08.13.26 | FINANCIAL LITERACY

Health Savings Accounts: Beyond the Basics

Most people first use a Health Savings Account, or HSA, as a checking account for medical bills. Money goes in, a deductible or prescription is paid, and the immediate tax benefit is captured.

That is useful, but it is only the beginning.

The more powerful feature of an HSA is control over timing. Money can pay medical expenses today, remain available for future care, or be invested for costs that may not arrive for decades. The best approach depends on cash flow, medical needs, investment risk, and the broader financial plan.

In the first article of this series, we covered the fundamentals: eligibility, contributions, qualified expenses, and withdrawal rules. Part two focuses on the strategic question: Once an HSA is funded, how should the money be used?

ONE ACCOUNT, THREE POSSIBLE JOBS

An HSA can serve three roles:

- **A spending account** for current medical bills
- **A reserve** for larger or less predictable expenses
- **A long-term asset** invested for future health care costs

These roles can work together. Part of the account can remain in cash while another portion is invested. The right mix depends on when the money may be needed.

The central principle of HSA planning is that every dollar still needs a job.

MATCH THE INVESTMENT STRATEGY TO THE TIME HORIZON

Many HSA providers allow balances to be invested after a required amount is held in cash. Investing can create long-term growth potential, but it also introduces market risk.

Money needed for next month's deductible should not be treated like money intended for medical expenses 20 years from now. A practical structure is to keep near-term medical needs and a reasonable cushion in cash, then consider investing dollars unlikely to be needed for several years.

There is no universal cash target. Someone with recurring prescriptions, planned procedures, or limited emergency savings may need more liquidity. A household with predictable expenses and strong reserves may be comfortable investing more.

The goal is not to invest as much as possible, but rather to invest only what can remain invested through normal market volatility.

SHOULD YOU SPEND THE HSA OR PRESERVE IT?

When a qualified medical bill arrives, the owner can withdraw from the HSA or pay from regular cash flow.

Using the HSA immediately is not a mistake. Tax-free withdrawals reduce the after-tax cost of care and can keep medical bills from straining savings or creating debt.

Paying out of pocket may make sense when cash flow is strong and the owner wants to preserve the HSA. Money left in the account can continue growing without current federal income tax, and qualified withdrawals may remain tax-free later. Unused balances carry forward rather than expiring.

Preserving an HSA is not worthwhile if it drains the emergency fund, creates high-interest debt, or weakens financial stability. A future tax benefit should not create a present-day cash-flow problem.

THE DELAYED-REIMBURSEMENT OPPORTUNITY

A person who pays a qualified expense personally may reimburse themselves from the HSA in a later year. Current federal guidance imposes no deadline, provided the expense occurred after the HSA was established, was not reimbursed elsewhere, and was not previously claimed as an itemized medical deduction.

Suppose an HSA owner pays $4,000 of qualified expenses from checking and retains the records. Years later, that person may be able to withdraw $4,000 from the HSA tax-free, even if the cash is then used for something unrelated to health care. The earlier medical expense supports the tax-free reimbursement.

This can turn saved receipts into future tax-free liquidity during retirement, a career change, or another period when cash is needed.

The strategy only works if the documentation survives. Records should identify the patient, provider, service, date, amount paid, and proof that the expense was not reimbursed elsewhere. A secure digital system is more reliable than paper receipts.

THE HSA'S ROLE IN RETIREMENT

Health care does not disappear when retirement begins. Even with Medicare, retirees may face premiums, deductibles, prescriptions, dental and vision care, hearing expenses, and other out-of-pocket costs.

After age 65, HSA funds can be used tax-free for certain Medicare and other health coverage premiums, although Medigap premiums do not qualify. Certain long-term-care insurance premiums may also qualify, subject to age-based limits.

The account also becomes more flexible after age 65. Nonmedical withdrawals remain taxable as ordinary income, but the additional 20% tax no longer applies. Qualified medical withdrawals remain tax-free. An HSA can therefore serve as both a tax-free source for health care and a taxable backup source for other retirement spending. It does not replace a 401(k), IRA, Roth account, or cash reserve; it complements them.

WHERE SHOULD THE HSA FIT AMONG OTHER PRIORITIES?

The HSA's tax benefits are compelling, but they do not override every other financial priority.

Before paying medical bills out of pocket simply to preserve the HSA, a household should have adequate emergency savings, avoid expensive debt, capture any available employer retirement-plan match, and meet immediate obligations comfortably.

For households with strong cash flow and sufficient reserves, funding and investing an HSA may be attractive. For those with substantial current medical costs or tighter liquidity, using the account today may be the more disciplined decision.

The right strategy is not the one that appears most tax-efficient on paper. It is the one the household can sustain.

DO NOT OVERLOOK THE BENEFICIARY DESIGNATION

If a spouse is the designated beneficiary, an HSA becomes the spouse's HSA after the owner's death. If the beneficiary is not a spouse, the account stops being an HSA and its value becomes taxable to that beneficiary in the year of death. If the estate is named, the value is generally included on the owner's final income-tax return.

As HSA balances grow, beneficiary designations should be reviewed after marriage, divorce, death, or another major family change.

COMMON WAYS THE STRATEGY BREAKS DOWN

HSA planning can fail when someone:

- Invests money that may be needed soon
- Preserves the account while weakening emergency savings
- Loses the receipts needed for future reimbursement
- Reimburses an expense that was already covered elsewhere

- Overlooks investment fees or limited fund choices
- Treats the HSA separately from the rest of the financial plan

The account should also be reviewed periodically. Medical needs, insurance coverage, cash flow, investment options, and retirement timing can all change.

A DISCIPLINED PLANNING PERSPECTIVE

An HSA can be a spending account, a medical reserve, an investment account, or a source of future tax-free liquidity. Its value comes from being able to serve each role at the appropriate time.

The planning questions are practical: How much may be needed for health care soon? How strong are the household's reserves? Which dollars can remain invested through a market decline? Are receipts being preserved? How does the account fit with retirement and estate planning?

Used thoughtfully, an HSA does more than reduce the cost of today's medical bills. It creates options–and in financial planning, the ability to choose when and how money is used can be as valuable as the tax benefit itself.

This article is part of an ongoing series aimed to help build overall financial literacy and was authored by Grimes & Company's 2026 Intern John Grimes. While not a comprehensive deep dive into every single topic, it is designed to provide a helpful overview to key topics within the world of investing and financial planning. Please ***reach out to connect*** *with an advisor or expert on the subject to learn more and start planning for your financial future.*