Wednesday, November 11, 2020

The Healthcare Puzzle

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By Kim Painter

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As many people nearing or past their 65th birthdays can attest, you haven't really experienced the byzantine nature of the nation's health insurance system until you face signing up for Medicare, the federal insurance program for seniors.

The complexity of a system that contains an alphabet soup of parts may come as no surprise. But the costs of health care in retirement might come as a shock.

"A lot of people think that, once they retire, they are going to go on Medicare and they'll pay nothing out of pocket," says Ted Lew, a CAPTRUST vice president and financial advisor based in San Ramon, California.

The truth: Healthcare costs in retirement are significant and should be a major part of your financial planning, Lew and other experts say.

Yet, a survey from the Insured Retirement Institute found that just 25 percent of people aged 56 to 72 in 2019 had factored healthcare costs into their retirement savings plans. The number was a little better, 48 percent, among those consulting with financial advisors.

The number one reason for leaving health care out of planning was the misperception that Medicare would cover everything, the survey found. And the number two reason for lack of planning was uncertainty about how much health care might cost.

How Expensive Is It?

Cost estimates vary. One calculation, from Fidelity Investments, found that a 65-year-old couple retiring in 2020 could, over their lifetimes, expect to pay $295,000 in current dollars for insurance premiums, co-pays, and out-of-pocket expenses, not including non-prescription drugs or most dental services.

HealthView Services put the lifetime bill for the same couple at $387,644 in 2019, with a calculation that included some additional expenses, such as hearing, dental, and vision care. Neither estimate included the costs of long-term care, which can be substantial and are not covered by Medicare.

As of 2019, a private room in a nursing home cost a median of $8,500 a month, and a home health aide cost more than $4,000 a month, according to Genworth, an insurance company.

“People can experience a bit of sticker shock” when they read such numbers, says Matthew Rutledge, a researcher at the Center for Retirement Research at Boston College.

In a paper published in 2019, Rutledge and a colleague reported that people over age 75 spend an average of 20 percent of their annual incomes on out-of-pocket healthcare costs. They concluded that, while most people can manage those costs, the picture becomes more worrisome when long-term care is included—and when those with the greatest healthcare needs are considered.

Using data that included long-term care, they found that, at ages 75 to 84, the top 10 percent of spenders needed more than half of their incomes for health care; at ages 85 and over, the top 10 percent needed 142 percent of their incomes to cover health costs.

“It gets scary when you are in the top five to ten percent,” Rutledge says.

Of course, no one knows whether they will end up as a big spender, needing years of support after developing dementia, frailty, or other costly problems.

But here’s an important consideration: If you are quite healthy in your mid-life and early retirement years, you are likely to spend more than your unhealthy peers.

“It’s a surprising fact,” Rutledge says. “We tend to think that the unhealthy ones will be the big spenders, but they tend to die sooner, so they don’t spend as much.”

HealthView Services provides this example: A healthy 55-year-old woman can expect to live to age 89, paying $13,165 a year for health care, while a 55-year-old woman with type 2 diabetes can expect to live to age 80, spending $16,635 a year. That nine-year gap in life expectancy means the healthy woman will spend $424,875, while the woman with diabetes spends $266,163.

Such calculations are no reason to give up healthy habits. But they are a reminder that even the healthiest among us need to plan for substantial costs.

The Medicare Decision

Ready or not, at age 65, most people face a decision: whether to sign up for Medicare. Usually, the answer should be yes, says Sarah Murdoch, director of client services at the Medicare Rights Center, a nonprofit advocacy and education group.

That’s because you could face costly penalties and gaps in coverage if you do not sign up when you become eligible for Medicare Part B, the part that covers most routine care and requires premiums, she says. That initial eligibility period spans the three months before and three months after your 65th birthday.

If you are working for and insured by a large employer, you don't have to sign up for any part of Medicare until you leave your job. That also goes for your covered spouse.

Just about everyone else needs to take action. That includes people without health insurance, but also those with individual policies, retiree coverage, COBRA policies, or coverage from an employer with fewer than 20 workers, Murdoch says. Those policies no longer have to act as your primary insurance once you are eligible for Medicare, meaning they could stop covering your bills.

That's not all. If you sign up for Medicare Part B late, you pay higher premiums for the rest of your life. You also can expect to wait months for coverage to kick in.

"It is really important for people to know their timelines," Murdoch says. "We see people making truly innocent mistakes all the time, and it can have sad consequences."

When you do sign up, you face another choice. Your first option is to stick with traditional Medicare, with its core Part A (hospital) and Part B (doctor and outpatient) coverage. The alternative is Medicare Advantage, coverage from a private insurer that combines Parts A and B, often with additional benefits. Medicare Advantage typically restricts you to a network of providers.

The best choice varies, Lew says. He says some clients go for traditional Medicare because they have doctors who don't participate in an Advantage plan or because they are retiring in an area with few or no network providers. Others like the one-stop shopping of a network plan.

> *If you do choose traditional Medicare, be sure to add a supplemental Medigap plan. That's because traditional Medicare puts no cap on out-of-pocket costs, but all supplemental policies do.*
>
> *Ted Lew, Financial Advisor*

But buyer beware: While your mailbox may overflow with pitches from supplemental insurers, you can get better information at *medicare.gov*, Lew says.

Tailoring a Plan for You

When Doug and Teresa Wright started retirement planning a few years ago, the couple realized they would face some new costs when Doug left his job that provided health insurance for both of them. They would have to pay Medicare premiums for Doug and buy individual coverage for Teresa, who is a decade younger.

"When I worked, I didn't pay anything," says Doug, 65, now retired from his job as vice president of a Silicon Valley manufacturing company. The couple now pays about $1,000 a month just for premiums, mostly for Teresa, "but we planned for that," Teresa says.

Planning for such individual circumstances is crucial, Lew says. How much you need for health costs can vary widely, depending on factors ranging from your health history to where you plan to live. For example, if you live outside the country, you won't be able to use Medicare while abroad.

How you save for retirement healthcare expenses can also vary. One increasingly popular choice is to fund a health savings account (HSA) while you are still working. The accounts are not available to everyone—you can only contribute if you are enrolled in a high-deductible health insurance plan. But, if you are eligible, it's smart to open an HSA as soon as possible, Lew says, because the accounts "have a triple tax advantage." Contributions, earnings, and withdrawals for eligible health expenses are all tax-free.

Many people also consider buying long-term care insurance, but that can be a difficult decision, Lew says. Generous, affordable policies available years ago turned out to be a bad deal for insurers, who "lost their shirts," he says. As a result, "the current policies tend to be very pricey," but some people will find them worthwhile, he says.

An alternative is to set apart some money as a self-insurance pot for long-term care, says Lew.

In the end, he says, health isn't just one more thing to consider in your retirement planning—it may be the most important thing.

"If you don't have your health," he says, "nothing else really matters."

Ready for Medicare?

If so, you need to know your ABCs and D—the major parts of the government health insurance plan for people over age 65 (and for some younger disabled people).

PART A | Hospital Coverage

This covers hospital stays, hospice care, and some short-term skilled nursing care—such as when you need a rehabilitation center after you've been hospitalized for an illness or injury.

Most people don't pay premiums for Part A because they've already paid for it through payroll taxes. But you still pay deductibles and co-pays for certain services. The 2020 deductible for a hospital stay is a hefty $1,408. Many people buy supplemental Medigap policies to help cover such costs.

PART B | Doctor and Outpatient Services

This covers doctors' bills, outpatient lab tests, preventative services, mental health visits, ambulance transport, and some medical supplies.

You pay a premium for Part B. The 2020 rate is $144.60 for people with individual annual incomes up to $87,000. Those with higher incomes pay more—as much as $491.60. There's also a modest annual deductible and a 20 percent co-pay for many services.

PART C | Medicare Advantage

This is not really a third part of Medicare. It's private insurance that covers everything in Medicare's Parts A and B. These plans often cover services, such as routine vision, hearing, and dental care and fold in prescription drug coverage. You may pay an added premium on top of your Part B premium.

These plans are generally run by health maintenance organizations (HMOs) or preferred provider organizations (PPOs) that restrict you to network providers. Costs and coverage vary. Some rural areas have no Medicare Advantage providers; some urban areas have dozens.

PART D | Prescription Drug Coverage

You buy this coverage through a private insurer, as part of a Medicare Advantage plan or in addition to traditional Medicare Parts A and B.

These plans generally come with premiums and other out-of-pocket costs, which can include deductibles and co-pays. Different plans cover different medications, so it's crucial to check their drug lists—called formularies—through *medicare.gov* for any medications you take regularly. This coverage can be invaluable given the high prices of many medications.

To Learn More: In addition to *medicare.gov*, you can get free counseling from the Medicare Rights Center at 800.333.4114. The center also offers Medicare Interactive, a free online reference tool for consumers, and Medicare Interactive Pro, paid online courses for professionals.

Have questions? Need help? Call the CAPTRUST Advice Desk at 800.967.9948 or schedule an appointment with a retirement counselor today.