



## CRS Report for Congress

### Medicare: Part B Premium Penalty

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#### Summary

Medicare is the nation's health insurance program for individuals aged 65 and over and certain disabled persons. Medicare consists of four distinct parts: Part A (Hospital Insurance [HI]); Part B (Supplementary Medical Insurance [SMI]); Part C (Medicare Advantage [MA]); and Part D (the new prescription drug benefit added by the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 [MMA]). The Part A program is financed primarily through payroll taxes levied on current workers and their employers. The Part B program is financed through a combination of monthly premiums paid by current enrollees and general revenues. The 2007 monthly premium is \$93.50. Beneficiaries can choose to receive all their Medicare services through managed care plans under the MA program; payment is made on their behalf in appropriate parts from the Part A and B trust funds. Part D is financed through general revenues and beneficiary premiums (which vary by the plan selected).

Medicare Part B is a voluntary program. People generally enroll in Part B when they turn 65. Persons who delay enrollment in the program after their initial enrollment period are subject to a premium penalty. This penalty is a surcharge equal to 10% of the premium amount for each 12 months of delayed enrollment. There is no upper limit on the amount of the surcharge that may apply. Further, the penalty continues to apply for the entire time the individual is enrolled in Part B.

The Part B delayed enrollment penalty provision was included in the original Medicare legislation; it was included to prevent adverse selection. Adverse selection occurs when only those persons who think they need the benefit actually enroll in the program. When this happens, per capita costs are driven up, thereby causing more persons (presumably the healthier, and less costly, ones) to drop out of the program. The intention was to encourage all persons to enroll. Since most persons over 65 are enrolled in Part B, the costs are spread over the majority of this population group. Per capita costs are less than would be the case if adverse selection had occurred. This report discusses how the Part B premium penalty operates and reviews exceptions to the penalty (including those for certain military retirees). This report is a supplement to CRS Report RL32582, *Medicare: Part B Premiums*, by Jennifer O'Sullivan. This report will be updated if legislative changes occur.

## Enrollment in Medicare Part B

**Aged.** Most persons become entitled to Medicare Part A when they turn age 65. This entitlement is based on their own or their spouse's work in covered employment and the payment of the Medicare payroll tax during their working careers. Persons who have applied for Social Security or railroad retirement benefits automatically receive a Medicare card when they turn 65. Persons who have not applied for Social Security or railroad retirement benefits must file an application for Medicare benefits.

An individual who becomes entitled to Medicare Part A is automatically enrolled in Part B unless he or she specifically refuses this coverage. An aged person not entitled to Part A may still enroll in Part B.<sup>1</sup>

**Disabled.** Medicare coverage is available for persons who have received cash payments for 24 months under the Social Security or railroad retirement disability programs. These persons automatically receive a Medicare card and are automatically enrolled in Part B unless they specifically decline such coverage.

**Initial Enrollment Periods.** Some persons are required to file an application for Medicare benefits. These include persons who have not applied for Social Security or railroad retirement benefits because they are still working. Also included are certain federal, state and local government workers who are not entitled to cash benefits under these programs, but who are entitled to Medicare benefits. Further, aged persons not entitled to Part A must file an application if they wish to obtain Part B coverage.

A person required to file an application for Medicare benefits should do so during an *initial enrollment period* in order to avoid the Part B delayed enrollment penalty. A person's initial enrollment period is seven months long. It begins three months before the month in which the individual first meets the eligibility requirements.

**General Enrollment Period.** If an individual does not establish eligibility during his or her initial enrollment period, that individual must wait until the next general enrollment period. In addition, persons who specifically decline Part B coverage, or terminate Part B coverage, must also wait until the next general enrollment period to enroll or reenroll.

There is a three-month general enrollment period from January 1 to March 31, each year. Coverage does not begin until July 1 of that year. Further, a delayed enrollment penalty may apply.

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<sup>1</sup> All persons entitled to Part A are entitled to enroll in Part B. An aged person not entitled to Part A may enroll in Part B if he or she is a resident of the United States. Further, the individual must either be a citizen or an alien lawfully admitted for permanent residence who has resided in the United States continuously for the immediately preceding five years.

## Enrollment Penalty

The Part B monthly premium is increased for persons who enroll after their initial enrollment period and/or reenroll after a termination of coverage. This is known as the “delayed enrollment penalty.” The penalty is a 10% surcharge for each 12 months of delay in enrollment and/or reenrollment. The length of the period equals: (1) the number of months that elapse between the end of the initial enrollment period and the end of the enrollment period in which the individual actually enrolls; and (2) for a person that reenrolls, the months that elapse between the termination of coverage and the close of the enrollment period in which the individual enrolls. For example, if an individual’s first enrollment period ends in September 2003, and the individual enrolled in the 2006 general enrollment period, the surcharge would be 20%. (This is a total of 30 months delayed enrollment — but only two full 12-month periods.)

There is no upper limit on the amount of the surcharge that may apply. Further, the penalty continues to apply for the entire time the individual is enrolled in Part B.

Approximately 4% of Medicare enrollees are subject to higher premiums based on their higher incomes. However, it should be noted that the delayed enrollment surcharge applies only to the standard monthly premium amount.

## Exceptions to Penalty

**Working Aged.** A working individual and/or spouse of a working individual may be able to delay enrollment in Medicare Part B without being subject to the delayed enrollment penalty. Delayed enrollment is permitted when an individual 65 or over has group health insurance coverage based on the individual’s or spouse’s *current employment* (with an employer with 20 or more employees).

Delayed enrollment is also permitted for certain disabled persons. These are persons who have group health insurance coverage based on their own or a family member’s *current employment* with a large group health plan. A large group health plan is one which covers 100 or more employees.<sup>2,3</sup>

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<sup>2</sup> Persons permitted to delay coverage without penalty are those persons whose Medicare benefits are determined under the Medicare secondary payer (MSP) program. Under MSP, an employer (with 20 or more employees) is required to offer workers aged 65 and over (and workers spouses aged 65 and over) the same group health insurance coverage as is made available to other employees. The worker has the option of accepting or rejecting the employer’s coverage. If he or she accepts the coverage, the employer plan is primary (i.e., pays benefits first) for the worker and/or spouse over age 65. Medicare becomes the secondary payer (i.e., fills in the gaps in the employer plan, up to the limits of Medicare’s coverage). Similarly, a group health plan offered by an employer with 100 or more employees is the primary payer for employees or their dependents who are on the Medicare disability program.

<sup>3</sup> The Balanced Budget Act of 1997 (BBA 97) added an additional exception to the penalty. This exception is for disabled persons who: (a) at the time they first become eligible for Part B are enrolled in a group health plan (regardless of size) by virtue of their current or former employment, and (b) whose continuous enrollment under the plan is involuntarily terminated at  
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Individuals who are permitted to delay enrollment have their own *special enrollment periods*. A special enrollment period begins when current employment ends or when coverage under the plan ends. The special enrollment period ends eight months later. Individuals who fail to enroll in this period are considered to have delayed enrollment and could become subject to the penalty.

**Military Retirees.** Health care coverage for military retirees was expanded by the FY2001 Defense authorization bill (P.L. 106-398). This legislation authorized a permanent comprehensive health care benefit for Medicare-eligible retirees who are enrolled in Part B. These military retirees were made eligible for health care within TRICARE, the military health care system, effective October 1, 2001. TRICARE for Life serves as a second payer to Medicare, paying cost sharing amounts for services covered under Medicare. The beneficiaries are eligible for TRICARE for Life benefits not covered by Medicare. It should be noted that eligibility for TRICARE for Life is contingent on enrollment in Part B. Any person not currently enrolled must do so in order to obtain the TRICARE benefits.

Section 625 of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (MMA) waived the Part B enrollment penalty for military retirees, age 65 and over, who enrolled in the TRICARE for Life program from 2001-2004. A special enrollment period applied for these persons, which ended December 31, 2004. The waiver applied to premiums for months beginning January 1, 2004.<sup>4</sup>

## Related Part A Provisions

The vast majority of persons turning age 65 are automatically entitled to Medicare Part A based on their own or their spouse's work in covered employment. Most persons not automatically covered under Part A have health insurance coverage through a former government employer. However, some persons may need Part A protection. These persons may voluntarily purchase Part A coverage.<sup>5</sup> The Part A premium is equal to the actuarial value of the Part A benefit (\$410 in 2007). Persons who have at least 30 quarters

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<sup>3</sup> (...continued)

a time when their enrollment in the plan is by virtue of their or their spouse's former (i.e., not current) employment. These individuals have a special six-month enrollment period beginning on the first day of the month in which the termination occurs. Individuals who fail to enroll during this period would be considered to have delayed enrollment.

<sup>4</sup> The Secretary of the Health and Human Services was required to rebate any penalties paid for months on or after January 2004, which were no longer applicable as a result of this provision.

<sup>5</sup> An individual eligible to enroll must be a resident of the United States. Further, the individual must either be a citizen or an alien lawfully admitted for permanent residence who has resided in the United States continuously for the immediately preceding five years.

of covered employment have a reduced Part A premium (\$226 in 2007).<sup>6,7</sup> Persons who voluntarily purchase Part A must also purchase Part B.

A penalty is imposed for persons who delay Part A enrollment beyond their initial enrollment period (which is the same seven-month period applicable for enrollment in Part B). However, both the amount of the penalty and the duration of the penalty are different than under Part B. Persons who delay Part A enrollment for at least 12 months beyond their initial enrollment period are subject to a 10% premium surcharge.<sup>8</sup> The surcharge is 10% regardless of the length of the delay. Further the surcharge only applies for a period equal to twice the number of years (i.e., 12-month periods) during which an individual delays enrollment. Thus, an individual who delays enrollment for three years under Part A would be subject to a 10% penalty for six years. A person who delays enrollment for the same three-year period under Part B would be subject to a permanent 30% penalty.<sup>9</sup>

## Issues

The Part B delayed enrollment penalty provision was included in the original Medicare legislation which was enacted in 1965.<sup>10</sup> This provision was included to prevent

<sup>6</sup> BBA 97 specifies that the Part A premium amount is zero for certain public retirees. An individual covered under this provision is one who establishes to the satisfaction of the Secretary that the individual was receiving cash benefits under a qualified state or local government retirement system on the basis of the individual's employment over at least 40 calendar quarters (or on the basis of some combination of such covered employment and quarters of coverage under social security totaling at least 40 quarters). For each of the preceding 84 months the individual must have been enrolled in Part A and not have had his or her premium paid by a governmental entity.

<sup>7</sup> On December 21, 2000, the President signed into law P.L. 106-554, the Consolidated Appropriations Act, 2001. This law exempts certain state and local retirees, retiring prior to January 1, 2002, from the Part A delayed enrollment penalty. These are groups of persons for whom the state or local government elects to pay the Part A delayed enrollment penalty for life. The amount of the penalty which would otherwise be assessed is to be reduced by an amount equal to the total amount of Medicare payroll taxes paid by the employee and the employer on behalf of the employee. The provision applies to premiums beginning January 2002.

<sup>8</sup> An individual enrolled in a health maintenance organization (HMO) can sign up for Part A at any time while in the HMO and up to eight months after HMO coverage has ended. Any time the individual is enrolled with the HMO does not count toward determining whether the individual has delayed enrollment.

<sup>9</sup> Prior to enactment of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), there was no upper limit on the amount of the Part A surcharge or duration of the surcharge. COBRA limited the amount of the Part A surcharge to 10% and the duration to twice the period of delayed enrollment.

<sup>10</sup> Since 1965, some changes have been made to the Part B enrollment provisions. The Social Security Amendments of 1972 (P.L. 92-603) removed the prior three-year limit for initial enrollment and reenrollment after an initial termination. Also in 1972, enrollment in Part B was made automatic for those entitled to Part A. Since most persons voluntarily enroll in Part B, there was now less likelihood that a person might inadvertently not obtain Part B protection;

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adverse selection. Adverse selection occurs when only those persons who think they need the benefit actually enroll in the program. When this happens, per capita costs are driven up, thereby causing more persons (presumably the healthier, and less costly, ones) to drop out of the program. The intention was to encourage all persons to enroll. Since most persons over 65 are enrolled in Part B, the costs are spread over the majority of this population group. Per capita costs are less than would be the case if adverse selection had occurred.

Periodically, proposals have been offered to modify or eliminate the Part B premium penalty either for all enrollees or alternatively for a selected population group. For example, a number of persons suggested that the penalty should not apply to certain military retirees who declined Part B coverage. As noted above, these persons now have access to TRICARE for Life, provided they enroll in Part B. MMA waived the Part B penalty for persons enrolling in both programs by the end of 2004.

Some have suggested further modifying the penalty provision to limit both the amount and the duration of the surcharge, such as is the case for delayed Part A enrollment. While some of the reasons for limiting the Part A penalties could also be offered for Part B, there are some significant differences. First, since almost all aged persons are automatically entitled to Part A, the Part A delayed enrollment penalty could potentially affect only a small number of persons compared to the potential number under Part B. Second, persons who voluntarily enroll in Part A pay the full actuarial cost of Part A coverage; conversely, Part B enrollees pay only 25% of the actuarial cost with federal general revenues picking up the remainder. Third, the amount of the maximum 10% Part A surcharge is considerably larger than what a maximum 10% Part B surcharge would be and thus is more likely to serve as a disincentive to delayed enrollment.

As of this writing, the 110<sup>th</sup> Congress does not appear to be considering further modifications to the delayed enrollment penalty provisions.

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<sup>10</sup> (...continued)

these persons still retained their right to reject Part B coverage. The Omnibus Budget Reconciliation Act of 1980 (P.L. 96-499) provided for continuous open enrollment; further, the provision preventing reenrollment more than twice was removed. The Omnibus Budget Reconciliation Act of 1981 (P.L. 97-35) repealed the 1980 continuous open enrollment provision; the provision permitting unlimited reenrollment was retained. Other conforming changes have also been made over the period, reflecting such things as the coverage of the disabled population and the addition of special enrollment periods for persons with group health plans.