

When Should I Use My Health Savings Account?

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Many savers don't realize they may have a valuable retirement account at their disposal until it's too late. The Health Savings Account (HSA) is an often underutilized tool that can provide a trifecta of tax benefits: tax deduction on contributions, tax-deferred growth on investments, and tax-free withdrawals (for qualified medical expenses). Unfortunately, many eligible individuals view HSAs as a go-to fund for immediate medical needs instead of taking advantage of it as an additional form of retirement savings.

How Can HSA Funds Be Used?

You can access your HSA tax-free and penalty-free to pay for qualified medical expenses at any time, including after you retire. The IRS determines the types of expenses that are qualified and lists them in IRS Publication 502. The list is extensive and includes health plan deductibles and coinsurance, most medical, dental, vision, and chiropractic services, and Medicare premiums (if age 65 or older).

You can take distributions to pay for your spouse's or dependents' medical expenses as well as your own. This is true even if your spouse or dependent has their own medical insurance that is not HSA-eligible. Moreover, you can take distributions in the current year to reimburse yourself for medical expenses in a previous year, as long as the expenses were incurred after your HSA was established. There is no deadline for making withdrawals.

If you use HSA funds for non-qualified medical expenses, you will have to pay regular income tax **plus a 20% penalty**. However, once you reach age 65 or become disabled, distributions are no longer subject to the penalty.

What's The Best HSA Strategy?

If you are eligible to contribute to an HSA and have the financial means to cover your current healthcare costs, the best strategy is to contribute as much as possible, invest the money in the account, and avoid tapping into the funds until retirement. While many use their HSA to cover current prescription copays or high premiums, you will get the most out of this account if you wait to spend it until you're older and have significantly more medical expenses. Waiting allows you to take advantage of the tax-deferred growth on investments in the account, cushioning your retirement savings even more.

The Bottom Line

Thinking about the future cost of health care isn't fun but preparing ahead of time makes any challenge more manageable. By waiting to use your HSA, you can take advantage of its tax-deferred growth and build up a significant amount of retirement savings. With careful planning and a long-term strategy, your HSA can play a key role in your financial future.