



# **An Introduction to Health Savings Accounts**

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**For Individuals and Employees**

# Contents

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- Objective
  - Provide overview of Health Savings Accounts (HSAs)
  - Answer common questions
  
- Contents
  - Background
  - How does an HSA work?
  - What's a High Deductible Health Plan?
  - Who can have an HSA?
  - How much can I contribute?
  - How do I get the tax benefits?
  - How do I use the HSA?
  - What's an "eligible" medical expense?
  - How do I check to see if my expense is "eligible"?
  - How do I open an HSA?

Sample

# HSA Background

- **Introduced to support Consumer Driven Health Care**
  - Provide consumers greater control over health care dollars.
  - Reduce health care costs by putting consumers in charge
  - Give employers struggling to pay health care insurance a lower cost alternative and to encourage employers that do not offer health insurance to do so
- **Strong Growth so Far**
  - Over 11.4 million people have HDHP/HSA coverage as of January 2011<sup>1</sup> (up from 10 million in 2010, 9 million in 2009, 6 million in 2008, 4.5 million in 2007 and 3.2 million in 2006), estimates vary as to how many eligible individuals open HSAs.
  - Exceed \$10 billion in deposits<sup>2</sup>
- **Initial Results Positive**
  - HSA owners are more value conscious of health care expenses<sup>3</sup>
  - HSA owners engage in improved wellness behavior
  - HSA insurance plans are not increasing in cost as much as other plans

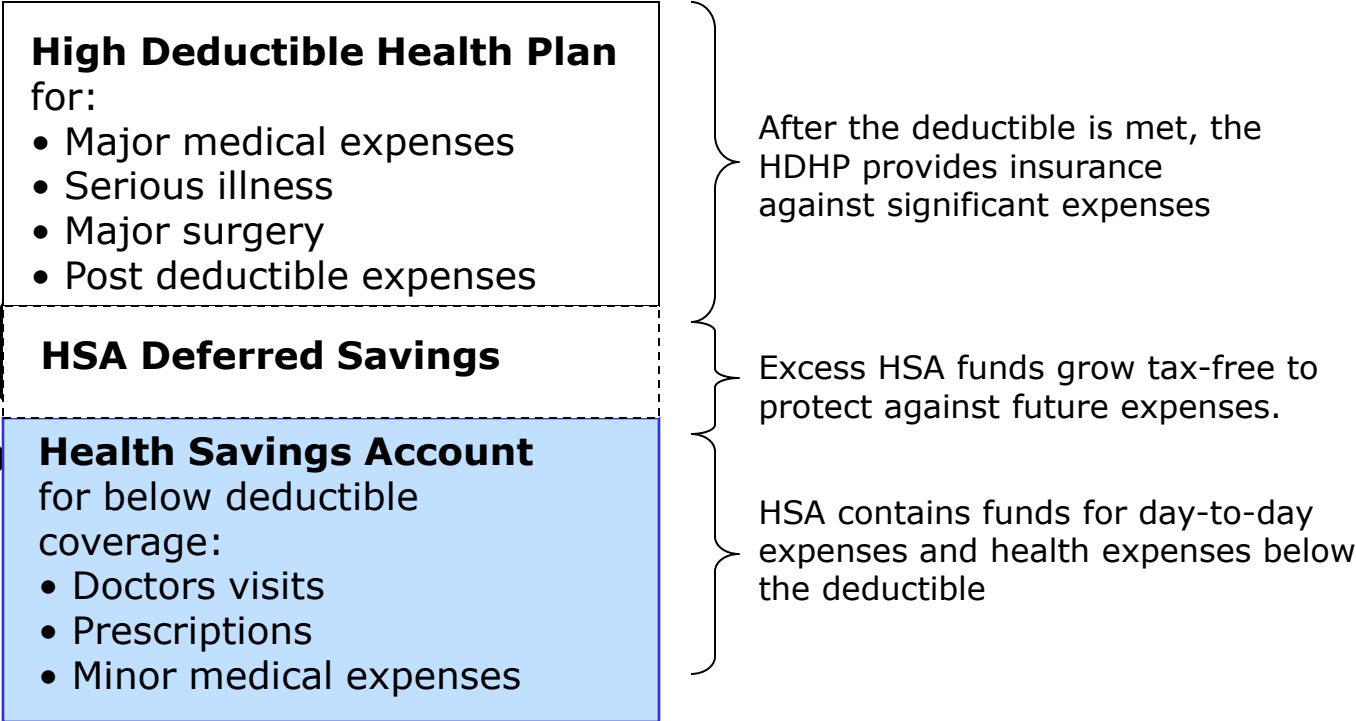
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<sup>1</sup> Study released by America's Health Insurance Plans, June 16, 2011  
<sup>2</sup> Health Savings Accounts Surpass \$10 Billion in Total Deposits, Press Release from Devenir, Feb 24, 2011  
<sup>3</sup> Consumer-Directed Health Plan Report – Early Evidence is Promising, McKinsey & Company, June 2005

# How does an HSAs work?

HSAs work in combination with a High Deductible Health Plan (HDHP), also referred to as “catastrophic” insurance or major medical. The HSA pays for the day-to-day medical expenses while the HDHP pays for major expenses (above the deductible amount). The law is designed so that you can put roughly the amount of your deductible in an HSA – see the next slide for details.

Sample



# What's a high deductible health plan?

- **High Deductible Health Plan (HDHP).** You must be covered under an HDHP plan to qualify for an HSA. Ask your insurance provider if your plan qualifies. Generally, HDHPs require a minimum annual deductible and place a limit on the total out-of-pocket payments allowed:

HDHP Requirements	Individual	Family
<b>Annual Deductible</b>	At least \$1,200 for 2011 At least \$1,200 for 2012	At least \$2,400 for 2011 At least \$2,400 for 2012
<b>Out-of-Pocket Max</b>	Not more than \$5,950 for 2011 Not more than \$6,050 for 2012	Not more than \$11,900 for 2011 Not more than \$12,100 for 2012

- **No Other Insurance allowed – Except “Permitted” Insurance.** To prevent people from obtaining the benefits of an HSA while protecting themselves with other health insurance plans, the law restricts the other coverage you may have. Listed below are some of the big exceptions:
  - Term and life insurance
  - Accident insurance
  - Insurance for a specific disease or illness
  - Insurance that pays for a fixed amount per day for hospitalization

Sample

# Who can have an HSA?

## ■ General Requirements

- Covered under an HDHP
- Not be covered under another health plan
- Not a dependent on another's tax return
- Under age 65 (and not covered by Medicare)

- **Eligibility Worksheet** - The Eligibility and Contribution Worksheet to the right can help you determine if you are eligible. Please contact your tax advisor if you have any questions.

Sample

### HSA Eligibility and Contribution Worksheet

**Purpose:** Use this form to verify your eligibility for an HSA and determine the amount you may contribute. You are responsible for properly determining your eligibility and contribution amount. This worksheet is simply a tool to aid you in that effort. If you have any questions, please consult with your tax or legal counsel.

**1 HSA Eligibility.** You must answer "True" to each of the following in order to be eligible for an HSA. See definitions on back for help.

a. I am covered under an HDHP True  False

b. I am not covered by another non-HDHP health plan other than "permitted insurance" True  False

c. I am not eligible for Medicare (age 65) or if I am eligible, I am not enrolled in Part A, B or D. True  False

d. I am not a dependent on another person's tax return True  False

Not Eligible

**2 Contribution Amount.** Use the table below to determine your amount.

Contribution Worksheet		Individual	Family
A	Federal Limit <sup>1</sup>	\$3,050 (2011) \$3,100 (2012)	\$6,150 (2011) \$6,250 (2011)
B	Catch Up <sup>2</sup> if Age 55 - 65 + \$1,000 (2011 or 2012)		
C	Total (add Federal Limit plus Catch-Up)		

<sup>1</sup>**Issues that Impact Contribution Amounts.** A number of issues potentially affect the amount of your HSA contribution.

A. **Less Than Full Year Eligibility - Eligible on December 1.** If you become eligible for an HSA sometime during the year, rather than on January 1, you can still contribute and deduct the full amount of the federal limit above if you remained eligible on December 1 of that year (this rule applies even if your first day of eligibility was December 1). However, if you fail to maintain your eligibility for a testing period then the amount you contributed under this rule is subject to taxation and a 10% penalty (except in the case of disability or death). The testing period is the period beginning in the last month of the taxable year (generally December 1) and ending on the last day of the 12<sup>th</sup> month following such month (generally December 31 of the next year). Please see our HSA Testing Period Worksheet for details.

B. **Less Than Full Year Eligibility - Not Eligible on December 1.** If you are not eligible for the HSA in all months of the year and are not eligible on December 1, a different rule applies. You must apply the *Sum of the Months* rule to determine the maximum amount of your HSA contribution. The *Sum of the Months* calculation requires you to determine your eligibility month-by-month and only contribute a pro-rata amount of the maximum federal HSA limit. Please use the chart on page 2.

C. **Multiple HSAs.** The total contribution amount may be split among multiple HSAs. For family coverage, the amount may be split between eligible spouses' HSAs.

D. **IRA to HSA Transfers.** You are allowed a one time transfer of funds from your Individual Retirement Account (IRA) into your HSA. This is limited to the amount you are eligible to contribute for the year and counts against that contribution (i.e. you cannot put in more than the Federal Limit, counting any IRA transfer). You cannot deduct the amount transferred from an IRA to an HSA; however, the amount taken from the IRA is not taxable as a distribution from the IRA. Please see our IRA to HSA Transfer Worksheet for details.

E. **Employer Contributions.** Caution: Employer contributions made to your HSA on a pre-tax basis count towards your total contribution amount but may not be deductible from your personal income.

<sup>2</sup>**Catch-Up Contributions.** For individuals (and their spouses covered under the HDHP) between ages 55 and 65, the HSA contribution limit is increased by \$1,000 for 2012. If both you and your spouse are between age 55-65, you each get a catch-up. You cannot contribute more than \$7,250 (\$6,250+\$1,000) into one HSA for 2012. Catch-up contributions should be made into each spouses' respective HSA.

Catch-Up Amount	Tax Year	2009	2010	2011	2012
Amount		\$1,000	\$1,000	\$1,000	\$1,000

**3 Need More Help?** You are encouraged to talk to a tax professional, your insurance representative or another professional to help determine your eligibility and contribution amount. IRS Notice 2008-59 and IRS Notice 2004-50 both provide examples and more detail on eligibility (caution some points in the 2004 IRS Notice are outdated).

# How much can I contribute?

- **General guidelines**
  - **Maximums.** HSA owners may contribute up to
    - \$3,100 for 2012 (\$3,050 for 2011) for individuals, and
    - \$6,250 for 2012 (\$6,150 for 2011) for families
  - **Catch-Up.** Plus catch-up contributions of \$1,000 for 2012 (same for 2011) for those age 55-65

Sample

- **Contribution Worksheet - The Eligibility and Contribution worksheet to the right shows you determine how much you can contribute. Please contact your tax advisor if you have any questions.**

### HSA Eligibility and Contribution Worksheet

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**1 HSA Eligibility.** You must answer "True" to each of the following in order to be eligible for an HSA. See definitions on back for help.

a. I am covered under an HDHP	True	False	Not Eligible
b. I am not covered by another non-HDHP health plan other than "permitted insurance"	True	False	
c. I am not eligible for Medicare (age 65) or if I am eligible, I am not enrolled in Part A, B or D.	True	False	
d. I am not a dependent on another person's tax return	True	False	

**2 Contribution Amount.** Use the table below to determine your amount.

Contribution Worksheet		Individual	Family
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**Issues that Impact Contribution Amounts.** A number of issues potentially affect the amount of your HSA contribution.

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**D. IRA to HSA Transfers.** You are allowed a one time transfer of funds from your Individual Retirement Account (IRA) into your HSA. This is limited to the amount you are eligible to contribute for the year and counts against that contribution (i.e. you cannot put in more than the Federal Limit counting any IRA transfer). You cannot deduct the amount transferred from an IRA to an HSA; however, the amount taken from the IRA is not taxable as a distribution from the IRA. Please see our IRA to HSA Transfer Worksheet for details.

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Catch-Up Amount	Tax Year	2009	2010	2011	2012
Amount		\$1,000	\$1,000	\$1,000	\$1,000

**3 Need More Help?** You are encouraged to talk to a tax professional, your insurance representative or another professional to help determine your eligibility and contribution amount. IRS Notice 2008-59 and IRS Notice 2004-50 both provide examples and more detail on eligibility (caution some points in the 2004 IRS Notice are outdated).

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# How do I get the tax benefits?

## Contributions

- Payroll deductions<sup>1</sup> – amounts contributed through payroll deductions are generally not included on your paychecks or W-2 as income.
- Personal contributions – amounts contributed to your HSA, whether by yourself or other individuals, may be taken as an “above the line” deduction. Meaning you do not have to itemize to get the tax benefit. Some states also provide the same benefit.

## HSA Account

- Earnings growth in the HSA are tax-exempt
- Distributions are tax-free when used for qualified medical expenses

## Tax Savings Worksheet - The Tax Savings Worksheet to the right can help you estimate your potential tax savings.

Sample

<sup>1</sup>Amounts contributed by your employer generally are not eligible for a personal deduction.

### HSA Tax Savings Worksheet

**Purpose:** This Tax Guide provides an estimate of your personal HSA tax savings. You are ultimately responsible for understanding your tax situation and you should consult with your tax or legal counsel for specific questions.

**1 Income Tax Savings.** The amount contributed to your HSA may be eligible for federal and state tax deductions. Complete the chart below to estimate your tax savings.

**A. HSA Contribution Amount.** Enter the amount you intend to contribute to your HSA in Section A. Use the Eligibility and Contribution Worksheet to determine your maximum amount.

**B. Federal Tax Rate.** Use the Federal Tax Table below to determine your marginal Federal tax rate based on your “taxable” income and enter it in Section B (see p. 2 of this form for additional details).

2011 Federal Tax Table		
Single	Married Filing Jointly	Marginal Tax Rate
\$0 - \$8,500	\$0 - \$17,000	10%
\$8,500 - \$34,500	\$17,000 - \$69,000	15%
\$34,500 - \$83,600	\$69,000 - \$139,350	25%
\$83,600 - \$174,400	\$139,350 - \$212,300	28%
\$174,400 - \$379,150	\$212,300 - \$379,150	33%
\$379,150 +	\$379,150 +	35%

HSA Income Tax Savings Calculator	
A	HSA Contribution Amount
B	Federal Income Tax Rate
C	Estimated Federal Income Tax Savings (Multiply A x B)
D	State Income Tax Rate
E	Estimated State Income Tax Savings (Multiply A x D)
F	Estimated Income Tax Savings (Add C + E)

**C. Federal Tax Savings.** Multiply your HSA Contribution (A) by your Federal Tax Rate (B) and enter the result in Section C.

**D. State Tax Bracket.** You may also be eligible for an HSA state income tax deduction. If your state has an income tax and allows you to deduct your HSA contribution, then enter your personal State Tax Bracket in Section D. Most states provide the same tax break for HSA contributions that the federal government allows. However, some states (e.g., AL, CA, & NJ) do not provide an income tax deduction for HSAs, please check with your tax advisor to obtain the most current information.

**E. State Tax Savings.** Multiply your HSA Contribution (A) by your State Tax Rate (D) and enter the result in Section E.

**F. Total Income Tax Savings.** Add the Federal Savings (C) and the State Savings (E) to get an estimate of your Total Tax Savings.

**2 Other Tax Benefits** You may also obtain other tax benefits from owning an HSA.

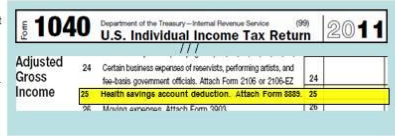
**A. Tax-Deferred Earnings.** Earnings on HSA assets are not subject to tax and are allowed to grow tax-free while held within the HSA. This works similar to investments in other tax-deferred plans like 401k or IRA plans.

**B. FICA and FUTA Tax Savings.** Employer contributions made to your HSA or contributions made through an employer provided Section 125 Cafeteria Plan are eligible for additional tax savings. These HSA contributions are not subject to taxes for Social Security (FICA) and Federal Unemployment Taxes (FUTA).

**3 How it works, Federal Tax Deduction for HSAs.** Either your HSA contribution is never counted as income to you or you may deduct your eligible HSA contribution directly on your tax return.

**A. Employer HSA Contributions.** Generally, employer contributions are not considered income to you because the contribution is made pre-tax and not included on your W-2.

**B. Non-Employer HSA Contributions.** Your HSA is a direct deduction from your Adjusted Gross Income, this means that every dollar contributed reduces your taxable income. You do not have to itemize your taxes to receive this benefit.



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# How can I use my HSA?

## ■ **Primary Purpose: to pay “Qualified” Medical Expenses – Tax Free.**

- You are not taxed on distributions used to pay for “qualified” medical expenses for yourself, your spouse, or your dependents (regardless of whether they are covered by the insurance plan).

## ■ **Other benefits**

- **Roll-over and deferred growth.** Unused funds remain in your HSA and continue to grow tax-free, year after year.
- **Pay COBRA if you become unemployed.** Should you lose your current job you can use your HSA funds to pay your COBRA premiums.
- **Long term care insurance.** Subject to certain limitations.
- **Pay insurance premiums at age 65.** At age 65 you can treat certain insurance premiums (Medicare Part A or B and employee share of employer-sponsored health care) as qualified medical expenses.
- **Use Retirement Fund at Age 65.** At age 65, you can take money out of your HSA for non-medical reasons, penalty free but subject to normal income tax. Basically turning your HSA into another retirement account.

- **Non-Eligible Distributions – Taxes Plus 20%.** If you take the money for another reason, you will be subject to taxes on the distribution plus a 20% penalty (10% penalty for years before 2011).

# What are "qualified" medical expenses?

## Most medical expenses covered

- Doctor visits
- Hospital expenses
- Prescription drugs
- Optical care
- Dental
- Note: Over-the-counter drugs are no longer eligible (aspirin and medicine, etc.). Non-drug over-the-counter medical items are still permissible (bandages, contact lenses cleaner, etc.)

## Who is covered

- Yourself
- Spouse and dependents (regardless of whether they are covered under your insurance plan)

## Qualified Medical Expense Listing -

The Listing to the right can help you determine which expenses are qualified and which are not.

### HSA Distribution Guide – Additional Detail

This Worksheet is based on IRS guidance regarding HSAs including IRA Notice 2004-2, IRS Notice 2004-50, and IRS Publication 969. The following list of qualified and non-qualified medical expenses is intended to provide a quick guide. For more information refer to IRS Publication 502, and talk to a tax or financial advisor. This Worksheet does not cover state taxes issues. Many, but not all, states provide similar tax treatment for HSAs.

#### Qualified Medical Expenses

Abortion	Guide Dogs	Orthopedist
Acupuncture	Gynecologist	Osteopath
Alcoholism*	Hearing Aids	Oxygen
Ambulance Services	Hospital Services	Pediatrician
Anesthetics	Insulin	Physician
Artificial Limbs	Laboratory Tests	Postnatal Treatments
Artificial Teeth	Prepaid Insurance Premiums*	Prenatal Care
Bandages	Lab Fees	Prescription Drugs
Breast Recon. Surgery*	Lead Based Paint Removal*	Prosthesis
Birth Control Pills	Legal Fees*	Psychiatric Care
Blood Tests	Lodging*	Psychoanalysis
Braces	Long Term Care*	Psychologist
Braille Books and Magazines*	Long Term Care Services*	Registered Nurse
Car modifications*	Meals*	Spinal Fluid Test
Cardiographs	Medical Information Plan	Splints
Chiropractor	Medical Services	Sterilization
Christian Science Practitioner	Medicines - prescriptions	Stop Smoking Programs*
Contact Lenses	Mentally Retarded, Homes*	Surgeon
Contraceptives	Prescription medicines*	Telephone*
Crutches	Neurologist	Therapy
Dental Treatment*	Nursing Home*	Transplants
Dermatologist	Nursing Services	Transportation
Diagnostic Devices and Fees	Obstetrician	Vacines
Disabled Dependent Care	Operating Room expenses	Vasectomy
Drug Addiction Therapy*	Operations	Vision Correction Surgery
Eyeglasses	Ophthalmologist	Weight Loss Programs*
Eye Surgery	Optician	Wheelchair
Fertility Treatments	Oral Surgery	Wigs*
Future Medical Care*	Orthopedic Shoes	X-rays

#### Non-Qualified

- Over-the-counter drugs (see below)
- Child Care
- Cosmetic Surgery
- Hair Transplants\*
- Health Club Dues
- Household Help
- Insurance Premiums\*
- Maternity Clothes
- Nutritional Supplements
- Teeth Whitening
- Vitamins

#### Over-the-Counter Drugs

Over-the-counter drugs and medicines are no longer eligible medical expenses starting January 1, 2011. If you get a prescription for an over-the-counter drug then you can still use your HSA. Insulin is an exception. This rule does not apply to non-drug over-the-counter items, such as bandages or blood pressure monitors.

\* Additional rules apply – more information at IRS Publication 502, or a tax professional.

#### Additional Distribution Events and Other Details on Distributions:

1. **Divorce.** In the case of a divorce with a "divorce or separation agreement," an HSA owner may transfer HSA assets to the spouse without taxes or penalties. A private separation agreement is not sufficient for this tax treatment.
2. **Spouse as Beneficiary.** A spouse named as a beneficiary is automatically deemed to be the HSA owner upon death of the original HSA owner. The surviving spouse may rollover, transfer and use the HSA as his or her own.
3. **Long-Term Care Premiums.** Long-term care distributions are limited in amount based on age (for 2011 it ranges from \$340 for individuals under age 40 to \$4,240 for individuals age 71 or over). The amount adjusts annually for cost-of-living increases. See Revenue Code 213(d)(10).
4. **Prohibited Transactions.** HSA owners engaging in "prohibited transactions" face potentially severe consequences and should seek professional help. The rules surrounding prohibited transactions are too complex for this Worksheet. Basically, a prohibited transaction occurs when a disqualified person (the HSA owner and others) engages in dealings with the HSA that permit opportunities for tax fraud. For example, an HSA owner cannot sell his or her HSA an asset the HSA owner owns (e.g., real estate).
5. **Pledging the HSA as Security for a Loan.** An HSA owner is not allowed to pledge the HSA as security for a loan and the amount so pledged is treated as a distribution and is subject to taxes and a penalty.
6. **Mistaken Distributions.** If there is clear and convincing evidence that amounts were distributed from an HSA because of a mistake of fact due to reasonable cause, the account owner can repay the mistaken distribution no later than April 15 following the first year the account owner knew or should have known the distribution was mistaken (subject to the custodian's allowance of this).
7. **Return of Excess Contributions.** If you contribute more to your HSA than you are eligible to contribute, you must remove the excess amount by your tax filing due date plus extensions. If you fail to remove the excess amount, plus any earning (e.g. interest) attributable to the excess by your tax filing due date, plus extensions, you will be subject to a 6% excise tax for years that you allow the excess to remain.
8. **Reimburse Yourself.** You can reimburse yourself for medical expenses that you pay for with other funds.
9. **Use Contributions for Future Expenses.** You can use a current year contribution to pay for future medical expenses.
10. **Use Future Contributions to Pay Current Expenses.** Assuming you established an HSA, you can pay for current medical expenses (expenses incurred after HSA established) with future year contributions.
11. **Insurance Premiums at Age 65.** Individuals over the age 65 can use the HSA to pay for premiums for Medicare Part A or B, Medicare HMO, and the employee share of premiums for employer-sponsored health insurance, including premiums for employer sponsored retiree health insurance. Premiums for Medigap policies are not qualified medical expenses. This applies to both insured and self-insured plans.



# How do I open my HSA?



1 Complete an HSA Application.



2 Send in your application and initial deposits.



3 Withdraw and open your HSA

Sample

### HSA Application

Complete electronically (Optional) Send applications here ▶

**1 Personal Information.**

Name \_\_\_\_\_ Soc. Sec. # \_\_\_\_\_ Date of Birth \_\_\_\_\_  
 Street \_\_\_\_\_ City \_\_\_\_\_ State \_\_\_\_\_ Zip \_\_\_\_\_  
 Address \_\_\_\_\_ City \_\_\_\_\_ State \_\_\_\_\_ Zip \_\_\_\_\_  
(if different from above)  
 Home Phone \_\_\_\_\_ Work Phone \_\_\_\_\_ Employer \_\_\_\_\_ Agent/Broker \_\_\_\_\_  
 E-mail \_\_\_\_\_ Driver's License \_\_\_\_\_ State Issued \_\_\_\_\_

**2 Contribution Information.**

(Note for Employer Plans: This section is not necessary if your HSA contributions are coming directly from your employer.)

**A. Type**  Regular  Rollover  Transfer  (complete Transfer Form)

**B. Tax Year:**  Current Year  Prior Year

**D. Automated Contributions:** If you want to set up monthly deposits to your HSA from your checking account, complete the following. You must attach a voided check from the account you wish to withdraw from.

Amount \$ \_\_\_\_\_ Day of Month  15th  30th

Make Check Payable to Financial Institution above	
Initial Contribution:	\$ _____
Fees (if applicable):	\$ _____
Other:	\$ _____
<b>Total:</b>	\$ _____

**3 Signatures.** I have received, read and agree to the terms in the Custodial Agreement and Disclosure Statement and I agree that those terms and conditions apply to this HSA and that I am bound by those terms and conditions. If applicable, I hereby designate the beneficiaries for this HSA as those named on the second page of this Application in the HSA Designation of Beneficiary section; if applicable, I hereby authorize the person named on the second page of this Application in the HSA Authorized Signer section as an authorized signer for this HSA. I understand that I am solely responsible to determine my eligibility to make this HSA contribution and to determine the tax deductibility of the contribution; including an understanding that I must be covered under a "High Deductible Health Plan" for annual contribution eligibility. I agree that I will consult with my tax or legal advisor if I need advice. I acknowledge that the Custodian named above cannot and does not provide me with tax or legal advice. I am solely responsible for determining the tax consequences of all distributions.

**T.I.N./Backup Withholding:** (Cross out item (3) if you are subject to backup withholding) Under penalties of perjury, I certify (1) that the number shown is my correct taxpayer ID number or social security number, (2) that I am a U.S. person (including U.S. resident alien), (3) and that I am not subject to backup withholding because (a) I am exempt from backup withholding or (b) because I have not been notified by the IRS that I am subject to backup withholding as a result of failure to report all interest or dividends or (c) because the IRS has notified me that I am no longer subject to backup withholding. The Internal Revenue Service does not require your consent to any provision of this document other than the certifications required to avoid backup withholding.

HSA Owner Signature \_\_\_\_\_ Date \_\_\_\_\_

Check here if you completed the second page of this application. Page 1 (this page) - Required information to open an HSA. Page 2 (next page) - Optional beneficiary and authorized signer information can be completed at any time.

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Click on form for more details