

Abstract: Many people don't know that you can transfer funds directly from an IRA to a Health Savings Account (HSA) without taxes or penalties. However, a taxpayer may do so only once during his or her lifetime. This article discusses some of the important points to consider when looking into an IRA-to-HSA transfer.

One-time thing: IRA to HSA transfers

Did you know that you can transfer funds directly from your IRA to a Health Savings Account (HSA) without taxes or penalties? According to the IRS, you're permitted to make *one* such "qualified HSA funding distribution" during your lifetime.

Ordinarily, if you have an IRA and an HSA, it's typically a good idea to contribute as much as possible to both to make the most of their tax benefits. But if you're hit with high medical expenses and have an insufficient balance in your HSA, transferring funds from your IRA may be a solution.

Calling in the cavalry

An HSA is a savings account that can be used to pay qualified medical expenses with pre-tax dollars. It's generally available to individuals with eligible high-deductible health plans. Currently, the annual limit on tax-deductible contributions to an HSA is \$3,600 for individuals with self-only coverage and \$7,200 for individuals with family coverage. If you're 55 or older, the limits are \$4,600 and \$8,200, respectively. Those same limits apply to an IRA-to-HSA transfer, reduced by any contributions already made to the HSA during the year.

Here's an example illustrating the potential benefits of a qualified HSA funding distribution from an IRA: Joe is 58 years old, with a self-only, high-deductible health plan. In 2021, he needs surgery for which he incurs \$5,000 in out-of-pocket costs. Joe is strapped for cash and only has \$500 left in his HSA, but he does have a \$50,000 balance in his traditional IRA. Joe may move up to \$4,600 from his IRA to his HSA tax- and penalty-free.

Considering other factors

If you decide to transfer funds from your IRA to your HSA, keep in mind that the distribution must be made directly by the IRA trustee to the HSA trustee, and the transfer counts toward your maximum annual HSA contribution.

Also, funds transferred to the HSA in this case aren't tax deductible but, because the IRA distribution is excluded from your income, the effect is the same (at least for federal tax purposes).

Exploring the opportunity

IRA-to-HSA transfers are literally a once-in-a-lifetime opportunity, but that doesn't mean they're the right move for everyone. If you're interested, our firm can help you explore the concept in the context of your distinctive tax and financial circumstances.