

Boomer Angle™

April 2014



Health Care Costs in Retirement

When you are planning for retirement one of your most important, and also potentially most variable, expenses will be health care costs. This will also be one of your largest expenses.

Some people make the mistake of ignoring health care costs as they make their retirement income plan. Others make woefully inadequate estimates. A new study of almost 2000 adults by Fidelity Investments found that 48% of respondents estimated they would spend \$50,000 per person for health care in retirement, a low number by most published research.

Different organizations publish estimates of health care costs in retirement. Prominent among these are the Employee Benefit Research Institute (EBRI) and Fidelity Investments. There is also an annual Consumer Expenditure Survey published by the US Government Bureau of Labor Statistics which summarizes total reported household spending including health care spending. Each study expresses their results somewhat differently adding a bit of confusion for the average person trying to plan for retirement.

Fidelity recently completed their 2013 Retirement Assessment Survey of almost 2300 households. In it they reported that the estimated retirement health care costs for a 65 year old couple retiring this year are approximately \$220,000.

Interestingly, Fidelity's estimate has dropped over the last three years from a high of almost \$250,000 in 2010. They attribute this drop to both lower utilization of health care and smaller payment increases to providers.

The Employee Benefit Research Institute (EBRI) produces in-depth numbers. Unfortunately the results are hard for many people to understand since they express their estimates in terms of median drug expenses, percentiles of drug expenditures and probabilities of success. Ouch!

Nevertheless, here goes....EBRI estimates a lifetime retirement health care spending of \$158,000 for a 65 year old couple retiring in 2010 or \$265,000 for the 65 year old couple retiring in 2020. However, these estimates represent only average drug expenses and only a 50% probability of success. If you need to plan for higher than average drug expenses or like your probabilities better than 50% think at least \$250,000 for that couple in 2010 or \$427,000 in 2020 for lifetime costs.

But what do you do with a \$250,000 lifetime sticker price? It very hard for many people to put such a large number into any practical context beyond causing stress and confusion. Yearly estimates, on the other hand, are something you can get your mind around and work into an annual budget.

The Consumer Expenditure Survey, in fact, reports health care spending in annual, not lifetime, amounts. Their 2012 survey, which is annually updated, finds that a 65 year old couple today will need approximately \$10,400/ year. Curiously they also find that reported health care costs are lower for people 75+, approximately \$9400/year.

I thank you God for this most amazing
day: for the leaping greenly spirits of
trees
and a blue true dream of sky; and for
everything
which is natural which is infinite
which is yes.

- e.e. cummings

All of these estimates come with important provisos. They vary by geography and income level (if you have more money you spend more on health care). Beyond that, there are three important caveats to these estimates: life expectancy, other costs and inflation.

1) Longevity - Most estimates presume average life expectancies of approximately 82 for men and 85 for women. If you are healthy or have known longevity in your family, congratulations on a longer expected lifespan, however you must pad the numbers accordingly.

2) Other Costs - These estimates typically include neither long term care costs for late life health and personal care nor do they include dental costs.

3) Inflation - Most confusingly, the lifetime spending estimates are based on how much you would need to have saved for health care cost by the time you retire at 65 not the literal dollar amounts you will spend as couple over your 20+ years of retirement. In other words, you need to remember inflation.

The size of these numbers can be shocking. Can they possibly be reasonable estimates? I think they are. Consider the three most common health care costs for people who are on standard Medicare.

- Medicare B copayments (automatically deducted from Social Security payments)
- Medigap Insurance
- Medicare D (also deducted from Social Security).

If you are on Medicare C (Medicare Advantage) the cost estimates will be different.

Medicare B covers all physician costs. Most people are paying around \$110/month today (\$220 for a couple.) For highest income level individuals this cost goes up. Medicare Supplemental Insurance (a.k.a. Medigap Insurance) averages about \$175/month for one person (\$350 for a couple). Medicare D (drug coverage) is approximately \$50/month for one (\$100 for a couple).

The total of these three together are \$670/month or \$8040/yr. Add on out-of-pocket drug costs and out-of-pocket dental costs and you are snugly in the neighborhood of \$10,000/year for an average couple at today's prices.

Are there ways to lower these costs? It may be possible to skimp on some drug coverage costs. There is less expensive Medicare Advantage coverage which could limit your doctor choices. One might travel to Mexican border town to get dramatically cheaper dental work. However, for most couples, \$8,000 - \$10,000/year, inflated for future years, is a reasonable

Social Security Blog



[WEP Ahead: Public Sector Workers May be Surprised at Social Security Reductions.](#)

[Social Security Deficits: Fact or Fiction](#)

(Click on links or go to Financial-Planning.com and search "norr".)

planning number to use for retirement health care expenses.

Although this may seem like a surprisingly high number, many families today don't realize that they spend close to that amount annually for groceries.

Even though these costs may be surprising, one will be better prepared for the future by squarely looking at these numbers and planning how to manage them rather than by ignoring them and simply hoping things work out.

Boomer-Angletm

Life, Retirement and Financial Planning for the Boomers and beyond.

Paul Norr, CFP®

www.paulnorr.com

pauln@bcfpg.com

Financial Planning and Investment Advisory Services offered through Bucks County Financial Planning Group Inc., a fee-only Registered Investment Advisor.

Bucks County Financial Planning Group

Offices in Westlake Village, CA and Bucks County, PA