Health Care Costs for Retirees—A Scary Story

Fidelity Investments made a detailed analysis of the amount of money a couple would have to save to pay for health care costs if they retired at 65 with deaths occurring after 17 years for the male and 20 years for the female.   They used a first year cost of $10,500 and escalated those costs to $25,000 after 15 years. This equates to a 6.4% inflation rate for health care. Then Fidelity calculated that it would take $240,000 savings to pay for the health care costs. (This requires a return on investment of 3.8% by my calculations.)   A projection of results for this case is shown in the attached figure. In our 23 years of retirement, we have spent more than $240,000, and our annual medical costs exceed $10,500.

The costs of $10,500 per year may be reasonable for most income recipients of Medicare paying about $112 per month per person for Medicare Parts B this year (Part B covers 80% of doctors' bills) plus Part D (for partial payment of drugs) plus $500 per month for a group Medigap policy for a couple plus about $1,800 a year for uninsured costs to round out Fidelity's $10,500.   Medicare premiums depend on income and increase each year at a rate higher than the CPI inflation rate. Higher income people pay up to $286 per month per person for Parts B and D of Medicare.   These costs go up almost every year. "Means testing" is being proposed as one way to reduce the Medicare deficits. It could mean increasing premiums, taxing the benefits and/or reducing benefits, each depending on income.

Medigap insurance costs are substantially lower for a 65 year old than an 80 year old. $500 per month is an in between ballpark number.   There are many choices for Medigap policies including a type in which the patient pays $2,000 per year (in 2012) before the insurer pays anything.   A Medigap policy may pay 80% of the part not paid by Medicare.

Uninsured costs include drug copayments and that part of doctor and hospital bills not covered by Medicare and Medigap policies. They also include all dental costs as well as most eye and ear costs because most of these are not covered by either Medicare or most Medigap policies. And, of course, there is no provision for long-term-care costs which might be $250 for each day of care required. (A long-term-care policy might cost $3,500 per year to cover about $150 a day starting after 90 days of long-term-care, but these rates are changing rapidly and fewer insurers are offering such policies.)

Of course more savings would be required if the male lived to more than 81 years old and the female past 84 years.   If they each lived five more years, the amount of savings would have to be $326,000 per my calculations using similar assumptions to those that produced Fidelity's results. (See attached figure.)   My own father lived to 96, fifteen more years than Fidelity's 81 year old man. If the object is to avoid getting on Medicaid and its debilitating requirements to spend down assets, then people have to plan on living longer than the average person. Fidelity's assumptions would suggest that at 65 we would need over a half-million dollars stashed for health care were I to live as long as my father.

There are many other estimates of how much should be saved for health care. A study in 2011 showed that these varied widely, depending on the assumptions. http://www.hvsfinancial.com/2011/05/health-care-costs-fidelity-ebri-reality-check-2. You can make your own estimate of the impact of health care costs by using the Special Events tab on the Pre and Post Retirement Planner from www.analyzenow.com as well as see the effects of both good and bad economic conditions.

The really big problem is for those who retire earlier than 65. Medicare premiums do not include the cost of any hospital care because the taxpayers pay for most of the hospital costs under Part A of Medicare which is largely free under Medicare—except for any uninsured hospital costs which can be substantial in some cases. For that reason, those who retire before age 65 have to get private health insurance that includes hospital care.   A typical policy might cost $28,000 a year for a couple and still does not cover dental, eye or ear care. Such a policy might have deductibles of $350 a year and copayments of $5 for drugs, $15 per doctor appointment and $50 for each emergency room visit. The total annual cost including the uninsured care for the first year might be close to $30,000.

The savings required for health care is brutal when retiring early. For example, retiring at age 60 could incur total costs close to $427,000 if the male lives to just 81 and the female to 84 as in the Fidelity example. (See attached figure.) Obviously, living longer could easily require much more than a half million dollars for medical care as could retiring earlier than 60. Retiring under Medicare is costly, but retiring before Medicare kicks in is often prohibitively expensive for a retiree.

That said, retiring before 65 without any medical insurance can be even more brutal. Dental problems and uninsured drug costs can mount up in the thousands, emergency care in the tens of thousands, and hospital stays in the hundreds of thousands. That's why health insurance costs so much before 65. We know people who have tried to get by without medical insurance for a couple of years who have been devastated by the resulting financial outcomes. You don't want to end up having to retire with little savings left.

In addition to the cost issues, there's another fundamental problem. It's very difficult to find a doctor who will take Medicare patients in many locales. The difficulty of finding Medicare doctors and long queues for appointments has encouraged many people to use "concierge" doctors. A common work load for general practitioners is about 3,000 patients. Concierge doctors take on as few as 300 patients and come at a price of perhaps $5,000 per couple per year in addition to their Part B and D costs. The doctor shortage will grow because of the decline in medical students willing to go into general practice or geriatrics because specialty pay is so much more. It is estimated that there will be a deficit of 45,000 primary-care doctors in ten years. (Kiplinger's Personal Finance, 7/12) At 3,000 patients per doctor, that's less care for about a third of our population.

The cost of medical insurance beyond what Medicare pays is quite variable. We have some friends on the concierge level, many more friends who pay something over $500 a month per couple for a Medigap policy, and some who live in an area where an HMO costs only several hundred dollars a month over their Medicare premiums. We also have several friends who now have little savings, do not have a Medigap policy and qualify for Medicaid.

Dental costs are almost always extra costs and vary widely—mostly by the condition of one's teeth. Root canals, crowns and implants are very expensive, yet are standard fare at some point for the majority of our friends. Several of our California friends go to Mexico for anything other than their regular teeth cleaning and get the work done at much lower prices.

The amount of uninsured care varies a great deal, and not just because of the difference in fine print in a Medigap policy. My wife and I are in our late seventies, many of our friends are in their eighties and some in their nineties. Some have had heart attacks, strokes, hip and knee replacements, all kind of abdominal problems, arthritis, cataracts, macular degeneration, hearing aids, and even one who has felt the wrath of flesh eating disease.

Yet the majority of these are very active people, many of which golf, ski, play tennis, hike and regularly use a bicycle, treadmill or elliptical. I know that keeping both mentally and physically active is extraordinarily important, not just in keeping medical costs low, but in the quality of life we enjoy. Some of our most active friends with whom we ski and golf are in their eighties, have hip and knee replacements, have gone through bypass surgery, and other major problems including the survivor of the flesh eating disease. My wife and I ski seventy to eighty days a year many times with our older friends, adult children, thirteen grandchildren and their spouses. We look forward to teaching our great grandchildren how to ski as well in a couple of years.

Of course some of our friends are in assisted care facilities and nursing homes after valiant service by their spouses to keep them at home. Alzheimer's and serious strokes are devastating. Worse may be broken backs and subsequent almost complete paralysis as has happened to two of our friends. These are the things that long-term-care insurance can help ease financial pains, but long-time-care is one of the most uncertain of all insurance bets and has caused many insurers to drop out of the field. Also, the

great increase in premium costs has forced many subscribers to drop their insurance both because of the difficulty of funding the premiums and because they may see that they won't be able to even afford the remaining uninsured costs.

Health care costs have to be one of the most important drivers in determining how much retirement savings we need. Yet such costs are dependent on many unknowns including future inflation, returns, taxes, how the government will change Medicare to solve its underfunding problem, individual health conditions during retirement, and how long we will live. A combination of prudent choices of insurance and individual savings is likely to make a huge quality-of-life difference in what may exceed a quarter of our lifespans. We'll never find the perfect solution for the events we will encounter during retirement, but this is not an area to be financially optimistic in my view.

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Analysis on the page that follows:

Fidelity case for couple retiring at 65 when Medicare starts.

	Health Costs			Balance
Age	Him	Her	Total	240,000
65	5,250	5,250	10,500	238,333
66	5,586	5,586	11,171	235,919
67	5,943	5,943	11,885	232,687
68	6,323	6,323	12,645	228,559
69	6,727	6,727	13,453	223,452
70	7,157	7,157	14,313	217,278
71	7,614	7,614	15,228	209,938
72	8,101	8,101	16,202	201,331
73	8,619	8,619	17,238	191,344
74	9,170	9,170	18,339	179,859
75	9,756	9,756	19,512	166,748
76	10,380	10,380	20,759	151,872
77	11,043	11,043	22,086	135,085
78	11,749	11,749	23,498	116,228
79	12,500	12,500	25,000	95,131
80	13,299	13,299	26,598	71,612
81	14,149	14,149	28,298	45,476
82		15,054	15,054	31,850
83		16,016	16,016	16,731
84		17,040	17,040	0

3.8% Return
6.4% Health Inflation

Retire at 65 but live five years longer.

	Health Costs			Balance
Age	Him	Her	Total	326,222
65	5,250	5,250	10,500	327,800
66	5,586	5,586	11,171	328,752
67	5,943	5,943	11,885	329,013
68	6,323	6,323	12,645	328,510
69	6,727	6,727	13,453	327,164
70	7,157	7,157	14,313	324,891
71	7,614	7,614	15,228	321,601
72	8,101	8,101	16,202	317,195
73	8,619	8,619	17,238	311,568
74	9,170	9,170	18,339	304,606
75	9,756	9,756	19,512	296,189
76	10,380	10,380	20,759	286,184
77	11,043	11,043	22,086	274,450
78	11,749	11,749	23,498	260,837
79	12,500	12,500	25,000	245,181
80	13,299	13,299	26,598	227,308
81	14,149	14,149	28,298	207,030
82	15,054	15,054	30,107	184,146
83	16,016	16,016	32,032	158,440
84	17,040	17,040	34,080	129,681
85	18,129	18,129	36,258	97,620
86	19,288	19,288	38,576	61,991
87		20,521	20,521	43,417
88		21,833	21,833	22,807
89		23,228	23,228	0

Retire at 60, Private Insurance till 65

	Health Costs			Balance
Age	Him	Her	Total	426,932
60	15,000	15,000	30,000	412,431
61	15,959	15,959	31,918	395,431
62	16,979	16,979	33,958	375,713
63	18,064	18,064	36,129	353,041
64	19,219	19,219	38,438	327,164
65	7,157	7,157	14,313	324,891
66	7,614	7,614	15,228	321,601
67	8,101	8,101	16,202	317,195
68	8,619	8,619	17,238	311,568
69	9,170	9,170	18,339	304,606
70	9,756	9,756	19,512	296,189
71	10,380	10,380	20,759	286,184
72	11,043	11,043	22,086	274,450
73	11,749	11,749	23,498	260,837
74	12,500	12,500	25,000	245,181
75	13,299	13,299	26,598	227,308
76	14,149	14,149	28,298	207,030
77	15,054	15,054	30,107	184,146
78	16,016	16,016	32,032	158,440
79	17,040	17,040	34,080	129,681
80	18,129	18,129	36,258	97,620
81	19,288	19,288	38,576	61,991
82		20,521	20,521	43,417
83		21,833	21,833	22,807
84		23,228	23,228	0