Voya Perspectives

Retirement at Risk: The relationship between overspending on health care and retirement readiness

High costs, combined with the complexity of choosing the right plan, can make health care decisions difficult for employees—many of whom are already struggling to save for retirement. Here's what employers and plan sponsors can do about it.

Produced by Voya's Thought Leadership Council and SAVVI Financial LLC.
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Health plan selection: An important decision, made in minutes

Employees make a number of quick decisions during annual enrollment. While selecting options like health care and voluntary benefits, they may be considering the question, "What do I expect to need in the year ahead?" The question they're not likely to be asking, however, is "And what will the impact of this choice be on my savings and spending in retirement?"

After all, most employees are making all of these critical decisions—including their health plan selection—in less than 17 minutes. That's less time than the average streaming service user spends scrolling through their options as they decide what to watch.[1] It's not a lot of time to get to know the nuances of each different plan type, let alone calculate the premium differences, tax implications and benefits of each choice.

The average employee spends just

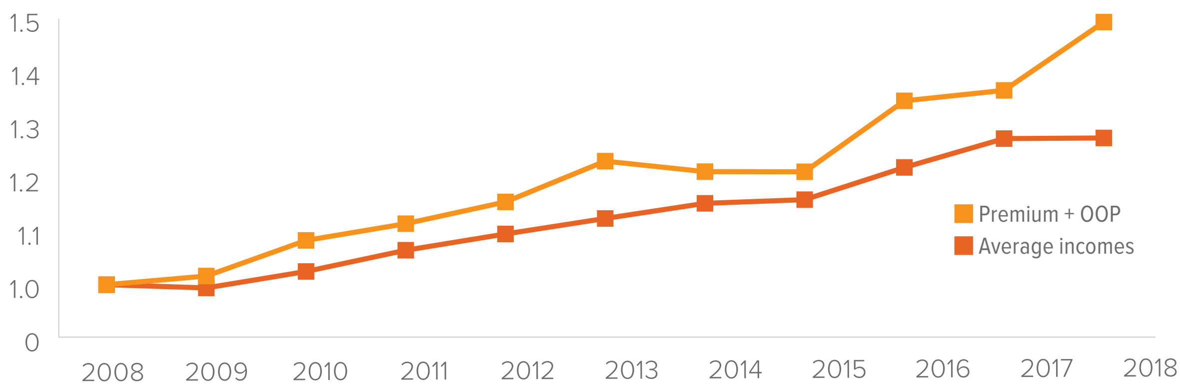
17

minutes enrolling in benefits—including health plan selection, voluntary benefits and more.[1]

The decision they are making is crucial; especially when looked at through the lenses of current financial stress and future financial priorities. According to a recent survey by PwC, finances are their #1 stressor, with 59% of employees reporting that financial or money matters cause them the most stress.[2]

Meanwhile, health care costs are rising twice as fast as incomes[3], putting pressure on how much employees are able to save for retirement.

Health care costs are rising twice as fast as incomes



Source: Medical Expenditure Panel Survey; Agency for Healthcare Research and Quality

[1] Businessolver "What Netflix Can Teach You About How Employees Shop for Benefits," 2018
[2] PWC Employee Financial Wellness Survey, 2018
[3] Based on 2018 data from the U.S. Agency for Healthcare Research and Quality's Medical Expenditure Panel Survey

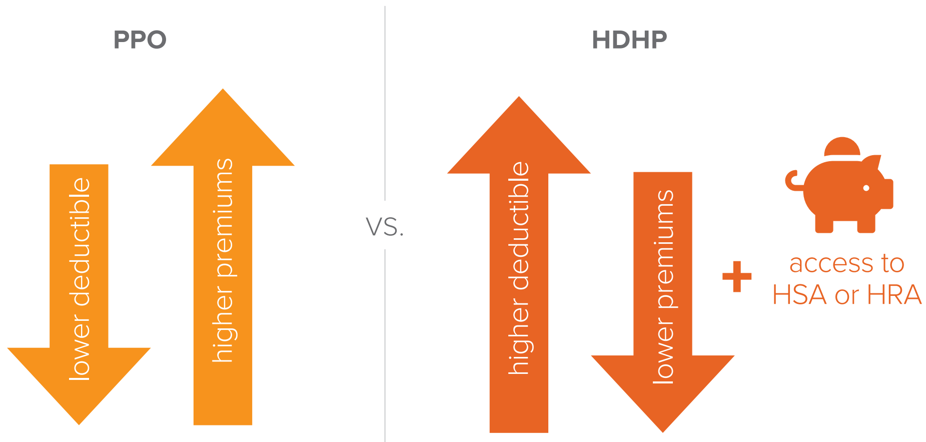
According to data from EBRI's 2020 Retirement Confidence Survey[4], a sizable percentage of workers have just a small amount saved for the future. Among survey respondents providing this type of information, 35% report that the total value of their savings and investments, excluding the value of their primary home, is less than $25,000. This includes 18% who say they have less than $1,000 in savings.

Equipping employees to make wise decisions today could help drive positive outcomes tomorrow. As health care costs continue their rapid rise—health plan selection may be a great place to start.

18% of participants in EBRI's 2020 Retirement Confidence Survey have **less than $1,000** saved for the future[4]

Employees have many factors to consider when choosing a plan

Employees have access to many of types of medical plans through the workplace, but the most common are the Preferred Provider Organization (PPO) and High Deductible Health Plan (HDHP). PPOs tend to have a lower deductible with higher premiums, while HDHPs typically have higher deductibles with lower premiums and can be paired with a savings option like a Health Savings Account (HSA) or Health Reimbursement Arrangement (HRA).

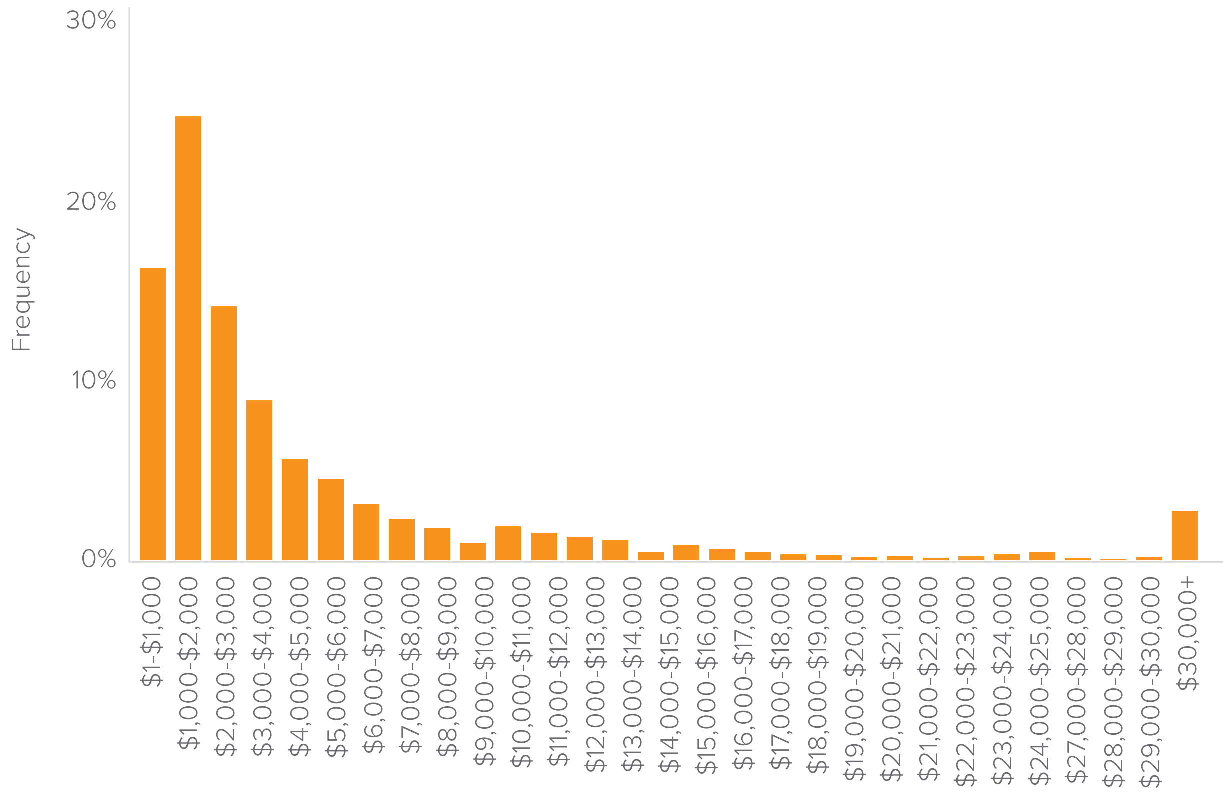


[4] EBRI/Greenwald Retirement Confidence Survey, 2020

In order to understand whether a PPO or HDHP is the best fit for an employee, a number of factors need to be taken into consideration. For example, how likely is it that an employee may need to make a medical claim? What is the out-of-pocket cost for the employee if they do? Is the employer making a contribution to an HSA on behalf of the employee? How would an individual's tax bracket impact their overall savings?

Perhaps the most important of these considerations is the employee's expected health care utilization in the upcoming year. With information like the chart below, which illustrates that in 2018, almost 60% of employees had less than $2,000 in claims, where savings under an HDHP plan are highest—and approximately 16% had no claims at all—employees can gain a starting point in choosing the plan that is the best fit:

Total payments to providers (excluding premiums) for single employees with individual coverage, 2018

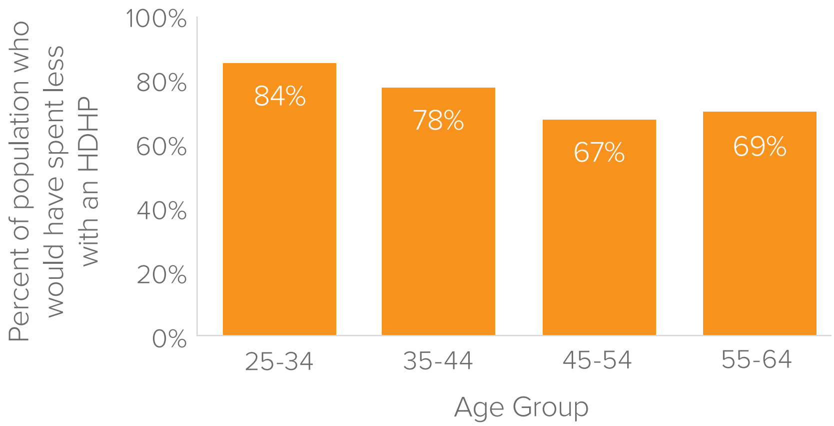


Based on 2018 data from the U.S. Agency for Healthcare Research and Quality's Medical Expenditure Panel Survey.
Analysis completed by SAVVI Financial, LLC.

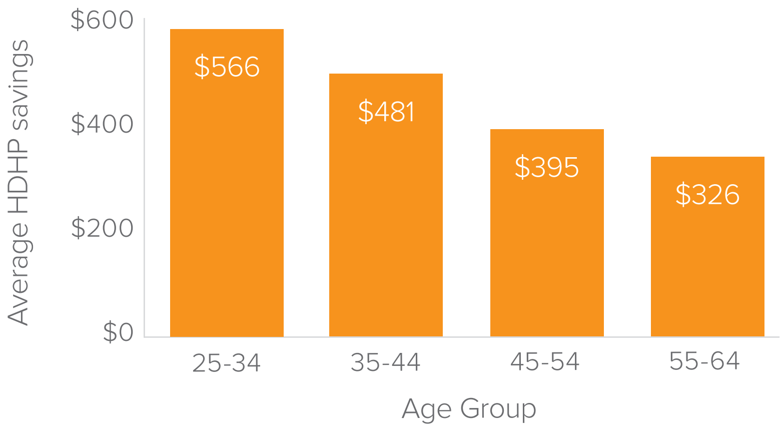
High-deductible health plan (HDHP) or preferred provider option (PPO)?

In order to understand the financial impact of enrolling in a plan that isn't the right fit, Voya teamed up with SAVVI Financial, a leading technology-enabled financial wellness platform, who conducted an analysis using a national database of claims information provided by the U.S. Agency for Healthcare Research and Quality. With that claims data, we could see how employees would have fared financially if they had an "average" (according to data from the Kaiser Family Foundation[5]) PPO or HDHP.

According to the analysis[5], in 2018 a majority of the U.S. population would have spent less on health care costs[6] by choosing an HDHP across a variety of age ranges:



The analysis also showed the average amount individuals would have saved annually[6] by choosing an HDHP over a PPO plan:



While these numbers apply to single employees with individual coverage, when extended to include family groups the analysis showed that the cost savings associated with choosing an HDHP may be even higher. Compounded over time, if this amount were to be saved for retirement, it has the potential to have a significant impact.

[5] The plan designs in this analysis were based the Kaiser Family Foundation's Employer Health Benefits 2020 Annual Survey, which includes data from 2018. This analysis is focused on individuals and individual plan designs, and the HDHP included employer contributions to an HSA that were also based on averages from Kaiser Family Foundation. Results are directional, highlighting a general trend; whether this trend can be replicated within an employer group will depend on the group's plan design.

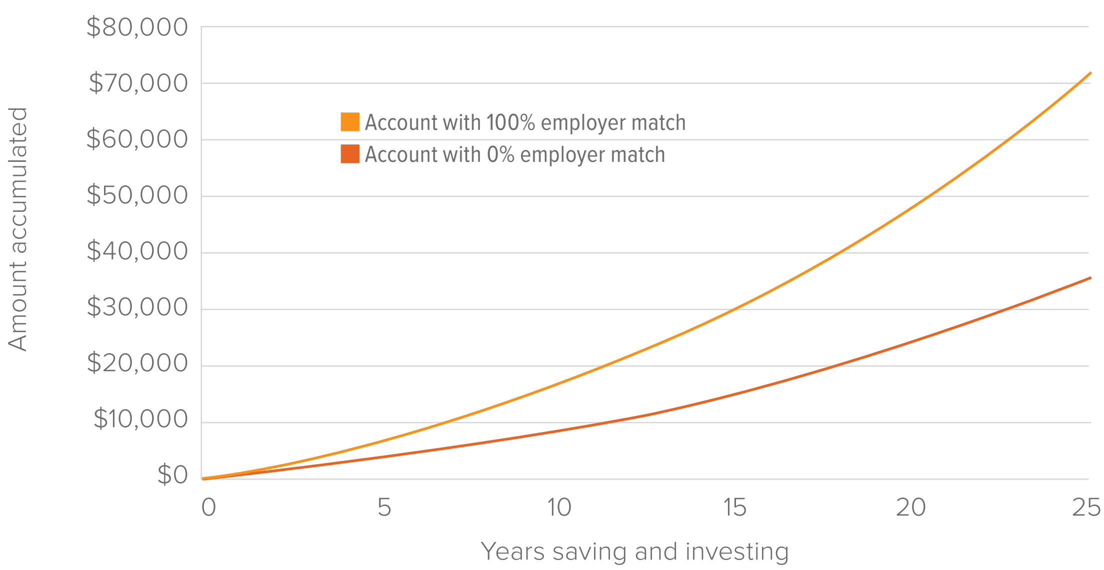
[6] Costs for a PPO plan are calculated as premiums plus out of pocket costs, less federal tax savings from contributing to an FSA to pay out of pocket costs up to current contribution limits. Costs for an HDHP plan are calculated as premiums, plus out of pocket costs, less average employer HSA contribution, less federal tax savings from contributing to an HSA to pay out of pocket costs up to current contribution limits to the extent these quantities exceed employer contribution. Federal tax savings for FSA and HSA are calculated corresponding to a 22% marginal federal bracket and 7.65% FICA payroll tax.

The impact of the optimal plan on future retirement savings

Additional analysis—again, taking into account the types of factors employees must consider, such as whether they have an employer match, whether or not the employee elects to invest their contributions and subsequently how those investments potentially perform, plus the tax implications of how they choose to spend those funds—offers more insight into how a different health plan selection could impact savings for the future.

Here's just one example: The illustration below shows what could happen if a 40-year-old individual retiring in 25 years turned their annual savings from choosing an HDHP over a PPO into annual retirement account or HSA contributions. The individual could have chosen to spend $481 and gotten the PPO, or spent the money on something else. Alternatively, the individual could have improved their retirement savings by taking that $481 and contributing $617 (the pre-tax equivalent assuming the 22% marginal federal tax bracket) to a pre-tax account:

Retirement value accumulation



$27,973

The additional amount a 40-year-old employee could have at retirement in 25 years if they spent $481 less on health care costs each year with an HDHP and made pre-tax contributions toward retirement instead, assuming a 6% return with 0% employer match and a lump-sum withdrawal in retirement.[7]

If employees trade overspending on health care with saving for expenses in retirement, the results could be powerful.

[7] For illustrative purposes only. Assumes annual contributions of $617 to a pre-tax account (which correlates to an after-tax amount of $481 assuming a 22% federal marginal bracket); 6% return on investment, interest compounded annually, no withdrawals; contributions are made and invested at the beginning of each year for 25 years. Does not consider any applicable reduction in payroll tax or FICA if HSA contributions. Does not consider state tax implications. Amounts shown for 100% employer match assume a $617 employer match is received and invested at the beginning of each year. Total amount accumulated after 25 years with 0% employer match equals $35,863. Lump sum withdrawal after 25 years at assumed retirement age of 65, with 22% effective federal tax rate assumed at time of withdrawal, for after-tax value of $27,973 for the 0% employer match accumulation example shown. Assumes funds distributed in this way from an HSA are not used for qualified medical spending which would lead to a reduction in tax. This hypothetical example does not predict or project the performance of any particular investment or investment strategy, does not reflect actual client accounts or experiences, and is not a guarantee of future results. The illustration does not consider investment fees or expenses that would lower performance. Actual rates of return will fluctuate.

The retirement savings shortfall

According to EBRI's 2019 Retirement Security Projection Model®, 40.6% of U.S. households (with the head of household between ages 35-64) are projected to run out of money in retirement.[8]

Many employees choose the less-optimal plan

This modeling is helpful, but most employees don't have the information and calculation skills needed to evaluate their options in this way during enrollment. Even professionals, like economists recently interviewed by the *New York Times*[9], find health plan selection difficult.

And while our analysis showed that 75% of individuals could benefit from selecting an HDHP, statistics from the Kaiser Family Foundation show that only 31% of covered employees are enrolled in one.[10] Whether or not an employee is offered a PPO plan, an HDHP, or some combination of the two varies by firm size—but as research shows, even when both are offered, employees don't always make the optimal choice.

In fall 2020, Voya launched a study[11] to better understand how people make health plan decisions and why they choose the plans that they do during open enrollment. In one part of the study, participants were presented with two different plans, and told to think of them as identical in quality of care, access to care, and all other features beyond cost. The only difference in these two plans was the premiums and deductibles:

PPO Plan	
Deductible	$1,500
Out of pocket max	$5,000
Coinsurance	80%
Employee annual premium	$3,000

High Deductible Plan	
Deductible	$4,000
Out of pocket max	$5,000
Coinsurance	80%
Employee annual premium	$500

When the plans were branded to include the phrase "high-deductible," almost two-thirds of study participants chose the PPO plan, despite the fact that the high deductible plan used in the study scenario was the more optimal financial choice:

In Voya's study scenario[11]					
An employee with...		would spend this much on their deductible	this much on premiums	and this much on coinsurance	for an annual expenditure of
$0 in claims	PPO:	$0	$3,000	$0	$3,000
	HDHP:	$0	$500	$0	**$500**
$1,500 in claims	PPO:	$1,500	$3,000	$0	$4,500
	HDHP:	$1,500	$500	$0	**$2,000**
$4,000 in claims	PPO:	$1,500	$3,000	$500	$5,000
	HDHP:	$4,000	$500	$0	**$4,500**
$50,000 in claims	PPO:	$1,500	$3,000	$3,500	$8,000
	HDHP:	$4,000	$500	$1,000	**$5,000**
Yet 65% of respondents chose the PPO plan.					

[8] EBRI Retirement Security Protection Model®, 2019
[9] "It's Not Just You: Picking a Health Insurance Plan Is Really Hard." The New York Times. December 11, 2020
[10] Employer Health Benefits 2020 Annual Survey, Kaiser Family Foundation
[11] Based on an online survey conducted by Voya Financial, in partnership with Russell Research, between September 2-6, 2020 among 315 U.S. Consumers currently enrolled in an employer-sponsored health plan. For research-related inquiries, email info@russellresearch.com.

Why do many employees choose the less-optimal option?

Voya's research included three key reasons that employees may be choosing health plans that aren't the optimal financial fit: The naming of plans, inertia among employees, and a general aversion to deductibles.

The name of the plan has an influence on enrollment

In this study, the name of the plan had a clear impact on employee choice. In fact, participants were almost twice as likely to choose a PPO plan over an HDHP when the plan was branded to include the words "high deductible" in the plan name. Yet when the plan names were unbranded, the gap was much smaller. Participants were almost just as likely to pick an HDHP (47%) vs. a PPO (53%).[11]

This research aligns with other studies that have been done, such as findings published in the academic journal *Behavioral Science & Policy*[12], which showed the use of labels like Gold, Silver and Bronze in ACA exchanges could be influencing enrollees to choose plans that offered more coverage than they actually needed. When those plan names were changed to generic or medical-use labels, study participants chose plans that were a more appropriate fit.

Many employees prefer to "set-and-forget"

Another key factor in the Voya study was the propensity of employees to simply duplicate their previous year's plan selection. 89% of respondents said they just pick the same health plan from the prior year, especially those currently enrolled in a PPO vs a HDHP. (94% vs. 80%, respectively).[11]

A majority of employees avoid deductibles

Finally, another significant factor in the Voya study was an aversion to deductibles in general. Almost two-thirds of participants (63%) said they pick the plan with the lowest deductible. This applied to those choosing a PPO plan, as well as other plan types represented in the study.[11]

Study participants were almost

twice as likely

to choose a PPO over an HDHP if the plan was branded to include the words "high deductible" in the plan name[11]

94%

of study participants with PPO plans choose the same plan they had in the previous year[11]

80%

of study participants with HDHPs choose the same plan they had in the previous year[11]

63%

of study participants said they pick the plan with the lowest deductible[11]

The cost of focusing on the lowest deductible

A study published in the *Quarterly Journal of Economics* showed the majority of employees at a Fortune 100 company showed deductible bias – choosing the plan with the lowest deductible, despite the premium costs. This resulted in them spending 24% more on health insurance than they needed to, or about 2% of their annual salary.[13]

[11] Based on an online survey conducted by Voya Financial, in partnership with Russell Research, between September 2-6, 2020 among 315 U.S. Consumers currently enrolled in an employer-sponsored health plan. For research-related inquiries, email info@russellresearch.com.

[12] "The Costs of Poor Health (Plan Choices) and Prescriptions for Reform." *Behavioral Science & Policy*, 2017

[13] "Choose to Lose: Health Plan Choices from a Menu with Dominated Options." *The Quarterly Journal of Economics*, Volume 132, Issue 3, August 2017.

Key takeaways

Retirement plan sponsors often see employees struggling to increase their savings and overall financial wellness. At the same time, health care costs are on the rise for both employers and employees. Offering a high deductible health plan with a health savings account could be a solution that effectively addresses each of these challenges.

Voya's analysis showed that, for a majority of employees, it could be important to consider enrolling in this type of plan. Depending on the plan design, time left to save, and rate of return on the health savings account (should employees elect to invest), there is an opportunity for employees to significantly increase their retirement savings.

When given the opportunity to enroll in this type of plan, however, many do not. Plan sponsors may be able to overcome the barriers to enrolling in an optimal plan by taking these steps:

- **Carefully consider the name of the plan.** Our research shows that the "high deductible health plan" label may be a barrier in itself. Consider labeling plans with a more generic (Plan A, Plan B, etc.) or descriptive names.
- **Encourage employees to review each year.** As we found in our research, many employees prefer to roll over their plan each year. Requiring employees to re-enroll each year may help encourage them re-evaluate their options.
- **Help employees explore their own situation.** For employees who prefer to set-and-forget, as well as those who are deductible-averse, it may help to augment the support provided to employees during benefit selection and enrollment with decision support tools. These complex recommendation engines have the potential to help employees quickly and easily evaluate the wide range of factors they need to consider while enrolling in benefits.
- **Show the value of saving the difference.** Express the importance of applying the premium difference toward health care expenses today, as well as health care and other expenses in the future, by putting it into a health savings account. This is an essential step for financial wellness, and an important one for employees to take.

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