Medicare and its Relation to Health Savings Accounts and Health Care Sharing Arrangements; and Making a QCD from a 401(k) Account-Can it be Done?

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Overview

There are two excellent ways to reduce the cost of health care, particularly for sole proprietorship farming and ranching operations (and for other small businesses and individuals). These are Health Savings Accounts (HSAs) and Health Care Sharing Ministries (HCSMs). But when a person is enrolled in Medicare there can be impacts with HSAs and HCSMs. It's important to understand how the interactions work.

Also, another common estate and financial planning issue is whether a qualified charitable distribution (QCD) can be made from an existing 401(k) or 403(b) plan.

These are the topics of today's post.

HSAs and Medicare

You can deduct contributions to a health savings account; account earnings are tax-free; and distributions to pay for qualified medical expenses are also not taxed. That's a triple tax benefit that you really can't find anywhere else in the Code. Qualified expenses include Medicare premiums, or any other qualified expenses incurred before retirement if you have receipts. But Medicare enrollment complicates things.

Once you enroll in any part of Medicare, you can't contribute to an HSA. But merely being eligible for Medicare doesn't prevent additional contributions. You can contribute to your HSA past age 65 if you delay enrolling in Medicare. If your spouse enrolls in Medicare, you can still contribute to your HSA if you aren't also enrolled.

Even after you enroll in Medicare you can still withdraw funds from your HSA tax-free to pay for qualified medical expenses, and you can use the account funds to pay for various Medicare-related expenses including premiums, deductibles, copays and coinsurance. In addition, once you reach age 65, you can withdraw money from your HSA for any reason without incurring a tax penalty. But those withdrawals are taxable income.

If you start taking Social Security before age 65, Medicare enrollment starts at age 65. When you enroll in Medicare after age 65, you are deemed to enroll six months before your application date or age 65, whichever is later.

HCSMs and Medicare

Health care sharing ministries are organizations where members with common beliefs share medical costs. Members contribute a monthly amount, and those funds help pay for other members' eligible medical expenses. An HCSM can be a great way to reduce the cost of what would otherwise be paid for health insurance. Medicare is a federal health insurance program primarily for people aged 65 or older. Can you be part of a health sharing arrangement and be enrolled in Medicare at the same time?

As noted, Medicare is a government-run health insurance program, while health sharing arrangements are cost-sharing mechanisms among groups, often with shared religious beliefs. HCSMs do not typically coordinate benefits with Medicare in the same way that traditional insurance plans do.

If you have Medicare, it will generally pay for Medicare-covered services first. The HCSM *might* help with some out-of-pocket costs that Medicare doesn't cover, but it really depends on the specific rules of the health sharing arrangement.

HCSMs are not like traditional health insurance. They may have restrictions on what they cover, such as pre-existing conditions. Medicare provides more comprehensive and guaranteed coverage.

So, you can have both, but they operate independently. Medicare will be your primary coverage, and the health sharing arrangement will be secondary. Check with your health care sharing ministry to learn what it covers.

Making a Qualified Charitable Distribution from a 401k – Is it Possible?

This year you can make a contribution of up to $108,000 to a qualified charity direct from an IRA if you're at least 70 and a half. The amount distributed is excluded from your taxable income. But you can't also claim a charitable deduction for the contribution. If you're 73 or older, a contribution can count towards satisfying your Required Minimum Distribution (RMD) for the year. But you can't do the same thing with a 401(k) or 403(b) plan. The technique only works with traditional IRAs, rollover IRAs, inherited IRAs, inactive SEP IRAs, and inactive SIMPLE IRAs.

But there's a way to do it if you want to make a direct contribution to a qualified charity from your 401(k). Roll over the funds into a traditional IRA. Once the funds are in the IRA, and if you are age 70 and a half or older, you can then make a qualified charitable distribution (QCD) directly from the IRA to an eligible charity. From a tax standpoint make sure you roll funds from a traditional 401(k) to a traditional IRA or from a Roth 401(k) to a Roth IRA – those rollovers are tax-free. But only the earnings portion of a Roth IRA counts as a qualified contribution.

Conclusion

Make sure to visit with your financial and/or retirement planner for the best application of these rules to your specific situation.