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**PayDay**

## THE BASIC TAX CONCEPT

**Health Savings Account ("HSA") contributions are tax-deductible by "qualifying individuals" in one of the following ways:**

- Employer contributions to employee HSAs are not taxable to the employee and are reported on Form W-2, Box 12, Code W;
- Employee contributions to their HSAs via payroll deduction on a "pre-tax basis" reduce their Form W-2 Box 1 taxable wages (like a 401K contribution). Those pre-tax contributions (made pursuant to the employer's Section 125 "cafeteria plan") are also reported as "Code W" on Box 12 of their Form W-2.

**NOTE - HSA contributions reported on Form W-2 as Box 12 Code W should not be deducted again on the employee's personal tax return Form 1040.**

- Employee contributions made "after-tax" via payroll withholding or paid personally are tax-deductible on the employee's Form 1040, by completing IRS Form 8889.

**NOTE - If an employee is not sure whether their HSA contributions paid via payroll withholding were "pre" or "post" tax, they should ask their payroll administrator.**

## FORM W-2 REPORTING - A SUMMARY

- A correct Form W-2 adds the employer contributions with the employee's pre-tax contributions and reports the total in Box 12 of Form W-2 with a "W" code (meaning they are not again deductible by the employee in their personal tax return); and
- An employer is not required to report after-tax employee contributions from payroll to an employee. The employee should deduct after-tax HSA contributions in their personal income tax returns.

## IRS FORM 8889 REPORTING

Every individual who contributes to an HSA account should complete IRS Form 8889 and attach it to their Form 1040. Form 8889 is used to report contributions to a HSA, report distributions from the HSA, and also to calculate and claim an HSA tax deduction.

## HSA FUNDING LIMITS/TAX RULES

Tax law limits annual HSA contributions to the following amounts:

| | 2008 | 2009 |
|---|---|---|
| Under Age 55: | | |
| Single Coverage | $2,900 | $3,000 |
| Family Coverage | $5,800 | $5,950 |
| Additional "catch-up" amount if age 55 or more | $ 900 | $1,000 |

Once an individual reaches age 65, they can no longer contribute to their HSA account. They can continue to hold funds in their HSA and withdraw them tax-free for medical expenses after age 65.

## PARTNERS & 2% + S CORP SHAREHOLDERS

Payments made on behalf of partners and 2% + "S" corporation shareholders are treated as taxable compensation to those small business owners. They in turn can complete Form 8889 and claim personal tax deductions for their HSA funding up to each year's annual funding ceiling.

## IN CONCLUSION

Accurate HSA tax reporting requires good communication between the employer and their payroll company and also their employees. Now is also an excellent time to make sure that HSA funding is an "includable benefit" in your Company's Section 125 "cafeteria plan". HSA's funded by employers or pre-tax by employees through their employer's Section 125 cafeteria plan save employer and employee FICA/Medicare taxes in addition to income taxes.

**HSA tax reporting is relatively new and absolutely confusing. Call one of AccuPay's "CPP/CPA client services teams" at 885-7600 if you have specific questions about HSA payroll and income tax reporting.**

*PayDay is an email communication of payroll news, legal updates and tax considerations intended to inform clients and colleagues of AccuPay about current payroll issues and planning techniques. You should consult with your CPA or tax advisor before implementing any ideas, comments or planning techniques.*

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