

30 Employee Health Benefits

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■ New for 2025 ■

- **HSA and MSA limitations.** The HSA and Archer MSA limitations have been adjusted for inflation. See *HSA Limitations* and *Archer MSA Limitations*, below.

HSA Limitations (page 30-8)

Annual contribution is limited to:	2025	2024	2023
Self-only coverage, under age 55	\$4,300	\$4,150	\$3,850
Self-only coverage, age 55 or older	\$5,300	\$5,150	\$4,850
Family coverage, under age 55*	\$8,550	\$8,300	\$7,750
Family coverage, age 55 or older*	\$9,550	\$9,300	\$8,750
Minimum annual deductibles:			
Self-only coverage	\$1,650	\$1,600	\$1,500
Family coverage	\$3,300	\$3,200	\$3,000
Maximum annual deductible and out-of-pocket expense limits:			
Self-only coverage	\$8,300	\$8,050	\$7,500
Family coverage	\$16,600	\$16,100	\$15,000

* Assumes only one spouse has an HSA. If both spouses have HSAs, see *Both spouses age 55 or older*, page 30-9.

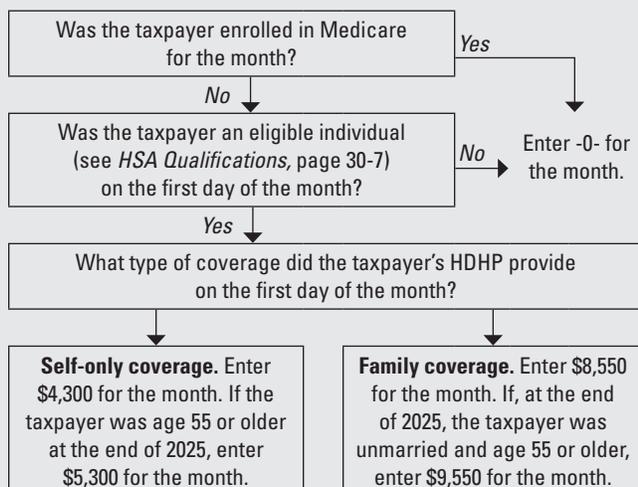
Note: For tax years 2021–2026 limits see *Health Care*, page 1-5.

HSA Penalties (page 30-12)

Possible HSA Error	Additional Tax
Excess contributions.	6% of excess contributions not withdrawn by the tax return due date.
Failure to remain an eligible individual during test period.	10% of contributions to HSA that would have been made except for the last-month rule.
Distributions not used for qualified medical expenses.	Before age 65, 20% of ineligible distribution.

2025 HSA Limit Chart (page 30-8)

Use this chart if taxpayer is not an eligible individual on December 1 or changed coverage (individual—family) during the year. Go through the chart for each month of 2025. Then sum the monthly amounts and divide by 12.



Where to Deduct Employer HSA Contributions (page 30-13)

If employer is a:	Deduct employee HSA contribution on:
Sole Proprietor	Line 14, Schedule C (Form 1040)
Farmer (Sole Proprietor)	Line 15, Schedule F (Form 1040)
C Corporation	Line 24, Page 1, Form 1120
S Corporation	Line 18, Page 1, Form 1120-S
Partnership	Line 19, Page 1, Form 1065

Archer MSA Limitations (page 30-13)

Minimum annual deductibles:	2025	2024	2023
Self-only coverage	\$2,850	\$2,800	\$2,650
Family coverage	\$5,700	\$5,550	\$5,300
Maximum annual deductibles:			
Self-only coverage	\$4,300	\$4,150	\$3,950
Family coverage	\$8,550	\$8,350	\$7,900
Annual out-of-pocket expense limits			
Self-only coverage	\$5,700	\$5,550	\$5,300
Family coverage	\$10,500	\$10,200	\$9,650

Note: For tax years 2021–2026 limits see *Health Care*, page 1-5.

30-2 Employee Health Benefits

2025 Medical Fringe Benefit Plans

	Eligibility*	Contributions	Health Plan Deductibles	Carryover from Year to Year	Distributions	Portability	Rollovers
Flexible Spending Arrangement (FSA) — IRC §125 (see page 30-5)	Must work for an employer that sets up a written cafeteria plan for eligible employees allowing them to choose between taxable wages or qualified benefits which are excluded from taxable wages. Qualified benefits can include accident and health benefits. Self-employed persons are not eligible for an FSA.	Employee decides at the beginning of the year how much to set aside from wages to fund health benefits. Contributions are limited to \$3,300.	There is no health insurance minimum or maximum deductible requirement.	Balances at year end are governed by plan document. An FSA is generally a “use-it-or-lose-it” plan with any remaining balance forfeited. However, a plan may allow either the use of the remaining balance by March 15 (grace period), or the carryover of up to \$660 of the remaining balance, but not both provisions.	Tax free if used to pay medical expenses. Cannot be used for long-term care or health insurance premiums. Distributions not allowed for non-medical expenses. <i>Exception: See Qualified Reservist Distribution, Tab 13.</i>	Benefits cannot be transferred to a new employer’s plan.	None allowed.
Health Reimbursement Arrangement (HRA) — IRC §105(b) (see page 30-4)	Must work for an employer that sets up a written plan for eligible employees. The individual must have minimum essential coverage. Self-employed persons are not eligible for an HRA.	The employer funds the reimbursements and decides the limit on the amount that may be reimbursed. The employee does not set aside any wages to fund the health benefits.	There is no health insurance minimum or maximum deductible requirement.	No limitation imposed by the IRC from carrying benefits over from year to year. However, the employer may impose a limit on the amount of benefits carried over to the next year.	Tax free if used to pay medical expenses, including the cost of long-term care and health insurance premiums paid by the employee. Distributions for non-medical expenses are taxable and included in employee’s gross income.	Generally no restriction on transferring benefits to new employer if the employer’s plan permits.	None allowed.
Health Savings Account (HSA) — IRC §223 (see page 30-7)	The individual must have qualifying high-deductible health insurance. The individual cannot have any other health coverage (certain exceptions apply for disability, dental, vision, and long-term care insurance). The individual cannot be enrolled in Medicare. The individual cannot be claimed as a dependent on someone else’s tax return.	The participant either makes tax deductible contributions to his or her HSA, the employer contributes tax-free money to the plan on behalf of the employee, or a combination of both. Contributions are not limited by compensation. See <i>HSA Limitations</i> , page 30-8.	Health insurance deductible for self-only coverage must be at least \$1,650. The deductible for family coverage must be at least \$3,300. Maximum annual deductible and out-of-pocket expense limit is \$8,300 for self-only coverage and \$16,600 for family coverage.	Funds left in the health savings account at the end of the year carry over to the following year. The participant is always 100% vested in the savings account balance.	Tax free if used to pay medical expenses. Distributions for non-medical expenses are taxable and subject to a 20% penalty. The penalty does not apply after the participant’s death, disability, or reaching age 65.	The HSA remains with the employee (or self-employed individual) even after leaving the job.	A rollover from one HSA to another HSA is allowed. A rollover from one MSA to an HSA is allowed. Rollovers are not subject to annual contribution limits. Same 60-day and 1-year rollover rules for IRAs apply. A one-time rollover from an IRA to an HSA is allowed.
Medical Savings Account (Archer MSA) — IRC §220 (see page 30-13)	The individual must have qualifying high-deductible health insurance and work for a small employer with 50 or fewer workers, or be self-employed. New MSAs cannot be established after 2007 unless the individual was an active MSA participant before 2008, or the individual becomes eligible for coverage under an existing MSA plan of an employer.	The participant either makes tax deductible contributions to his or her MSA, or the employer contributes tax-free money to the plan on behalf of the employee, but not a combination of both. Self-only coverage contributions limited to 65% of health insurance plan deductible. Family coverage contributions limited to 75% of health insurance plan deductible. Contributions cannot exceed compensation.	Health insurance deductible for self-only coverage must be between \$2,850 and \$4,300. The deductible for family coverage must be between \$5,700 and \$8,550. Maximum annual out-of-pocket expense limit is \$5,700 for self-only coverage and \$10,500 for family coverage.	Funds left in the medical savings account at the end of the year carry over to the following year. The participant is always 100% vested in the savings account balance.	Tax free if used to pay medical expenses. Distributions for non-medical expenses are taxable and subject to a 20% penalty. The penalty does not apply after the participant’s death, disability, or reaching age 65.	The MSA remains with the employee (or self-employed individual) even after leaving the job.	A rollover from one MSA to another MSA is allowed. A rollover from one MSA to an HSA is allowed. Rollovers are not subject to annual contribution limits. Same 60-day and 1-year rollover rules for IRAs apply.

* The spouse and dependents of an eligible individual may generally be included in the medical plan coverage assuming all other eligibility requirements are met.

Employer Contributions to Accident and Health Plans

Cross References

- IRC §106, *Contributions by employer to accident and health plans*
- IRC §4980H, *Shared responsibility for employers regarding health coverage*
- Reg. §1.106-1
- Notice 2013-54

Related Topics

- Medical Expenses, page 4-2
- Self-employed health insurance deduction, Tab 5
- Premium Tax Credit, Tab 11
- Employee Fringe Benefits, page 22-2
- Credit for Small Employer Health Insurance Premiums (Form 8941), Tab 31

Employer-Provided Medical Coverage

In general, gross income of an employee does not include employer-provided coverage under an accident or health plan. [IRC §106(a)]

Employer-provided coverage refers to contributions made by the employer to an accident or health plan (through insurance or otherwise) as a form of employee compensation to cover personal injuries or sickness incurred by an employee, the employee's spouse, and the employee's dependents. Employees include retired employees and surviving spouses of employees and retired employees. (Reg. §1.106-1)

Adult children. Health insurance coverage for any child of the employee who has not attained age 27 at the end of the tax year is also excluded from income. Child means a son, daughter, stepson, stepdaughter, or eligible foster child but does not include grandchildren or the spouse of a child.

Author's Comment: The rules for claiming a dependent do not apply to this exclusion. The adult child does not need to be a student or a dependent. The adult child can be married.

Plans that offer dependent coverage are required to make coverage available for children until they turn age 26. This rule applies to:

- All plans in the individual market and to new employer plans.
- Existing employer plans unless the adult child has another offer of employer-based coverage (such as through his or her own job).

Types of employer contributions. The employer may contribute to an accident or health plan either by:

- Paying the premium (or a portion of the premium) on a policy of accident or health insurance covering one or more employees, or
- Contributing to a separate trust or fund that provides accident or health benefits directly or through insurance to one or more employees.

If the policy, trust, or fund provides other benefits, IRC section 106 applies only to the portion of the employer's contribution allocable to accident or health benefits. (Reg. §1.106-1)

Fringe benefit. Employer contributions to an accident and health plan are tax free to the employee and deductible by the employer.

Form W-2 reporting. Employers are required to report the cost of employer-provided health care coverage in box 12 (code DD), Form W-2, *Wage and Tax Statement*. The amount reported with code DD is not taxable. The IRS provided relief for smaller

employers (those filing fewer than 250 Forms W-2 in the preceding calendar year) by making this requirement optional until further notice.

HSAs, MSAs, and long-term care benefits. An IRC section 106 plan may include employer contributions to an Archer MSA or an HSA. This includes employer contributions to the cost of qualified long-term care insurance but does not include long-term care benefits provided through flexible spending arrangements (FSAs). [IRC §106(c)]

COBRA

The Consolidated Omnibus Budget Reconciliation Act (COBRA) gives workers and their families who lose their health benefits the right to choose to continue group health benefits for a limited time under certain circumstances (voluntary or involuntary job loss, reduction in hours worked, transition between jobs, death, divorce, and other life events). Qualified individuals may be required to pay the entire premium for this continuation coverage, up to 102% of the cost to the plan.

COBRA generally requires that group health plans sponsored by employers with 20 or more employees in the prior year offer employees and their families continuation coverage. It also requires employers and plans to provide notice. (IRC §4980B)

Excludible COBRA benefits. If former employees continue to receive health benefits under their former employer's plan, the benefits are excluded from income.

Employer Shared Responsibility Provisions

Applicable large employers (ALEs) must either offer minimum essential health coverage that is affordable to full-time employees (and dependents) or potentially pay a penalty to the IRS. The employer shared responsibility provisions are also referred to as the employer mandate.

ALE. An ALE is an employer that has on average at least 50 full-time employees (including full-time equivalents) during the preceding calendar year.

Dependent. For purposes of the employer mandate, a dependent is an employee's child who has not reached the age of 26. Spouses are not considered dependents and neither are stepchildren or foster children.

Penalty. An ALE may be subject to one of two employer shared responsibility payments.

Failure to offer minimum essential coverage. An ALE will owe this penalty if, for any month, it does not offer minimum essential coverage to at least 95% of its full-time employees (and dependents), and at least one full-time employee receives the Premium Tax Credit for purchasing coverage through the marketplace.

Failure to offer affordable minimum essential coverage that provides minimum value. If an ALE is not subject to the failure to offer minimum essential coverage penalty, the ALE may still be liable for a penalty for each full-time employee who receives the Premium Tax Credit for purchasing coverage through the marketplace. A full-time employee could receive the Premium Tax Credit if the minimum essential coverage offered is:

- Not affordable,
- Covers less than 60% of the total allowed cost of benefits under the plan, or
- Not offered to the employee.

Cafeteria plans. If an employee wants to purchase a health plan through the marketplace, he or she cannot use funds contributed to a cafeteria plan to pay for coverage [IRC §125(f)(3)]. For more information on cafeteria plans, see *Cafeteria Plans (IRC §125)*, page 22-3.

Credit for Small Employer Health Insurance Premiums

This credit is designed to encourage small employers to offer health insurance coverage or to maintain the coverage they already have. Only premiums paid by the employer for employees' health insurance coverage purchased through the Small Business Health Options Program (SHOP) Marketplace under a qualifying arrangement are counted in calculating the credit. See *Credit for Small Employer Health Insurance Premiums (Form 8941)*, Tab 31.

Health Reimbursement Arrangement (HRA)

Cross References

- IRS Pub. 15-B, *Employer's Tax Guide to Fringe Benefits*
- IRS Pub. 969, *Health Savings Accounts and Other Tax-Favored Health Plans*
- IRC §105(b), *Amounts expended for medical care*
- IRC §501(h)(3)(B), *Exclusion of certain employees*
- TD 9949
- Notice 2017-67

Related Topics

- Medical Expenses, page 4-2
- Self-employed health insurance deduction, Tab 5
- Premium Tax Credit, Tab 11
- Employee Fringe Benefits, page 22-2

HRA Tax Benefits

Health reimbursement arrangements (HRAs) are funded solely by an employer. Employees are reimbursed tax free for qualified medical expenses (including health insurance premiums) up to a maximum dollar amount for a coverage period. An HRA may be offered with other health plans, including flexible spending arrangements (FSAs).

Benefits of an HRA include the following.

- Employer contributions can be excluded from the employee's gross income.
- Reimbursements are generally tax free if the employee pays qualified medical expenses.
- Any unused amounts in the HRA can be carried forward for reimbursements in later years.

Qualifying for an HRA

HRAs are employer-established benefit plans that may be offered in conjunction with other employer-provided health benefits.

The plan cannot discriminate in favor of highly compensated individuals. The employer can exclude employees who:

- Have not completed at least three years of service,
- Have not attained age 25,
- Are part-time or seasonal employees,
- Are certain union employees, or
- Are nonresident aliens with no U.S. source wages.

Self-employed persons are not eligible for HRAs.

Certain limitations may apply to highly-compensated participants.

To maintain tax-qualified status, HRAs must comply with certain requirements that apply to other accident and health plans. See IRS Pub. 15-B, *Employer's Tax Guide to Fringe Benefits*.

PCORTF fee. An employer that offers an HRA is considered the plan sponsor of an applicable self-insured health plan and therefore, is liable for the Patient-Centered Outcomes Research Trust Fund (PCORTF) fee. The fee is an excise tax that is reported

and paid annually for the second quarter (due date July 31) by filing Form 720, *Quarterly Federal Excise Tax Return*. The fee is computed using the average number of individuals covered under the plan and the adjusted applicable dollar amount of \$3.47 (per participant) for plan years ending on or after October 1, 2024, and before October 1, 2025. (Notice 2024-83)

HRA Contributions

HRAs are funded solely by employer contributions. Employees may not contribute. HRAs may not be funded by employee salary deferrals under a cafeteria plan. Contributions are not includible in income and the employee does not pay federal income tax or employment taxes on contributions to the HRA.

Amount of contribution. There is no limit on the amount an employer can contribute to an HRA. Some, but not all, HRAs permit amounts that remain in the HRA at the end of the year to be carried to the next year. The employer is not permitted to refund any part of the balance to the employee. These amounts may never be used for anything but reimbursements for qualified medical expenses.

HRA Distributions

Distributions from an HRA must be paid to reimburse the employee for qualified medical expenses. The expense must have been incurred on or after the date the employee was enrolled in the HRA.

If the plan permits distributions for a reason other than the reimbursement of qualified medical expenses, all distributions from the HRA in the current year (including reimbursements of qualified medical expenses) are included in employee gross income. This rule applies if, for example, the plan permits amounts to be:

- Paid to the employee in cash at the end of the year or on termination of employment,
- Paid in cash to the employee's beneficiary or estate,
- Paid as medical benefits to a designated beneficiary other than the employee's spouse or dependents, or
- Transferred at the end of the year to a retirement plan.

Reimbursements under an HRA can be made to the following.

- Current and former employees.
- Spouses and dependents of those employees.
- Employee's child under age 27 at the end of the tax year.
- Any person the employee could have claimed as a dependent on his or her return except that:
 - The person filed a joint return,
 - The person had gross income of \$5,200 (2025) or more, or
 - The employee, or spouse if filing jointly, could be claimed as a dependent on someone else's 2025 return.
- Spouses and dependents of deceased employees.

For this purpose, a child of parents that are divorced, separated, or living apart for the last six months of the calendar year is treated as the dependent of both parents, whether or not the custodial parent releases the claim to the child's exemption.

Qualified medical expenses. Qualified medical expenses include the following.

- Expenses that would generally qualify for the medical and dental expenses deduction. See *Deductible Medical Expenses*, page 4-2.
- Over-the-counter medicine, menstrual care products, and condoms.
- Health insurance premiums.
- Long-term care coverage premiums.
- Amounts not covered under another health plan.
- Amounts paid for telehealth or other remote care.

For employees covered under both an HRA and a health FSA, see IRS Notice 2002-45, Part V.

Excepted Benefit HRA

An excepted benefit HRA can reimburse individual insurance premiums if it covers only excepted benefits. Other group health plan coverage that is not limited to excepted benefits and that is not an HRA must be available from the employer. [Reg. §54.9831-1(c)(3)]

Excepted benefits. Limited-scope dental and vision benefits, or long-term care benefits are excepted if provided under a separate policy and not an integral part of a group health plan.

Contribution limit. The maximum annual employer contribution is \$2,150 (2025).

Qualified Small Employer HRA (QSEHRA)

QSEHRAs allow eligible small employers to pay or reimburse medical care expenses, including health insurance premiums, of eligible employees and their family members. A QSEHRA is not a group health plan, and, therefore, is not subject to group health plan requirements. Generally, payments from a QSEHRA to reimburse an eligible employee's medical expenses are not includible in the employee's gross income if the employee has coverage that provides minimum essential coverage.

A QSEHRA is an arrangement that meets all the following requirements.

- The plan is funded solely by the employer. Salary reduction contributions are not allowed.
- The plan provides for payment or reimbursement of medical expenses incurred by the employee or the employee's family members (after the employee provides proof of coverage).
- The annual amount of payments and reimbursements cannot exceed \$6,350 (2025) for self-only coverage and \$12,800 (2025) for family coverage.
- The plan is generally provided on the same terms to all eligible employees.

Eligible employer. An eligible employer must have less than 50 full-time (including full-time equivalent) employees and must not offer any employees a group health insurance plan (including an HRA or health FSA).

Reporting requirements. Report in box 12, Form W-2, using code FF, the amount of payments and reimbursements the employee is entitled to receive from the QSEHRA for the year without regard to the amount of payments or reimbursements actually received.

Individual Coverage HRA (ICHRA)

An ICHRA reimburses employees for medical expenses, up to a maximum dollar amount that the employer makes available each year. The employer can allow unused amounts in any year to roll over from year to year. Employees must be enrolled in individual health insurance or Medicare for each month the employee is covered by the ICHRA. This can be individual health insurance purchased on or off the marketplace. However, it cannot be short-term, limited-duration insurance or coverage consisting solely of dental, vision, or similar excepted benefits.

An ICHRA is available to employers of all sizes, however, certain conditions must be met. (Reg. §54.9802-4)

- The individual and dependents must be enrolled in individual health insurance coverage that complies with Reg. §54.9815-2711(a)(2) and Reg. §54.9815-2713(a)(1).
- The employer may not also offer a traditional group health plan to the same class of employees.
- Coverage must be offered on the same terms to all employees within each class.
- An eligible individual must be permitted to opt out of and waive future reimbursements each year.
- Reasonable procedures for coverage substantiation must be implemented.

- Written notice about the ICHRA, including its interaction with the Premium Tax Credit, must be provided to each individual at least 90 days before the beginning of each plan year.

Health Care Sharing Ministry (HCSM)

An HCSM is defined as the following.

- It must be a tax-exempt organization,
- Its members must share a common set of ethical or religious beliefs and share medical expenses among themselves in accordance with those beliefs and without regard to the state in which the member resides or is employed,
- Its members must retain membership even after they develop a medical condition,
- It must have been in existence at all times since December 31, 1999, and the medical expenses of its members must have been shared continuously and without interruption since at least December 31, 1999, and
- It must conduct an annual audit which is performed by an independent certified public accounting (CPA) firm in accordance with generally accepted accounting principles (GAAP), and be made available to the public upon request.

Current regulations. Under current regulations, membership fees are not considered health insurance (although they do qualify for an exemption under the minimum essential coverage mandate), and HCSMs cannot integrate with an individual coverage HRA.

REG-109755-19. In June 2020, the IRS issued proposed regulations allowing the treatment of expenses relating to HCSMs, among others, as eligible medical expenses under IRC section 213(d).

Medical insurance. The proposed regulations provide that payments for membership in an HCSM are medical insurance under IRC section 213(d)(1)(A).

HRAs and HSAs. Under the regulations authorizing individual coverage HRAs, HCSMs cannot integrate with an individual coverage HRA. However, under these proposed regulations, an IRA may reimburse payments for membership in an HCSM as a medical care expense. Because the proposed regulations provide that payments for membership are medical insurance that is not permitted insurance, membership in an HCSM would preclude an individual from contributing to an HSA.

Flexible Spending Arrangement (FSA)

Cross References

- IRS Pub. 15-B, *Employer's Tax Guide to Fringe Benefits*
- IRS Pub. 969, *Health Savings Accounts and Other Tax-Favored Health Plans*
- IRC §125, *Cafeteria plans*
- Notice 2013-71

Related Topics

- Medical Expenses, page 4-2
- Self-employed health insurance deduction, Tab 5
- Premium Tax Credit, Tab 11
- Employee Fringe Benefits, page 22-2

FSA Tax Benefits

Health flexible spending arrangements (FSAs) are employer plans that allow employees to be reimbursed for medical expenses. FSAs are usually funded through voluntary salary reduction agreements, although the employer may also contribute. FSA funds may not be used to pay for health insurance premiums.

Benefits of an FSA include the following.

- Contributions made by employers are excluded from employee gross income.
- No employment or federal income taxes are deducted from contributions.
- Withdrawals are generally tax free if the taxpayer pays qualified medical expenses.
- Employees can withdraw funds from the FSA before their own funds have been placed in the account (the FSA must be able to pay the employee's entire annual contribution at any time during the plan year).

Qualifying for an FSA

Health FSAs are employer-established plans. These may be offered in conjunction with other employer-provided benefits as part of a cafeteria plan. Employees must be offered coverage under an employer-sponsored group health plan.

For a health FSA to maintain tax-qualified status, employers must comply with certain requirements that apply to cafeteria plans. For example, there are restrictions for plans that cover highly-compensated employees and key employees. See *Nondiscrimination Rules for Fringe Benefits*, page 22-2.

The plans must also comply with rules applicable to other accident and health plans. See IRS Pub. 15-B, *Employer's Tax Guide to Fringe Benefits*.

Note: Self-employed persons are not eligible for an FSA.

FSA Contributions

Employees contribute to an FSA by electing an amount to be voluntarily withheld from pay by their employer. The employer may also contribute to the FSA if specified in the plan.

Employees do not pay federal income tax or employment taxes on their own contributions or on employer contributions.

Exception: Contributions made by employers to provide coverage for long-term care insurance are included in income but are not subject to employment taxes.

When to contribute. Prior to the beginning of the plan year, the employee designates how much he or she wants to contribute. The employer then deducts amounts periodically in accordance with the annual election. Elections can be changed or revoked only if there is a change in employment or family status that is specified by law and the plan.

Contribution limitations. An employer can contribute the greater of \$500 or a match to the employee contribution of up to \$3,300 (2025). [Reg. §54.9831-1(c)(3)(v)(B)]

Employee limitations. Employee contributions to a health FSA are limited to \$3,300 (2025). A cafeteria plan that does not limit health FSA contributions will result in all amounts becoming taxable to the employee.

Balance at year-end. Amounts in the account at the end of the plan year are generally forfeited.

Grace period. Normally, plans can provide for a grace period of up to 2½ months after the end of the plan year. Expenses incurred in the grace period can be paid from the previous year's balance.

Carryover rule. Employers have the option to allow employees to carry over a limited amount (\$660 in 2025) of the balance in their account to the following year.

Employers have the option to specify an amount lower than the maximum carryover amount or not permit any carryover at all. Employers cannot have both a carryover and a grace period provision. (Notice 2013-71)

Use of carryover. The carryover balance may be used to pay or reimburse medical expenses incurred during the year to which it is carried. For this purpose, the amount remaining at the end of the year is the amount unused after medical expenses have been reimbursed at the end of the plan's run-out period for the plan year. A run-out period is the period immediately following the end of the year during which the participant can submit a claim for reimbursement of expenses incurred for qualified benefits during the plan year.

FSA Distributions

Generally, distributions from a health FSA must be paid only to reimburse the employee for qualified medical expenses incurred during the period of coverage. The employee must be able to receive the maximum amount of reimbursement (the amount the employee elected to contribute for the year) at any time during the coverage period, regardless of the amount the employee has contributed to date.

Qualified medical expenses. Qualified medical expenses for a health FSA include the following.

- Expenses that would generally qualify for the medical and dental expenses deduction on Schedule A (Form 1040). See *Deductible Medical Expenses*, page 4-2.
- Amounts paid for over-the-counter medicine, menstrual care products, and condoms.

Qualified medical expenses are those incurred by the following persons.

- The employee and his or her spouse.
 - All dependents claimed by the employee on his or her tax return.
 - Any person the employee could have claimed as dependent on his or her tax return except that:
 - The person filed a joint return,
 - The person had gross income of \$5,200 (for 2025) or more, or
 - The employee, or spouse if filing jointly, could be claimed as a dependent on someone else's 2025 tax return.
 - The employee's child under age 27 at the end of the tax year.
- FSA distributions cannot be received for:
- Amounts paid for health insurance premiums.
 - Amounts paid for long-term care coverage or expenses.
 - Amounts that are covered under another health plan.

Substantiation. Medical expenses submitted for reimbursement must be substantiated. Employer-provided debit, credit, and stored value cards can be used to reimburse participants in an FSA.

Qualified reservist distribution. FSAs can be distributed to reservists ordered or called to active duty, if the plan allows these distributions. The employer must report the distribution as wages on Form W-2, *Wage and Tax Statement*, for the year in which the distribution is made. The distribution is subject to employment taxes and is included in the employee's gross income.

A qualified reservist distribution is allowed if the employee was (because he or she was in the reserves) ordered or called to active duty for a period of more than 179 days, or for an indefinite period, and the distribution is made during the period beginning on the date of the order or call and ending on the last date that reimbursements could otherwise be made for the plan year that includes the date of the order or call.

Health Savings Account (HSA)

Cross References

- Form 1099-SA, *Distributions From an HSA, Archer MSA, or Medicare Advantage MSA*
- Form 5498-SA, *HSA, Archer MSA, or Medicare Advantage MSA Information*
- Form 8889, *Health Savings Accounts (HSAs)*
- IRS Pub. 15-B, *Employer's Tax Guide to Fringe Benefits*
- IRS Pub. 969, *Health Savings Accounts and Other Tax-Favored Health Plans*
- IRC §223, *Health savings accounts*

Related Topics

- Medical Expenses, page 4-2
- Self-employed health insurance deduction, Tab 5
- Premium Tax Credit, Tab 11
- Health Savings Accounts (HSAs) (IRC §223), page 22-6

HSA Tax Benefits

An HSA is a tax-exempt trust or custodial account set up with a qualified HSA trustee to pay or reimburse certain medical expenses. No permission or authorization from the IRS is necessary to establish an HSA, assuming the participant is otherwise eligible to set up an HSA. A qualified HSA trustee can be a bank, an insurance company, or anyone already approved by the IRS to be a trustee of individual retirement arrangements (IRAs) or Archer MSAs. The HSA can be established through a trustee that is different from the health plan provider.

HSA benefits include the following.

- Contributions outside of payroll made by the participant, or someone other than the employer, are deductible even if the participant does not itemize deductions.
- Contributions made by the employer (including contributions made through a cafeteria plan) are excluded from the employee's gross income.
- Contributions remain in the account from year-to-year until the participant withdraws funds from the account.
- Interest or other earnings on the assets in the account accumulate tax free.
- Distributions are tax free if used to pay qualified medical expenses.
- An HSA stays with the participant even if he or she changes employers or leaves the work force.

HSA Qualifications

To be an eligible individual and qualify for an HSA, an individual must meet the following requirements.

- The individual must be covered under a high deductible health plan (HDHP) on the first day of the month.
- The individual must have no other health coverage. For exceptions, see *Other health coverage*, page 30-8.
- The individual is not enrolled in Medicare.
- The individual cannot be claimed as a dependent on someone else's 2025 tax return.

See *Last-month rule*, page 30-8.

Spouse with non-HDHP coverage. An individual can be an eligible individual even if his or her spouse has non-HDHP family coverage, provided the spouse does not cover the individual.

Author's Comment: Because a health flexible spending arrangement (FSA) and a health reimbursement arrangement (HRA) can be used to reimburse the expenses of a spouse, if the spouse with non-HDHP coverage is covered by either of these options, the spouse with HDHP coverage is not an eligible individual. For exceptions, see *Other employee health plans*, page 30-8.

No joint HSAs. Each spouse who is an eligible individual must set up a separate HSA. However, an eligible individual with an HSA may take tax-free distributions from the account to pay qualified medical expenses of his or her spouse even if the spouse does not have his or her own HSA.

High deductible health plan (HDHP). An HDHP has:

- A higher annual deductible than typical health plans, and
- A maximum limit on the sum of the annual deductible and out-of-pocket medical expenses that the participant must pay for covered expenses. Out-of-pocket expenses include co-payments and other amounts, but do not include premiums.

See *HSA Limitations* chart, page 30-8.

Out-of-network services. The maximum annual deductible and other out-of-pocket expense limitations do not apply to deductibles and expenses for out-of-network services if the plan uses a network of providers. Instead, only deductibles and out-of-pocket expenses for services within the network should be used to calculate whether the limits apply. See *HSA Limitations* chart, page 30-8.

Preventive care benefits. An HDHP may provide preventive care benefits without a deductible or with a deductible below the minimum annual deductible.

For more information on preventative care, see Notice 2024-75.

Telehealth and other remote care. An HDHP may have a zero deductible for telehealth and other remote care services.

Surprise billing. An HDHP may provide benefits under federal and state surprise billing laws with a zero deductible.

Insulin products. AN HDHP may have a zero deductible for selected insulin products.

COVID-19 testing and treatment. For plan years ending after December 31, 2024, an HDHP is not permitted to provide health benefits associated with testing for and treatment of COVID-19 without a minimum deductible. (Notice 2023-37)

Self-only and family coverage. Self-only HDHP coverage is an HDHP covering only an eligible individual. Family HDHP coverage is an HDHP covering an eligible individual and at least one other individual (whether or not that individual is an eligible individual).

Example: Jenny is an eligible individual and qualifies to contribute to an HSA. She has one dependent daughter, Elsie. Both Jenny and Elsie are covered under an "employee plus one" HDHP offered by Jenny's employer. Jenny's coverage is considered a family HDHP even though her daughter Elsie is not considered an eligible individual.

Family plans that do not meet the high deductible rules. Some family plans have deductibles for both the family as a whole and for individual family members. Under these plans, if a person meets the individual deductible, that person is not required to meet the higher annual deductible amount for the family. If either the deductible for the family as a whole, or the deductible for an individual family member, is below the minimum annual deductible for family coverage, the plan does not qualify as an HDHP.

Example: Bernie has family health insurance coverage in 2025. The annual deductible for the family plan is \$5,000. This plan also has an individual deductible of \$3,000 for each family member. The plan does not qualify as an HDHP because the deductible for an individual family member is below the minimum annual deductible (\$3,300) for family coverage in 2025.

Other health coverage. An individual (and spouse if there is family coverage) generally cannot have any other health coverage that is not an HDHP. However, an individual can still be an eligible individual even if his or her spouse has non-HDHP coverage, provided the individual is not covered by the non-HDHP.

Exception: An individual can be an eligible individual with other insurance in addition to HDHP coverage if the additional insurance provides benefits only for the following items.

- Liabilities incurred under workers' compensation laws, tort liabilities, or liabilities related to ownership or use of property.
- A specific disease or illness.
- A fixed amount per day (or other period) of hospitalization.

Indian Health Services (IHS). An individual eligible to receive medical services at an IHS facility, but has not actually received such services during the previous three months, is eligible to establish and make contributions to an HSA. (Notice 2012-14)

Limited coverage. An eligible individual can also have coverage (whether provided through insurance or otherwise) in addition to HDHP coverage for the following items.

- Accidents.
- Disability.
- Dental care.
- Vision care.
- Long-term care.

Note: Plans in which substantially all the coverage is for the above listed items are not HDHPs. For example, if a plan provides coverage substantially all of which is for a specific disease or illness, the plan is not an HDHP for purposes of establishing an HSA.

Prescription drug plans. An individual can have a prescription drug plan, either as part of an HDHP or a separate plan (or rider), and qualify as an eligible individual if the plan does not provide benefits until the minimum annual deductible of the HDHP has been met. If an individual can receive benefits before that deductible is met, the individual is not an eligible individual for purposes of making contributions to an HSA.

Other employee health plans. An employee covered by an HDHP and a health FSA, or an HRA that pays or reimburses qualified medical expenses, generally cannot make contributions to an HSA.

Exceptions: An employee can make contributions to an HSA while covered under an HDHP and one or more of the following arrangements.

- **Limited-purpose health FSA or HRA.** These arrangements can pay or reimburse the items listed under *Other health coverage*, above, except long-term care. These arrangements can also pay or reimburse preventive care expenses without needing to satisfy the deductible.
- **Suspended HRA.** Before the beginning of an HRA coverage period, an employee can elect to suspend the HRA. The HRA does not pay or reimburse, at any time, the medical expenses incurred during the suspension period except preventive care and items listed under *Other health coverage*, above. When the suspension period ends, the employee is no longer eligible to make contributions to an HSA.
- **Post-deductible health FSA or HRA.** These arrangements do not pay or reimburse any medical expenses incurred before the minimum annual deductible amount is met. The deductible for these arrangements does not need to be the same as the deductible for the HDHP, but benefits may not be provided before the minimum annual deductible amount is met.

- **Retirement HRA.** This arrangement pays or reimburses only those medical expenses incurred after retirement. After retirement, the individual is no longer eligible to make contributions to an HSA.

Health FSA—grace period. Coverage during a grace period by a general purpose health FSA is allowed if the balance in the health FSA at the end of its prior year plan is zero. See *Grace period*, page 30-6.

HSA Contributions

Any eligible individual can contribute to an HSA. For an employee's HSA, the employee, the employee's employer, or both may contribute to the employee's HSA in the same year. For an HSA established by a self-employed (or unemployed) individual, the individual can contribute. Family members or any other person may also make contributions on behalf of an eligible individual.

Cash contributions only. Contributions to an HSA must be made in cash, not stock or property.

Author's Comment: Even though a taxpayer cannot contribute stocks or other property to an HSA, some HSA trustees will allow a portion of the funds to be invested.

Limit on Contributions

The amount an eligible individual or any other person can contribute to an HSA depends on the type of HDHP coverage, age, the date the individual became an eligible individual, and the date the individual ceases to be an eligible individual.

If an individual is considered an eligible individual for the entire year and did not change the type of coverage, the full amount listed on the *HSA Limitations* chart, below, may be contributed based on the type of coverage. If the individual is not an eligible individual for the entire year, or changed his or her coverage during the year, the contribution limit is the greater of:

- 1) The limitation shown on the last line of the *Line 3 Limitation Chart and Worksheet* in the instructions for Form 8889, *Health Savings Accounts (HSAs)*, or
- 2) The maximum annual HSA contribution based on the HDHP coverage (self-only or family) on the first day of the last month of the tax year.

HSA Limitations

Annual contribution is limited to:	2025	2024	2023
Self-only coverage, under age 55	\$4,300	\$4,150	\$3,850
Self-only coverage, age 55 or older	\$5,300	\$5,150	\$4,850
Family coverage, under age 55*	\$8,550	\$8,300	\$7,750
Family coverage, age 55 or older*	\$9,550	\$9,300	\$8,750
Minimum annual deductibles:			
Self-only coverage	\$1,650	\$1,600	\$1,500
Family coverage	\$3,300	\$3,200	\$3,000
Maximum annual deductible and out-of-pocket expense limits:			
Self-only coverage	\$8,300	\$8,050	\$7,500
Family coverage	\$16,600	\$16,100	\$15,000

* Assumes only one spouse has an HSA. If both spouses have HSAs, see *Both spouses age 55 or older*, page 30-9.

Note: For tax years 2021 – 2026 limits see *Health Care*, page 1-5.

Last-month rule. Under the last-month rule, if an individual is an eligible individual on the first day of the last month of the tax year, the individual is considered an eligible individual for the entire year. The individual is treated as having the same HDHP coverage for the entire year as the coverage on the first day of the last month.

Example: During 2025, Rodney (who is under age 55) and his family were covered under his employer's health insurance plan until the day he quit on November 30, 2025, to start his own business as a self-employed individual. His former employer's health insurance plan was not an HDHP. On December 1, 2025, Rodney purchased family HDHP coverage. Rodney may contribute up to \$8,550 to his HSA for 2025 because he had HDHP coverage on the first day of the last month of the tax year.

Testing period. If contributions were made to an HSA based on the individual being an eligible individual for the entire year under the last-month rule, the individual must remain an eligible individual during the testing period. For the last-month rule, the testing period begins with the last month of the tax year and ends on the last day of the 12th month following that month. For example, December 1, 2025 through December 31, 2026.

If an individual fails to remain an eligible individual during the testing period (other than because of death or becoming disabled), the individual must include in income the total contributions made to the HSA that would not have been made except for the last-month rule. Include this amount in income in the year in which the individual failed to be an eligible individual. This amount is also subject to a 10% additional tax. The income and additional tax are reported on Part III, Form 8889, *Health Savings Accounts (HSAs)*.

Example: Chris, age 53, becomes an eligible individual on December 1, 2025. He has family HDHP coverage on that date. Under the last-month rule, he contributes \$8,550 to his HSA. Chris fails to be an eligible individual in June 2026. Because Chris did not remain an eligible individual during the testing period, he must include in his 2026 income the contributions made in 2025 that would not have been made except for the last-month rule. Chris uses the worksheet for line 3 in the Form 8889 instructions to determine this amount. Without the last-month rule, he would have only been entitled to contribute \$713 to his HSA ($\$8,550 \div 12$). Chris must include \$7,837 ($\$8,550 - \713) in gross income on his 2026 tax return. A 10% additional tax also applies to this amount.

Example: Erika, age 39, has self-only HDHP coverage on January 1, 2025. Erika changes to family HDHP coverage on November 1, 2025. Because Erika has family HDHP coverage on December 1, 2025, she contributes \$8,550 to her HSA for 2025. Erika fails to be an eligible individual in March 2026. Because she did not remain an eligible individual during the testing period (December 1, 2025 through December 31, 2026), she must include in income the contribution made that would not have been made except for the last-month rule. This amount is calculated as follows.

2025 Month	Allowable Contribution	2025 Month	Allowable Contribution
January	\$4,300	July	\$4,300
February	4,300	August	4,300
March	4,300	September	4,300
April	4,300	October	4,300
May	4,300	November	8,550
June	4,300	December	8,550
Total for 2025			\$60,100
Limitation: Divide total by 12			\$5,008

Erika must include \$3,542 ($\$8,550 - \$5,008$) in gross income on her 2026 tax return. A 10% additional tax also applies to this amount.

Age 55 or older additional contribution. The contribution limit is increased \$1,000 for an individual age 55 or older. For example, an eligible individual age 55 or older with self-only coverage can contribute \$5,300 in 2025 (\$4,300 contribution limit plus \$1,000 additional contribution).

More than one HSA. If an eligible individual has more than one HSA, the total contributions to all the HSAs cannot be more than the limits listed on the *HSA Limitations* chart, page 30-8.

Coordination with Archer MSA. The HSA contribution limit (including any additional contribution) is reduced by the amount of any contribution made to an Archer MSA (including employer contributions) for the year.

Rules for married people. If either spouse has family HDHP coverage, both spouses are treated as having family HDHP coverage. If each spouse has family coverage under a separate plan, the contribution limit for 2025 is \$8,550. Reduce the limit on contributions, before taking into account any additional contributions, by the amount contributed to both spouse's Archer MSAs. After that reduction, the contribution limit is split equally between the spouses unless they agree on a different division. The rules for married people apply only if both spouses are eligible individuals.

Both spouses age 55 or older. If both spouses are age 55 or older and not enrolled in Medicare, each spouse's contribution limit is increased by the additional contribution. Thus, for 2025, total contributions under family coverage (both spouses age 55 or older) cannot be more than \$10,550 ($\$8,550 + \$1,000 + \$1,000$). Each spouse must make the additional contribution to his or her own HSA.

Author's Comment: If only one spouse has an HSA, even if both spouses are age 55 or older and each is considered an eligible individual, the family coverage limit for 2025 is \$9,550 ($\$8,550 + \$1,000$).

Example: For 2025, Joe and his wife, Jolene, are both eligible individuals. They each have family coverage under separate HDHPs. Joe is 58 years old, and Jolene is 53. Joe and Jolene can split the family contribution limit (\$8,550) equally, or they can agree on a different division. If they split it equally, Joe can contribute \$5,275 to his HSA [(50% of $\$8,550$) + \$1,000], and Jolene can contribute \$4,275 to her HSA (50% of $\$8,550$).

Alternatively, if Joe contributes \$1,000 (0% of $\$8,550 + \$1,000$), Jolene can contribute up to \$8,550 (100% of $\$8,550$).

Employer contributions. The eligible contribution amount to an HSA must be reduced by any employer contributions to an employee's HSA that are excludable from income. This includes amounts contributed to an employee's account by an employer through a cafeteria plan.

Enrolled in Medicare. Beginning with the first month an individual is enrolled in Medicare, the HSA contribution limit is zero.

Example: Jeff turned age 65 in July 2025 and enrolled in Medicare that same month. Jeff had an HDHP with self-only coverage and is eligible for an additional contribution of \$1,000. His HSA contribution limit for 2025 is \$2,650 ($\$5,300 \div 12 \times 6$).

Qualified HSA funding distribution. A qualified HSA funding distribution may be made from a traditional IRA or Roth IRA to an HSA. This distribution cannot be made from an ongoing SEP IRA or SIMPLE IRA. For this purpose, a SEP IRA or SIMPLE IRA is ongoing if an employer contribution is made for the plan year ending with or within the tax year in which the distribution would be made.

The maximum qualified HSA funding distribution depends on the HDHP coverage (self-only or family) on the first day of the month in which the contribution is made and the age of the individual as of the end of the tax year. The distribution must be made directly by the trustee of the IRA to the trustee of the HSA. The distribution is not included in income, is not deductible, and reduces the amount that can be contributed to the individual's

HSA. The qualified HSA funding distribution is shown on Part I, Form 8889, for the year in which the distribution is made.

An individual can make only one qualified HSA funding distribution during his or her lifetime. However, if a distribution is made during a month when the individual has self-only HDHP coverage, that individual can make another qualified HSA funding distribution in a later month in that tax year if he or she changes to family HDHP coverage. The total qualified HSA funding distribution cannot be more than the contribution limit for family HDHP coverage, plus any additional contribution to which the individual is entitled.

Qualified HSA funding distribution testing period. An individual must remain an eligible individual during the testing period. For a qualified HSA funding distribution, the testing period begins with the month in which the qualified HSA funding distribution is contributed and ends on the last day of the 12th month following that month. For example, if a qualified HSA funding distribution is contributed to an HSA on August 15, 2025, the testing period begins in August 2025 and ends on August 31, 2026.

If an individual fails to remain an eligible individual during the testing period, other than because of death or becoming disabled, include in income the qualified HSA funding distribution. Include this amount in income in the year in which the individual fails to be an eligible individual. This amount is also subject to a 10% additional tax. The income and the additional tax are shown on Part III, Form 8889.

Each qualified HSA funding distribution allowed has its own testing period.

Example: Michael is an eligible individual, age 45, with self-only HDHP coverage. On June 18, 2025, he makes a qualified HSA funding distribution of \$4,300. On July 27, 2025, he enrolls in family HDHP coverage and on August 17, 2025, he makes a qualified HSA funding distribution of \$4,250 (\$8,550 – \$4,300). His testing period for the first distribution begins in June 2025 and ends on June 30, 2026. His testing period for the second distribution begins in August 2025 and ends on August 31, 2026.

Last month rule—qualified HSA funding distribution. The testing period rule that applies under the last-month rule does not apply to amounts contributed to an HSA through a qualified HSA funding distribution. If an individual remains an eligible individual during the entire funding distribution testing period, then no amount of that distribution is included in income and will not be subject to the additional tax for failing to meet the last-month rule testing period.

Rollovers

A rollover contribution is not included in income, is not deductible, and does not reduce the contribution limit for the year.

Archer MSAs and other HSAs. An individual can roll over amounts from Archer MSAs and other HSAs into an HSA.

Eligible individual. The individual does not need to be an eligible individual at the time when a rollover contribution from an existing HSA is made into a new HSA.

Cash rollovers. Rollover contributions do not need to be in cash.

Contribution limits. Rollovers are not subject to the annual contribution limits.

60-day rule. A distribution from an HSA must be rolled over within 60 days after the date of receipt.

1-year rule. Only one rollover contribution to an HSA can be made during a 1-year period. A trustee to trustee transfer is not considered a rollover and is not subject to the 1-year rollover limit rule.

Contribution Deadline

HSA contributions for 2025 must be made by April 15, 2026. If an individual fails to be an eligible individual during 2025, contributions can still be made up until April 15, 2026, for the months the individual was an eligible individual.

Employer contributions. Employers can make HSA contributions on behalf of their employees anytime during 2025, and between January 1, 2026 and April 15, 2026, that are allocated to 2025. The employer must notify the employee and the trustee of an HSA that such a contribution made in 2026 prior to the deadline is for 2025. The employer must also report the contribution using code W in box 12 on the employee's 2025 Form W-2.

Reporting Contributions

An individual can deduct his or her own HSA contributions, and contributions made by any other person (other than an employer) on behalf of the individual, as an adjustment to income. Deductible contributions are entered on line 13, Schedule 1 (Form 1040), *Additional Income and Adjustments to Income*.

Employer contributions. Contributions made by an employer are not included in the employee's income and are not deducted by the employee on the employee's tax return. Contributions to an employee's account by an employer using the amount of the employee's salary reduction through a cafeteria plan are treated as employer contributions.

Partnership contributions. Contributions by a partnership to a bona fide partner's HSA are not contributions by an employer. If the HSA contribution is not for services rendered, the contribution is treated as a distribution of money and is not deductible by the partnership and is not included in the partner's gross income. If the HSA contribution is for services rendered by the partner, the contribution is treated as a guaranteed payment, is deductible by the partnership, and includible in the partner's gross income and subject to self-employment tax. In both situations, the partner can deduct the HSA contribution on the partner's tax return. (Notice 2005-8)

See *Health savings accounts*, Partnership Example, page 20-23.

S corporation contributions. Contributions by an S corporation to a 2% shareholder-employee's HSA for services rendered are treated as wages and are deductible by the S corporation and includible in the shareholder-employee's gross income. The shareholder-employee can then deduct the HSA contribution on the shareholder-employee's tax return. (Notice 2005-8)

See *Health savings accounts*, S Corporation Example, page 19-19.

Form 8889, Health Savings Accounts (HSAs). Form 8889 must be filed with Form 1040 to report all HSA contributions for the year. Include contributions made for 2025, including those made by April 15, 2026, that are designated for 2025. Contributions made by the employer and qualified HSA funding distributions are also reported on Form 8889.

Two or more HSAs. If the taxpayer is the beneficiary of two or more HSAs, or the taxpayer is a beneficiary of an HSA and also has his or her own HSA, complete a separate Form 8889 for each HSA. Enter "statement" at the top of each Form 8889 and complete the form as instructed. Next, complete a controlling Form 8889 combining the amounts shown on each of the statement Forms 8889. Attach the statements to the tax return after the controlling Form 8889.

Form 5498-SA, HSA, Archer MSA, or Medicare Advantage MSA Information. The HSA participant should receive Form 5498-SA from the trustee showing the amount contributed to the HSA during the previous year and its FMV by May 31.

Form W-2, Wage and Tax Statement. Employer contributions, including amounts contributed to an employee's account by an employee through a cafeteria plan, should be shown with code W in box 12, Form W-2.

Excess contributions. Excess contributions are contributions for the year that exceed the limits shown on the *HSA Limitations* chart, page 30-8. Excess contributions are not deductible. Excess contributions made by an employer are included in gross income. If the excess contribution is not included in box 1, Form W-2, report the excess as Other Income on line 8z, Schedule 1 (Form 1040), *Additional Income and Adjustments to Income*.

Form 5329, Additional Taxes on Qualified Plans (including IRAs) and Other Tax-Favored Accounts. A taxpayer must pay a 6% excise tax on excess contributions. See Form 5329 to calculate the excise tax. The excise tax applies to each tax year the excess contribution remains in the HSA.

How to avoid the penalty on excess contributions. A taxpayer may withdraw some or all of the excess contributions and not pay the excise tax on the amount withdrawn if the following conditions are met.

- The excess contributions are withdrawn by the due date, including extensions, of the tax return for the year the contributions were made.
- Any income earned on the withdrawn contributions is withdrawn and included in earnings as Other Income on the tax return for the year the contributions and earnings are withdrawn.

Note: If an individual fails to remain an eligible individual during any of the testing periods discussed earlier, the amount included in income is not treated as an excess contribution. If those amounts are withdrawn, the amount is treated as a distribution and reported as income subject to 10% penalty on Form 8889.

Deducting an excess contribution in a later year. An excess contribution for a previous year may be deductible in the current year if it is still in the HSA. The deductible excess contribution in the current year is the lesser of the following two amounts.

- The maximum HSA contribution limit for the current year minus any amounts contributed to the HSA for the current year.
- The total excess contributions in the HSA at the beginning of the year.

Amounts contributed for the year include contributions by the taxpayer, the employer, and any other person. It also includes any qualified HSA funding distribution made to the HSA. Any excess contribution remaining at the end of the tax year is subject to the 6% excise tax on Form 5329.

HSA Distributions

In general, a participant in an HDHP will pay medical expenses during the year without being reimbursed by the HDHP until the annual deductible for the plan is reached. The participant of the HDHP can use funds in the HSA to pay qualified medical expenses that are not reimbursed by the HDHP.

A participant can receive tax-free distributions from the HSA to pay or be reimbursed for qualified medical expenses incurred after the HSA is established. Medical expenses incurred prior to the establishment of the HSA cannot be reimbursed by the HSA tax free. State law determines when an HSA is established. An HSA that is funded by amounts rolled over from an Archer MSA or another HSA is established on the date the prior account was established.

If, under the last-month rule, an individual is considered to be an eligible individual for the entire year for determining the contribution amount, only those expenses incurred after the individual actually establishes the HSA may be reimbursed by the HSA tax free.

Note: HSA distributions do not need to be made each year. If an individual is no longer an eligible individual, the individual can still receive tax-free distributions to pay or reimburse qualified medical expenses.

Author's Comment: There is no rule that requires the HSA to reimburse a medical expense in the same year the expense is incurred. Thus, a taxpayer could pay for medical expenses with after-tax funds in one year, and then take a tax-free distribution from the HSA as a reimbursement in a following year, provided the HSA was established prior to the date the medical expense was incurred.

Example: Terje contributes the maximum amount allowed to his HSA every year. Each year he pays all medical expenses not reimbursed by his HDHP with after-tax funds. He saves all medical expense receipts paid with after-tax-funds in a special folder. He does not take a medical expense deduction for these expenses on Schedule A (Form 1040). After 10 years, his HSA has grown to \$60,000. His folder with 10 years of medical expense receipts equals \$20,000. Terje withdraws \$20,000 from his HSA tax free to reimburse himself for his medical expenses and uses the \$20,000 as a down payment on a cabin. See *Recordkeeping*, page 30-12.

Taxable distributions. If a distribution is for any reason other than to reimburse a qualified medical expense, the amount withdrawn is subject to income tax and may also be subject to an additional 20% penalty tax. There is no additional tax on distributions made after the participant is disabled, reaches age 65, or dies.

Form 1099-SA, Distributions From an HSA, Archer MSA, or Medicare Advantage MSA. A distribution is money received from an HSA. Total distributions include amounts paid with a debit card and amounts withdrawn from the HSA by other designated individuals. The trustee of the HSA reports total distributions on Form 1099-SA.

Qualified medical expenses. Qualified medical expenses include the following.

- Expenses that would generally qualify for the medical and dental expenses deduction on Schedule A (Form 1040). See *Deductible Medical Expenses*, page 4-2.
- Amounts paid for over-the-counter medicine, menstrual care products, and condoms.

Qualified medical expenses are those incurred by the following persons.

- The HDHP participant and his or her spouse.
- All dependents claimed by the participant on his or her tax return.
- Any person the participant could have claimed as a dependent on his or her tax return except that:
 - The person filed a joint return,
 - The person had gross income of \$5,200 (for 2025) or more, or
 - The HDHP participant, or his or her spouse if filing MFJ, could be claimed as a dependent on someone else's 2025 tax return.

For HSA purposes, a child of parents that are divorced, separated, or living apart for the last six months of the calendar year is treated as the dependent of both parents, whether or not the custodial parent releases the claim to the child's exemption.

Author's Comment: An adult child, under the age of 26, may be covered under his or her parent's health plan. However, HSA distributions for the adult child might not qualify if he or she does not meet the qualifications listed above.

No double benefit rule. If a medical expense is paid for, or reimbursed by, a tax-free HSA distribution, the expense is not deductible as an itemized deduction on Schedule A (Form 1040).

Insurance premiums. An HSA participant cannot treat insurance premiums as qualified medical expenses unless the premiums are for:

- 1) Long-term care insurance.
- 2) Health care continuation coverage (such as coverage under COBRA).
- 3) Health care coverage while receiving unemployment compensation under federal or state law.
- 4) Medicare and other health care coverage if the participant is 65 or older (other than premiums for a Medicare supplemental policy, such as Medigap).

Item 1. The premiums for long-term care insurance that may be treated as qualified medical expenses are subject to the limits based on age and are adjusted annually. See *Long-Term Care Premium Limits by Age—2025*, Tab 4.

Items 2 and 3. These can be for the participant's spouse or a dependent meeting the requirement for that type of coverage.

Item 4. If the account participant is not age 65 or older, Medicare premiums for coverage of the participant's spouse or a dependent who is age 65 or older generally are not qualified medical expenses.

Premium Tax Credit. A taxpayer cannot claim the Premium Tax Credit for premiums paid with a tax-free distribution from an HSA. See *Premium Tax Credit*, Tab 11.

Deemed distributions from HSAs. The following situations result in deemed taxable distributions from an HSA.

- A participant engaged in a prohibited transaction with respect to any of his or her HSAs at anytime during the year. The account ceases to be an HSA as of January 1 and the taxpayer must include the fair market value of all assets in the account as of January 1 on Form 8889.
- The participant used any portion of any of his or her HSAs as security for a loan at any time during the year. The participant must include the fair market value of the assets used as security for the loan as income on Form 1040.

Any deemed distribution will not be treated as used to pay qualified medical expenses. These distributions are included in the taxpayer's income and may be subject to the additional 20% penalty tax.

Prohibited transactions. Examples of prohibited transactions include the direct or indirect:

- Sale, exchange, or leasing of property between the participant and the HSA,
- Lending of money between the participant and the HSA,
- Furnishing goods, services, or facilities between the participant and the HSA, and
- Transfer to, or use by, the participant, or for the participant's benefit, any assets of the HSA.

Recordkeeping. Taxpayers must keep records sufficient to show that:

- The distributions were used exclusively to pay or reimburse qualified medical expenses,
- The qualified medical expenses had not been previously paid or reimbursed from another source, and
- The medical expenses had not been taken as an itemized deduction in any year.

Reporting Distributions on the Tax Return

How distributions are reported on the tax return depends on whether or not the taxpayer used the distributions for qualified medical expenses.

- If distributions from an HSA were used for qualified medical expenses, the taxpayer does not pay tax on the distribution. Report the distribution on Form 8889.
- The distribution of an excess contribution taken out after the due date, including extensions, of the tax return is subject to tax even if used for qualified medical expenses. Report the entire distribution on Form 8889 and the taxable portion on line 8f, Schedule 1 (Form 1040), *Additional Income and Adjustments to Income*. An additional 6% penalty tax may also apply to the taxable distribution.
- If a distribution from an HSA was not used for qualified medical expenses, the distribution is taxable. Report the entire distribution on Form 8889 and the taxable portion on line 8f, Schedule 1. An additional 20% penalty tax may also apply to the taxable distribution.
- HSA administration and maintenance fees withdrawn by the trustee are not reported as distributions from the HSA.

Reporting penalty taxes. Report the 6%, 10%, and 20% penalty taxes as follows.

Calculate the 6% additional tax on excess contributions considered taxable distributions in Part VII, Form 5329 which is carried to line 8, Schedule 2 (Form 1040), *Additional Taxes*.

Calculate the 10% additional tax for failure to maintain HDHP coverage during the testing period in Part III, Form 8889 which is carried to line 17d, Schedule 2.

Calculate the 20% penalty tax for using distributions for purposes other than qualified medical expenses in Part II, Form 8889 which is carried to line 17c, Schedule 2.

Balance in an HSA

Funds in an HSA are exempt from tax. An employee is always 100% vested in his or her HSA. Amounts that remain in the HSA at the end of the year are carried over to the next year. Earnings on amounts in an HSA are not included in income while held in the HSA. There are no minimum required distributions for HSAs.

Death of HSA Holder

An individual with an HSA should choose a beneficiary when the HSA is set up. What happens to that HSA at death depends on who is designated as the beneficiary.

Spouse is the designated beneficiary. If the spouse of the individual is the designated beneficiary of the HSA, it will be treated as the spouse's HSA after the individual dies.

Spouse is not the designated beneficiary. If the spouse of the individual is not the designated beneficiary of the HSA:

- The account stops being an HSA after the individual dies, and
- The fair market value of the HSA becomes taxable income to the beneficiary in the year in which the individual dies. No penalty applies.

If the individual's estate is the beneficiary, the value of the HSA at death is included on the decedent's final income tax return (Form 1040).

Qualified medical expenses at death. The amount taxable to a beneficiary other than the estate is reduced by any qualified medical expenses for the decedent that are paid by the beneficiary within one year after the date of death.

Medical Savings Account (MSA)

Employer Participation

The following rules apply to employers if they decide to make HSAs available to their employees.

Health plan. Before an employer can contribute to an employee's HSA, the employee must have an HDHP. The employer cannot provide any additional health plan coverage other than those exceptions listed under *Other health coverage*, page 30-8.

Contributions. The employer can make contributions to an employee's HSA. The employer deducts the contributions on the "Employee benefit programs" line on the employer's business income tax return for the year in which the contribution is made. If the contribution is allocated to the prior year, the employer still deducts it in the year in which the contribution is made.

Where to Deduct Employer HSA Contributions

If employer is a:	Deduct employee HSA contribution on:
Sole Proprietor	Line 14, Schedule C (Form 1040)
Farmer (Sole Proprietor)	Line 15, Schedule F (Form 1040)
C Corporation	Line 24, Page 1, Form 1120
S Corporation	Line 18, Page 1, Form 1120-S
Partnership	Line 19, Page 1, Form 1065

For more information on employer contributions, see Notice 2008-59.

Comparable contributions. If an employer makes HSA contributions on behalf of employees, the employer must make comparable contributions to all comparable participating employees' HSAs. Contributions are comparable if they are either:

- The same amount, or
- The same percentage of the annual deductible limit under the HDHP covering the employees.

Comparable participating employees. Comparable participating employees:

- Are covered by the employer's HDHP and are eligible to establish an HSA,
- Have the same category of coverage (either self-only or family coverage), and
- Have the same category of employment (part-time, full-time, or former employees).

Cafeteria plan. The comparability rules do not apply to contributions made through a cafeteria plan.

Nonhighly-compensated employees. For purposes of making contributions to HSAs of nonhighly-compensated employees, highly-compensated employees shall not be treated as comparable participating employees.

Excise tax. If an employer makes contributions to employee HSAs that are not comparable, the employer must pay an excise tax of 35% of the amount contributed.

Employment taxes. Amounts contributed to employee HSAs are generally not subject to employment taxes (FICA, FUTA). Report the contributions in box 12, code W, Form W-2, filed for each employee. This includes the amounts the employee elected to contribute through a cafeteria plan.

Cross References

- Form 1099-SA, *Distributions From an HSA, Archer MSA, or Medicare Advantage MSA*
- Form 5498-SA, *HSA, Archer MSA, or Medicare Advantage MSA Information*
- Form 8853, *Archer MSAs and Long-Term Care Insurance Contracts*
- IRS Pub. 969, *Health Savings Accounts and Other Tax-Favored Health Plans*
- IRC §220, *Archer MSAs*

Related Topics

- Medical Expenses, page 4-2
- Self-employed health insurance deduction, Tab 5

Qualifying for an MSA

No new MSAs. After December 31, 2007, contributions cannot be made unless:

- The taxpayer was an active MSA participant for any tax year ending before January 1, 2008, or
- The taxpayer became an active MSA participant for a tax year ending after December 31, 2007, by reason of coverage under a high deductible health plan (HDHP) of an MSA participating employer.

In addition, the taxpayer must be:

- A self-employed person (or the spouse of a self-employed person) who maintains an HDHP. For the definition of HDHP, see the *2025 Medical Fringe Benefit Plans* chart, page 30-2, or
- An employee (or the spouse of an employee) of a small employer that maintains an HDHP.

The taxpayer can have no other health or Medicare coverage other than those exceptions listed under *Other health coverage*, page 30-8.

For annual deductibles and out-of-pocket expense limits, see *Archer MSA Limitations* chart, below.

For information on MSA contributions and distributions, see *2025 Medical Fringe Benefit Plans* chart, page 30-2.

Archer MSA Limitations

	2025	2024	2023
Minimum annual deductibles:			
Self-only coverage	\$2,850	\$2,800	\$2,650
Family coverage	\$5,700	\$5,550	\$5,300
Maximum annual deductibles:			
Self-only coverage	\$4,300	\$4,150	\$3,950
Family coverage	\$8,550	\$8,350	\$7,900
Annual out-of-pocket expense limits			
Self-only coverage	\$5,700	\$5,550	\$5,300
Family coverage	\$10,500	\$10,200	\$9,650

Note: For tax years 2021–2026 limits see *Health Care*, page 1-5.

Excess Medical Reimbursements

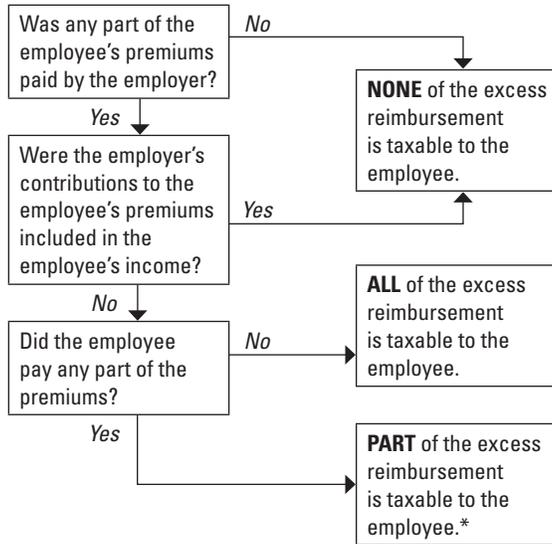
Cross References

- IRS Pub. 502, *Medical and Dental Expenses*
- IRC §105, *Amounts received under accident and health plans*
- IRC §106, *Contributions by employer to accident and health plans*

Related Topics

- Recoveries, Tab 3
- Medical Expenses, page 4-2
- Employee Fringe Benefits, page 22-2

Are Excess Medical Reimbursements Taxable



* See *Premiums paid by the employee and the employer*, below.

If insurance payments or other reimbursements are more than an employee's total medical expenses for the year, the employee has excess reimbursements.

Premiums paid by the employee. Excess reimbursements are not included in gross income if the employee pays either the entire premium for medical insurance or all the costs of a plan similar to medical insurance.

Exception: Gross income does include payments in excess of \$420 (2025) per day for qualified long-term care services. See Section C, Form 8853, *Archer MSAs and Long-Term Care Insurance Contracts*.

Premiums paid by the employer. If the employer or former employer pays the total cost of the employee's medical insurance plan, and the contributions are not included in the employee's gross income, all excess reimbursements are taxable to the employee.

Premiums paid by the employee and the employer. If both the employee and the employer contribute to the employee's medical insurance plan, and the employer's contributions are not included in the employee's gross income, the employee must include in gross income the part of the excess reimbursement that is from the employer's contribution.

If the employee is not covered by more than one policy, calculate the amount of the excess to include in gross income using the *Excess Reimbursement—One Policy Worksheet*, next column.

Excess Reimbursement—One Policy Worksheet

Use this worksheet to calculate the amount of excess reimbursement to include in income when both the employer and employee contributed to the employee's medical insurance and the employer's contributions were not included in the employee's gross income.

- Enter the amount contributed by the employer to the employee's medical insurance for the year 1) _____
- Enter the total annual cost of the insurance policy... 2) _____
- Divide line 1 by line 2..... 3) _____
- Enter the amount of excess reimbursement..... 4) _____
- Multiply line 3 by line 4. This is the amount of excess reimbursement to include as Other Income, line 8z, Schedule 1 (Form 1040), *Additional Income and Adjustments to Income*..... 5) _____

More than one policy. If the taxpayer is covered under more than one policy, the cost of at least one of which is paid by both the employee and the employer, the employee must first divide the medical expenses among the policies to calculate the excess reimbursement from each policy. Then divide the policy costs to calculate the part of any excess reimbursement that is from the employer's contribution. Any excess reimbursement that is due to the employer's contributions is included in the employee's income.

Calculate the part of the excess reimbursement that is from the employer's contribution by using the *Excess Reimbursement—More Than One Policy Worksheet*, below. Use this worksheet only if both the employee and the employer paid part of the cost of at least one policy.

Excess Reimbursement—More Than One Policy Worksheet

Use this worksheet to calculate the amount of excess reimbursement to include as income when the employee is reimbursed under two or more health insurance policies, at least one is paid for by both the employee and the employer, and the employer's contributions are not included in the employee's gross income. If the employee and the employer did not share in the cost of at least one policy, do not use this worksheet

- Enter the reimbursement from the employer's policy 1) _____
- Enter the reimbursement from the employee's policy 2) _____
- Add lines 1 and 2 3) _____
- Divide line 1 by line 3..... 4) _____
- Enter the total medical expenses the employee paid during the year. If this amount is at least as much as the amount on line 3, STOP here. There is no excess reimbursement 5) _____
- Multiply line 4 by line 5..... 6) _____
- Subtract line 6 from line 1..... 7) _____
- Enter the employer's contribution to the annual cost of the employee's policy 8) _____
- Enter the total annual cost of the employer's policy.... 9) _____
- Divide line 8 by line 9..... 10) _____
- Multiply line 7 by line 10. This is the amount of total excess reimbursement that must be reported by the employee as Other Income, line 8z, Schedule 1 (Form 1040)..... 11) _____