Health Insurance, Taxes & Financial Planning

ACA'S ADVANCE PREMIUM TAX CREDIT AND MEDICARE IRMAA

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The challenges of planning for health insurance costs in retirement do not receive the attention that they deserve. Even one dollar of extra income can boost annual Medicare premiums by hundreds or thousands of dollars for millions of Americans. While such increases constitute a hardship for many senior citizens, relief is available for those who qualify. This short article will describe how the Affordable Care Act's Advance Premium Tax Credit ("APTC") and Medicare's income-related monthly adjusted amount ("IRMAA") can be used as part of an integrated financial plan to help defray such costs as much as $20,000 annually.

BACKGROUND

When the Supreme Court (SCOTUS) ratified the constitutionality of the ACA, it ruled that healthcare costs are a tax because the costs incurred by an uninsured person are ultimately borne by the insured. Therefore, the ruling codifies the link between taxable income and health insurance premiums. That link remains in place today, and its effects have been compounded by the Inflation Reduction Act.

MEDICARE IRMAA

Since 2007, high-income Medicare enrollees have been required to pay the IRMAA surcharge for Part B coverage. An IRMAA surcharge for Part D premiums took effect in 2011.

Medicare beneficiaries who earn over $97,000 a year – and who are enrolled in Medicare Part B and/or Medicare Part D – pay the income-related monthly adjusted amount (IRMAA) – a surcharge added to the Part B and Part D premiums. The threshold for IRMAA surcharges adjusts annually, due to inflation (CPI-W).

IRMAA is determined annually by the income from your income tax return, filed two years prior. This means that for your 2023 Medicare premiums, your 2021 income tax return was used. This amount is recalculated annually. The IRMAA surcharge is added to your 2023 premiums if your 2021 income was over $97,000 (or $194,000 if you are married). You will receive notice from the Social Security Administration informing you if you are being assessed IRMAA. You can appeal this assessment, using Form SSA-44. Further, you can also apply for a refund of past, inaccurate IRMAA assessments.

At the end of this article, a reprint of Table 1 from the Congressional Research Service shows that Modified Adjusted Gross Income (MAGI) for both Medicare and the ACA is slightly different from MAGI used for income tax purposes. Further, you will notice that the IRMAA table displays discrete cutoffs among MAGI brackets.

INDIVIDUAL MODIFIED ADJUSTED GROSS INCOME	JOINT MODIFIED ADJUSTED GROSS INCOME	PART B PREMIUM	PART D PREMIUM
$97,000 or less	$194,000 or less	$164.90	$12.20 + Plan Premium
$97,001 - $123,000	$194,001 - $246,000	$230.80	$31.50 + Plan Premium
$123,001 - $153,000	$246,001 -$306,000	$329.70	$50.70 + Plan Premium
$153,001 - $183,000	$306,001 - $366,000	$428.60	$50.70 + Plan Premium
$183,001 - $499,999	$366,001 - $749,000	$527.50,	$70.00 + Plan Premium
$500,000+, $750,000+	$750,000+	$560.50	$76.40 + Plan Premium

The implication is that caution should be exercised when MAGI approaches a cutoff point, in order to avoid an IRMAA assessment.

AFFORDABLE CARE ACT ADVANCE PREMIUM TAX CREDIT

The American Rescue Plan Act widened the availability of Medicaid expansion under the Affordable Care Act. Further, the expansion was set to expire at the end of 2023, but the Inflation Reduction Act has formally lengthened the effective termination date to the end of 2025. "Medicaid expansion" is a confusing term, since Medicaid is a state and federal health insurance program, administered by each state individually. Under the ACA, Medicaid expansion is extended to households that earn up to 400% of the Federal Poverty Level, for those states that have adopted Medicaid expansion.

It is important to note that the APTC is entirely different from Medicaid, the state-federal financial assistance program, which depends not only on income but also on financial resources. It is yet another example of a 'naming problem,' in which erroneous impressions are left with the potential users of financial instruments.

HOW IT WORKS

The APTC is a tax credit, which can be taken in advance to lower your monthly health insurance payment. You can also elect to defer this credit, in part or in whole, through the end of a calendar year. You must purchase your health insurance through healthcare.gov or the state-sponsored health insurance portal, in those states where this is available. There are additional stipulations that restrict the ability to claim the tax credit (Medicare-eligible, offered health insurance through an employer, Medicaid-eligible are the most prevalent examples, in which a person cannot receive the APTC).

The APTC depends on an estimate that you provide to the IRS. At the end of the year, IRS Forms 1095-A and 8962 are used to reconcile the APTC with the applicant's actual MAGI; under and over-assessments of the APTC will either increase or reduce the income tax due for that calendar year. Notably, dividends and year-end distributions are overlooked when mutual funds are held within non-qualified funds and can result in erroneous estimations of MAGI. The excess tax credits would then need to be repaid when an income tax return is filed.

In addition to the reduction in monthly premiums, it is possible that the deductible, copays, and out-of-pocket maximum limit are reduced, depending on the plan selected. These are called cost-sharing reductions (CSRs) that can reduce the financial downside to a household if extensive and/or expensive healthcare costs are incurred.

There are important caveats to this table. First, the selection of which health insurance plan is an entirely different, complicated topic, beyond the scope of this note. Second, the table does not address the lower de-

Real-Life Example of the APTC: Married couple, ages 61 and 62, in Tampa FL (Hillsborough County).

JOINT MODIFIED ADJUSTED GROSS INCOME	APTC	UNADJUSTED PREMIUM*	ADVANCE PREMIUM TAX CREDIT (APTC)	ADJUSTED HEALTH INSURANCE PREMIUM
$50,000	$1809/month	$2228/month	$1809/month	$419/month
$100,000	$1305/month	$2228/month	$1305/month	$923/month
$200,000	$597/month	$2228/month	$597/month	$1631/month
$300,000	$243/month	$2228/month	$0	$2228/month

* *This example takes the median premium amount of a Silver plan on healthcare.gov. Premiums vary by county, and is adjusted annually, and are subject to Medical Loss Ratio (MLR) rules as governed by the ACA. The range for Silver plans is $2,012-4,120 / month in Hillsborough County, FL.*

ductibles and out-of-pocket maximum limits(CSRs), in case high healthcare costs are incurred. Third, if the APTC expires at the end of 2025, as is currently legislated, then a return to the expanded Federal Poverty Level determinations will be used to calculate the APTC. We will leave predictions of future political negotiations and legislative outcomes to others, with the sole observation being that the Affordable Care Act and most key provisions of the ACA have survived notable challenges over the past decade.

IMPLICATIONS OF THE APTC & FINANCIAL PLANNING

Due to the high cost of health insurance, the financial value of understanding the APTC, and the financial planning implications should be self-evident. For those who have planned and created tax-favorable cash flows to support living expenses, the difference can be over $20,000 annually until reaching Medicare eligibility. This represents a largely unreported benefit to a wide range of financial strategies, including, but not limited to taking Roth IRA distributions, and annuitization from Non-Qualified funds due to the exclusion ratio.

Since money is fungible, misunderstanding the APTC and IRMAA can also be considered an opportunity cost or tax. For example, withdrawals from qualified accounts are taxed as earned income, which could either reduce the APTC or result in an assessment of IRMAA. The result is that these issues are now linked, in the same way that capital gains are considered when adjusting an investment portfolio.

For those who have created financial planning structures to optimize cash flows for expenses and taxes, this can entirely alter the retirement decision timeline. When assisting households in financial planning, helping them address the uncertainty over health insurance costs is usually at the top priority. For certain households, the APTC can be used to address this priority.

CONCLUSION

"Can I afford to retire?" is a question that usually centers around income sources and expected returns of portfolios. In addition to these inputs, a key source of uncertainty is health insurance costs. When combined with annuities and/or other tax-favorable approaches, the APTC can be used as part of a bridge to Medicare. Once Medicare-eligible, it can be combined with an awareness of how Medicare's IRMAA works, with the goal of reducing health insurance costs under retirement. As this short note states, the financial impact is noteworthy, and for some, the results can help make the goal of a stable retirement a reality.

Table 1. Additions and Subtractions to Federal Adjusted Gross Income (AGI) to Calculate Modified Adjusted Gross Income (MAGI) for Health Programs

	Modified Adjusted Gross Income				
		ACA Individual Mandate			
Description of Income	Medicare Premiums	Exemption[b]	Penalty[c]	ACA Premium Credit	Initial Medicaid Eligibility[a]
Tax-exempt interest income received or accrued (e.g., interest from state and local bonds)[d]	Added to AGI	Added to AGI	Added to AGI	Added to AGI	Added to AGI
Interest from U.S. savings bonds used to pay higher education tuition and fees[e]	Added to AGI	Added to AGI	Added to AGI	Added to AGI	Added to AGI
Earned income of U.S. citizens living abroad that was excluded from gross income[f]	Added to AGI	Added to AGI	Added to AGI	Added to AGI	Added to AGI
Non-taxable portion of Social Security benefits[g]				Added to AGI	Added to AGI
Income from sources within Guam, American Samoa, the Northern Mariana Islands,[h] or Puerto Rico,[i] not otherwise included in AGI	Added to AGI				

Source: Congressional Research Service, The Use of Modified Adjusted Gross Income (MAGI) in Federal Health Programs Updated December 6, 2018 https://crsreports.congress.gov/product/pdf/R/R43861