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Social Security and Medicare – The Basics

As Americans begin to think about retirement, it is important to have an understanding of our nation's benefits. Social Security should be considered an inflation-protected annuity that supplements primary retirement benefits. Medicare's purpose is to provide health insurance for all Americans age 65 and older regardless of their net worth. Both systems are subject to complicated eligibility and operational rules. This paper seeks to provide an overview of the benefits of both systems.

SOCIAL SECURITY

Eligibility for Social Security Benefits

To be eligible for Social Security benefits, an American worker must pay into the system for 40 quarters or 10 years. The work need not occur in consecutive years and benefits are based on how much was earned during those working years. Aside from earnings, the key determinant of the amount of benefit received is the age at which benefits begin.

Social Security should be considered an inflation-protected annuity that supplements primary retirement benefits. Medicare's purpose is to provide health insurance for all Americans age 65 and older regardless of their net worth.

Full retirement benefits are payable based upon a person's full retirement age. Full retirement age has slowly been increasing such that for individuals born in 1960 or later, it will be upon reaching age 67. Benefits may be received as early as age 62 or as late as age 70. There will be a reduction in benefits if they are received before full retirement age and, conversely, benefits will be increased if initiated beyond full retirement age.

Spousal Benefits

Spouses are also eligible for benefits based upon a working spouse's work history in addition to any benefits they personally accrue. Spousal benefits may not exceed $\frac{1}{2}$ of the working spouse's total benefit. Spousal benefits are only available once the working spouse has filed for his or her own benefits. The recipient spouse must be age 62 or older unless they are caring for a child who is younger than age 16 or is disabled. Spousal benefits are reduced until the spouse reaches his or her full retirement age. A spouse will only be allowed to collect a benefit on a worker's record if the worker is actually receiving benefits.

Working and Social Security

An increasing number of Americans are working into their retirement years. This does not impact Social Security benefits unless benefits are received prior to full retirement age. For example, if someone begins receiving benefits at age 62 and continues to work while receiving benefits, there is a maximum that can be earned or benefits will be reduced. If benefits were reduced due to earnings in the years prior to full retirement age, benefits will be increased at full retirement age to reflect the benefits withheld due to the earnings limit.

Taxation of Social Security

Social Security benefits are nontaxable in very limited situations. Taxability is determined based upon combined income. Combined income is defined as the sum of:

- Adjusted gross income
- Tax-exempt interest
- One-half of Social Security benefits

The table below illustrates the taxable portion of Social security for taxpayers based on their combined income:

TYPE OF TAXPAYER	TAXABLE PORTION OF SOCIAL SECURITY	
	COMBINED INCOME :: 50%	COMBINED INCOME :: 85%
Single or Head-of-Household	Over \$25,000	Over \$34,000
Married Filing Jointly	Over \$32,000	Over \$44,000

For married taxpayers who file separately, 85% of Social Security benefits are taxable regardless of income level.

Timing of Benefits

As stated earlier, full retirement benefits are payable upon reaching full retirement age. The earliest age at which benefits may begin is 62. For a person whose full retirement age is 67, if benefits are initiated at age 62, there will be a 31% reduction from the full retirement benefit amount. Conversely, if benefits are not initiated until age 70, there will be a 25% premium over the full retirement benefit.

Future social security benefits are adjusted for cost of living adjustments (COLA) as measured by the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W).

MEDICARE

Eligibility

Some individuals are eligible and begin receiving Medicare automatically:

- Already receiving Social Security or Railroad Retirement – Medicare Part A and Part B coverage begins automatically on the first day of the month of 65th birthday (if birthday is on the first of the month, coverage begins on the first day of the prior month)
- Under age 65 and disabled – Medicare Part A and Part B coverage begins automatically after receiving Social Security disability benefits for 24 months (Medicare begins on the first day of the 25th month)

- Individuals with ALS (Lou Gehrig's disease) – Medicare Part A and Part B begins automatically when Social Security disability benefits begin

All other individuals must proactively enroll with Medicare to begin receiving benefits. The timing of enrollment depends upon whether an individual is covered by a group health plan upon reaching age 65.

Timing of Enrollment

The enrollment process may begin 3 months before turning 65 and ends 3 months after turning age 65. Enrollment in Part A may be done at any time during or after this initial enrollment period. Enrollment in Part B must be done during this initial enrollment period to avoid the payment of an annual late enrollment penalty of 10% for each full 12 month period of missed Part B coverage.

Exception: For individuals who are still working upon reaching age 65 and who are covered under a group health plan with their employer and the employer has 20 or more employees, a special enrollment period applies. These individuals may apply for Part A or Part B at any time while covered by the employer health plan or at any time during the 8 month period after the first to end of employment or group coverage. The late enrollment penalty does not apply during this special enrollment period.

If the special enrollment period does not apply and enrollment was not completed during the initial enrollment period, general enrollment occurs each year between January 1 and March 31 with coverage beginning on July 1 subject to the higher premium for late enrollment.

Group Health Coverage Enrollment Issues

Individuals who reach age 65 while still maintaining group coverage due to employment are eligible for the special enrollment period discussed above if their employer has 20 or more employees. They also must decide whether to enroll in Part A immediately or wait until they enroll in Part B. Once they enroll in Part A, they are no longer eligible to contribute to a Health Savings Account but may continue to receive distributions for qualified medical expenses. For individuals whose group health insurance is primary, Medicare will pay uncovered costs of the primary insurance subject to Medicare limits.

Cost of Coverage

There is no charge for Part A premiums for anyone who has worked at least 40 quarters and paid Medicare employment taxes during their lifetime. Part B premiums are revised annually. The standard monthly premium for 2023 is \$164.90. However, higher income taxpayers must pay a higher premium which depends upon their level of income.

Part B premiums will automatically be deducted from Social Security benefit payments. If not in payment status, the premiums will be billed. In addition to Part B premiums, there are deductibles and coinsurance amounts for Parts A and B services. The 2023 amounts are shown below:

SERVICE	2023 AMOUNT
Part A Inpatient Hospital Deductible	\$1,600.00
Part A Daily Coinsurance for Days 61-90 of Inpatient Hospital Stay	\$400.00
Part A Daily Coinsurance for Lifetime Reserve Days (up to 60 days over lifetime)	\$800.00
Part A Skilled Nursing Facility Coinsurance for Days 21-100	\$200.00
Part B Deductible (Coinsurance is generally 20% of covered services)	\$226.00

Medicare pays 100% of the first 20 days in a skilled nursing facility after a 3 day medically necessary hospital stay. Medicare does not cover any costs related to long term care. Medicare does not generally cover any medical expenses outside of the United States. Medicare does cover an annual “Wellness” visit.

Medicare Advantage Plans – Part C

For most individuals, Parts A and B do not provide sufficient coverage to offer peace of mind that their medical expenses will be manageable. There are numerous insurance options for obtaining supplemental coverage for services not covered by original Medicare.

One of the options is a Medicare Advantage Plan, also known as Part C. These plans are offered by private insurance companies that are Medicare-approved and that must follow rules set by Medicare. If an individual enrolls in a Medicare Advantage Plan, all of their Medicare coverage will be provided through the Medicare Advantage Plan so that one insurance card will be used for all of the medical services.

While Medicare Advantage Plans are approved by Medicare and must follow Medicare's rules, they can charge different out-of-pocket costs and have different rules about whether referrals are required for specialist visits and which medical providers are covered as part of the plan. The plan can change the network providers at any time during the year.

Medicare Advantage Plans have a yearly limit on out-of-pocket costs for medical services. Once the limit is reached, the plan will pay all remaining expenses incurred during the year.

Medicare Advantage Plans may also offer extra coverage such as vision, hearing and dental. Most also include Medicare Prescription Drug coverage known as Part D.

Medicare Supplements (Medigap)

An alternative to Medicare Advantage Plans are Medicare Supplements, also known as Medigap Plans. These policies are sold by private insurance companies and cover items not covered by Original Medicare including medical care during foreign travel. Medigap Plans do not cover long-term care, vision, dental, hearing aids, eyeglasses or private-duty nursing. Medigap Plans can no longer be sold with prescription drug coverage so individuals must obtain a separate Medicare Prescription Drug Plan.

Medigap Plans are for single individuals only so a married couple must have a separate plan for each spouse. It is vital that each spouse consider coverage specific to their individual needs.

Every Medigap Plan must adhere to federal and state regulations and must be labeled as Medicare Supplement Insurance. All Medigap Plans are standardized and identified by letters. All policies identified by a particular letter provide the same benefits. Costs vary by plan and state.

Prescription Drug Coverage – Part D

Prescription Drug coverage can be obtained through either a Medicare Advantage Plan or a separate Medicare Prescription Drug Plan. An individual is not permitted to have a separate Medicare Prescription Drug Plan if their Medicare Advantage Plan includes prescription drug coverage. Like Part B of Original Medicare, an individual must enroll within certain periods or be subject to a late enrollment penalty for as long as their coverage continues. The initial enrollment period is the same as Part B. Open enrollment for changing plans is between October 15 and December 7 of each year with coverage beginning on January 1 of the following year.

Premiums for prescription drug coverage vary by plan. Premiums may be deducted from Social Security benefits by notifying the drug plan. Part D premium amounts are dependent upon income levels as Part B premiums are. This extra premium amount is payable to Medicare and not the drug plan. If receiving Social Security benefits, the amount will be automatically deducted.

Each Part D plan may also have an annual deductible as well as copayments and coinsurance amounts which vary by plan. Each plan has its own list of covered drugs as well as a tier system for these drugs. Each drug is assigned to a tier which determines the cost of the drug. Drugs in higher tiers cost more so it is important for individuals to know how their drugs are classified by the plans they are considering.

Medicare Advantage v. Medigap + Medicare Prescription Drug Plan

There is no easy answer as to which type of policy is best. Each individual must examine their current health and financial situation to determine what option works best for them. It is also possible that spouses will choose different policies. The chart below highlights some of the differences between the two options:

	MEDICARE ADVANTAGE (WITH PRESCRIPTION DRUG COVERAGE)	MEDICARE SUPPLEMENT (MEDIGAP) + MEDICARE PRESCRIPTION DRUG PLAN
Copayments/ Coinsurance/Deductibles	Varies by plan	Varies by plan
Health Care Provider	Varies by plan; typically pay less if using an in-network provider	Coverage for any Medicare provider
Financial Considerations	Less expensive than Medigap Plans	Good option if frequent medical care needed or prefer certain providers
Medical Underwriting	Not required	May be required
Foreign Travel	Minimal or no coverage	Coverage varies by plan

SUMMARY

As you can see, the rules surrounding these benefits are complex. Please contact us if you have questions or would like assistance with assessing the various options available to you and your spouse. This paper is intended to be educational in nature and does not replace the need for analysis of individual circumstances.

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