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The small change that can save you thousands of dollars a year in health costs

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By Jonnelle Marte November 11 Follow @jonnelle

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Welcome to open enrollment season. That time of year when you get e-mail after e-mail from your employer reminding you of all the changes you need to make to your benefits.

Of all the decisions that need to be made around now, one that often gets looked over is the chance to open a health savings account.

Most people can probably feel their eyes glaze over at the sound of the term. After all, you've probably got your hands

full trying to make sure that your plan still covers the medication you need and the doctor you like to visit (that's if you aren't just closing your eyes and hoping nothing has changed).

But for some workers, ignoring the tax-deferred accounts is about equal to turning down a check for several thousand dollars. For a family saving the maximum of $6,550, it can translate to more than $2,000 a year in tax savings.

Sure, they're kind of a pain to use. And you can only use them if you have a high deductible health plan. You need to figure out how much money you might spend next year on health care. Keeping track of receipts on small purchases may not seem worth the savings. But the process doesn't have to be all that complicated.

Here's seven things you need to know to make sure you get the biggest, fattest tax deduction off your health spending.

1. Figure out how much to save. Health care being what it is, it's not easy to know how much you'll spend each year. Find yourself in a car accident and you may easily wipe out what you put into the account, leaving you with hundreds or thousands of dollars more in medical bills — that you won't get to pay with pre-tax dollars. Save too much, and you might wish you had that cash around to pay for that iPad you've been eyeing. The good news is that any money that isn't spent in one year can be rolled over to pay for next year's medical bills.

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Some people might simplify the math by putting at least enough money into the accounts to cover the maximum out-of-pocket health expenses they might face for the year, says John Barkett, director of health policy affairs for Towers Watson, a human resources consulting firm. For a family with a $6,000 deductible, for instance, setting aside at least that much into the account can help them be sure they'll have the cash on hand to pay for copayments and other bills until their full coverage kicks in – and they'd save the money throughout the year instead of scrambling to cover big bills when they come up.

2. Know what's covered. It's easy to shrug off the HSA with the assumption that chances are low that you'll face a major accident in the coming year. And if you're preparing for a costly procedure like a surgery, signing up can be a no brainer. But the tax-free accounts can also be used to pay for minor medical expenses, like doctor's visits, eye glasses, bandages, birth control and breast pumps. Over-the-counter drugs can also qualify if people get prescriptions for them. But if you make a mistake, any money used inappropriately would be taxed and may be subject to an additional 20

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percent tax penalty.

3. Understand how to take the money out. Keeping track of these small expenses may seem like a pain. Generally, people need to file a claim to be reimbursed for cash spent on a qualifying expense. (Who wants to file a reimbursement claim for $9 spent on bandages?) But some plans will make it easier to access the cash by providing a debit card that can be used to pay for expenses directly. Still, holding on to receipts may be a good idea on the chance that the IRS audits the account at the end of the year.

4. Calculate the tax benefits. Like with any tax break, people in higher tax brackets will save more than people with lower incomes and lower tax rates, says Carolyn McClanahan founder and director of financial planning at Life Planning Partners. But you don't need to be rich to see the savings add up. People struggling to figure out if the savings will be worth it for them can use calculators to help them crunch the numbers. JPMorgan Chase offers a simple calculator, and Aetna has a more advanced tool, but chances are your insurance company provides its own calculator. Consider a family contributing the maximum $6,550 each year. In the 25 percent tax bracket, they would save more than $1,600 in federal income taxes for the year. In the 35 percent tax bracket, they would save close to $2,300.

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5. Roll over the extra cash — all the way to retirement. If you don't use all of the money in your HSA one year, the savings can be rolled over and used in the following years for qualifying health care costs. "You may be healthy this year, but one day you're going to have some costs," Barkett says. "And when that day comes, you're going to want to pay for those costs with dollars you didn't have to pay taxes on." People who don't use all of the savings can eventually use the cash to pad their retirement savings. After age 65, account holders only have to pay income taxes on distributions just as they would with a traditional IRA.

6. Name a beneficiary. Like a retirement account, HSA funds can be passed on to a spouse or a family member after the original owner passes away. A spouse can inherit the account and continue to use the funds, tax-free, on qualified medical expenses. For other beneficiaries, the account will stop being an HSA and the person will pay taxes on the account.

7. Look into other options. Some people who don't qualify for HSAs may be able to use similar accounts that

come with slightly different rules. For instance, flexible spending arrangements let workers stash pretax money that can be used to cover health expenses, but with FSAs, some people can roll over up to $500 from one year to the next. Medical Spending Accounts can be used by people who are self-employed or who get insurance through a small business.

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