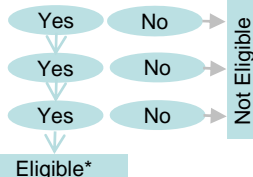


**Purpose:** Use this Worksheet to gain a better understanding of the special rules for moving funds from an Individual Retirement Account (IRA) into a Health Savings Account (HSA). Please see IRS Notice 2008-51 for additional information. We do not provide tax or legal advice. Please seek tax or legal advice from your own tax or legal advisors.

**IRA to HSA Overview.** The law allows you to move money from your IRA into your HSA and avoid the taxation and penalties generally associated with early withdrawals from an IRA. HSA owners face a potentially troubling issue of large medical expenses without the funds to pay for it. Allowing HSA owners to access their IRA funds provides another option to fund the HSA. This option; however, is limited by the rules discussed below and on page 2.

## 1 Are You Eligible for an IRA to HSA Contribution?

- A. Are you eligible for an HSA?<sup>1</sup>
- B. You have not already moved an IRA to an HSA?<sup>2</sup>
- C. You have an IRA?<sup>3</sup>



\*You must answer all questions "Yes" to be eligible.

### Footnotes

- <sup>1</sup> You must be eligible for an HSA to move money from an IRA to an HSA. Please see the HSA Eligibility and Contribution Worksheet to determine your HSA eligibility.
- <sup>2</sup> You are only allowed to do an IRA to HSA direct transfer once-in-a-lifetime. See "change in HDHP status" in the next step for an exception and see p.2 for additional details.
- <sup>3</sup> You can only move funds from a traditional or Roth IRA and in some cases SEP or 401(k) into an HSA. You cannot move funds directly from a 401(k) to an HSA. See p.2 for details.

## 2 How Much of the IRA Can You Move to the HSA? See definitions and examples on page 2 for help.

- A. **Federal HSA Limits Apply.** You cannot contribute more than the applicable HSA federal limit: \$2,900 for individuals in 2008 (\$3,000 for 2009) and \$5,800 for family HDHP coverage in 2008 (\$5,950 for 2009) plus a catch up of \$900 for 2008 if between ages 55 and 65 (\$1,000 for 2009). If you do not, you can contribute any amount up to the applicable federal HSA limit for the year taking into account the paragraph immediately below. See HSA Eligibility and Contribution Worksheet for details on your eligible amount.
- B. **IRA to HSA Contribution Counts Against Federal Limit.** Your IRA to HSA contribution counts against the applicable federal limit. All of the following types of contributions count against the HSA federal limit: IRA to HSA direct transfers, employer HSA contributions, rollover deferral HSA contributions and regular HSA contributions.
- C. **Change in HDHP Status.** If your status changes from self-only HDHP coverage to family HDHP coverage during the year of the contribution, you may be able to move additional funds from your IRA to your HSA. See page 2 for details.

## 3 What Are the Tax Implications? See additional tax issues on p.2 – plus consult with your tax advisor.

- A. **HSA Treatment - Not Deductible.** IRA to HSA contributions are not tax deductible as an HSA contribution.
- B. **IRA Treatment - Not Taxable.** A qualified HSA funding distribution from an IRA enjoys an exception to the normal rule that IRA distributions are subject to tax and possibly a 10% penalty. The law allows for the basis (after-tax dollars) to remain in the IRA to the extent that such amount does not exceed the aggregate amount which would have been so included if there were a total distribution from the IRA or Roth IRA owner's accounts. Basis is an important, but confusing, tax concept - See p. 2 for details.
- C. **Testing Period.** You will be subject to a testing period if you complete an IRA to HSA direct transfer. If you fail to maintain your HSA eligibility for the testing period, taxes and penalties apply. See p.2 for details.

## 4 How Do I Move My IRA to My HSA?

The IRA to HSA transaction must be done as a "direct transfer". That means the IRA assets must move directly to the HSA and cannot be paid to the IRA owner. A common approach is for you to request and complete a "transfer form" from your HSA provider. The HSA provider forwards the form to the IRA provider. The IRA provider then writes a check directly to the HSA provider for the benefit of the HSA owner and sends the check directly to the HSA provider. The rules permit the IRA/HSA owner to hand carry a check made payable to the HSA custodian or trustee.

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## IRA to HSA – Definitions and Additional Detail

- 1. Additional Background.** The IRA to HSA direct transfer allows you to fund your HSA with your IRA. Generally, distributions from an IRA are subject to taxation plus a 10% penalty if you fail to meet a qualified distribution reason (age 59 ½, death, disability, etc.). The taxes and penalties do not apply to HSA to IRA direct transfers that meet the requirements. The IRS refers to the process of moving funds from an IRA to an HSA as a trustee-to-trustee “direct transfer” and it refers to the distribution from an IRA for use in funding an HSA as a “qualified HSA funding distribution” from the IRA.
- 2. Types of IRAs Permitted for HSA Funding.** A qualified HSA funding distribution may be made from a traditional IRA or a Roth IRA, but not from an ongoing SIMPLE IRA or a SEP IRA. A SEP or a SIMPLE is considered ongoing if an employer contribution is made for the plan year ending with or within the IRA owner’s taxable year in which the qualified HSA funding distribution would be made. You cannot move money directly from a 401(k) into an HSA; however, you may be able to move the money from a 401k to an IRA and then to an HSA. You also cannot use your spouse’s or someone else’s IRA. But see “inherited IRAs.”
- 3. Inherited IRAs.** After the death of an IRA or Roth IRA owner, a qualified HSA funding distribution may be made from an IRA or Roth IRA maintained for the benefit of an IRA or Roth IRA beneficiary. This distribution will be taken into account in determining whether the required minimum distribution has been satisfied from the IRA.
- 4. Once Per Lifetime Rule.** Generally only one qualified HSA funding distribution is allowed during your lifetime. An exception exists if you changed your HDHP status from single to family during the same taxable year – see paragraph 6 below.
- 5. Multiple IRAs.** If you own two or more IRAs, and want to use amounts in multiple IRAs to fund your HSA, you must first consolidate the IRAs into a single IRA, and then make the one-time qualified HSA funding distribution from that IRA.
- 6. Change from Single HDHP Coverage to Family HDHP Coverage.** You are allowed a second qualified HSA funding distribution if you change your HDHP status from single coverage to family coverage in the same taxable year. Both distributions count against your maximum HSA contribution for that taxable year. For example, Jim enrolls in self-only HDHP coverage on July 1, 2008. Jim does a direct transfer from his IRA to his HSA in the amount of \$2,900 to fund the HSA. On September 1, 2008, Jim switches insurance to a family HDHP. Jim may do a second IRA to HSA direct transfer prior to the end of the year in an amount up to \$2,900 (\$5,800 family federal maximum - \$2,900 already contributed in the first IRA to HSA direct transfer). Jim would have two different testing periods for the two separate IRA to HSA transactions. See paragraph 9 below.
- 7. Change from Family HDHP Coverage to Single HDHP Coverage.** You are not eligible to do a second IRA to HSA funding transaction if you change from family HDHP coverage to single HDHP coverage. However, you also do not need to adjust your contribution, taxes or penalties provided you meet your testing period. For example, assume you enroll in a family HDHP on January 1, 2008 and remain eligible for an HSA through December 31, 2009. On March 18, 2008 you complete an IRA to HSA direct transfer of \$5,800. On June 1, 2008, you change your family HDHP to a single HDHP policy. The \$5,800 IRA to HSA direct transfer met the maximum limit at the time of the transfer and is permissible because you met the testing period.
- 8. Two IRA to HSA Direct Transfers In Violation of Once-in-Lifetime Rule.** If you complete two IRA to HSA transactions and do not meet the exception for change in status discussed above, your second IRA to HSA transfer is not a qualified HSA funding distribution and will be included in gross income and subject to the additional 10% tax for early withdrawals from an IRA. The treatment from an HSA perspective depends upon whether the federal HSA limit was exceeded. If not, the amount is deductible as an HSA contribution. If exceeded, the amount is treated as an excess contribution to the HSA.
- 9. Testing Period.** If you complete an IRA to HSA direct transfer you are subject to a testing period. You must maintain your HSA eligibility for the testing period. The testing period begins with the month in which the qualified HSA funding distribution is contributed to the HSA and ends on the last day of the 12<sup>th</sup> month following that month. Each qualified funding distribution allowed has a separate testing period. If at any time during the testing period, you cease to be eligible for the HSA, the amount of the IRA to HSA distribution is included in income for the taxable year in which you first failed to be an eligible individual. Plus, you will face an additional 10% penalty tax, unless the failure to meet the testing period is due to death or disability. Please see our HSA Testing Period Worksheet for additional details.
- 10. IRA to HSA Attributable to Year Actually Made.** A qualified HSA funding distribution relates to the taxable year in which the distribution is actually made. You cannot complete an IRA to HSA direct transfer for the previous year.
- 11. Basis Recovery Rules for Roth and Nondeductible IRAs.** This rule allows for an IRA owner to protect their non-deductible basis in a traditional IRA or Roth IRA to the extent possible by using the basis to remain with the IRA and to transfer the taxable portion to the HSA. For example, suppose an individual who has \$200 of basis in an IRA with a fair market value of \$2,000 makes a qualified HSA funding distribution of \$1,500, the individual retains \$200 of basis in an IRA that has a fair market value of \$500. If a qualified funding distribution from an individual’s IRA or Roth IRA exceeds the aggregate amount which would have been included in gross income if there were a total distribution from that individual’s IRA or Roth IRA account, the basis does not carry over to the HSA. Assume the same facts as the previous example, except that the individual directly transferred all \$2,000 from the IRA to the HSA. The \$200 of basis is lost in the IRA because the IRA is empty and the basis does not transfer to the HSA. You cannot maintain basis in an HSA. Get tax advice if you plan to move Roth or nondeductible IRA assets to an HSA.
- 12. IRA to HSA Contribution More than Federal HSA Limits.** Special rules apply if you move more than the federal HSA limits from your IRA to your HSA. For example, assume you have a family HDHP and are eligible for an HSA contribution of \$5,800 (2008). You transfer \$10,000 from your IRA to your HSA. The \$4,200 (\$10,000-\$5,800) does not enjoy the benefit of the tax-free penalty-free withdrawal rules from the IRA and will be subject to taxes and penalties on the IRA distribution. Additionally, the \$4,200 is also subject to the taxes and penalties from the HSA for exceeding the federal HSA limits unless corrected. Seek professional guidance if you are in this situation.
- 13. IRA Substantially Equal Period Payments.** If the qualified IRA to HSA funding distribution results in a modification of a series of substantially equal periodic payments that, prior to the modification, qualified as an exception to the 10% early distribution penalty for IRAs, then the recapture tax applies to the payments made before the date of the qualified HSA funding distribution if you complete the IRA to HSA transfer. If you are currently taking substantially equal period payments from your IRA seek professional guidance before taking a qualified HSA funding distribution from your IRA because of the potentially serious adverse tax impact.
- 14. FSA/HRA Direct Transfers to HSA.** This Worksheet is not intended for individuals moving money from a Flexible Spending Account (FSA) or Healthcare Reimbursement Account (HRA). The rules for FSA or HRA direct transfers are complex and very different than the rules for IRA to HSA.