HSA and Medicare

HSA and Medicare parts A & B do not go well together if you plan to continue contributing to your HSA account. You can't contribute to an HSA once you enroll in any part of Medicare.

Today, however, many Medicare beneficiaries are still working at large companies. Some are enrolled in group health insurance plans which are HSA-compatible.

This means that the insurance plan has a high deductible and is a qualified plan for which employees can open health savings accounts to save money toward future medical expenses. These contributions have many benefits for the employee, including tax savings benefits.

Both the employee and the employer can contribute funds to the health savings account ***as long as the employee has no other insurance***.

Enrolling in Medicare Part A (or any part of Medicare) makes you ineligible to contribute to an HSA. It's important that employees with health savings accounts look carefully at these rules, which we'll cover below.

Benefits of HSA Plans

As an individual with a high-deductible health plan, you can enjoy considerably lower premiums than a regular health insurance plan. However, that's not the only benefit. When you open the health savings account that goes alongside your health insurance, you now have an opportunity to contribute money into the account tax-free. This means you pay no income taxes or Social Security/Medicare taxes on that money.

You also pay no taxes on the money when you pull it out for qualified medical expenses, which include dental and vision expenses. You can even use funds in your health savings account to pay for qualified medical expenses of your dependents, whether they are on the health insurance policy with you or not.

What's more, is that this money is yours forever. It compounds over time and can grow into a great nest egg of money you can use for medical expenses, including Medicare premiums, during retirement.

With all of these great benefits, it's easy to see why someone working at age 65 wants to continue contributing to their health savings account as long as possible. You must know that you can't keep contributing to that HSA if you enroll in any part of Medicare.

Medicare Part A & Group Health Coordination

Most Medicare beneficiaries still working at age 65 choose to enroll in Medicare Part A. That's because Part A can limit your hospital spending to $1,556 (in 2022) if you ever have a hospital stay.

Let's say your group health insurance has a $5000 deductible. This is a considerable financial exposure, especially for someone retiring in a few years. If this person has a hospital stay of just 1 or 2 days, the likelihood that he would spend that $5K toward his deductible is pretty high.

However, assume you enroll in Part A at age 65 and let Part A coordinate with your group insurance. Then that same hospital stay would cost you only $1,556 (the Part A deductible). Medicare would pay the rest of the charges for the hospital stay itself. Part A would cost nothing if you worked in the United States for at least 10 years. Enrolling in it at age 65 is a no-brainer.

This works beautifully unless that group health insurance plan is HSA compatible and you actively contribute to a health savings account.

The HSA and Medicare Exception

HSA and Medicare do not go together.
Let's first define what an HSA is. HSA stands for Health Savings Account. This is a tax-favored account that eligible individuals can open to save money for medical expenses. To be eligible, that individual must be enrolled in a qualified high-deductible health plan (HDHP) **and must NOT be enrolled in any other insurance, including Medicare.**

As mentioned above, this savings account can be used for certain medical expenses for the policyholder or dependents. The employee and the employer can contribute to this account up to the allowed limits set by the IRS.

Unfortunately, Medicare Part A is a form of health insurance. **The IRS does not allow the employee or the employer to make tax-free contributions into a health savings account for any employee who enrolls in ANY form of Medicare (Part A, B, C, or D).**

If you want to continue contributing to your health savings account after age 65, you should not enroll in any part of Medicare. Then you can continue contributing to the health savings account even past age 65. You will continue to be able to make those contributions tax-free.

You will postpone applying for Medicare (or Social Security income benefits) until you decide to retire. There is no late enrollment penalty for Part A or Part B as long as you maintain your group health insurance and that insurance is primary to your Medicare.

The Potential Consequences of Having HSA and Medicare

What if you didn't realize this and have already signed up for Part A *and* Social Security income benefits? You would need to stop contributing to the health savings account. However, you can use the funds already in your health savings account for qualified medical expenses until you exhaust the account.

Do not attempt to cancel Part A, which is already in force. It can affect your Social Security income benefits. (You cannot cancel Part A after beginning your Social Security benefits. If you do, you'll have to pay back all the money you have already received from Social Security.)

Instead, you can use the funds already in the savings account toward Medicare Part A, B, and D premiums. Funds can also be used for ordinary approved medical expenses, such as doctor visits, lab work, etc.

If you have not yet enrolled in Social Security income benefits, you can withdraw your application for Medicare Part A. Please note that later on, when you decide to apply for Social Security income benefits, it will automatically trigger your enrollment into Part A retroactively for 6 months.

You'll need to speak with your accountant about any penalties you may owe for contributing to your HSA over the prior six months. Plan ahead for when you will enroll in Social Security income benefits. Then discontinue contributions into your HSA 6 months before you apply for income benefits and trigger your Part A enrollment.

Late Enrollment Penalty for Part D

There can be an IRS penalty with Medicare and an HSA. There can also be a late penalty for not enrolling in Part D if your group coverage is not considered creditable.

Many high-deductible health plans do not have drug coverage that is considered creditable for Part D. In other words, the insurance plan will not pay as much as the standard Part D plan. If that is the case, your employer is responsible for sending you an annual Medicare Part D notice before October 15th. They must advise you that your drug coverage is not creditable for Part D.

Common Questions about HSA and Medicare

Can you pay Medicare premiums from health savings accounts?

In a health savings account, you can pay for Medicare premiums, deductibles, copays, and coinsurance from existing funds. If you have long-term care insurance, you can also use HSA funds for those premiums. You cannot, however, pay your Medigap premiums with these funds.

Should I delay Medicare enrollment to continue contributing to my HSA?

This depends on the situation. If your employer is a small employer, then Medicare is primary. You must enroll in Medicare A and B and stop contributing to the HSA. If your employer is a large employer and contributes a fair amount of money each year into your HSA, then delaying Medicare might be wise.

Can my spouse continue contributing to the HSA even if I don't?

Yes, as long as the qualifying insurance covers your spouse, he can continue contributing to the account in his name. The contribution can't be in your name. You can also use funds already in the account to pay for expenses for both of you until the funds are exhausted.

Can you contribute to an HSA if you are on Medicare?

No. Your spouse can, but you cannot. The IRS does not allow this. Medicare and HSA plans do not mix.

What is the penalty for having an HSA and Medicare?

The IRS usually imposes a penalty on you if you are audited. The amount would depend entirely on your specific circumstances. You would pay taxes on the HSA funds that contributed and took deductions for penalties. Your contributions might also be considered excess contributions by the IRS, and then they would be subject to an additional 6% in excise tax when you withdraw those funds.