tax.

Example 5. Individual D, age 57, enrolls in family HDHP coverage on December 1, 2008 and is an eligible individual on that date. D was not an eligible individual in any other month in 2008. D contributes \$6,700 to his HSA on December 1, 2008 and remains an eligible individual through December 31, 2009.

D is an eligible individual with family HDHP coverage on December 1, 2008 and remains an eligible individual through December 31, 2009. D's full contribution limit

under § 223(b)(8) for 2008 is \$6,700 (\$5,800 family coverage contribution + \$900 catch-up contribution). The sum of the monthly contribution limits is \$558.33 $((1/12 \times \$5,800) + (1/12 \times \$900))$. D's annual contribution limit for 2008 is \$6,700, the greater of \$6,700 or \$558.33.

Example 6. Individual E, age 35, has self-only HDHP coverage and is an eligible individual for the months of May, June, and July 2008.

The full contribution limit under § 223(b)(8) does not apply to E for 2008 because E is not an eligible individual on December 1, 2008. E's contribution limit for 2008 is \$725 $(3/12 \times \$2,900)$.

Example 7. Individual F, age 46, enrolls in family HDHP coverage on January 1, 2008 and is an eligible individual on that date. F contributes \$5,800 to an HSA on January 1, 2008. F ceases to be covered by an HDHP on August 1, 2008. On December 15, 2008, F withdraws from the HSA \$2,416.67 $(\$5,800.00 - 3,383.33)$, plus \$45 earnings attributable to the \$2,354.16.

F ceases to be an eligible individual on August 1, 2008. The full contribution limit does not apply to F for 2008 because F is not an eligible individual on December 1, 2008, and the testing period in § 223(b)(8)(B)(i) does not apply to F. F's HSA contribution limit for 2008 is \$3,383.33 $(7/12 \times \$5,800)$. The \$2,416.67 is an excess contribution for purposes of § 4973, but is not subject to the six percent excise tax under § 4973 because F withdrew the excess contribution and earnings attributable to the excess contribution by the due date, with extensions, for filing her 2008 federal income tax return. F reports the \$45 withdrawn earnings as gross income on her 2008 federal income tax return. The gross income inclusion and 10 percent tax in § 223(f)(3) for distributions not used for qualified medical expenses in § 223(f)(2) do not apply because F withdrew an excess contribution.

Example 8. Individual G, age 38, enrolls in family HDHP coverage on January 1, 2008 and is an eligible individual on that date. G's coverage changes to self-only HDHP coverage on September 1, 2008 and he retains that coverage through December 31, 2008. G is an eligible individual for all 12 months in 2008. G contributes \$4,833.33 $((8/12 \times \$5,800) + (4/12 \times \$2,900))$ to an HSA for 2008. G ceases to be an eligible individual on January 1, 2009.

G is an eligible individual with self-only HDHP coverage on December 1, 2008. G's full contribution limit under § 223(b)(8) for 2008 is \$2,900. G's sum of the monthly contribution limits is \$4,833.33 $((8/12 \times \$5,800) + (4/12 \times \$2,900))$. G's annual contribution limit is \$4,833.33, the greater of \$2,900 or \$4,833.33. The testing period for 2008 HSA contributions ends on December 31, 2009. G ceases to be an eligible individual during the testing period. Because G's contribution of \$4,833.33 is not greater than the sum of the monthly contribution limits, there is no inclusion or additional tax when G ceases to be an eligible individual during the testing period.

Example 9. Individual H, age 25, enrolls in self-only HDHP coverage on June 1, 2008 and is an eligible individual on that date. H is not an eligible individual prior to June 1, 2008. H contributes \$2,900 to an HSA on July 1, 2008. H is an eligible individual on December 1, 2008, and continues to be an eligible individual until February 1, 2009. On February 2, 2009, H withdraws \$1,208.33 from his HSA. The \$1,208.33 distribution is not used for H's qualified medical expenses (as defined in § 223(d)(2)).

H is an eligible individual with self-only HDHP coverage on December 1, 2008. H's full contribution limit under § 223(b)(8) for 2008 is \$2,900. H's sum of the monthly contribution limits is \$1,691.67 ($7/12 \times \$2,900$). H's annual contribution limit is \$2,900, the greater of \$2,900 or \$1,691.67. The testing period for 2008 HSA contributions ends on December 31, 2009. In 2009, H ceases to be an eligible individual during the testing period. In 2009, H must include in gross income \$1,208.33, the amount contributed to the HSA minus the sum of the monthly contribution limits (\$2,900.00 - \$1,691.67). In addition, the 10 percent additional tax (\$120.83) in § 223(b)(8)(B)(i) applies to the amount.

The \$1,208.33 withdrawn from the HSA is not used for qualified medical expenses and is not a withdrawal of an excess contribution. Therefore, under § 223(f)(2), \$1,208.33 is also included in H's gross income and is also subject to the 10 percent additional tax in § 223(f)(4). As a result, H includes \$2,416.66 (\$1,208.33 with respect to § 223(f)(4) and \$1,208.33 with respect to § 223(b)(8)) in gross income in 2009 and an additional tax of \$241.66 (\$120.83 with respect to § 223(f)(4) and \$120.83 with respect to § 223(b)(8)).

Example 10. Individual J, age 27, is eligible for medical benefits through the Department of Veterans Affairs (VA). As a result of medical care (other than disregarded coverage or preventive care) that J received from the VA in January 2008, he is not an eligible individual in January, February, March, or April 2008. J has self-only HDHP coverage and is otherwise an eligible individual from May 1, 2008 through December 31, 2009.

J is an eligible individual with self-only HDHP coverage on December 1, 2008. J's full contribution limit under § 223(b)(8) for 2008 is \$2,900. J's sum of the monthly contribution limits is \$1,933.33 ($8/12 \times \$2,900$). J's annual contribution limit for 2008 is \$2,900, the greater of \$2,900 or \$1,933.33.

Example 11. Same facts as Example 10, except that J also receives medical care (other than disregarded coverage or preventive care) from the VA in October 2008. J is an eligible individual with self-only HDHP coverage in May through September 2008.

The full contribution limit does not apply to J for 2008 because J is not an eligible individual on December 1, 2008. J's 2008 contribution limit is determined under the sum of the monthly contribution limits and is \$1,208.33 ($5/12 \times \$2,900$).

Example 12. Individual K, age 64, enrolls in family HDHP coverage on April 1, 2008 and is an eligible individual from April 1, 2008 through December 31, 2008. K was not an eligible individual prior to April 1, 2008. K contributes \$6,700 to his HSA for 2008 on April 1, 2008. K attains age 65 and enrolls in Medicare on March 24, 2009 and ceases to be an eligible individual.

K is an eligible individual with family HDHP coverage on December 1, 2008. K's full contribution limit under § 223(b)(8) for 2008 is \$6,700 (\$5,800 family coverage contribution + \$900 catch-up contribution). K's sum of the monthly contribution limits is \$5,025 $((9/12 \times \$5,800) + (9/12 \times \$900))$. K's annual contribution limit for 2008 is \$6,700, the greater of \$6,700 or \$5,025. The testing period for 2008 HSA contributions ends on December 31, 2009. In 2009, K ceases to be an eligible individual during the testing period. In 2009, K must include \$1,675, the amount contributed to the HSA minus the sum of the monthly contribution limits $(\$6,700.00 - \$5,025)$ in gross income. In addition, the 10 percent additional tax $(\$167.50)$ in § 223(b)(8)(B)(i) applies to the amount.

Example 13. Same facts as Example 12, except that before enrolling in Medicare, K ceases to be an eligible individual during the testing period as a result of becoming disabled. Because K ceases to be an eligible individual due to becoming disabled, no amount is required to be included in income in 2009 or is subject to the additional tax in § 223(b)(8).

Example 14. Individuals L and M, both age 40, are a married couple. L and M enroll in family HDHP coverage on December 1, 2008 and are otherwise eligible individuals on that date. L and M are not eligible individuals in any other month in 2008. L and M divide the contribution limit equally between them. On or after December 1, 2008, L contributes \$2,900 to his HSA and M contributes \$2,900 to her HSA. On June 1, 2009, M switches to self-only HDHP coverage and remains an eligible individual through December 31, 2009. L ceases to be an eligible individual in June 2009.

L and M are eligible individuals with family HDHP coverage on December 1, 2008. L and M's combined full contribution limit for 2008 is \$5,800. L and M's combined sum of the monthly contribution limits is \$483.33 $(1/12 \times \$5,800)$, or \$241.67 each $((1/12 \times \$5,800)/2)$. L and M's combined annual contribution limit under § 223(b)(8) is \$5,800, the greater of \$5,800 or \$483.33. The testing period for 2008 HSA contributions ends on December 31, 2009. During the testing period for 2008, M remains an eligible individual but L ceases to be an eligible individual. Because M is an eligible individual during the testing period, no amount of M's \$2,900 contribution is included in M's gross income and M is not subject to the 10 percent additional tax. In 2008, L must include \$2,658.33 in gross income, the amount contributed to the HSA minus the sum of the monthly contribution limits $(\$2,900 - \$241.67)$. In addition, the 10 percent additional tax $(\$265.83)$ in § 223(b)(8)(B)(i) applies to that amount.

Example 15. Same facts as Example 14, except M contributes \$5,800 to M's HSA and L contributes \$0 to L's HSA. No amount is taxable to either L or M.

NO EFFECT ON HSA ESTABLISHMENT DATE

Expenses incurred before an HSA is established are not qualified medical expenses. Notice 2004-2, Q&A-26. Although § 223(b)(8) and this notice provide that certain individuals are treated as eligible individuals on the first day of the taxable year in determining the contribution amount, an HSA is not established before the date that the HSA is actually established. See also Notice 2007-22, 2007-10 I.R.B. 670.

REPORTING

Neither employers nor trustees are responsible for reporting whether an individual remains an eligible individual during the testing period.

EFFECTIVE DATE

Section 223(b)(2)(A) and (B) and § 223(b)(8), allowing full contributions for months preceding the month that an individual is an eligible individual, are effective for taxable years beginning after December 31, 2006.

INTERACTION WITH § 408(d)(9)

See Notice 2008-51, also published in 2008-25 I.R.B.

EFFECT ON OTHER DOCUMENTS

Notice 2004-2 and Notice 2004-50 are modified.

DRAFTING INFORMATION

The principal author of this notice is Leslie R. Paul of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). For further information regarding this notice contact Ms. Paul at (202) 622-6080 (not a toll-free call).