HSA & FSA Comparison and Take Aways

Self-employed people can open an HSA but not an FSA. To be FSA or HSA eligible, you have to meet specific guidelines. Following are some of the things you'll need to consider before taking the steps to open your own account.

KEY TAKEAWAYS

- Health savings accounts and flexible spending accounts are two fringe benefits offered by some employers that allocate pre-tax dollars for special purposes.
- HSAs and FSAs, while structurally similar, are intended for different purposes and must be used accordingly.
- Contributions to HSAs are made with pre-tax dollars and are associated with high-deductible health insurance plans to help defray some of the high-deductible costs and can be rolled over each year.
- Contributions to FSAs are also made on a pre-tax basis and cover a wider variety of activities, such as child care if you designate the account as a Dependent Care FSA, but you must use-it-or-lose-it.

Health Savings Account (HSA)

An HSA is offered by employers in conjunction with a high-deductible health plan (HDHP).[4] Self-employed people who have high-deductible plans can also set up HSA accounts.

The employer or self-employed individual deposits all or a portion of the deductible into an HSA to cover costs until the deductible is met and the health insurance policy takes over the financial burden.

Once the account is set up, an employee can contribute additional money to the HSA via a payroll deduction from gross income. The money contributed to an HSA account is made with pretax dollars, which reduces the amount of income reported for tax purposes. Interest or earnings on the money in the account is also tax-free

Flexible Spending Account (FSA)

An FSA is similar to an HSA, but there are a few key differences. For one, self-employed individuals aren't eligible.

One of the biggest benefits of an FSA is that it can be set up as a Dependent Care FSA (DCFSA) to allow withdrawals for childcare expenses. It is also possible to have a separate, regular FSA to cover medical expenses depending on your company's plan.

Like the HSA, you can contribute to an FSA using your gross pay, making the contributions tax-free. As long as you use the funds to pay for qualified medical expenses, you probably won't owe taxes on withdrawals.

Key Differences

A withdrawal from an HSA can be used for a broad range of medical expenses including eyeglasses, contacts, chiropractic care, and prescription drugs as well as doctor visits and hospital stays.

The HSA is a portable account so you keep your money even if you switch jobs.[8] To qualify for an HSA, you have to be enrolled in a high-deductible health plan.[4] In most cases, you are not eligible if you have other health coverage or can be claimed as a dependent by someone else.[7]

Aside from setting up your FSA as a DCFSA, which allows withdrawals for eligible childcare expenses, you can also have a separate, regular FSA to cover medical expenses depending on your company's plan.

Like the HSA, you can contribute to an FSA using your gross pay, making the contributions tax-free. As long as you use the funds to pay for qualified medical expenses, you probably won't owe taxes on withdrawals.

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Special Considerations

Unlike an HSA, you have to declare how much you would like your employer to deduct from your gross pay to fund your FSA in each calendar year. Once that declaration is made, you generally can't change it.

If you declined the FSA during the open enrollment period, you'll likely have to wait until the next open enrollment.

Your declared funds must be spent within the tax year, although a grace period is sometimes granted.[10] The money you contribute can be lost if you don't spend it all by the deadline.

You don't have to be covered under a health insurance policy to be eligible, but FSA funds are not an adequate substitute for health insurance. You also can't use an FSA to pay for your health insurance premiums.

If you can't afford both, it would be better to put those funds toward health insurance.

The table below shows the differences and similarities between both health accounts:

HSA vs. FSA

	HSA	FSA
Eligibility	Must have a qualified high-deductible health plan (HDHP). Self-employed can contribute.	All employees are eligible regardless of whether they have insurance or not. Self-employed cannot contribute.
2021 Contribution Limit	$3,600 Individual Coverage, $7,200 Family Coverage	$2,750
Contribution Source	Employer and/or employee	Employer and/or employee
Account Owner	Employee	Employer
Rollover	Unused contributions can be rolled over to the next year.	Unused contribution is lost at end of the year.
Withdrawals	Allowed, but includes tax withheld plus 10% penalty.	Not allowed.
Interest Earned	Interest earned in the account is tax-free.	Account does not earn interest.
Portability	The employee keeps account even if they changes jobs.	The account is forfeited after a job change.
Accessibility	Can only access what has been contributed to the account.	Complete access to the annual election amount, regardless of whether the account has been fully funded or not.
Contribution Amendment	Employees can change contribution amount during the year.	The employee is stuck with the contribution amount chosen at the beginning of the year.

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