Why Recent Updates to Medicare and Social Security Matter
Changes to Medicare and Social Security

Over the last two-and-a-half years, Social Security and Medicare have implemented a number of changes that will reduce benefits, increase future health care costs, and significantly impact current and future retirees.

The timeline above (Figure A) shows seven events since October of 2015 that will impact Social Security and Medicare beneficiaries. The changes fall into three main categories: Medicare Means Testing, Social Security Cost of Living Adjustments (COLAs), and Social Security claiming strategies.
Medicare Means Testing

Modifications to Medicare income thresholds will, at first, only apply to affluent Americans; however, since the brackets have not been indexed to inflation, over time, more retirees will be subject to surcharges.

FEBRUARY 9, 2018
BIPARTISAN BUDGET ACT OF 2018: INDEXING DELAYED; SIXTH MEANS TESTING BRACKET ADDED

The “Medicare Modernization Act of 2003” brought substantial changes (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 will now begin indexing the brackets for inflation in 2028 instead of 2020. In essence, Medicare delayed the index for eight more years, which means that as incomes grow over time, more Americans will eventually face Means Testing.

Given the continued pressure on the Medicare Trust Fund, it is a safe bet that indexing will be suspended even further.

The delay in indexing will have an impact on many future retirees, whose surcharges will be higher as a result.

A 38-year-old couple each earning $45,000 will pay an additional $218,000* in surcharges throughout retirement if MAGI is not indexed. If the brackets were indexed as planned in 2020, the couple would have faced no surcharges1.

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, combined with the postponement of indexing, occur less than two months after brackets three through five were lowered. So while the new threshold will only be felt by a small percentage of affluent Americans, it is another example of Medicare pursuing additional revenue sources.

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.

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1. Data provided by HealthView Services

*Costs shown throughout this paper are in net present value unless otherwise indicated.
As stated in the previous section, Medicare recently lowered MAGI brackets three, four, and five. As a result, some individuals moved from the third to fourth bracket, and all fourth bracket beneficiaries migrated to the fifth.

<table>
<thead>
<tr>
<th>Bracket</th>
<th>Individuals</th>
<th>Couples</th>
<th>Individuals</th>
<th>Couples</th>
<th>Average Change in Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>1st</td>
<td>&lt;$85,000</td>
<td>&lt;$170,000</td>
<td>&lt;$85,000</td>
<td>&lt;$170,000</td>
<td>-</td>
</tr>
<tr>
<td>2nd</td>
<td>$85,001-$107,000</td>
<td>$170,001-$214,000</td>
<td>$85,001-$107,000</td>
<td>$170,001-$214,000</td>
<td>36%</td>
</tr>
<tr>
<td>3rd</td>
<td>$107,001-$160,000</td>
<td>$214,001-$320,000</td>
<td>$107,001-$133,500</td>
<td>$214,001-$267,000</td>
<td>92%</td>
</tr>
<tr>
<td>4th</td>
<td>$160,001-$214,000</td>
<td>$320,001-$428,000</td>
<td>$133,501-$160,000</td>
<td>$267,001-$320,000</td>
<td>148%</td>
</tr>
<tr>
<td>5th</td>
<td>$214,000+</td>
<td>$428,000+</td>
<td>$160,000+</td>
<td>$320,000+</td>
<td>203%</td>
</tr>
</tbody>
</table>

Congress lowered these brackets in the “Doc Fix” law, which primarily focused on how doctors would be paid when accepting Medicare patients. Limited attention was paid to how lowering income thresholds would affect current and future retirees.

The legislation also contained a two-year look-back policy, which meant that surcharges would be assessed on 2016 income, rather than 2018.

What are the implications? A 40-year-old man currently earning $93,000 – with a 3% annual salary increase and 85% income replacement ratio (IRR) in retirement – will be earning approximately $161,000 at age 65.

The lowering of the brackets would move this 40-year-old from the fourth to fifth income level, resulting in an additional 55% surcharge on Parts B and D. This change would result in an estimated $57,000 ($173,000 in future value) in total lifetime costs.

A 40-year-old making $93,000 today is expected to earn $161,000 in retirement, placing them in the fifth surcharge bracket.

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4. Data provided by HealthView Services. Assumes income remains stagnant from age 65 retirement to age 87 death.
Social Security
Cost-of-Living Adjustments

Over the last three years, Social Security’s Cost-of-Living Adjustments (COLAs) have provided little financial relief for millions of retirees.

OCTOBER 15, 2015
0.0% COLA ANNOUNCED FOR 2016

Every year since 1975, the Social Security Administration has announced a COLA that is applied to all benefits the following year. The aim is to offset the rising cost-of-living in retirement due to inflation. The Social Security Administration determines its annual COLA based on CPI-W, the Consumer Price Index for Urban Wage Earners and Clerical Workers. The 2015 COLA of 0% (which affected 2016 benefits) came as a surprise. Although CPI-W may have remained flat, older Americans still experienced an increase in day-to-day expenses because of the U.S. inflation rate (2.2%). The average retiree had to pay more for essential products and services, such as health care, housing, and food, without the benefit of additional Social Security income.

OCTOBER 13, 2016
0.3% COLA ANNOUNCED FOR 2017

Social Security benefits only increased by three-tenths of one percent from 2016 to 2017, marking the first time that a non-zero COLA of less than 1% was implemented. Year-over-year, average beneficiaries received an almost-negligible extra $4 per month in their checks to offset an overall rise in CPI of 1.8%.

From 2015 to 2017, Part B premiums rose at a rate more than 92x greater than two combined years of COLAs.

5. https://data.bls.gov/timeseries/CUUR0000SA0L1E?output_view=pct_12mths
Medicare’s “Hold Harmless” provision was initiated to protect those in the first Means Testing bracket (who earn less than $85,000 if single, $170,000 if married). From one year to the next, subscribers who fall in this income range will not be financially responsible for any Part B increase greater than the value of that year’s Social Security COLA. This ensures that a beneficiary’s income will not be lowered in years when the COLA is small or zero.

Despite a 2.0% COLA in 2018, the actual impact on beneficiaries was not as positive as it may appear. Part B Premiums rose from $104.90 in 2015 to $121.80 in 2016; however, recipients who fell under “Hold Harmless” income thresholds had the same premium because they received no COLA. When in 2017, Part B premiums jumped to $134.00, beneficiaries had to pay the value of their benefit increase to cover the higher Medicare costs (a few dollars per month).

In 2018, after the 2.0% COLA was announced, beneficiaries learned that most (or all) of their additional income (an average of $25-$30 per month) would be earmarked to the $134.00 Part B premium, which did not increase from 2017. While Social Security income did rise, when factoring in Medicare costs, there was no added net benefit for those who were “Held Harmless.”

Social Security accounts for approximately 33% of an (average) elderly American’s income. The small rise in COLAs over the last three years, coupled with higher inflation and health care costs growing at 5-7% annually, means that Social Security income simply cannot keep pace with the cost of living.

An average 68-year-old couple receiving the first significant Social Security increase in two years in 2018 will, due to Hold Harmless, spend 96% of their additional COLA benefit (over $510 this year) on readjusted Part B premiums.

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Social Security Eliminates Filing Strategies

Changes to Social Security filing strategies over the last three years have reduced the potential value of lifetime benefits.

APRIL 30, 2016
“FILE & SUSPEND” EFFECTIVELY ELIMINATED FOR MOST AMERICANS

This now effectively-defunct strategy gave beneficiaries the option to “File and Suspend” their Social Security at Full Retirement Age (FRA), allowing a spouse to claim a traditional spousal benefit, or “File Restricted” during that time without taking his/her own retirement payout.

While Congress provided a six-month grace period for those planning to take advantage of “File and Suspend,” this change will affect virtually all future beneficiaries.

OCTOBER 28, 2015
“FILE RESTRICTED” EFFECTIVELY ELIMINATED FOR MOST AMERICANS

“Filing Restricted” was a Social Security claiming strategy available to many beneficiaries after the “Senior Citizens’ Freedom to Work Act of 2000.” With this option, at FRA, individuals were able to collect half of their spouse’s benefit without being considered “Deemed Filing.” (A beneficiary filed for either his/her benefit or a spouse’s benefit and was “deemed” to be applying for both.) This would have allowed a married person to collect full benefits – plus gain eight percent per year for delaying claiming (ideally until age 70) – resulting in a 32% increase in Social Security benefits.

“The Bipartisan Budget Act of 2015” eliminated this option. Though there is a grace period for some, anyone born after 1953 is unable to use this strategy. (It is important to note that this choice is still available to widows eligible for a survivor benefit.)

Due to the removal of “File Restricted” and “File and Suspend,” the average 58-year-old American couple who can no longer use these strategies will lose an estimated $37,000 ($72,000) in total lifetime benefits.10

10. Data provided by HealthView Services. Assumes national average primary insurance amounts and COLAs based on SSA projections. Life expectancy: Husband 87; Wife, 89. Claim ages: Husband, 70; Wife, 66.
Conclusion

Demands for large-scale changes to Medicare and Social Security inevitably result in opposition. Congress has adopted policies designed to reduce benefits and increase costs that have not drawn significant attention or criticism. This makes it more likely that we will see similar adjustments in the future. If this trend persists, retiring Americans will continue to pay more for Medicare benefits and receive less in Social Security income.

As a direct result of the changes discussed in this paper, a 55-year-old couple each earning $70,000 in 2018 will face the following retirement challenges:

The cumulative cost of the delay in Means Testing indexing, combined with the lowering of brackets three through five, will increase their lifetime surcharges by almost $122,000 (over $272,000 in future value).

The elimination of “File Restricted” and “File and Suspend” claiming strategies will result in the loss of over $36,000 (nearly $78,000 in future value) in potential lifetime Social Security benefits.

Together, these changes will have a $158,000 ($350,000 in future value) impact on this couple's retirement. Even for middle-class retirees, modifications to Medicare and Social Security are no small matter.

If future COLAs are consistent with the latest Social Security Trustee projections (2.6%), the couple will require 123% of their Social Security income to meet their future health care expenses. Reflecting all of these changes - and running projections in the future value - their total lifetime retirement health care costs will be over $1.33 million, while their Social Security income will be just shy of $1.09 million.11

While the changes detailed in this paper may ultimately serve to strengthen Medicare and Social Security, the growing number of retiring Baby Boomers will continue to strain the two programs. As a result, retirees must anticipate continued changes that will impact their retirement outlook.

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11. Data provided by HealthView Services. Assumes national average primary insurance amounts and COLAs based on SSA projections. Life expectancy: Husband 87; Wife, 89. Claim ages: Husband, 70; Wife, 66. Income based on 2018 value. 3% annual income increase assumed. 85% income replacement ratio assumed at age 66 retirement.
About HealthView Services

Founded in 2008 by a team of seasoned financial professionals, health care industry executives, and expert physicians, HealthView Services is the nation’s leading producer of health care cost-projection software. The firm’s suite of tools is designed to prepare current and future retirees for the impact of retirement health care costs.

The company’s signature service, HealthWealthLink, is an integrated retirement-planning platform that draws upon cost data from more than 70-million annual health care cases to create personalized estimates of retirement health care 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.

HealthView has emerged as a respected thought leader in addressing the issue of affording quality health care in retirement, and the company has produced extensive educational content on the importance of integrating medical expenses into the planning process. The company has also released white papers on topics ranging from health care cost-management strategies to income replacement ratios to unique challenges that women face in retirement.

HealthView’s unique approach to retirement planning and unparalleled expertise in health care cost projections has placed the firm at the forefront of this emerging domain.

In 2017, HealthView and Mercy Health founded HealthyCapital, a firm that produces an application which incentivizes individuals to make healthy choices leading to increased longevity and greater retirement savings.