The new “medical IRA”:

Using an HSA for tax-free retirement income

Key takeaways

- Most people use an HSA to contribute money each year and then withdraw it that same year to pay for current medical expenses.
- Keeping funds invested in an HSA for many years allows clients to take advantage of the potential for tax-free growth over many years — similar to investing in an IRA.
- Maximizing HSA contributions can lower an individual’s tax liability — a big benefit, especially for high-earners.
- Saving receipts of qualified medical expenses is key, because the client could withdraw HSA funds as reimbursements years or even decades later.
- Educating clients on the short- and long-term potential of HSAs is another way to strengthen your relationships with them.

Don’t underestimate the potential of a health savings account (HSA). Designed as a tax-advantaged savings vehicle for medical expenses, HSAs can also be powerful tools for long-term investing (yes, investing) and tax-savvy financial planning.

The tax advantages of HSAs are well-known. Clients with qualified high-deductible health plans (HDHPs) can use HSAs to stash away pretax dollars, avoid taxes on earnings, and withdraw funds tax-free for qualified medical expenses.

What’s often overlooked, however, is the ability to use an HSA as a sort of “medical IRA.” As a financial professional, you can demonstrate your expertise and strengthen clients’ loyalty to you by educating them on this forward-thinking strategy.

What’s missing from the usual HSA approach

Most people use an HSA as simply a tax-advantaged savings account. They contribute money each year but usually withdraw it that same year to pay for current medical expenses. As a result, the HSA has little to no opportunity to grow over time.

While this approach is beneficial in the short run, it doesn’t help clients plan for their health care costs during retirement — which could be significant. The Employee Benefit Research Institute (EBRI) estimates that to have a 90% chance of meeting their health care spending needs in retirement, a 65-year-old woman would need $217,000 — and a 65-year-old man $184,000. EBRI projects that a couple with high prescription drug costs would need $413,000 to meet that 90% target.[1]

To have a 90% chance of meeting their health care spending needs in retirement:

A 65-year-old woman would need

A 65-year-old man would need

A couple with high prescription drug costs would need

[1] “Projected Savings Medicare Beneficiaries Need for Health Expenses Increased Again in 2023,” EBRI, https://www.ebri.org/docs/default-source/ebri-issue-brief/ebri_ib_599_savingstargets-18jan24.pdf?sfvrsn=1b23072f_4 (January 18, 2024).

The “medical IRA” strategy

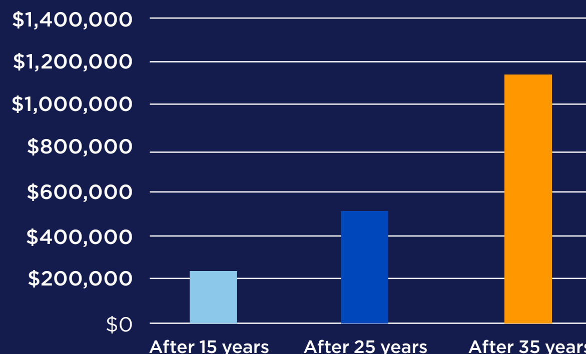
An alternate approach involves keeping funds invested in the HSA for many years to take advantage of the potential for tax-free growth over time — similar to investing in an IRA.

1. The HSA is held within an account with a selection of investment options. If needed, an HSA can be moved — or a new HSA set up — to improve the client’s access to investment options.
2. The investment allocation is aligned with the client’s retirement accounts. This keeps the client’s overall portfolio in line with their goals and tolerance for risk.
3. The client contributes to the HSA each year — ideally up to the maximum. The 2025 limits are $4,300 for individual-only coverage and $8,550 for family coverage. In each year, those 55 and older can contribute an extra $1,000.
4. As medical costs are incurred, the client pays for them out of pocket, saving all receipts for HSA-eligible expenses. Saving receipts is key, because there’s no time limit on HSA reimbursements. The client could withdraw HSA funds as reimbursements for qualified medical expenses years or even decades later.
5. By keeping the HSA funds invested, the account has the potential to grow over many years. When withdrawals are used for qualified medical expenses, those withdrawals are 100% tax-free. Starting at age 65, HSA withdrawals can be used for any purpose without penalty — but HSA funds used for nonmedical expenses will still be taxed as income. (As a reminder, HSA contributions must stop upon enrollment in any part of Medicare.)

As an example of the potential long-term compounding opportunity of this approach, consider a hypothetical client, Raj. He’s 50 years old and has an HSA-qualified HDHP that covers his family. Using the 2025 guidelines, he’s eligible to contribute up to $8,550 per year — or approximately $712 per month.

If he keeps up that contribution level for 15 years and makes no withdrawals, he’ll have $214,813 at age 65 (assuming a 7% annual rate of return). He could then withdraw funds tax-free to spend on a wide range of health care costs — including Medicare premiums, prescription drugs, co-pays and more.

The earlier Raj starts this strategy, the greater the potential impact. Take a look at the examples here.



Assumptions: $712 monthly contribution, 7% annual return, no withdrawals.

This illustration is hypothetical and is not intended to serve as a projection of the investment results of any specific investment. Actual results will vary.

FOR FINANCIAL PROFESSIONAL USE — NOT FOR DISTRIBUTION TO THE PUBLIC

Lowering income taxes with an HSA

Of course, there are certainly still short-term benefits to HSAs. Money that's contributed to an HSA lowers the amount of income subject to federal, state and FICA taxes. That in turn lowers an individual's tax liability — a big benefit, especially for high-earners.

Here's an example to illustrate the tax-reducing benefit of a health savings account. Adam and Ruth both work at the same company but are at different stages of their careers. Their employer offers an HSA-eligible health care plan and will match employee contributions each year up to $500 for single employees and up to $1,000 for those employees who are covering spouses or family members in the company's health care plan.

Let's consider Adam's situation first. Adam is young, single and healthy. He's just starting his career and earns an annual salary of $52,000 or $2,000 each biweekly period. Most of Adam's paycheck goes to covering his basic living expenses, but he wants to take advantage of the opportunity to put money aside in an HSA. Also, he likes that his employer will chip in $500 to his HSA.

Adam figures he can contribute $100 per paycheck to his HSA, which he expects to use mostly for future medical expenses.

Combining Adam's pretax HSA annual contribution with the $500 employer contribution, he's able to save $3,100 in his HSA this year. That's under the $4,300 annual contribution limit for single taxpayers, which includes both individual and matching contributions. And if Adam uses the money to pay for qualified medical expenses, he'll save more than $850 this year by reducing federal, state and FICA taxes.

	Pay period	Annual
Gross salary	$2,000.00	$52,000.00
HSA employee contribution	$100.00	$2,600.00
HSA employer contribution		$500.00
Tax savings		
Federal tax (22%)	$22.00	$572.00
State tax (3.226%)	$3.23	$83.98
FICA tax (7.65%)	$7.65	$198.90
Total tax savings	**$32.88**	**$854.88**

FOR FINANCIAL PROFESSIONAL USE — NOT FOR DISTRIBUTION TO THE PUBLIC

Let's turn to Ruth, who is 60 years old and looking forward to retirement. She earns an annual salary of $104,000, or $4,000 per biweekly period. Ruth and her spouse, Stan, are both covered in Ruth's HSA-eligible health care plan at work.

Because of the $1,000 employer contribution to her HSA, Ruth is limited to how much she can contribute from her paycheck by the annual HSA contribution limit of $8,550 for families. She can, however, take advantage of the additional $1,000 catch-up contribution thanks to her age — bringing her total 2025 contribution to $9,550.

Still, Ruth can enjoy significant tax savings this year by maximizing how much she contributes to her HSA.

	Pay period	Annual
Gross salary	$4,000.00	$104,000.00
HSA employee contribution	$328.84	$7,550.00
HSA employer contribution		$1,000.00
Catch-up contribution		$1,000.00
Total HSA contribution		$9,550.00
Tax savings		
Federal tax (22%)	$80.80	$2,101.00
State tax (3.226%)	$11.84	$308.00
FICA tax (7.65%)	$28.09	$730.57
Total tax savings	**$120.73**	**$3,139.57**

If she uses the HSA savings to cover qualified medical expenses for herself and her spouse, she'll reduce her federal, state and FICA taxes by more than $2,700 this year.

Talk to your clients about HSAs

If you haven't yet **discussed HSAs with your clients**, consider bringing it up soon. Educating clients on the short- and long-term potential of these accounts is another way for you to strengthen your relationships with them while providing a much-needed service.

For more information about the benefits of HSAs and other strategies for preparing for health care costs in retirement, visit **Nationwide.com/SimplifyHealth CareCosts**.

FOR FINANCIAL PROFESSIONAL USE — NOT FOR DISTRIBUTION TO THE PUBLIC

This material is not a recommendation to buy or sell a financial product or to adopt an investment strategy. Investors should discuss their specific situation with their financial professional.

HSAs are not taxed at a federal income tax level when used appropriately for qualified medical expenses. Also, most states, but not all, recognize HSA funds as tax-free. Please consult a tax advisor regarding your state's specific rules.

Federal income tax laws are complex and subject to change. This information is based on current interpretations of the law; it is not guaranteed and has not been endorsed by any government agency. This information is general in nature and is not intended to be tax, legal, accounting or other professional advice.

Nationwide and its representatives do not give legal or tax advice. An attorney or tax advisor should be consulted for answers to specific questions.

Before investing, clients should consider the investment's objectives, risks, charges and expenses. Investing involves market risk including loss of principal.

Nationwide Investment Services Corporation (NISC), member FINRA, Columbus, Ohio. The Nationwide Retirement Institute is a division of NISC.

Nationwide, the Nationwide N and Eagle and Nationwide Retirement Institute are service marks of Nationwide Mutual Insurance Company. © 2024 Nationwide

NFM-24053AO.1 (10/24)