



A Guide to Health Care Costs in Retirement

Although health care is one of the biggest expenses for retirees, your clients may greatly underestimate its cost. Some may even believe that Medicare will cover most of their health care needs—when the financial reality is far different. So, how can you help your clients develop a successful retirement income plan and execute that plan in the way your clients intend?

To answer this question, you can begin by analyzing the variety of potential health care costs, as well as incorporating solutions for paying those costs into your clients' plans.

Known versus unknown

When it comes to health care, there are both known and unknown costs. **Known costs** include Medicare, Medigap, and long-term care premiums. **Unknown costs** include Medicare co-pays, out-of-pocket costs, uncovered prescription medication costs, dental and vision costs, and uncovered long-term care costs. Just how costly these expenses could be for your clients depends on various factors.

What factors affect health care costs in retirement?

- 1 Inflation.** Historically, health care costs have outpaced both the rate of inflation (2.5 percent over the last 10 years) and social security increases (typically around 2 percent per year). According to the U.S. Bureau of Labor Statistics, health care increases have averaged more than 5 percent per year over the past 10 years.
- 2 Longevity.** Healthier people have a longer life expectancy, resulting in many more years of health care expenses. Although this may sound counterintuitive, healthier people need long-term care services much more frequently than do unhealthy people. Longevity, which is often considered a desirable condition, actually complicates the health care picture: Super-elderly individuals (those in their 90s and 100s) are most likely to deal with expensive long-term care and end-of-life heroic measures. Women, with their greater longevity as compared with men, are also particularly susceptible to high medical expenses in the last years of life.

To illustrate this point, [Fidelity Investments](#) estimates that a 65-year-old couple retiring today will need \$260,000 to cover future medical costs through age 85. This includes premiums, deductibles, co-pays, and miscellaneous out-of-pocket expenses but does *not* include long-term care. Another study by [HealthView Services](#) finds that a 66-year-old couple retiring this year with average social security benefits can expect medical costs to consume 67 percent of the benefits they will receive in retirement. As previously mentioned, however, the super-elderly typically incur the greatest costs, so these projections understate the problem.

What does Medicare cover, and how much does it cost?

Medicare Details	What's Covered	What It Costs
Part A (hospital insurance)	<ul style="list-style-type: none"> In-patient hospitalization Short-term skilled nursing facilities 	<ul style="list-style-type: none"> No monthly premiums, deductible, daily co-pays for first 150 days of treatment
Part B (medical insurance)	<ul style="list-style-type: none"> Doctor services Preventive services Durable medical equipment Outpatient services 	<ul style="list-style-type: none"> Monthly premiums Yearly deductible Co-pays
Part D (prescription drugs)	<ul style="list-style-type: none"> Plans offered by private insurance companies approved by Medicare Covered drugs vary by plan 	<ul style="list-style-type: none"> Monthly premiums Yearly deductible Co-pays
Part C (Medicare Advantage)	<ul style="list-style-type: none"> Offered by private insurance companies approved by Medicare Includes Parts A and B Most plans include Part D May cover hearing, dental, and vision 	<ul style="list-style-type: none"> Monthly premium for Part B Deductibles and co-pays
Medicare Supplemental (Medigap plans)	<ul style="list-style-type: none"> Covers services not covered by Medicare, including co-payments, coinsurance, and deductibles While Medigap policies are optional, you must have Medicare Parts A and B to purchase a Medigap policy 	<ul style="list-style-type: none"> Average cost nationwide is \$185 per month Actual cost varies by carrier, age, and geography

Average Minimum Monthly Medicare Premiums*	
Part A	\$0
Part B	\$121.80
Part D	\$33.13
Medigap	\$185.00
Total per person	\$339.93 (\$4,079 per year)
Total per couple	\$679.86 (\$8,158.32 per year)

*Based on a 65-year-old who made less than \$85,000 in 2014 (the year 2016 premiums are based on). Premiums may be higher for individuals and couples with higher incomes.

Parts B and D. Medicare Parts B and D premiums are now means-tested. If your clients have a modified adjusted gross income (which includes social security, required minimum distributions, and capital gains) above \$85,000 (individual) or \$170,000 (married filing jointly), Part B and Part D premiums will be higher. Those higher premiums can range from \$170.50 to \$389.90 per month for Part B. Part D premiums can cost up to an additional \$72.90 per month over the regular plan premium.

Medicare prescription drug plans. Most of these prescription drug plans have a coverage gap known as the “donut hole,” meaning there is a temporary limit on coverage. The coverage gap begins after an individual has spent a certain amount for covered drugs. In 2016, once your client and his or her plan have spent \$3,310 on covered drugs (the combined amount plus deductible), that individual will be in the coverage gap. Once in the coverage gap, your client will be required to pay 45 percent of the plan’s cost for covered brand-name prescription drugs. (**Please note:** The Affordable Care Act has helped people in the donut hole get discounts on prescriptions.)

Medigap. A Medicare supplement insurance policy, sold by private companies, can help your client pay some of the health care costs that Medicare doesn’t cover, such as co-payments, coinsurance, and deductibles. But Medigap policy premiums can vary greatly depending on where a person lives, the carrier, and plan—with average premiums of \$185 per month. To find more information on Medigap plans and premiums by ZIP code, go to <http://medicare.gov/find-a-plan/questions/medigap-home.aspx>.

Out-of-pocket costs

When it comes to evaluating the costs of health care in retirement, premiums are just part of the picture. Although Part A has no premium, the deductibles and co-payments can be steep. For example, if your client is hospitalized, there is a \$1,288 deductible for each benefit period:

- Days 1–60: No coinsurance
- Days 61–90: \$322 per day co-pay
- Day 91 and beyond: \$644 per day co-pay per each “lifetime reserve day”

Lifetime reserve days are additional days that Medicare will pay for when an individual is in the hospital for more than 90 days. Everyone is entitled to a total of 60 reserve days that can be used during their lifetime. Beyond lifetime reserve days, your client will be responsible for all costs.

- For skilled nursing facility stays, your client will have the following costs:
 - Days 1–20: No cost
 - Days 21–100: Coinsurance cost of \$161
 - Day 101 and beyond: Patient responsible for *all* costs (There is no payment for custodial care.)

Let's look at how these costs can vary based on length of stay:

Example 1. Your client spends **7 days** in a hospital followed by **30 days** in a skilled nursing facility for rehabilitation:

Hospital stay	=	\$1,288.00 (deductible)
Skilled nursing	=	<u>\$1,449.00</u>
Total	=	\$2,737.00

Example 2. Your client spends **70 days** in a hospital followed by **100 days** in a skilled nursing facility for rehabilitation:

Hospital stay	=	\$4,186.00
Skilled nursing	=	<u>\$11,109.00</u>
Total	=	\$15,295.00

As you can see, if your client ever requires long-term care, the cost can be significant.

Cost of long-term care

When estimating the potential cost of long-term care, consider the annual median rates for the nation:

Home health care	\$51,308
Adult day care	\$24,820
Assisted-living facility	\$45,536
Nursing home (semiprivate room)	\$82,125
Nursing home (private room)	\$92,345

Be aware, however, that these are the *median* costs. Your clients should expect the actual costs to be much higher if they live in a large city (e.g., Boston, New York, Los Angeles):

	Boston	New York	Los Angeles
Home health care	\$59,484	\$50,336	\$51,480
Adult day care	\$17,676	\$49,400	\$18,850
Assisted-living facility	\$74,400	\$17,304	\$48,000
Nursing home (semiprivate room)	\$137,244	\$164,250	\$83,220
Nursing home (private room)	\$146,004	\$164,250	\$108,036

Source: Genworth 2016 Cost of Care Survey

Long-term care insurance

Given these potential costs, one option your clients have to mitigate the potential risk is to purchase long-term care insurance. Premiums will vary based on age, gender, state of residence, health, and coverage levels. Typical premiums for a 60-year-old couple range from \$4,000 to \$6,000 per year. Linked-benefit long-term care involves repositioning an existing asset into the policy, which will provide a death benefit and long-term care benefits.

Potential solutions

One of the more popular options in planning software is MoneyGuidePro®. Specifically, its Health Care SMART Goal module can be used to monetize health care costs for your client. Once these potential costs have been determined, you can then discuss the various financial solutions that could best meet their needs. For example:

- **Known costs** can be met using social security, pensions, annuities, and income from investments.
- **Unknown costs** can be met using annuities, long-term care insurance, and linked-benefit long-term care products, which combine life and annuity vehicles with long-term care benefits.

The takeaway

Health care costs are high and must be factored into your client's budget and retirement income plan. If you are knowledgeable about these costs, you'll be well positioned to counsel clients on the facts and solutions. In turn, you will bring value to every client relationship by providing true, holistic planning that protects all parties.



Founded in 1979, Commonwealth Financial Network, member FINRA/SIPC, is the nation's largest privately held independent broker/dealer-RIA, with headquarters in Waltham, Massachusetts, and San Diego, California. The firm supports more than 1,650 independent advisors nationwide in serving their clients as registered representatives, investment adviser representatives, and registered investment advisers, as well as through hybrid service models. For more information, please visit www.commonwealth.com.

Waltham Office
29 Sawyer Road
Waltham, MA 02453-3483
Toll-Free: 866.462.3638
Phone: 781.736.0700
Main Fax: 781.736.0793

San Diego Office
110 West A Street, Suite 1800
San Diego, CA 92101-3706
Toll-Free: 866.462.3638
Phone: 619.471.9700
Main Fax: 619.471.9701

commonwealth.com
Commonwealth Financial Network®
Member FINRA/SIPC