July 2019

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Summer Vacation
Bill was away the week of July 1st to visit Acadia National Park with his family hiking, fishing, biking, kayaking, and eating lobster rolls!

Mallard E-Mail Update
Are you receiving our e-mail newsletters (which are different from this quarterly newsletter)? If not, let us know by sending an e-mail requesting to be added to our e-mail newsletter list.

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MALLARD ADVISORS LLC

Comprehensive Financial Planning & Wealth Management Solutions

THE QUARTERLY MALLARD CALL

Demystifying Health Care Costs in Retirement

As retirement nears, we begin to consider several important questions such as:

- When can I stop working?
- When should I take Social Security?
- How much can I spend / withdraw each year from my portfolio?
- How much will health care cost and how will I pay for it?

While each of these has its own concerns, the health care question may be the most daunting. PricewaterhouseCoopers' financial wellness study found that 38% of baby boomers said health care costs are a top fear. So, not only is the cost anxiety provoking, it is also quite uncertain. This newsletter will review the potential retirement health care costs, thereby demystifying this topic to some extent.

When it comes to the retiree health care costs, there are two distinct stages that result in very different considerations, decisions, and costs. The first is the retiree who has yet to reach age 65 (Medicare age). The second is the retiree who is 65 years old or older.

Health Care Costs Prior to Age 65
For those who retire prior to age 65 (Medicare age), total health care costs can vary widely depending upon two primary factors: your income and your health. The good news is that the Affordable Care Act made obtaining health insurance a guarantee regardless of pre-existing conditions and employment status. In the past, for most individuals, the only affordable and guaranteed access to health insurance was found by staying with an employer-sponsored plan *instead of retiring*. In other words, health care kept many people chained to their desk until Medicare would kick in at age 65.

This new freedom to retire comes with considerable uncertainty regarding the cost. Previously, while employed, your employer might have heavily subsidized your health insurance costs (average of $5,300 per year). Now, this subsidy will be gone unless you are one of the few lucky ones with pre-65 retiree insurance from your employer.

Retiring prior to your age 65 without employer-provided coverage generally means you will either elect COBRA coverage, or more likely, you will obtain your insurance from the "HealthCare.gov Marketplace". Since COBRA is temporary and expensive, let's stay focused on the Marketplace coverage.

Your Marketplace health care costs will be made up of a monthly premium and out-of-pocket costs such as a deductible or co-pays. Your premium is driven by your age, location, tobacco use (in some states), the number of family members covered, and the plan type (i.e., Bronze, Silver, Gold,

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Platinum, etc). Next, the premium may be lowered through receipt of the **Premium Assistance Tax Credit** if your income is low enough (based upon your family size). This Premium Assistance Tax Credit is available to those of "low income" even if you have "high assets". This is because there is no practical, easy way for the IRS to consider net worth. Therefore, eligibility for the tax credits are based solely on income. This can create incentives to keep your "taxable income" purposely low by delaying collection of a pension, Social Security, or avoiding taking IRA withdrawals / conversions. Then, living expenses are simply paid with after-tax investments/cash. In other words, it is possible to have your premium largely subsidized and still be an IRA millionaire!

Your Marketplace out-of-pocket costs are harder to estimate but are driven largely by your *usage* of health care services. The health reform laws set limits on the amounts you have to pay out-of-pocket each year. For example, a Silver Plan has a maximum (in-network) out-of-pocket cost of $7,900/year. Your usage of health care services during the year is what will determine how much of this maximum you use.

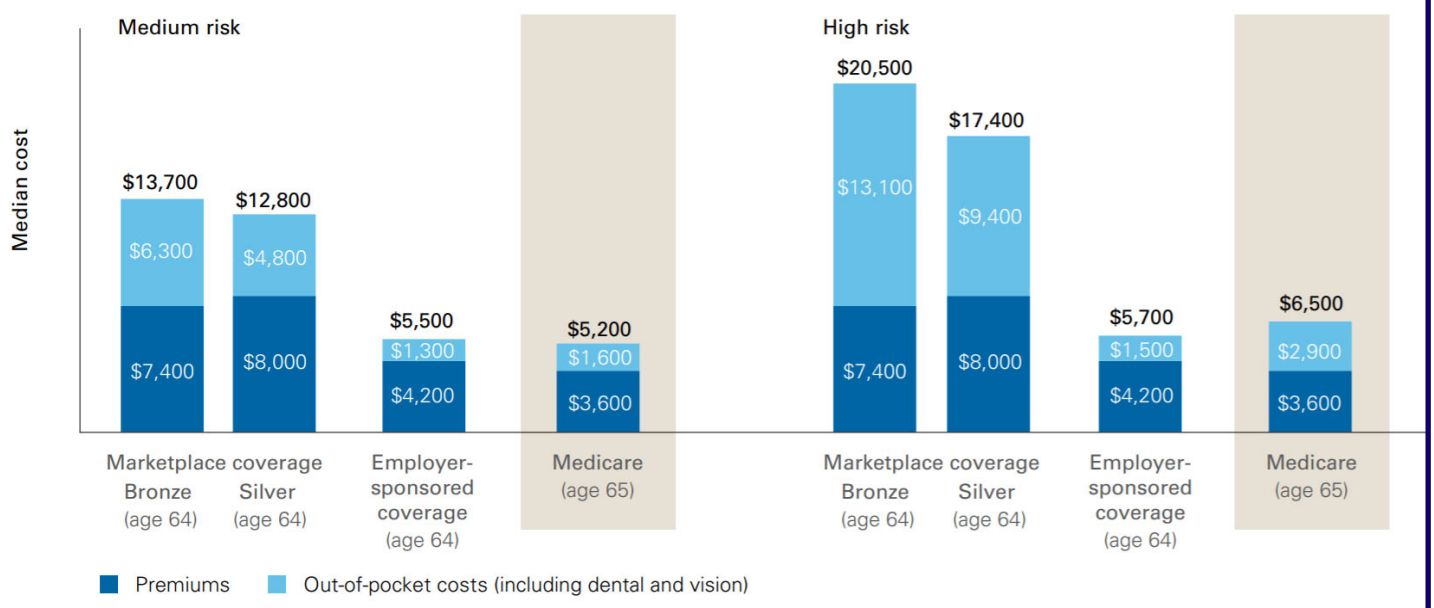
How do you estimate what your total premium (net of the Tax Credit) and your potential out-of-pocket costs will be?

The easiest method is use of the Health Insurance Marketplace Calculator found at the ***Henry J. Kaiser Family Foundation*** website. This calculator takes all of the above criteria into account without having to wrestle with the actual HealthCare.gov website. Once done, you will have a good estimate of your pre-65 health care expenses. For example, let's assume this total cost amounts to $15,000/year and is made up of a non-subsidized premium of $8,000, and $7,000 of out-of-pocket costs. Prior to retirement, it may have only been $5,000/year, so this is an increase in annual health care expenses of about $10,000/year.

Health Care Costs After Age 65

Once you have reached age 65, you are now eligible for Medicare as your primary insurance coverage and will *also need* some sort of supplemental coverage as well (typically known as Medigap). Recently, Vanguard and Mercer Health published some research on the topic of health care in retirement. One thing that was made quite clear from their research is the fact that there is a strong drop in total health care costs after age 65, but with a much narrower range of costs (even when considering your health situation). **In other words, there is much more certainty of expenses and at a lower total cost than prior to age 65.**

Figure 3. Presence or lack of subsidized coverage for pre-Medicare retirees can significantly affect costs



Source: Mercer-Vanguard health care cost model, 2018.

As shown in the graphic on the prior page, a 64-year-old person with "medium health risk" pays a total of $12,800 prior to age 65, but only $5,200 after age 65 while on Medicare (including the cost of supplemental coverage). Even a 64-year-old person with "high health risk" who had paid $17,400 prior to age 65, would only pay $6,500 after age 65. *Please note the visual shows only median costs (and it also is NOT adjusted for those of higher income). Naturally, one with multiple chronic conditions could end up spending quite a bit more.*

Just like prior to age 65, your health is a major factor in your expected costs, but income also remains an important component in determining your costs. While there is no premium assistance tax credit for Medicare recipients, there is a **Medicare Premium Surcharge** for those of higher income. This surcharge increases Medicare Part B (Medical), and Medicare Part D (Drug Plan) premiums from their base amount. In fact, these surcharges at the highest income level can increase your Medicare costs by $4,829 annually ($3,900+$929 as shown in the last row in the table below).

Medicare Premiums + IRMAA Surcharges (2019)

MAGI Single	MAGI Joint	Part B Annual Premium	Part B Income Related Increase	Part D Ave Est. Annual Premium*	Part D Income Related Increase	Total Part B & D Premium Annual
<$85,000	<$170,000	$1,626	$0	$30	$0	$1,656
Up to $107,000	Up to $214,000	$1,626	$649	$30	$149	$2,454
Up to $133,500	Up to $267,500	$1,626	$1,625	$30	$383	$3,664
Up to $160,000	Up to $320,000	$1,626	$2,600	$30	$617	$4,873
Up to $500,000	Up to $750,000	$1,626	$3,575	$30	$851	$6,082
Over $500,000	Over $750,000	$1,626	$3,900	$30	$929	$6,485

* This is an estimate

While nearly all retirees age 65 or over will enroll in Medicare, the question becomes how will you cover the gaps (in Medicare) as it's only designed to cover part of the expenses related to hospital visits and other medical services. In fact, if you only enrolled in Medicare, you would be subjecting yourself to unlimited risk. So how can you limit this risk? Most people have three choices:

1. Employer (Retiree) sponsored supplemental heath care coverage;
2. Medicare Supplement Plan (aka Medigap Plan); or
3. Medicare Advantage (Part C) Plan

Most retirees only have the choice of the second or third option above since employer supplemental health insurance in retirement is becoming more and more uncommon.

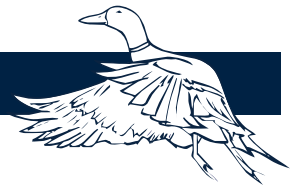
The choice between Medicare Advantage and a Medigap Plan is a very important one and should be considered with care. While both plans limit the risk of your health care expenses, it's important to understand some of the differences between the two. Medigap plans typically come with higher premiums than Medicare Advantage Plans, but have few, if any, out-of-pocket expenses. This can make Medigap a better fit for those who are willing to pay a little more in premiums to stabilize their total health care costs. This could also be a better fit if you have major or ongoing medical issues and/or you want more flexibility of which doctors you would like to see regardless of network. The only other cost you would need to consider is your prescription drug coverage through part D.

Medicare Advantage Plans may be a better **all-in-one solution** as most plans include part D and work very similar to most folk's current employer-sponsored health plans. Once again, this is a complex decision. Therefore, we refer clients to local Medicare consultants that can strip the confusion and anxiety out of these decisions.

After age 65, you will have Medicare premiums (which will be influenced by your income), some sort of supplemental insurance premiums, and out-of-pocket costs (which will be influenced by your health care consumption). However, assuming you remain in similar health, your costs will likely be lower and more stable than what you paid as a pre-age 65 retiree with the Marketplace insurance coverage.

Hopefully this review has demystified health care costs both prior to Medicare age, and after and will result in better financial planning for these expenses.

Market Commentary



The last month of 2018 included a painful decline before the markets took a sharp (and unexpected) turn to deliver the biggest one-quarter gain since the third quarter of 2009. Even better, the surprise upward trend continued through the second quarter of 2019, but with more modest gains. Now, the S&P 500 is up 27% from its Christmas Eve low, and 19.3% this calendar year through the close on Friday, July 5th and this does not even include dividends. If we could simply stop the year at this point, the gains would be unusually high for a typical *12-month* period; for six months, they are extraordinary. Just about every investment asset produced gains in 2019's second quarter as shown in the table below.

It's tempting to think that the bull market is running out of steam, in part due to the fact that it's not easy to see how valuations can go much higher. There is also growing uneasiness about a global slowdown in economic activity. Also, the threat of trade wars is not likely to boost the global economy and therefore stock prices. However, on the positive side, the Federal Reserve has made it clear it will cut short-term rates if the economy falters or if inflation stays low. As the election in 2020 approaches, we also think the next several months are more likely to lead to trade deals than an expansion of tariffs,

Considering the downturns at the end of 2018, the roaring start to 2019 has been a very pleasant surprise. There will be more surprises in store, but don't bother trying to listen to what the experts say the markets will do in the final half of this year. No one knows...but everyone has an opinion. These prognosticators are frequently wrong, but never in doubt! It is better to doubt the direction of the market, but to be right in the long-run by maintaining a globally diversified, and balanced portfolio through thick and thin.

Summary of Asset Class Total Returns *(as of 06/30/2019)*

Asset Class*	Ticker	One Month	2nd Qtr	YTD	12 Mo's	*Annualized* 3 Year	*Annualized* 5 Year
GLOBALLY DIVERSIFIED BALANCED PORTFOLIO**							
60% Equity / 40% Bond	DGSIX	4.4%	2.7%	11.4%	4.1%	7.8%	4.7%
STOCKS							
Larger-Cap	VFINX	7.0%	4.3%	18.5%	10.3%	14.0%	10.6%
Smaller-Cap	NAESX	7.0%	2.9%	19.5%	2.1%	12.3%	7.6%
International - Developed Mkts	VGTSX	5.9%	2.8%	13.3%	0.6%	8.9%	2.3%
International - Emerging Mkts	VWO	5.7%	1.0%	12.4%	3.5%	9.4%	2.3%
Real Estate	VGSLX	1.7%	1.7%	19.3%	12.2%	4.0%	7.7%
Inflation Hedges	*	9.6%	0.3%	12.0%	(7.9%)	6.0%	(2.3%)
BONDS							
U.S. Investment Grade Bonds	VBMFX	1.2%	3.1%	6.1%	7.8%	2.1%	2.8%
Global Bonds	VTABX	1.7%	2.9%	6.1%	7.8%	3.4%	4.3%

** Each asset class is represented by a relevant Vanguard Index fund except for Inflation Hedges where the Morningstar Category average for* ***"Natural Resources"*** *is used. All data is provided by Morningstar.*

** All returns are net of (i.e., after) fund fees, and include reinvested dividends.*

** Past performance is not indicative of future results.*

*** This portfolio is represented by the DFA Global Allocation Fund (60% Equity / 40% Bond) - DGSIX*