

August 31, 2004

Subject: Credit unions are authorized to act as trustee or custodian for Health Savings Accounts
DCU Interpretative Letter I-04-04

Dear "A":

This opinion is in response to your question whether a Washington state chartered credit union may act as a trustee or custodian for Health Savings Accounts (HSA). You have cited the amendments to 12 C.F.R. 721 [Incidental powers] and 12 C.F.R. 724 [Trustee and Custodian Plans] as providing authority for federal chartered credit unions to act as a trustee or custodian for Health Savings Accounts (HSA) and you have asked if a Washington state chartered credit union may invoke federal parity to provide similar HSAs.

Background:

Health Savings Accounts (HSAs) were created by H. R. 1, the "Medicare Prescription Drug, Improvement and Modernization Act of 2003," signed into law by President Bush on December 8, 2003. HSAs are intended to help individuals save for future qualified medical and retiree health expenses on a tax-free basis.

Any individual who is covered by a high-deductible health plan may establish an HSA. Amounts contributed to an HSA belong to the individual establishing the account and are completely portable. Every year the money not spent stays in the account and gains interest tax-free, similar to an Individual Retirement Account (IRA). Unused amounts remain available for later years (unlike amounts in Flexible Spending Arrangements that are forfeited if not used by the end of the year). Tax-advantaged contributions can be made in three ways: the individual and family members can make tax deductible contributions to the HSA even if the individual does not itemize deductions; the

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individual's employer can make contributions that are not taxed to either the employer or the employee; and employers with cafeteria plans can allow employees to contribute untaxed salary through a salary reduction plan. Funds distributed from the HSA are not taxed if they are used to pay qualifying medical expenses. To encourage saving for health expenses after retirement, HSA owners between age 55 and 65 are allowed to make additional catch-up contributions (\$500 in 2004) to their HSAs. Individuals eligible for Medicare may not open an HSA.

Additional information about HSAs is available from the Public Affairs Office of the U.S. Department of Treasury. The information is also available on the Treasury web site at <http://www.ustreas.gov>.

Analysis:

A. State Incidental Powers Provision

The Washington Credit Union Act grants a Washington state chartered credit union (WaSCUs) certain incidental powers. A WaSCU may:

Exercise such incidental powers as are necessary or convenient to enable it to conduct the business of a credit union.

RCW 31.12.402 (23) (state incidental powers provision).

The Director of Credit Unions (Director) issued an opinion No. 01-8 dated November 8, 2001 citing the criteria to determine whether new activities are authorized as incidental powers for a WaSCU. A new activity to be authorized under incidental powers must meet one of the following:

1. the three-part test derived from the U.S. Supreme Court decision in Nationsbank of North Carolina v. Variable Annuity Life Insurance Co., 513 U.S. 251 (1995) (VALIC) or
2. the test in 12 C.F.R. 721.7.

WaSCUs are authorized to provide other tax-advantaged savings plans for retirement, pension, and education savings accounts for their members. As with an Individual Retirement Account, an individual who maintains a HSA has an option to direct the investment choices. HSAs meet the criteria for a new activity authorized under incidental powers as follows: (1) HSAs help meet the mission of WaSCUs to promote thrift among its members, (2) HSAs are a logical outgrowth of other tax-advantaged savings plans authorized by WaSCUs, and (3) HSAs involve the same kinds of risks already part of the business of credit unions.

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B. Federal Parity Provision

WaSCUs are granted federal credit union (FCU) powers in accordance with RCW 31.12.404. Specific findings by the Director are required to grant WaSCUs any FCU powers and authorities that the FCU's received after July 22, 2001. The required findings are as follows:

...if the director finds that the exercise of the power and authority serves the convenience and advantage of members of credit unions, and maintains the fairness of competition and parity between credit unions and federal or out-of-state credit unions.

RCW 31.12.404(2).

The Director's authority to make such findings and to interpret Chapter 31.12 RCW generally has been delegated to the Director of the Division of Credit Unions. Effective July 29, 2004, the NCUA amended its regulations to allow federal chartered credit unions to provide member HSAs as an incidental power pursuant to 12 C.F.R. 721 and as a tax-advantaged savings plan pursuant to 12 C.F.R. 724 with a new title of Trustees and Custodians of Certain Tax-Advantaged Savings Plans.

In accord with the requirements of RCW 31.12.404, the Director finds that granting WaSCUs the power and authority to serve as trustee or custodian for member HSAs serves the convenience and advantage of members. In addition, the Director finds that authorization of WaSCUs to provide member HSAs maintains the fairness of competition and parity between state-chartered credit unions and federal credit unions.

Of course, in exercising an FCU power, WaSCUs must comply with any restrictions or limitations on the specific exercise of the power under NCUA statutes or rules. RCW 31.12.404(3).

Conclusion:

WaSCUs have two choices of statutory authority for member HSAs.

1. WaSCUs may serve as a trustee or custodian for member HSAs within the category of activities of preapproved incidental powers under RCW 31.12.404 (23). The Director expects WaSCUs will comply with all applicable guidelines for trustees or custodians of HSAs as established by the Internal Revenue Service and, any guidance on HSAs published by the U.S. Department of Treasury.

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Conclusion continued:

2. WaSCUs may choose to invoke federal parity for member HSAs as an incidental power for federal chartered credit unions and by using federal parity, the WaSCU must comply with the restrictions or limitations contained in 12 C.F.R. 721 and 12 C.F.R. 724. The WaSCU should show in the Board minutes when it invoked federal parity for authority to offer member HSAs.

Sincerely,

Linda K. Jekel
Director of Credit Unions