Latest Budget Bill Restricts Social Security Planning Strategies

File & Suspend, Restricted Applications Going Away

Congress recently managed to avoid a government shutdown with the passage of the Bipartisan Budget Act of 2015, but it came at a steep price for those working to maximize their Social Security retirement benefits. Under the terms of this latest budget agreement, an increase in overall spending is being offset, in part, by the elimination of two popular Social Security claiming strategies – the file & suspend technique and the filing of a restricted application.

Congress also addressed the potential spike in Medicare Part B premiums for 2016 by limiting the increase in premiums for Medicare recipients that cannot be held harmless, but the changes to Social Security have soon-to-be-retirees rethinking their Social Security strategies.

Background on the File & Suspend and Restricted Application Techniques

As a part of the Senior Citizens Freedom to Work Act of 2000, two concepts were introduced into the Social Security system – file & suspend and restricted application – that lead to increased claiming options for married couples.

Under file & suspend, an individual at full retirement age could file for Social Security benefits, thereby opening up their earnings record for other beneficiaries (most often their spouse) to claim benefits based on that filer's work history. Then the worker would immediately suspend the payment of benefits, allowing that worker to continue earning delayed retirement credits until age 70. Those credits equate to an 8% annual increase in benefits. At age 70, the worker would then resume the payment of benefits, resulting in a higher benefit because of the delayed retirement credits earned.

At full retirement age, spouses also had the option of filing a restricted application. This allowed a person to collect benefits based solely on their spouse's earnings record (assuming they had already filed) while allowing their own benefit to continue to earn delayed retirement credits until age 70.

The combination of these two provisions created powerful planning opportunities for spouses who could afford to wait before collecting Social Security benefits.

Elimination of the File & Suspend and Restricted Application provisions

The Bipartisan Budget Act of 2015 has significantly altered the rules regarding these provisions, essentially eliminating both file & suspend and filing a restricted application as planning strategies. Both of these strategies had been described as "loopholes" and "aggressive" by members of Congress and the President and had increasingly been on the radar for reform.

The first change is related to the "deemed filing" rule. This rule stated that, when filing for Social Security *before* full retirement age, a person was deemed to be filing for all benefits they were eligible for at that time

Robert W. Baird & Co. does not provide tax advice. Please consult with your tax advisor.
©2015 Robert W. Baird & Co. Incorporated. Member FINRA & SIPC.
Robert W. Baird & Co. 777 East Wisconsin Avenue, Milwaukee, Wisconsin 53202. 1-800-RW-BAIRD. www.rwbaird.com
First Use: 11/2015

(their own plus spousal). Someone applying after full retirement age, however, could restrict their application for benefits to just a spousal benefit only.

Under the new legislation, the deemed filing rule now applies at all ages, regardless of when you apply for benefits. **This change applies to anyone who reaches age 62 after 2015**. Anyone who is already 62 by the end of 2015 (born in 1953 or earlier) will still be able to utilize the restricted application.

To further limit some of the perceived loopholes, the law also changed the file & suspend rule. Now if someone chooses to suspend their benefits:

- **All benefits payable to that individual will be suspended**, regardless of whether the benefits are their own or based on any other person's earnings record (typically from a spouse)
- **No other individual will be eligible for benefits** based on the earnings record of the person who voluntarily suspended.
- When suspended benefits are resumed, they will be paid going forward only, with the benefit of the delayed retirement credit. **There will no longer be an option to take a lump sum payment of the suspended benefit** and forego the credit.

The new rules limiting suspended benefits will apply to anyone who suspends benefits after a 6 month grace period that starts on the effective date of the legislation.

Social Security Planning Under These New Rules

Anyone who has reached their full retirement age before the end of the 6 month grace period should consider filing and suspending. This won't impact their future benefit amount, and will preserve some potential for spousal planning. Anyone who does not reach full retirement age by the end of this window will no longer be able to take advantage of this planning strategy.

If that individual who files and suspends has a spouse who is at least age 62 by the end of 2015, the traditional marital planning strategy appears to still apply. The new limits on restricted applications don't apply to those over age 62, even though they would not actually file the restricted application until much later.

- **Example**: A husband is age 66, meaning he is eligible to file and suspend if he does so within the next 6 months. His wife is at least age 62 by the end of 2015. Because the husband has filed for benefits, the wife can then file a restricted application for spousal benefits once she turns 66. She could collect a benefit on his work history, and then switch to her own – now larger – benefit at her age 70.

Lastly, a person who has already begun benefits will still have the ability to suspend benefits at their full retirement age or later in order to earn delayed retirement credits. Doing so would also suspend any other benefits being paid on that person's work history, so retirees need to understand the implications of a suspension. Lastly, when suspended benefits are resumed, the recipient will **not** have the ability to revert back to the amount immediately prior to suspension and collect a lump sum payment for the payments that were withheld. They will simply be paid the new, increased benefit amount they are entitled to going forward.

Robert W. Baird & Co. does not provide tax advice. Please consult with your tax advisor.
©2015 Robert W. Baird & Co. Incorporated. Member FINRA & SIPC.
Robert W. Baird & Co. 777 East Wisconsin Avenue, Milwaukee, Wisconsin 53202. 1-800-RW-BAIRD. www.rwbaird.com
First Use: 11/2015

Projected Spike in 2016 Part B Medicare Premiums Mitigated

Under what's referred to as the Hold Harmless Provision, approximately 70% of Medicare recipients would have avoided an inflation adjustment to their premiums for 2016. As a result, the expected increase in Medicare costs had to be spread over the remaining 30% of participants, leading to their premiums increasing more than 50% for 2016.

The majority of that spike was eliminated with the passing of the Budget Bill. The base Part B premium for those protected by Hold Harmless will remain at $104.90 per month in 2016. However, this bill prevented the remaining 30% of participants from having to cover the entire inflation adjustment in their premiums. For those not protected by Hold Harmless and for new Medicare enrollees, the new base Part B premium will be limited to $120 per month, plus a $3-per-month surcharge (rather than the $160 previously projected).

Higher income beneficiaries subject to the Income-Related Annual Adjustment Amount (IRMAA) premium increase will see an additional surcharge imposed. The below table compares the 2015 and 2016 Medicare Part B premiums for the various income tiers:

Modified Adjusted Gross Income (2014 MAGI determines 2016 premium)		Medicare Part B Premium	
Single	**Married Filing Joint**	**2015**	**2016***
$85,000 or less	$170,000 or less	$104.90	$104.90 (under hold harmless) $120.00 (not held harmless)
$85,001 - $107,000	$170,001 - $214,000	$146.90	$171.00
$107,001 - $160,000	$214,001 - $320,000	$209.80	$243.00
$160,001 - $214,000	$320,001-$428,000	$272.70	$315.00
$214,001 and above	$428,001 and above	$335.70	$387.00

* The $3 per month surcharge is not reflected in the 2016 premium amounts shown above.

The cost of the Medicare Part B portion of the Budget Bill will be covered by a loan from the Treasury and paid back over time by a gradual increase in Medicare Part B premiums.

Tax Extenders Still Not Addressed

Every year, Congress typically passes a package of dozens of tax breaks, often referred to as "tax extenders", because they extend into the current year tax breaks that expired in the previous year. The tax extenders package typically includes provisions to assist families, individuals and small businesses, and incentivize research and development. Some of the more popular provisions are deductions for mortgage insurance premiums, state and local sales taxes for teachers for certain job-related expenses, the deduction for mortgage insurance premiums, and the ability to take tax-free distributions from retirement plans for charitable purposes (qualified charitable distributions). The tax extenders were not addressed as a part of this legislation.

Robert W. Baird & Co. does not provide tax advice. Please consult with your tax advisor.
©2015 Robert W. Baird & Co. Incorporated. Member FINRA & SIPC.
Robert W. Baird & Co. 777 East Wisconsin Avenue, Milwaukee, Wisconsin 53202. 1-800-RW-BAIRD. www.rwbaird.com
First Use: 11/2015