Health FSA vs. HSA: Which Type of Account Is Best?

TOWNE BENEFITS

Health flexible spending accounts (FSAs) and health savings accounts (HSAs) are popular types of medical savings accounts. Both health FSAs and HSAs allow employees to set aside pre-tax dollars to cover out-of-pocket medical expenses; yet, there are several important differences between the two. For example, while HSAs must be paired with high deductible health plans (HDHPs), health FSAs are typically offered with traditional group health plans that have lower cost-sharing requirements.

Employers should weigh several factors when deciding between a health FSA paired with a traditional health plan or an HSA/HDHP pairing, including workforce demographics, employer resources and overall benefits strategies. A health FSA paired with a traditional health plan may be more appropriate for an older workforce (or employees who frequently use healthcare services), as lower deductibles help budget for medical expenses. An HSA/HDHP pairing may appeal more to younger workers or healthier populations who are less likely to utilize healthcare services beyond preventive care.

Health FSAs trigger significant compliance obligations that do not apply to HSAs, such as those under ERISA, COBRA and HIPAA. However, an HSA/HDHP pairing requires more employee education and involvement to manage out-of-pocket healthcare costs.

Links and Resources

- IRS Publication 969, Health Savings Accounts and Other Tax-favored Health Plans
- IRS Publication 502, Medical and Dental Expenses
- IRS Notice 2004-50, which includes Q&As on a variety of HSA topics
- IRS Notice 2012-40, which includes rules on the health FSA contribution limit

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Comparison Chart

	HSA	Health FSA
Type of account	An HSA is an individually owned account maintained by an HSA trustee or custodian.	A health FSA is an employer-sponsored, self-funded health plan.
Account owner	The employee owns the account.	The employer owns the account.
Type of main health plan	An HSA must be paired with an HDHP. To qualify as an HDHP, a health plan must provide significant benefits and meet the following cost-sharing limits for plan years beginning in 2026: • **The minimum deductible** is $1,700 for self-only coverage and $3,400 for family coverage. For 2027 plan years, these limits increase to $1,750 and $3,500, respectively. • **The out-of-pocket maximum** is $8,500 for self-only coverage and $17,000 for family coverage. For 2027 plan years, these limits increase to $8,700 and $17,400, respectively.	A health FSA may be offered with any type of group health plan.
Source of contributions	Contributions can be made by anyone, including the account owner and their employer. Employees' pre-tax contributions must be made through an Internal Revenue Code (Code) Section 125 cafeteria plan.	Contributions can be made by employees and the employer, depending on the health FSA's design. Employees' pre-tax contributions must be made through a Code Section 125 cafeteria plan.
Eligible employees	To be eligible for HSA contributions, an employee must: • Be covered under an HDHP; • Not be covered by other health coverage (with limited exceptions); • Not be enrolled in Medicare; and • Not be eligible to be claimed as a tax dependent.	Employees who are eligible to participate in the employer's main group health plan can be eligible for the health FSA. Employers can impose additional eligibility requirements, subject to applicable nondiscrimination rules under Code Sections 105(h) and 125.
Termination of employment	HSAs are nonforfeitable and portable, which means an employee keeps their account upon termination of employment.	The account is forfeited when an employee terminates employment, unless COBRA applies.
Unused funds	Unused funds can be rolled over to the next year. There is no deadline for using HSA money.	Unused funds cannot be rolled over to the next year, with two limited exceptions. A health FSA may include a 2.5-month grace period after the end of the plan year to spend unused funds. Alternatively, a health FSA may allow employees to carry over up to $500 (as adjusted for inflation) in unused funds into the next plan year. The carryover limit for plan years beginning in 2026 is $680. The carryover

		limit for plan years beginning in 2027 has not yet been released.
Employee contribution limit	For 2026, the contribution limit is $4,400 for individuals with self-only HDHP coverage and $8,750 for individuals with family HDHP coverage. These limits will increase to $4,500 and $9,000, respectively, for 2027. Individuals age 55 or older by the end of the year can increase their contribution limit up to $1,000 per year as a catch-up contribution.	For plan years beginning in 2026, an employee's pre-tax contributions may not exceed $3,400 for the year. The contribution limit for plan years beginning in 2027 has not yet been released. Employers may impose lower limits on employee health FSA contributions.
Employer contribution limit	The contribution limit applies to all money contributed to an HSA by (or on behalf of) an employee, regardless of the source. For 2026, the contribution limit is $4,400 for individuals with self-only HDHP coverage and $8,750 for individuals with family HDHP coverage ($4,500 and $9,000, respectively, for 2027). An additional $1,000 catch-up contribution is available for eligible individuals.	If an employer makes contributions, they must be limited to the greater of: • Two times the participant's salary reduction election under the health FSA for the year; or • The amount of the participant's salary reduction election for the health FSA for the year, plus $500.
Mid-year election changes	An employee who elects to make pre-tax HSA contributions may change the amount of those contributions (or start or stop contributions) at any time during the plan year, provided the change is effective prospectively.	In general, employees cannot change their pre-tax health FSA contributions during the plan year. However, as a plan design option, health FSA participants may be allowed to change their contributions for the remaining portion of a year on account of and consistent with certain midyear election events recognized by the IRS.
Nondiscrimination testing	If employees can make pre-tax HSA contributions, the employer's contributions are subject to the nondiscrimination tests for Section 125 cafeteria plans. If an employer does not allow employees to make pre-tax HSA contributions, the employer's contributions are subject to the comparability rules under Code Section 4980G.	As a self-insured health plan, employer health FSA contributions are subject to nondiscrimination testing under Code Section 105(h). The Code Section 125 nondiscrimination rules also apply.
Eligible expenses	HSAs can pay otherwise unreimbursed medical care expenses (as defined in Code Section 213(d)) of the account owner, spouse and tax dependents on a tax-free basis. The expenses must have been incurred after the HSA was established. HSAs can be used to pay for a qualifying child's medical care expenses until the child reaches age 19 (age 24 if the child is a full-time student). HSAs cannot reimburse insurance premiums, with exceptions for: • COBRA coverage; • Long-term care coverage; • Health coverage while receiving unemployment benefits; and	Health FSAs can pay otherwise unreimbursed Code Section 213(d) medical expenses of the employee, spouse, children up through age 26 and tax dependents that were incurred during the coverage period, subject to any employer limitations. Health FSAs cannot reimburse insurance premiums, without exceptions.

	• Medicare and other health coverage for an individual who has reached age 65, other than premiums for Medicare supplemental policies. HSAs can also reimburse membership fees for direct primary care service arrangements.	
Expense substantiation	HSA owners are solely responsible for maintaining records that substantiate their medical expenses.	Claims must be substantiated by the employer (or a third-party service provider) before they are reimbursed.
Amounts available for reimbursement	Reimbursements can only be made from funds that have been contributed to and are available in the HSA.	Once the plan year begins, an employee's maximum amount of reimbursement must be available at any time during the coverage period (reduced only for any prior reimbursements during the same coverage period), even if reimbursement would exceed the year-to-date contributions to the employee's health FSA. This is referred to as the uniform coverage rule.
ERISA	Not applicable	As a group health plan, a health FSA is subject to ERISA, unless the employer is a governmental entity or church. Being subject to ERISA means that certain fiduciary duty and claims procedure rules apply. It also means the employer must adopt a plan document, and participants must receive a summary plan description.
COBRA	Not applicable	A health FSA is subject to COBRA if the employer has at least 20 employees. However, under a special rule for health FSAs, an employer: • Is not required to offer COBRA coverage to qualified beneficiaries who have "overspent" their health FSA accounts; and • Must offer COBRA coverage to qualified beneficiaries who have "underspent" their health FSA accounts, but the COBRA coverage may terminate at the end of the year in which the qualifying event occurs.
Form 5500	Not applicable	All ERISA-covered health FSAs are subject to the Form 5500 annual reporting requirement, unless the plan is unfunded and has fewer than 100 participants.
HIPAA Privacy and Security Rules	Not applicable	As a self-funded health plan, a health FSA is subject to the full range of requirements under the HIPAA Privacy and Security Rules, unless the health FSA has fewer

		than 50 participants and is self-administered.