HSAs and Medicare

Medicare and HSA eligibility

Many individuals are confused at the intersection of health savings accounts (HSAs) and Medicare. Two different federal agencies have primary responsibility for these programs — the Department of Health and Human Services, for Medicare, and the Department of the Treasury, for HSAs. Each agency issues rules related to its products without consideration of the interaction with the other product, leaving Americans confused. The following information is designed to help you navigate this confusion so that you remain in compliance with HSA rules.

1. Do I lose my HSA eligibility at age 65?
No. You can open and contribute to an HSA at age 65 or later as long as you meet HSA eligibility requirements, which are:

- You're covered on an HSA-qualified medical plan.
- You're not someone's tax dependent.
- You don't have any conflicting coverage (including enrollment in Medicare).

Turning age 65 does not, in and of itself, preclude you from remaining HSA-eligible absent any disqualifying coverage.

2. Does enrollment in Medicare impact my HSA eligibility?
Yes. Medicare doesn't offer an HSA qualifying option. You can't make contributions to your HSA for any months after you enroll in any part of Medicare, even if you're also covered on an HSA qualifying plan.

3. Aren't I automatically enrolled in Medicare Part A at age 65?
No. You're enrolled in Part A (inpatient services) automatically only if you are age 65 or older and receiving Social Security or Railroad Retirement benefits. You're enrolled in Part A and Part B (outpatient services like doctor visits, lab work and imaging) automatically if you're collecting Social Security disability benefits or are diagnosed with amyotrophic lateral sclerosis (ALS, or Lou Gehrig's disease). Otherwise, you must sign up to receive coverage through Medicare.

For more information on Medicare enrollment, please refer to Medicare & You (available online) or call the Social Security Administration customer service center at 1-800-772-1213.

4. If my spouse and I are enrolled on my employer's HSA-qualified plan and I enroll in Medicare, can he open an HSA?
Yes, if your spouse is otherwise HSA-eligible. Individuals don't have to be the medical plan subscriber to be HSA-eligible. You or your spouse can then make tax-deductible contributions into their HSA, up to the family maximum if you remain covered on a family contract (even if only your spouse is HSA-eligible). For some couples, this provision in the law allows them to continue to contribute to an HSA (and build income tax-free balances for distribution in retirement) for several years after the older spouse enrolls in Medicare.

5. If I'm not HSA-eligible, can I enroll in my employer's HSA-qualified plan?
Yes. HSA eligibility refers to your ability to open and contribute to an HSA, not whether or not you can enroll in a medical plan. As long as you meet your employer's and the medical insurer's eligibility requirements, you can enroll in an HSA qualifying medical plan. If you're not HSA-eligible, though, you can't open and contribute to an HSA. Your employer may offer a health flexible spending account (FSA) or health reimbursement arrangement (HRA) through which you can reimburse eligible expenses income tax-free.

Medicare and HSA contributions

6. Can I continue to contribute to my HSA once I'm enrolled in Medicare?
No. You lose HSA eligibility once you enroll in Medicare, so you can't make additional contributions. You can contribute for months that you were eligible before you enrolled in Medicare. For example, if your 65th birthday is May 6 and you enroll in Medicare immediately, your effective date of Medicare coverage is May 1. You can make contributions for the months of January, February, March and April at any point up to the date that you file your personal income tax returns for that year, even though you may not be HSA-eligible at the time that you make your retroactive contribution for those months.

7. Can I contribute to my spouse's HSA if I'm enrolled in Medicare and no longer HSA-eligible?
Yes, if your spouse is HSA-eligible and has an HSA, you — or anyone else — can contribute to their HSA. Your enrollment in Medicare doesn't disqualify your spouse from contributing to (or accepting contribution from others into) their HSA. You can contribute personal funds, either through post-tax payroll (you can set up a payroll deduction to send money directly to your spouse's HSA) or with personal funds. Your spouse then deducts these contributions on their (or if you're filing jointly, your joint) personal income tax return.

Medicare and HSA distributions

8. I'm no longer HSA-eligible. Can I make income tax-free distributions for qualified medical expenses?
Yes. HSA eligibility relates to your ability to make contributions. Once you open an HSA, you can make income tax-free distributions for qualified medical expenses for the rest of your life, as long as you still have a balance in your account.

9. Which expenses can I reimburse from my HSA once I'm enrolled in Medicare?
You can still reimburse, income tax-free, all qualified medical out-of-pocket expenses not reimbursed by other insurance or other sources, including:

- Medical plan deductibles
- Copay and coinsurance
- Dental and vision expenses
- Insulin and diabetic supplies
- Over-the-counter drugs and medicine with a prescription

In addition, you can reimburse certain insurance premiums, including premiums for:

- Medicare Parts B and D
- Medicare Part C (Medicare Advantage — plans offered by private insurers that replace Medicare coverage)
- Some Medicare supplement plans

10. Whose qualified medical expenses can I reimburse income tax-free from my HSA?
You can reimburse your own, your spouse's and any tax dependents' (such as an adult disabled child's) expenses income tax-free from your HSA. These other family members don't need to be HSA-eligible themselves or covered on your medical plan for you to make income tax-free distributions from your HSA to reimburse their qualified medical expenses tax-free. Note: You can't reimburse your own or anyone else's Medicare premiums income tax-free until you, the account owner, turn age 65. If you have an older spouse and want to reimburse their Medicare premiums income tax-free, they must open an HSA before they enroll in Medicare and contribute at least the $1,000 annual catch-up contribution. They can use this to cover their Medicare premiums until you turn age 65 and can reimburse their premiums income tax-free from your HSA. In addition, when both of you are HSA-eligible and covered on a family HSA-qualifying or compatible medical plan, you can split the family maximum contribution between your two HSAs as you wish.

11. My spouse and I both have an HSA. Do we have to limit distributions from each HSA to our own expenses?

No. You can reimburse each other's expenses from your respective HSAs as long as you remain married. You can't combine accounts, but you may choose to reimburse both your and your spouse's expenses from one HSA to exhaust the balance in that account. Then, you have to manage (and perhaps pay monthly administration/maintenance fees) on only one account without losing the ability to reimburse an expense that either of you incurs (as long as you remain married).

12. Can I make income tax-free distributions from my HSA for non-qualified medical expenses when I turn age 65?
No. Distributions for non-eligible expenses are always included in your taxable income, putting these withdrawals on par with taxes on distributions from a traditional 401(k) or traditional IRA. Once you turn 65 or meet Social Security's definition of disabled, you can make distributions for items that aren't HSA-qualified without incurring the 20 percent additional tax (penalty) otherwise assessed to non-qualified medical expenses.

13. If I pass away first, can my HSA continue to reimburse my spouse's qualified medical expenses income tax-free?
You name a beneficiary when you enroll in your HSA, and you can change the designation at any time. If you name your spouse as beneficiary (the most common situation), upon your death your HSA passes to your spouse with balances and tax advantages intact. Your spouse can then reimburse their own eligible expenses income tax-free. In addition, if your spouse remarries, they can reimburse their new spouse's qualified medical expenses income tax-free. If you name any other person or entity as the beneficiary, the HSA is liquidated and the assets pass to that person or entity, who may incur a tax liability. That beneficiary doesn't enjoy the tax benefits and isn't constrained by the rules of an HSA.

Delaying enrollment in Medicare when first eligible to enroll

14. Do I face a penalty if I defer Medicare enrollment when I'm first eligible (65th birthday for most individuals)?
Possibly. Here are the potential tax consequences if you delay enrolling in Medicare around your 65th birthday when you're entitled to an Initial Enrollment Period:

- Part A (inpatient and home health care): If you (or your spouse) worked 40 employment quarters with income above the Medicare threshold, you receive Part A premium-free. You face no penalties for delaying enrollment past your Initial Enrollment Period.
- Part B (physician and outpatient services): If you don't enroll during the Initial Enrollment Period, you must maintain group coverage from your 65th birthday until you do enroll in Part B. For every 12 months past your 65th birthday that you don't maintain group coverage, you pay a 10 percent surcharge on your monthly Part B premium for the rest of your life. In addition, you may face a gap in coverage when you do want to enroll, since you'll have to wait until the next General Enrollment Period to enroll in benefits effective the following July 1.
- Part D (prescription drug coverage): If you don't enroll during the Initial Enrollment Period, you must maintain group or nongroup coverage that offers prescription drug benefits at least as rich as Part D. If you don't, you're assessed a permanent surcharge of 1 percent of the national base beneficiary premium for every month since your 65th birthday that your coverage isn't what's called Medicare Creditable Coverage (MCC). In addition, you may face a gap in coverage when you want to enroll. You'll have to wait for the next General Enrollment Period to enroll in benefits.

15. Given the penalty, should I just enroll in Parts B and D when I'm first eligible and stop contributing to my HSA?
That's a personal decision that you should discuss with your financial advisor. While your initial reaction might be to avoid penalties at all costs, note that (1) the penalties aren't a punishment for doing something illegal or immoral and (2) you may be better off financially by remaining in your HSA program, building HSA balances to cover future expenses, enjoying tax savings and later facing penalties.

Key considerations:

- What's the difference in current cost among (1) remaining covered on my employer's plan without enrolling in Medicare, (2) enrolling in Medicare only or (3) enrolling in both programs?
- What's the difference in benefits covered and financial responsibility between enrolling in either program or both programs?
- What tax advantages do I give up if I'm no longer HSA-eligible? Remember, you won't be able to reduce your taxable income through HSA contributions if you enroll in Medicare.
- What will be the financial consequences of my penalties? Remember, since the penalties represent additional premiums, they're eligible for income tax-free reimbursement from your HSA.
- Will I ever enroll in Parts B and D and face those penalties, or will I choose coverage (such as a Medicare Advantage plan) that doesn't require enrolling in coverage and paying premiums subject to penalties?

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Please note that this discussion is for informational purposes only and is based on current regulations. It doesn't represent, and shouldn't be construed as a substitute for professional advice. Please consult your personal legal, financial or tax counsel to discuss your personal situation and refer to IRS Publications 969 and 502.

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