




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HSAs and Medicare: Diagnose the possible pitfalls

Know the rules when you enroll in Medicare to avoid steep penalties.

Fidelity Viewpoints



Key takeaways

It's important to understand the implications of Medicare enrollment for future health savings account (HSA) contributions. You could be subject to tax penalties if you make HSA contributions after you enroll in Medicare or when your Medicare coverage begins.

When you enroll in any form of Medicare, neither you nor your employer should continue contributing to your HSA.

If you enroll in Medicare after turning 65, your coverage can become effective up to 6 months earlier. You and your employer will need to end your HSA contributions up to 6 months before enrolling in Medicare since Medicare back dates your Part A coverage from the date you enroll.

If you're age 60+, you probably have figured out how to use your health savings account (HSA) to help pay for qualified medical expenses—and even save something extra for unanticipated health care expenses you may soon be facing in retirement.

But watch out: There are a few important rules to follow if you want to avoid being subject to stern financial penalties when you enroll in Medicare in a few short years.

Like many things in health care, it's a bit complicated. So it's vitally important that you know when to stop contributing to your HSA along with when you can and cannot use HSA dollars to pay for medical expenses—before, during, and after you enroll in Medicare at age 65.

To get started, let's recap what HSAs offer.

Paying for medical expenses with an HSA—tax-free

HSAs work with HSA-eligible health plans to allow you to pay for qualified medical expenses. HSAs offer triple tax savings¹:

1. You can contribute pre-tax dollars.
2. Any earnings grow tax-deferred.
3. You can withdraw the money tax-free now or in retirement to pay for qualified medical expenses.

Feedback

You can use your HSA to pay for qualified medical expenses each year and let any leftover funds in the HSA grow for use in the future, including in retirement.² You can use your HSA to pay for qualified medical expenses in retirement, such as vision and dental care, hearing aids, and nursing services. You can also use your HSA to:

1. Help bridge the gap to Medicare

If you retired before age 65, you still need health care coverage before enrolling in Medicare. You may be able to use your HSA to pay for insurance premiums, but the situations in which you can do so are limited. For example, you can use HSA funds for health coverage purchased through an employer-sponsored plan under COBRA, or you can also use your HSA to pay health insurance premiums while receiving unemployment compensation. Other than these situations, you will not be able to pay for health insurance premiums from your HSA before age 65.

Tip: Use our [Health Insurance Before Medicare Planner](#) to see what options may be available to you.

2. Cover Medicare premiums

You can use your HSA to pay certain Medicare expenses, including premiums for Part A, Part B, Part C (Medicare Advantage), and Part D prescription drug coverage, but not premiums for a Medicare supplemental policy such as Medigap. Retirees over age 65 who have employer-sponsored health coverage can use their HSA to pay their share of those costs as well.

3. Pay for other expenses

Once you turn age 65, you can use your HSA to pay for any nonqualified medical expenses like buying a boat or new patio furniture, but you don't get to take full advantage of the tax savings; you're required to pay federal and potentially state taxes for such expenditures. (If you're not age 65 or older, you will pay a 20% penalty and taxes on withdrawals for anything other than qualified medical expenses.)

Avoiding the pitfalls

HSA eligibility rules state you can't contribute or receive contributions from your employer to your HSA when enrolled in any part of Medicare. Otherwise, you could be subject to tax penalties.

If you're currently contributing to your HSA and you plan to start your Medicare coverage the month you turn 65:

- Make sure all HSA contributions end before your 65th birthday month.
- If your birthday is on the first of the month, make sure you stop your contributions by the beginning of the month before your birthday month.

If you continue to work after age 65 and you or your employer is still contributing to an HSA:

- Stop making contributions to your HSA up to 6 months before applying for Medicare Part A only or Part A and Part B or starting your Social Security retirement benefits.
- When you receive Social Security retirement benefits, your Part A coverage is back-dated 6 months (but no earlier than the first month you're eligible for Medicare) to give you 6 months of back-dated benefits. If you contribute to your HSA during those 6 months, you may face a 6% excise tax and an income tax for those contributions.
- This "6-month lookback" starts when you enroll in Medicare or begin your Social Security retirement benefits. However, you can avoid the excise tax if you do the following:
 1. Withdraw your excess contributions by your tax filing deadline, including extensions, for the year you made them, and
 2. Withdraw any earnings attributed to the withdrawn excess contributions and include the earnings in "other income" on your tax return for the year you withdrew them.

This HSA restriction leads some working past age 65 to defer Medicare and maintain their current employer-based health insurance coverage so they can keep contributing to their HSA until they retire.

Learn more about excess contributions on the [IRS website](#).

Tip: Remember, after you enroll in Medicare, you can use existing funds in your HSA for qualified medical expenses, including your monthly premiums for Parts A, B, C, and D (but not premiums for a Medicare supplemental policy such as Medigap).

Summary

HSAs allow for spending for short-term qualified medical expenses and saving for long-term costs in retirement. If Medicare is in your near future, don't get penalized for making contributions after you're enrolled or when your Medicare coverage begins.

Get help

Looking for help to navigate your health care and retirement needs? Working with a financial professional can help you plan the course that's right for you.

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1. With respect to federal taxation only. Contributions, investment earnings, and distributions may or may not be subject to state taxation.

2. For more about qualified medical expenses, the IRS provides detailed information about [medical and dental expenses](#) and [health savings accounts](#).

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