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# How to Help Clients Claim Medicare

Most clients are guessing about how much Medicare will cover



Missing open enrollment for Medicare Part B means a 10% penalty for each year they wait.

Clients are concerned advisors don't have all the information they need to help them plan for health care in retirement, according to Peter Stahl, president of Bedrock Business Results. Unfortunately, they're not doing much better on their own.

Stahl told attendees at Schwab Impact on Thursday that 85% of women and 70% of men are guessing at how much of their health care costs will be covered by Medicare. Only 2% of women and 5% of men actually asked their advisor about it.

It's important for advisors to guide their clients through their Medicare decisions, Stahl said, because "Medicare is mandatory. It can be delayed or deferred," but you have to claim it. Once clients file for Social Security, even if they file and suspend, they've already pulled the trigger on Medicare.

Part B premiums are paid out of clients' Social Security benefits, Stahl said, but they're based on the client's salary from two years prior to claiming benefits. Stahl encouraged attendees to help their clients apply for reconsideration to have their premiums based on their current income, as retirement, loss of a spouse or divorce can all have a serious impact on income.

Clients generally have two options for Medicare coverage, Stahl said. They can use traditional coverage with Parts A, B and D and a Medigap plan to fill the holes in Parts A and B, or they can opt for a Medicare Advantage plan.

Stahl suggested advisors make a checklist of items to discuss with their clients regarding health care. Obviously, advisors aren't health care consultants, he said, but "clients want to connect." Advisors should help them calculate the potential costs and create a plan for income to pay for those costs.

They should also discuss using tax deferral to reduce the modified adjusted gross income used to determine Part B premiums. The problem for clients who have been faithfully saving in their 401(k) plans is that they have "80% to 90% of their income tied up in qualified plans." Stahl suggesting looking at tax deferred products to shelter clients' income.

While they're protecting their income they also need to keep growing it, he said. "Make sure they don't get too conservative" once they stop working, Stahl said. "They need to grow assets all the way through retirement."

Health savings accounts are another good way for clients to pay for health care costs in retirement, Stahl said. The money saved in health savings accounts grows tax free and rolls over from year to year, so Stahl suggested clients don't use it while they are working. Instead, "let it grow until retirement"; then they can "pay Medicare premiums with tax-free dollars."

Timing of enrollment matters, too. If clients want to defer Medicare, they have to defer Social Security. They have to be working at a firm with at least 20 employees, and prove that they have “creditable” coverage to replace Medicare.

Pay close attention to special enrollment periods, Stahl stressed. For example, if clients miss open enrollment for Part B when they retire, they incur a 10% penalty for every year they didn’t sign up that they must pay every year. COBRA, he pointed out, is not creditable coverage to replace Medicare, so clients who plan on paying for COBRA coverage for 18 months after they stop working could end up with a 20% Part B penalty.

Finally, Stahl pointed out 401(h) plans as a “wonderful niche” for small business owners. These plans are offered in addition to cash balance or defined benefit plans and can be used for medical expenses incurred by retirees and their spouses and dependents.

August 18, 2014

## Under The Hood: Medicare Parts A, B, C and D— What You Need to Know, Pt. 1



A primer on the four different parts of the Medicare system.

Medicare was created through *Title XVIII of the Social Security Act* in 1965 and became effective in 1966. This program, administered by the federal government, was originally created to provide medical coverage for qualifying individuals 65 and older and the disabled. However, I suspect that no one at that time predicted the medical advancements which were to come and the longer life expectancies which ensued.

In this article, we'll discuss the various parts of Medicare, some of its history, and the provisions of Medicare Parts A, B, C and D.

### **The History (and Side Effects) of Medicare**

In the beginning, Medicare was a bit more than a social health insurance program. It also played a role in the racial desegregation of America because payment to medical providers was conditional. In short, if the medical provider refused to accept minorities, the government refused to pay the provider.

Over the past 48 years, Medicare has added several illnesses to its coverage including hospice care in 1982 (made permanent in 1984); speech, physical and chiropractic therapy in 1992; and ALS (i.e.; Lou Gehrig's disease) in 2001, to name but a few. However, as mentioned, with the longer life expectancies experienced by the population since its inception, Medicare and Medicaid (i.e.; state insurance for the poor) have become the largest item (combined) in the federal budget today, with an estimated cost of over \$900 billion per year and rising. Medicare alone cost about \$492 billion in 2013.

In 1967 when the House Ways and Means Committee published its projected cost of Medicare in 1990, it figured it would be \$12 billion. The actual cost that year? A staggering \$98 billion.

## How to Qualify

Medicare covers those aged 65 and older, along with younger persons with disabilities and end-stage renal failure. To qualify at age 65, a person must have been a U.S. resident for at least five years and they or their spouse must have paid Medicare taxes for at least 10 years.

## Medicare Part A

Medicare Part A covers in-patient hospital expenses (with limits); skilled nursing care and nursing home care (under certain circumstances and with limits), and hospice care. As for the limitations to coverage, there is a limit of 90 days per stay in a hospital, plus a coinsurance. During the first 60 days there is no coinsurance. However, from day 61 to 90, the individual is responsible for a co-pay of \$304 per day. From the 91st day on, the coinsurance is \$608 per each "lifetime reserve day" up to a maximum of 60 days total over the individual's lifetime.

To clarify, a lifetime reserve day is any day over the first 90 days of an individual's lifetime. For example, if a Medicare patient were in the hospital for 100 days during one hospital stay, the last 10 days would be considered "lifetime reserve days" leaving the person with 50 of these days to use over their lifetime. The point here is that Medicare Part A has some potentially expensive gaps which is why a person should purchase a Medicare supplement plan (or see *Medicare Part C* below).

## Medicare Part B

Medicare Part B is optional and covers outpatient expenses such as lab tests, outpatient surgeries, doctor visits and limited outpatient prescription drugs (typically not drugs you would administer yourself). Coverage begins after meeting an annual deductible of \$147 (2014). After meeting the deductible, the individual must also pay a coinsurance of 20% of the Medicare-approved charges for services and drugs.

## Medicare Part C

Medicare Part C is not actually a separate coverage, but is the part of Medicare which allows private health insurers to create Medicare replacement policies. In short, an individual may elect to purchase one of these plans in lieu of Medicare and a supplement.

In the past, an individual with Medicare would often buy a Medicare supplement to cover procedures or illnesses which Medicare did not cover. However, when Congress passed the *Balanced Budget Act of 1997* it included a provision to allow what was originally called *Medicare +Choice* or *Part C* plans.

When Congress passed the *Medicare Prescription Drug, Improvement, and Modernization Act of 2003*, the name of these plans was changed to Medicare Advantage plans. Therefore, Medicare Part C created the Medicare Advantage plan which is an option that can be purchased in lieu of traditional Medicare. Normally, these plans are fairly comprehensive in coverage.

## Medicare Part D

This is the newest part of the Medicare program and covers prescription drugs. Moreover, it is also available to anyone with Medicare. There are two ways to obtain Medicare Part D coverage. They are:

- 1) Join a plan run by an insurance company or other private company approved by Medicare; or
- 2) Purchase a Medicare Advantage plan which covers prescription drugs (see Medicare Part C above).

Medicare Part D covers prescription drugs up to a maximum of \$2,970 per year.

To find a Medicare Part D program, you can view [the Medicare choices online](#) or call 800-633-4227.

## **Conclusion**

Medicare has become an integral part of the American fabric. Millions of individuals rely on it to pay for what has become a significant expense in their budget. As health care costs continue to rise, and life expectancies lengthen, it's clear that some action will need to be taken to preserve this important program.

I don't think many of the original legislators from 1965 could have imagined how costly Medicare would become and I doubt many of us today can fully appreciate the coming mushroom this program will create as the baby boomers cycle through the retirement turnstile. One thing seems certain, no politician or political party wants to be known as the party that killed Medicare.

AUGUST 22, 2014

# **Under the Hood: Medicare Premiums— What You Need to Know, Pt. 2**

Understanding the premiums for Medicare parts A, B and D, and some changes from the Affordable Care Act

This week we'll focus on Medicare premiums, which I believe are quickly becoming an integral part of the financial planning process; each advisor should have at least a cursory understanding of the cost of the program.

## **Medicare Part A Premiums**

As mentioned, this part of Medicare covers inpatient hospital, skilled nursing care, and nursing home and hospice care, within limits. Moreover, it is free to those who qualify for Medicare (i.e.; paid into Medicare for at least 10 years). This includes a spouse of those who have paid into Medicare, even if the spouse hasn't paid into the system.

If an individual is not eligible for free Part A, they may still purchase it by paying a premium up to \$426 per month. Moreover, if you don't qualify for free Part A, and you don't buy it when you first become eligible, you may be subject to a penalty equal to a 10% increase in the monthly premium.

For example, if you were eligible for Part A two years ago and you enroll today, you would pay the higher premium for two times the period for which you were eligible but not enrolled. Hence, the higher premium would last four years. There are, however, some exceptions which are beyond the scope of this article.

One final note on Part A. If you choose to buy Part A you must also purchase Medicare Part B.

## **Part B Premium**

This is the portion of Medicare which covers outpatient services and is optional. It should be noted that your premium for Part B will be based, in some cases, on your income from as many as two years. For example, if

you became eligible for Medicare in March 2014 and enroll in Part B, assuming you hadn't filed your 2013 tax return by then, Medicare would use your income tax return from 2012 to determine your premium. Hence, if your retirement income is much lower than your income while working, your Part B premium may cost you more than you anticipated.

The premium is based on income and, just like Medicare Part A, if you fail to enroll in Part B when first eligible and do not have a valid exception (again beyond the scope of this article), you may be subject to a penalty which is much more onerous than the penalty from Part A.

In short, the penalty is a 10% premium increase for each full 12-month period you are late in enrolling. Hence, if you were 38 months late (three full years plus two months), your premium will be 30% higher for as long as you have Part B.

The following table displays the cost of Medicare Part B and Part D which we'll discuss in the next section.

| <b>Medicare Part B &amp; Medicare Part D Premiums</b> |                            |                        |                          |
|---|----------------------------|------------------------|--------------------------|
| Monthly Plan Premium (PP) (Part B)                    | Annual Income <sup>1</sup> |                        | Monthly Premium (Part D) |
|   | Single                     | Married                |                          |
| \$104.90  | < \$85,000                 | < \$170,000            | Your plan premium (PP)   |
| \$146.90  | \$85,001 to \$107,000      | \$170,000 to \$214,000 | PP + \$12.10             |
| \$209.80  | \$107,001 to \$160,000     | \$214,000 to \$320,000 | PP + \$31.10             |
| \$272.70  | \$160,001 to \$214,000     | \$320,001 to \$428,000 | PP + \$50.20             |
| \$335.70  | \$214,001 +                | \$428,001 +            | PP + \$69.30             |

<sup>1</sup> Based on MAGI (AGI plus tax exempt interest income)

## Part D Premium

This part of Medicare covers prescription drugs and is available to anyone eligible for Medicare. In my last post on Medicare I included a link to the Medicare Plan Finder. This tool will allow you to select the Part D plan which suits your needs. As mentioned, one way to purchase this coverage is through a Medicare Advantage plan under Medicare Part C. Refer to the table above for the monthly premium. According the Medicare, most people won't have to pay a higher premium for Medicare Part D.

## Medicare Changes From the Affordable Care Act

With the implementation of the Affordable Care Act, aka Obamacare, several preventative medical procedures are now covered under Medicare with no deductible or coinsurance. These include items such as mammograms, colonoscopies, cancer screenings and yearly "Wellness" visits. In addition, there are lower prices on many covered brand-name drugs.

Another change affected by the Affordable Care Act has to do with the so-called prescription drug "donut-hole." Since Medicare Part D covers up to \$2,970 per year for prescription drugs, an individual will pay a co-pay of 47.5% for brand name drugs and 79% on generics when their total prescription drug bill exceeds the annual maximum. This gap will be closed by the year 2020. After that, individuals will pay a flat 25% for all prescriptions, brand name or generic.

If you have a Medicare Advantage plan, you may experience some differences between it and original Medicare (some better, some worse). Under the ACA, Medicare will be paying less to some Medicare Advantage plans.

As a result, some plans may cut benefits such as dental care or increase coinsurance requirements. You should check with your particular Medicare Advantage plan for details.

Finally, prior to the new law, when a patient had a surgical procedure, each medical practitioner involved would send a bill for their services. This is known as a fee-for-service model. Under the new law, the payment will be bundled. The expectation is that a bundled system will help reduce waste and unnecessary charges as each "episode of coverage" will be reimbursed according to a pre-determined schedule. Will this work as planned? We shall see.

## **Future Viability of the Program**

Medicare is one of the largest items in the federal budget with projected costs expected to reach \$858 billion by 2024. That equates to about 30% of today's federal revenue. Therefore, unless we grow our economy (which would increase tax revenue), we may be looking at a hefty tax hike down the road.

That is, unless Washington takes some sort of action such as raising the Medicare withholding tax percentage or the age of eligibility.

In general, this entitlement is only one of many which cause economists to worry that we are on a fiscally unsustainable path. According to one Federal Reserve President with whom I spoke recently, the current fiscal deficit is improving. However, it will begin expanding around 2020 when entitlements will cause stress to the budget.

For more information, you can download the official 2014 Medicare handbook [Medicare & You](#)." This 152-page book has everything you need to know about the program.

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# **Helping Retirees Dodge the Medicare Income-Based Surcharge**

The complex rules governing Medicare income-based premium surcharges can increase higher-income clients' health insurance costs by more than 200% percent during retirement. There are ways to alter a client's investment mix to generate income that is excluded from Medicare's income calculation, but the time to plan is now. Even middle-class clients may now be in for a big surprise when they see their monthly Medicare costs.

Medicare's income-based surcharges are not currently indexed for inflation, and, because they can often take income earned in the years prior to retirement into account, a growing number of clients will find themselves facing higher-than-expected premium costs in retirement.

Fortunately, there are ways to alter a client's investment mix to generate income that is excluded from Medicare's income calculation, but because Medicare looks to income earned prior to retirement in determining whether the surcharge applies, the time to plan is now.

## **Medicare Income-Based Surcharges**

Medicare income-based surcharges essentially increase the cost of premiums for Medicare Parts B and D for those clients who have modified adjusted gross income (MAGI) that exceeds \$85,000 for individuals or \$170,000 for married clients filing jointly. The surcharge is imposed based on a sliding scale, with the highest surcharge imposed upon single clients with MAGI exceeding \$214,400 and couples whose MAGI exceeds \$428,000.

While these income levels may seem relatively high for most retirees, they have not been adjusted for inflation since 2007 and have begun to impact a growing number of Medicare applicants, especially those who have not yet retired when they qualify for Medicare at age sixty-five.

Importantly, Medicare uses a two-year look-back period that is often overlooked by both clients and advisors.

The two-year look-back period means that the client's MAGI from two years prior is used in determining whether the client is subject to the income-based surcharges in the current year. Because MAGI includes most types of traditional income—including wages, Social Security, IRA and 401(k) distributions, dividends, earned interest, and capital gains—the risk that a client will be liable for Medicare surcharges, at least in the early years of retirement, is very high.

Medicare Part B premiums and income-based surcharges are deducted from clients' Social Security checks, meaning that without proper planning, the income that even your middle class clients have been counting on for retirement may be diminished.

### **Planning Tools for Avoiding the Surcharge**

The MAGI calculation used by Medicare to determine whether income-based surcharges will apply includes a wide range of income. For example, selling a house or receiving a bonus prior to Medicare qualification can push a client over the threshold. There are, however, types of tax-preferred products and vehicles that can help clients reduce their overall MAGI and potentially avoid the Medicare surcharges.

Income received on a tax-free basis in retirement is not included in calculating a client's MAGI. This means that income drawn from after-tax retirement savings vehicles, such as Roth IRAs or Roth 401(k)s, is excluded from a client's MAGI. Similarly, income drawn from a health savings account, which also allows tax-free savings to accumulate over the years, is excluded.

Further, income from tax-preferred financial products—such as annuity payments received from a nonqualified annuity or loans taken from a whole life insurance product—will not increase a client's MAGI for Medicare means-testing purposes.

### **Conclusion**

Medicare income-based surcharges can substantially increase the cost of clients' health coverage at a time when their earning capacity is diminished. Advanced planning using after-tax savings vehicles and financial products can help your clients avoid an unpleasant surprise upon Medicare qualification.