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2018 Retirement Healthcare Costs Data Report©

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SECTION 1: INTRODUCTION

Americans planning for retirement will find both positive and negative news in HealthView Services' 2018 Retirement HealthCare Costs Data Report.

First the good news. The projections for healthcare costs in retirement are a little lower than last year's report, primarily reflecting slower growth in the cost of prescription drugs. Unfortunately, recent legislative changes to Social Security and Medicare have eliminated strategies that increased lifetime benefits and elevated the number of retirees who will face Medicare surcharges. The long-term trend of cost-shifting health-related expenses to retirees continues.

The Report shows that retirement health expenses are projected to rise at an average annual rate of 4.22% for the foreseeable future, compared to 5.47% in last year's Report. This inflation rate is the principal driver of future healthcare costs, which will continue to out-pace U.S. inflation and expected Social Security cost of living adjustments (COLAs).

The Retirement Healthcare Cost Drivers section reviews recent trends that will impact future medical expenses and examines the reasons why drug prices are rising at a slower rate — including the growing utilization of generics over brand name drugs; the rise of rebates and preferred pharmacies; legislation that accelerated the closing of the Part D "Donut Hole", and shared-savings arrangements between plans and providers.

Despite the reduction in prescription-drug inflation, retirees still face a heavy healthcare-cost burden. The average healthy 65-year-old couple retiring this year can expect to pay $363,946[1] ($537,334 future value) in lifetime Medicare and supplemental insurance premiums and out-of-pocket costs.

The message from this report is relatively simple: while projections are lower, paying for the high cost of healthcare in retirement will be a challenge, but it is achievable through proper planning.

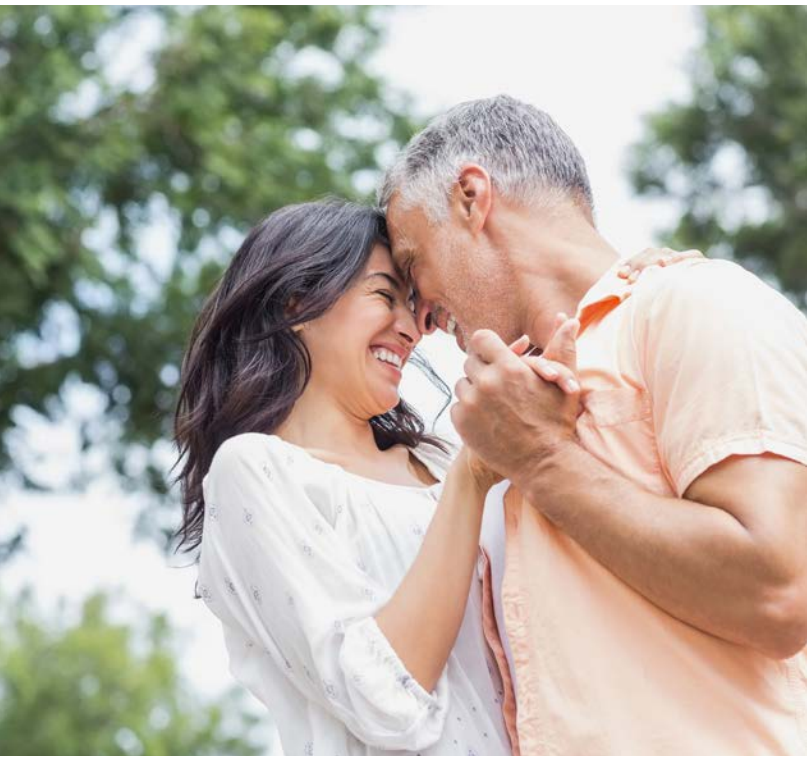
1 *Excludes long-term care*

SECTION 2: DATA & ASSUMPTIONS

HealthView Services draws upon healthcare claims from 70 million individual cases, actuarial, and government data to project retirement healthcare costs. The firm's rigorous bottom-up approach integrates specific variables that will drive future healthcare expenses, including health status, age, gender, income, and state of residence. The inflation expectations are consistent with government healthcare inflation forecasts.

Projections include Medicare Parts B and D, supplemental insurance premiums, and dental premiums. It is assumed that most Americans paid Medicare taxes while employed and will not be responsible for Medicare Part A. National averages are used for supplemental insurance and Part D premiums, which vary by state. Total lifetime projections comprise all out-of-pocket (OOP) expenses related to hospitalization, doctors and tests, prescription drugs, dental, vision, hearing services, and hearing aids.

Calculations assume actuarial longevity for different health conditions and ages. Unless otherwise indicated, the Report uses present-value dollar estimates.



Supplemental insurance (Plan G) is included in projections of premium and total lifetime expenses.

Long-term care expenses are not factored into cost estimates in this paper.

Unless otherwise indicated these numbers do not include Medicare surcharges and assume income in retirement will be less than $85,000 for an individual and $170,000 for a couple, the point in which surcharges begin.

As with any aspect of retirement planning, actual costs for individuals may vary from these averages.

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SECTION 3: HIGHLIGHTS

1. Retirement healthcare cost inflation is projected to rise by 4.22% for the foreseeable future, down from 5.47% in the 2017 Data Report. A slowdown in the growth rate of prescription drugs is the primary reason for this decrease.

2. Total projected lifetime healthcare costs for a healthy 65-year-old couple retiring this year are expected to be $363,946 in today's dollars ($537,334 in future value).

3. Driven primarily by the inflation rate, this couple's annual expenses at age 85 will be 170% higher than in their first year of retirement.

4. Living two years beyond their projected life expectancy of 87 (male) and 89 (female) would add $37,423 in today's dollars ($77,272 in future dollars) to total costs.

5. After no growth from 2017 to 2018, Medicare Part B premiums are expected to rise at an average of 4.7% per year. Medicare Part D is projected at 4.5%, and supplemental insurance — when including age-rating factors — will increase by an average of 5.65% for the near future.

6. Due to the removal of "File Restricted" and "File and Suspend" Social Security strategies, the average 58-year-old American couple will lose an estimated $37,000 ($72,000 in future value) in total lifetime benefits.

7. The lowering of Medicare Means Testing brackets three through five (effective 1/1/2018) will add $57,000 in additional lifetime surcharges for a 40-year-old male earning $93,000 today.

8. By taking steps to improve health and invest the savings, working Americans have an opportunity to significantly increase longevity and generate additional retirement savings.

9. A 55-year-old man with Type II diabetes can make a one-time lump-sum investment today of $29,789 — or make biweekly contributions of $147 for the next ten years — to cover his unfunded health expenses (assuming he makes health improvements to properly manage his condition).

SECTION 4: LEGISLATION UPDATE

The “Medicare Modernization Act of 2003” brought substantial changes to the program, including the introduction of Part D, which established prescription drug coverage. Another important, but sometimes overlooked, provision was Medicare Means Testing, which requires those with a high Modified Adjusted Gross Income (MAGI) in retirement to pay more for Medicare.

Implemented on January 1, 2007, the original proposal divided MAGI into five brackets. (The top four were surcharged. Part D surcharges were added four years later.) This marked the first time Medicare recipients had to pay extra for Part B and Part D because of their income.

In the 15 years since the law was established, Medicare has not adjusted the brackets for inflation. This was supposed to change in 2020 (as originally proposed in the 2003 Act.) However, Section 53314-c-3-C-ii of the Bipartisan Budget Act of 2018 indicates that Medicare rescinded their original plan to begin indexing the brackets for inflation in 2020, and HealthView’s position (and every projection in this report) remains that the brackets will never adjust for inflation.

Given the continued pressure on the Medicare Trust Fund, it is a safe bet that indexing will be suspended further into the future. Assuming MAGI brackets are not changed, a 38-year-old couple each earning $45,000 per year will pay $218,000* in surcharges throughout retirement (in addition to basic premiums). If the brackets were indexed as planned in 2020, the couple would have faced no surcharges**.

The Bipartisan Budget Act of 2018 also established a sixth threshold: individuals with MAGI over $500,000 and couples above $750,000 will now have to pay an even higher surcharge. The addition of the sixth bracket and the postponement of indexing followed the lowering of brackets three through five. While the new bracket will impact a small percentage of wealthy Americans, it serves as another example of Congress pursuing additional revenue sources and shifting costs to retirees.

Collectively, all of these modifications are designed to extend Medicare's long-term solvency. It is clear that Congress has no intention of "easing up" on Means Testing for the foreseeable future.

Supplemental insurance — otherwise known as Medigap — which provides retirees with additional insurance coverage beyond Medicare premiums, offers ten plans nationally (although not every plan is available in each state). Plan F — the most popular and most comprehensive — will not be available to new subscribers beginning in 2020. While those already on Medigap plans will not be forced to abandon Plan F coverage, anyone who is not Medicare eligible on January 1st, 2020 will need to consider other supplemental options, such as Plan G, which is structured similarly to Plan F with the exception of coverage for the Part B deductible. (In cost estimates throughout this paper, all cases utilize Plan G projections.)

In October, the presidential administration announced it would cease paying cost sharing reduction (CSR) payments unless Congress appropriated the funds. Regardless of whether the government reimburses insurers for CSR subsidies, they are still required under the ACA to offer reduced cost-sharing to consumers with incomes up to 250% of the poverty level. Many insurers anticipated the announcement and built this into their premiums. Because these changes primarily affect commercial health costs, not Medicare, they have little bearing on much of the data detailed throughout this report.

** Present Value, assuming 3% inflation per year. Also assumes 3% annual income growth, combined with IRR of 85% at age 65.*

*** Bracket indexing assumes 2% per year.*

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SECTION 5: RETIREMENT HEALTHCARE COST DRIVERS

HealthView Services analyzes claims data from over 70 million cases and reviews the findings with respected and experienced actuaries to produce the most accurate retirement healthcare cost projections possible. Over the past decade, the data tells a fairly consistent story (the 2018 data is no exception) and overall conclusions have remained the same year-over-year. Although this Report reveals a few noteworthy trends that are slowing the retirement healthcare inflation rate, the consistent theme remains: future medical expenses must be addressed through proper planning.

DRUG COSTS

There are a number of reasons why prescription drug costs are expected to rise more slowly than anticipated in the 2017 Data Report.

Increased generic utilization

As the price of brand-name drugs has risen, less expensive generic alternatives have become more popular. Part D plans encouraging generics — and customers subsequently purchasing them — are contributing to a slower rise in projected prescription drug expenses.

Increased rebates

Pharmacy Benefit Managers[2] (PBMs) have facilitated more rebates[3] on brand-name drugs. PBMs originally served as third-parties who processed drug claims for health plans, but recently, their roles have expanded to include — among other elements — pricing and rebate negotiations with drug makers. This also incorporates the development of "preferred networks" (similar to a provider network on a medical plan) in which PBMs offer higher rebates when plans use a preferred pharmacy. Part D plans have structured benefits intended to drive members to these providers.

PBMs are also offering rebate guarantees (agreements between the PBM and plan), which means if rebates fall below the intended price point, the PBM will make up the difference between the actual and target cost.

2 *As of 2015, the three largest PBMs, which cover most of the roughly 4 billion retail prescriptions filled in the U.S., were Express Scripts, CVS Caremark, and OptumRx.*

3 *Generics typically do not have rebates; rather, rebates have grown in prevalence as a response to generics.*

Part D Cost Sharing

Medicare Part D's "Donut Hole" represents the coverage gap in which individuals must pay a larger portion of their prescriptions when total expenditures are between $3,750 and $5,000. The Donut Hole has been gradually closing since 2011; however, because of a legislative change in the Bipartisan Budget Act of 2018, the coverage gap will end in 2019 — one year earlier than expected. Members will then be responsible for 25% of their drug costs in the coverage gap. Prior to the Affordable Care Act, they were responsible for 100% of drug costs in the coverage gap.

MEDICAL COSTS

Overall costs of medical services are growing at a slower rate as more and more providers participate in shared-savings arrangements.

Traditionally, in a shared-savings arrangement, both the plan and provider are at-risk for a plan's performance: the plan and provider agree on a cost target for overall patient treatments, and if actual overall costs are lower than the target, both parties split the savings; however, if actual overall costs are higher than the target, both parties share the loss. This dynamic has helped to control unit-cost increases.

Of particular note is the Medicare Shared Savings Program (MSSP), a voluntary program focused on lower expenditures and higher quality of care that offers interested providers with several options, depending on the level of risk/reward they wish to share. As of January 2018, the program had approximately 10.5 million Medicare beneficiaries assigned to participating providers.[4]

4 *Centers for Medicare & Medicaid Services, "2018 Shared Savings Program Fast Facts", (https://www.cms.gov/Medicare/Medicare-Fee-for-Service-Payment/sharedsavingsprogram/Downloads/SSP-2018-Fast-Facts.pdf).*

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SECTION 6: RETIREMENT HEALTHCARE COST PROJECTIONS

HEALTHCARE COSTS AND THE AVERAGE AMERICAN COUPLE RETIRING TODAY

Although general awareness of future healthcare costs is on the rise, many working Americans accustomed to paying 25–30% of group-plan premiums may be surprised that they must cover 100% of their retirement healthcare expenses, which include premiums and all additional out-of-pockets, such as copays and deductibles.

Table A displays future cost projections for couples retiring at age 65 today, in ten years, and in twenty years. All calculations assume that a healthy male and female will have life expectancies of 87 and 89 respectively, and will have a combined future Modified Adjusted Gross Income (MAGI) of under $170,000.

TABLE A

Cost Projections for Medicare Parts B and D, Supplemental Insurance Premiums, Dental Premiums, and Out-of-Pocket Expenses[5]

Couple	Premiums (PV)	OOP (PV)	Total (PV)	Total (FV)
65	$281,847	$82,099	$363,946	**$537,334**
55	$300,548	$87,265	$387,814	**$768,232**
45	$321,517	$93,299	$414,816	**$1,103,835**

According to the latest data, a 65-year-old couple will pay $363,946 in today's dollars ($537,334 future value) for total lifetime healthcare costs. This year's totals are lower than the projected $404,253 (and $607,662) in the 2017 report, which reflected last year's projected healthcare inflation rate of 5.47%.

Table B shows that as the 65-year-old couple ages, monthly premiums and out-of-pocket costs will increase dramatically over the course of retirement. A fairly manageable $979 monthly expense will almost double by age 75 and grow to $2,664 per month — a 172% increase — by age 85.

5 *Out-of-pocket costs include Hospitalization, Doctors & Tests, Prescription Drugs, Dental, Hearing Services, Hearing Aids, and Vision*

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TABLE B

Cost Projections for a 65-Year-Old Couple for Medicare Parts B and D, Supplemental Insurance, Dental Insurance and Out-of-Pockets (in Future Dollars)

	65	70	75	80	85	Total
Monthly	$979	$1,266	$1,662	$2,115	$2,664	
Annually	$11,752	$15,196	$19,942	$25,385	$31,966	**$537,334**

RETIREMENT HEALTHCARE INFLATION

As discussed, the primary driver behind rising costs is the retirement healthcare inflation rate, which is projected to be 4.22% for the foreseeable future.

This number reflects several components detailed in Table C, which provides anticipated inflation rates for Medicare Parts B and D, and supplemental insurance premiums.

TABLE C

Medicare Part B and D, and Supplemental Insurance Inflation Rates

Service	2017 to 2018	2019 to 2027
Part B	0%	**4.7%**
Part D	8.0%	**4.5%**
Medigap[6]	- -	**2.4%**

Following two years of price jumps averaging over 13%, Medicare Part B premiums did not increase from 2017 to 2018 and remained at $134 per month. Future projections published annually by the Medicare Trustees (these are not binding) average nearly 5%.

6 *The 2019–2027 figure represents Plan G. The 2017–2018 figure is not stated, since our 2017 report used Plan F. Starting in 2020, individuals beginning supplemental insurance coverage will be unable to sign up for Plan F. The overall cost difference between the two plans is marginal.*

As stated in the Retirement Healthcare Cost Drivers section, prescription drug costs through Medicare Part D have decreased, which is the primary cause of the lower retirement inflation rate of 4.22%.

In 2019, the inflation rate for supplemental insurance is projected to be 2.4%; however, age-rating (a Medigap rule that adjusts costs for older recipients) will tack on an additional 4.45% from age 65 to age 66 (the average age rating is 3.25%). A 65-year-old who paid $1,712 for the year (the national average) for supplemental plan G monthly premiums in 2018 can expect payments to rise to $1,830 in 2019 as a result of inflation and age rating. This nearly 7% increase is a combination of the 2.4% inflation and the 4.45% age rating, a cumulative 6.85% experienced inflation rate.

TABLE D

Projected Cost-Sharing (Out-of-Pocket Cost) Inflation Rate from 2018 to 2019

Service	Projected Inflation Rate
Hospitals	1.40%
Doctors and Tests	2.80%
Prescription Drugs	1.90%
Dental	4.50%
Hearing Services	3.00%
Hearing Aids	3.00%
Vision	3.00%

The majority of out-of-pocket costs stem from copayments and deductibles relating to hospitals, doctors and tests, and prescription drugs, which will increase by less than 3% over the next year. These rates remain relatively low and appear to be more aligned with historic U.S. inflation rates. Although dental rates are higher, other out-of-pocket expenses will increase by 3%.

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HEALTHCARE COSTS & SOCIAL SECURITY

Table E examines a 66-year-old couple[7] receiving Social Security benefits based on a Primary Insurance Amount (PIA) of $1,404 each per month ($16,848 per year), the 2018 national average. Using the HealthView Service Retirement HealthCare Cost Index (the ratio of lifetime costs to Social Security benefits), the chart reveals (in five-year increments) that retirement healthcare costs will require, on average, 39% of the couple's total Social Security income at age 70, which increases to 59% per year by age 87.

An average 66-year-old couple will spend an average of 48% of their Social Security income on healthcare; a 55-year-old couple, 57%; and a 45-year-old couple, 63%. At 87, the 45-year-old couple will need 72% of their Social Security checks to cover their health-related expenses.

Most notably, Table E shows that healthcare expenses will significantly out-pace the Social Security Trustees' long-term annual projected COLA of 2.6%.

TABLE E

Projected Percentage of Social Security Benefits Required to Cover Health Costs: Average 66-Year-Old Couple

Couple	Annual Health Costs	Social Security	Annual Difference	% of Soc. Sec. to Health Costs
70	$14,610	$37,302	$22,692	39%
75	$19,257	$42,412	$23,155	45%
80	$24,517	$48,218	$23,701	51%
85	$30,876	$54,822	$23,946	56%
87	$33,890	$57,710	$23,820	59%

7 Age 66 is chosen because it is their Full Retirement Age (FRA) for Social Security benefits. All projections are from FRA through age 87.

LONGEVITY & RETIREMENT HEALTHCARE

Drawing upon actuarial data, current healthy 65-year-olds are expected to live to age 87 (male) and 89 (female). Assuming they live two years beyond their average life expectancies,[8] (89 and 91 respectively), a couple would pay an additional $37,423 in today's dollars ($77,272 in future dollars) for Medicare Parts B and D, supplemental insurance premiums, and out-of-pocket costs. (Table F).

TABLE F

Difference in Healthcare Costs for a 65-Year-Old Couple That Lives Two Years Past Projected Life Expectancy

Couple's Life Expectancy	Total Healthcare Costs (Today's Dollars)	Total Healthcare Costs (Future Dollars)
87/89	$363,946	$537,334
89/91	$401,368	$614,606
Difference (Additional Cost)	**$37,423**	**$77,272**

8 *Based on actuarial data, there is a 25% chance that both spouses will live two years beyond their projected life expectancies.*

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SECTION 7: IMPROVING HEALTH MANAGEMENT TO REDUCE THE COST OF HEALTHCARE IN RETIREMENT

Retirement healthcare expenses are daunting, but steps can be taken to plan for, manage and even reduce these costs. HealthView has previously addressed this through a number of papers focused on planning strategies, such as optimizing income replacement ratios and avoiding Medicare Means Testing surcharges. The firm has recently conducted extensive research on the long-term financial benefits of condition management.

According to the Centers for Disease Control, one in two adult Americans suffers from some form of chronic condition, which are classified as cardiovascular disease, cancer, lung disease, stroke, Alzheimer's, or type 2 diabetes.[9] In a recent joint venture with Mercy, HealthView Services has developed a new data-driven application that targets this population by allowing participants to monitor their financial gains and track physical improvement through proper condition management. These individuals have the potential to substantially lower annual health expenses if they follow prescribed treatments, which can be as simple as taking medication as directed.[10]

Those who adjust behaviors and invest the savings can increase their life expectancies, bolster retirement savings, and offset healthcare costs in retirement.

Let's examine Paul, a 55-year-old male with Type II diabetes who is beginning to look ahead to his presumed retirement at age 65. He has a number of concerns, but none greater than his healthcare expenses. Paul hopes to address this challenge by setting aside enough money to fully cover his projected medical outlays, which include Medicare Parts B and D, supplemental insurance (Medigap), dental, and all out-of-pocket costs.

9 *https://www.cdc.gov/chronicdisease/about/infographic.htm*

10 *Half of Americans diagnosed with a condition stop taking prescribed medications after six months. US National Library of Medicine, National Institutes of Health, "Medication Adherence: WHO Cares?", (https://www.ncbi.nlm.nih.gov/pmc/articles/PMC3068890/).*

Since Part B premiums will automatically be deducted from Social Security benefits, a lifetime total of $242,091 can be funded with an initial investment of $29,789 (which will yield approximately $53,347 in ten years[11]), assuming he also allocates pre-retirement cost savings towards this goal, as detailed in the following paragraph. Biweekly installments of $147 for the rest of his working years will also cover the expense.[12] (Note that if this biweekly contribution was part of a 401(k) plan with a 50% employer match, the individual would only need to earmark $98 every other week — certainly a manageable figure.)

Paul will also be able to generate an average of $4,259 per year for the next ten years by taking steps to improve his health.[13] Investing the savings from his behavior modifications will produce an additional $56,763[14] from now to his retirement in ten years. Adding this to the initial investment ($53,347) will total $110,110 by age 65.

TABLES G-1 & G-2

Investment Required to Fund Retirement Health Expenses — Paul: 55-Year-Old Male with Type II Diabetes

Total Cost	**$242,091**
Part B Premium Paid Via Social Security	$59,948
Remaining Costs	$182,144
Retirement Savings Balance Required to Cover Remaining Costs	$110,110
Average Annual Pre-Retirement Savings from Improved Health	$4,259

Funding Options	
One-Time Lump Sum Today	**Biweekly Contributions During Working Years**
$29,789	**$147**

11 *Presuming a 6% annual rate of return*

12 *Paul does not need to determine a funding source for his Part B premiums as they are automatically deducted from this Social Security benefit.*

13 *This example assumes he improves from "Poorly Managed" to "Well Managed" categorization in his condition management, and shows costs savings from now until retirement. His wellness improvements would include monitoring his diet, properly taking any prescribed medication, and increasing his physical activity.*

14 *Presuming a 6% annual rate of return*

SECTION 8: CONCLUSION

As highlighted in the introduction, the slower growth of prescription drug costs has reduced the overall expected healthcare inflation rate. As a result, the cost projections in this report are lower than in 2017. Although this is positive, legislative changes mean many retirees will experience a decrease in lifetime Social Security benefits. A 66-year-old couple will need 48 percent of their Social Security income to healthcare, and a 45-year-old couple, 72 percent. Also, because Congress postponed the indexing of Medicare Means Testing brackets, many future retirees will be subjected to these changes.

Ultimately, healthcare remains a sizable component of overall retirement expenses; therefore, proper planning is critical.

According to recent surveys, 53 percent of pre-retirees expressed anxiety about their upcoming retirement,[15] and worries about paying for healthcare contribute to this sentiment.

Americans hoping to mitigate the impact of retirement healthcare costs can achieve this objective. As outlined in the Case Study, expenses can be significantly reduced by improving one's health, investing the savings, and combining the earnings with a lump-sum investment or regular contributions to a 401(k) plan.

15 *Associated Press: NORC, "Retirement Planning In America: Anxiety, Inequality, and the Role of Social Security, (http://www.apnorc.org/projects/Pages/HTML%20Reports/retirement-planning-in-america-anxiety-inequality-and-the-role-of-social-security-issue-brief.aspx).*

SECTION 9: ABOUT HEALTHVIEW

Founded in 2008 by a team of experienced financial professionals, healthcare industry executives, and expert physicians, HealthView Services is the nation's leading provider of healthcare cost-projection software to financial services firms and advisors. The firm's suite of tools is designed to help current and future retirees develop financial plans that incorporate retirement healthcare costs.

The company's signature service, HealthWealthLink, is an integrated retirement-planning platform that draws upon cost data from more than 70 million annual healthcare cases to create personalized estimates of retirement healthcare costs. The system also furnishes advisors with the necessary tools and information to implement financial strategies that can help clients offset this expense and achieve retirement goals.

With its unique expertise and data, HealthView is a respected thought leader on retirement healthcare, Social Security, and long-term care. The company has also released white papers on topics ranging from healthcare cost-management strategies to income replacement ratios to challenges that women face in retirement.

In 2018, HealthView and Mercy Health founded HealthyCapital, a firm that produced an application that incentivizes individuals to make healthy choices, leading to increased longevity and lower annual medical expenses.