

Choosing Between an FSA & HSA



Reducing the cost of employee benefits

The cost of employee health benefits is rising at an exponential rate. As an employer, you may be searching for ways to control costs—including exploring alternative benefit models or shifting more of the cost burden to your employees in the form of higher deductibles, more limited premium cost-sharing, or reduced coverage. However, cost reduction efforts must be balanced with the need to maintain employee satisfaction, and to attract and retain talent. Tax-advantaged benefit accounts represent a compelling way to help offset the increase in your employees' out-of-pocket healthcare costs. Flexible spending accounts (FSAs) and health savings accounts (HSAs) empower your employees to save for and better manage their healthcare costs. Every dollar that an employee contributes will reduce your payroll tax liability.

Differences between FSA & HSA



What is an FSA?

An FSA can be paired with any health plan and is set up and controlled by the employer. The account is funded by pre-tax payroll deferral in an amount elected during open enrollment. Participants can then use that money to pay for qualified healthcare expenses throughout the year. FSAs truly are a “spending” account, in that participants are required to spend the funds by the end of the plan year when they are forfeited—though certain plans may have features that allow for added flexibility. Expenses must be IRS-qualified medical expenses to be eligible for reimbursement with tax-free FSA dollars.



What is an HSA?

Unlike an FSA, an HSA requires that the insured be covered by a high-deductible health plan (HDHP). It also differs from an FSA because the account is owned by the participant. While most HSA participants enjoy the convenience of account contributions being deducted pre-tax from their paychecks, HSAs may also be funded by an employer or family member. The account owner can spend the funds on current eligible expenses or save them for future expenses. Because the account is owned by the individual, the participant is solely responsible for the substantiation of expenses and is not required to send receipts to their employer or administrator.

Criteria	FSA	HSA
Overview		
General Purpose	Funding predictable healthcare expenses in the current year with pre-tax dollars.	Funding a lifetime of healthcare expenses with pre-tax dollars.
Account Owner	Employer Because the account belongs to you, an employee's participation in the plan ends when employment is terminated.	Employee Because the account belongs to the employee, they maintain ownership after they leave the company.
Health Plan Pairings	Can be paired with any health plan.	Must be paired with a qualified HDHP: <ul style="list-style-type: none"> • Deductible not less than \$1,300 for single or \$2,600 for family (2015) • Annual out-of-pocket expenses do not exceed \$6,450 for single or \$12,900 for family. (2015)
Distribution of Funds	Eligible Medical Expenses Only Funds may be used to pay for eligible medical expenses only; cannot access for non-medical reasons.	Eligible Medical Expenses with Exceptions Funds are to be used to pay for eligible medical expenses, but may be withdrawn for non-medical expenses with 10% penalty.
Timing of Usage	FSA with Rollover Up to \$500 of remaining balance may be rolled over to be used in the following plan year. FSA with Grace Period Account balance must be used by the end of the grace period for that plan year; unused balance is forfeited.	Funds are Never Forfeited Reimbursement can be made for any eligible expense incurred from the HSA open date to the current date. Funds do not expire, making an HSA an excellent savings vehicle.
Earnings Investments	No earnings paid.	Some HSA offerings provide integrated investment options and/or interest benefits.
Tax Savings	Tax-deductible Employer contributions are tax-deductible. Tax-free Employee contributions made via payroll deduction are taken out prior to income tax assessment.	Tax-deductible Employer contributions and contributions made by employees above the line (i.e. from their bank account) are tax-deductible. Employee contributions by payroll deferral are pre-tax.
Contributions		
Source of Contributions	Employer: optional Payroll deferral: optional From employee bank account: not allowed	Employer: optional Payroll deferral: optional From employee bank account: optional
Contributions	Annual election amount is determined by the participant during open enrollment and deducted evenly per pay period; Changes may only be made due to a qualified life event (marriage, birth, etc.)	Annual election amount is determined by the participant during open enrollment and deducted evenly per pay period; Employees can adjust contributions throughout the year up to IRS limit; Employers may also contribute.
Contribution Limit	IRS limit of \$2,550	IRS limit of Single: \$3,350 / Family: \$6,750 (2016)
Disbursements		
Direct Access to Funds	Pay providers directly via debit card.	Pay providers directly via debit card or online bill pay, or on the provider's website via ACH.
Claims for Reimbursements	Submit a claim for reimbursement and receipts online, by fax, or using the mobile app.	There are no claims. Employees pay for eligible expenses directly from the account.
Substantiation Requirement	Receipts and Explanation of Benefits (EOBs) should be kept for all purchases. Your plan administrator will require them for reimbursement.	There is no requirement for substantiation. The participant is solely responsible for proper use of funds. Documentation should be kept in case of IRS audit.
Cash Withdrawal	Not permitted.	Cash withdrawals are allowed. The cash must be used on an eligible expense or be subject to a 10% penalty. After age 65, cash withdrawals can be made for non-eligible expenses penalty-free but subject to income taxes.

Primary Benefit of Both Plans

Both plans provide advantages for both the employee and the employer:

- ▶ Tax-free treatment of healthcare expenses.
- ▶ Contributions that are payroll-deferred are not reported as income to the employee, resulting in payroll tax savings for the employer and income tax savings for the employee.
 - Employers can save approximately 7.65%* in reduced payroll taxes on total contributions
 - Employees making contributions will save 15-40% by avoiding federal and state income taxes and the employee half of payroll taxes.

** These figures are based on the employer half of FICA and FUTA. The information detailed is for illustrative purposes only and is not legal or tax advice.*

Which Plan to Choose?

FSA

FSAs do not require participation in a HDHP, so they are most frequently offered in conjunction with traditional health plans. Traditional health plans limit out-of-pocket expenses for participants and make it easy for an employee to estimate annual medical expenses by calculating projected copays, deductible amounts, and co-insurance. Although the addition in 2013 of the rollover feature minimizes forfeited funds, employers still have the benefit of retaining any funds that are forfeited.

HSA

Employers who are seeking to minimize the cost of providing health benefits by offering an HDHP will generally offer an HSA. HSAs offer employees a broader value proposition: the ability to pay for current or future expenses without fear of forfeiting dollars, triple tax advantage, investment growth potential, and the option to pay for non-medical expenditures if necessary.



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