



FDIC

Federal Deposit Insurance Corporation
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Legal Division

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Thank you for your letter about how the Federal Deposit Insurance Corporation would insure Health Savings Accounts (“HSAs”), recently authorized in the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (Public Law No.108-173, December 8, 2003) (the “Act”). Under this legislation, HSAs may be established to pay “qualified medical expenses” of the individual who establishes the account or the individual for whom the account is established. Eligibility for HSAs is limited to individuals with “high-deductible” health insurance plans, defined as plans with designated minimum annual deductibles for individual coverage and for family coverage. With exceptions, individuals, their employers or both may contribute to HSAs tax-deductible funds each year up to the amount of the policy’s annual deductible, subject to specific caps for individuals and for families. Your question is how the FDIC will insure an HSA if it is held in the form of a deposit account at an FDIC-insured depository institution.

Technically a “Trust”

HSAs must be in the form of a *trust* established on behalf of the “account beneficiary,” defined as the individual on whose behalf the HSA is established. 26 U.S.C. 223(d)(1).¹ The Act requires that the trustee be a bank, an insurance company or other “person” specifically approved by the Internal Revenue Service. *Id.*

The FDIC has different rules for insuring different types of trust accounts. One set of rules applies to *irrevocable* trusts and another applies to *revocable* trusts. Thus, it is important for deposit insurance purposes to determine what type of trust an HSA is. The terms *irrevocable* and *revocable* are, for these purposes, self-descriptive. If the trust may not be revoked (that is, cancelled or modified by the owner) it is irrevocable; if it may be revoked, then it is revocable. The Act clearly contemplates that an HSA trust is revocable. This is evidenced primarily in the “distribution” provisions in the Act on the tax treatment and penalties for HSA “inclusions” “not used for ‘qualified medical expenses.’” 26 U.S.C. 223(f). The implication is that an account owner may use HSA funds for purposes other than those described in the Act (and in the trust), but he or she would incur adverse tax consequences for doing so. This implicit retained authority to use trust assets for purposes other than those indicated in the trust, in effect, renders the trust

¹ For ease of reference, citations to the Act are in the form of citations to the provisions of the Internal Revenue Code amended by the Act.

Although the Act specifies that an HSA must be in the form of a trust, IRS guidelines on HSAs (IRS Notice 2004-2) indicate that HSAs may be in the form of a trust or “custodial” account. Given the characteristics of an HSA, the deposit insurance coverage would be the same whether the account is held as a trust or pursuant to a custodial agreement.

revocable. Hence, the FDIC's insurance rules on insuring revocable trust accounts would apply to HSAs.

Revocable Trust Account Rules

Under section 330.10 of the FDIC's insurance rules (12 C.F.R. 330.10), revocable trust accounts evidencing an intent that the funds shall belong to named beneficiaries upon the owner's death are insured up to \$100,000 per "qualifying beneficiary" named in the account. (Qualifying beneficiaries are defined as the account owner's spouse, children, grandchildren, parents and siblings.) This coverage is separate from and in addition to the insurance available to revocable trust account owners who have other accounts at the same institution held in different ownership capacities. For example, a depositor's revocable trust account is insured separately from any *individual* accounts or *joint* accounts the owner has at the same institution. If a revocable trust account does not name any qualifying beneficiaries, then the funds in the account are insured as the individually owned funds of the account owner. As such, the trust account funds are added to any other individually owned funds the owner has at the same institution and insured to a combined limit of \$100,000. 12 C.F.R. 330.6.

Congress authorized HSAs to enable eligible individuals to accumulate funds on a tax-free basis to pay *qualified medical expenses*. An HSA is not testamentary by its nature and, thus, presumably an individual who establishes an HSA is not doing so to provide a bequest to named beneficiaries on the owner's death. It seems likely, therefore, that HSAs will be established by individuals without any designation of testamentary beneficiaries. In those cases, the HSA would be insured as the owner's individually owned funds. As noted, a depositor's individually owned funds are insured up to \$100,000. If the owner has other individually owned accounts at the same institution, the HSA funds would be added to the funds in those other individual accounts and insured to a combined limit of \$100,000.

The Act contemplates that owners might designate beneficiaries in HSAs. In particular, it has a special provision for the treatment of HSAs after the death of the account owner relative to rights of designated beneficiaries. 26 U.S.C. 223(f)(8). If an HSA owner designates that the funds shall belong to one or more named beneficiaries upon the account owner's death, then the account would be eligible for the per-qualifying-beneficiary revocable trust account coverage described above. For example, if a person has an HSA naming his or her two children as death beneficiaries of the account, then the account would be insured up to \$200,000 (\$100,000 per qualifying beneficiary). As noted, this insurance coverage would be in addition to coverage afforded to the depositor with respect to other accounts he or she has at the same institution in different ownership capacities, including the individual ownership capacity.

In this connection it is important to note that, if an owner has an HSA naming qualifying beneficiaries, the coverage on that account would be combined with the coverage afforded to other revocable trust accounts (such as payable-on-death ("POD") and "living trust" accounts)

the owner has at the same insured institution. An HSA owner would not be entitled to coverage on the HSA separate from the coverage on other revocable trust accounts naming the same beneficiaries. Also, FDIC insurance rules require, in order for an account owner to be eligible for per-qualifying-beneficiary coverage, that: (1) such revocable trust accounts indicate in their title that the account funds shall pass to named beneficiaries upon the owner's death; and (2) the institution's deposit account records specify the names of the account beneficiaries. If these requirements are not met, then the account is treated for deposit insurance purposes as an individual account of the account owner.

HSA's Established by an Employer

The Act contemplates that HSA's may be established by employers for employees.² Under the FDIC's deposit insurance rules, separate "pass-through" coverage is provided for employee benefit plan deposits (12 C.F.R. 330.14). That means coverage is available up to \$100,000 for the non-contingent interest of each employee covered by the plan. The FDIC's regulations refer to the Employee Retirement Income Security Act of 1974 for the definition of "employee benefit plan." That definition, found in 29 U.S.C. 1002, would seem to encompass HSA's established by employers.³ If so, each employee for whom an employer establishes an HSA with an FDIC-insured institution would be insured up to \$100,000 under the employee benefit plan category of the FDIC's deposit insurance regulations. This coverage would be separate from the other categories of coverage to which the employee would be entitled, such as individual, joint and revocable trust accounts. Any other employee benefit accounts at the same institution established by the same employer for the same employee, however, would be added to the employee's HSA and insured to a limit of \$100,000. Also, the depository institution would have to meet prescribed regulatory capital standards for this employee benefit plan "pass-through" coverage to be available. See 12 CFR 330.14.

What about MSAs and IRAs?

² For example, section 223(d)(4)(C) refers to "employer payments." 26 U.S.C. 223(d)(4)(C).

³ The term "employee welfare benefit plan" is defined at 29 U.S.C. § 1002(1) as:

any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or both, to the extent that such plan, fund, or program was established or is maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or otherwise, (A) medical, surgical, or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits, apprenticeship or other training programs, or day care centers, scholarship funds, or prepaid legal services

HSA's are the successor to Medical Savings Accounts ("MSAs"). In June 1998 the FDIC issued a legal opinion concluding that, for deposit insurance purposes, we would consider an MSA as an individual ownership account of the individual who establishes the MSA. As such, MSA funds would be added to any other funds the same individuals held in other individual ownership accounts at the same insured bank or thrift and insured up to \$100,000. We also concluded that: if an individual established an MSA as a revocable trust account, designating qualifying beneficiaries, the account would be insured under that ownership category up to \$100,000 per qualifying beneficiary, assuming the other applicable requirements were met; and if an employer established an MSA for an employee the account would be treated as a employee benefit plan account for deposit insurance purposes. For depositors who have both an MSA and an HSA (both either naming no "qualifying beneficiaries" or the same "qualifying beneficiaries"), funds in those accounts would be aggregated and insured to the limits explained above for revocable trust accounts and individually owned accounts.

By statute, an Individual Retirement Account ("IRA") is entitled to separate insurance under a separate category of coverage. 12 U.S.C. 1821(a)(3). Thus, a depositor's HSA would be insured separately from an IRA the depositor might have at the same FDIC-insured institution.

Summary

In summary:

- Because an HSA is technically a revocable trust, the FDIC's rules on revocable trust account coverage apply.
- An HSA naming no qualifying beneficiaries would be insured as the individual funds of the owner. As such, the funds in the HSA would be added to any other individual account funds the owner has at the same institution and insured to a limit of \$100,000.
- An HSA naming qualifying beneficiaries would be insured up to \$100,000 per qualifying beneficiary named in the account, providing the FDIC's recordkeeping rules for revocable trust account coverage are met. HSAs structured this way would be added to any other revocable trust accounts (such as POD and "living trust" accounts) that the owner has at the same institution and insured to a combined limit of \$100,000 per qualifying beneficiary.
- An HSA established by an employer might be eligible for deposit insurance under the employee benefit plan category of coverage, with potential separate coverage up to \$100,000 per employee. The FDIC's employee-benefit-plan-account requirements would have to be met.

- An HSA and MSA owned by the same individual in the same manner would not be insured separately because they come within the same deposit insurance ownership capacity.
- IRA coverage generally is separate from other categories of coverage and, thus, would not be aggregated with HSA coverage.