Retirement Plan

Update

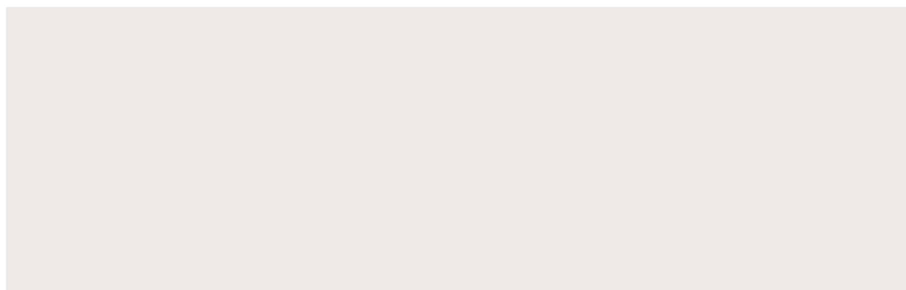
Issue 4, 2019

Because the time is now...

Planning for health care costs in retirement

For most people, a long, enjoyable retirement is the reward for a lifetime of work. Retirement also marks the transition from earning a living to living off money set aside for the non-working years.

Like others, you may have very clear ideas about how you want to spend your retirement. And you may have built your retirement planning around these goals. You may have estimated how much money you will need to set aside to enjoy the retirement lifestyle you envision. However, if your retirement planning does not adequately address the costs of your health care during retirement, you may need to revisit and reexamine your numbers.



People are living longer and spending more years in retirement. According to data from the Center for Retirement Research at Boston College,* the average retirement is expected to last 19 years in 2020, 20 years in 2030, and 21 years in 2040. And while you should plan for routine health care costs for all these years in retirement, you should also consider the possibility of a serious accident or illness that could be very expensive. Planning for health care costs in retirement is a critically important issue that you need to address.

How expensive could health care costs be in retirement? Very expensive, according to recent research. Using data from the Health and Retirement Survey and Medicare Current Beneficiary Survey, the research** shows that once households reach age 70, they will spend an average of $122,000 in out-of-pocket medical costs over the remainder of their lifetimes. However, an individual's personal health and the cost of medical care in the particular location where the individual resides can impact the amount that will be spent.

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Life lessons: don't have a mid-career savings crisis

Working adults should prioritize saving for their retirement even though there may be many other spending priorities competing for their paychecks.

Life can get in the way of saving enough for retirement, especially when you are busy with your job, family, and the other things that are important to you right now. However, keep in mind that your future financial security may depend on how much you save during your working years. Avoid getting so caught up in what's going on today that you neglect to prepare for tomorrow.

Dueling goals

If one of your financial goals is to help your children pay their college costs, it's likely that those expenses will occur before you retire. You may even consider waiting to save more for retirement until after your kids' college tuition is paid. However, if you keep putting saving for retirement last on your list of financial priorities, you may not have time to save enough for your retirement.

If you have to choose between funding your retirement and funding your children's college education, keep in mind that you're probably going to need a lot more money for a comfortable retirement than your kids will need for college. When the time comes for college, your children may qualify for financial aid. And they can always pay some of their college costs by working part-time while in school.

No time to lose

You may reach your mid-career years and realize that life has gotten in the way and you don't have as much saved for retirement as you'd like. Don't panic. You still could have several years left to accumulate money in your plan account. Increasing the amount you contribute by even a small amount potentially can have a big impact on your account value at retirement. The more money you save now, the better off you're likely to be later on. And the sooner you start saving more for retirement, the more time your money will have to benefit from potential compounding.

Put your plan to work

It's easy to save more for your future. Once you decide to increase your contribution amount, that money will be automatically deducted from your paycheck each pay period and put into your plan account where you won't be tempted to spend it on anything else.

Consider maintaining a portion of your portfolio in stock investments because of their growth potential.[2] Though the stock market can be volatile over the short term, stocks have historically produced higher long-term returns than the other major asset classes. (Past performance is no guarantee of future results.) When you are in your mid-career years, you still may have several years left before you plan to retire to recover from any market downturns that occur.

Your situation is unique, so consider consulting a professional before taking action.

Increasing contributions now may mean more money at retirement.[1]

	Saving at same rate	Increased saving rate
Account value at age 40	$50,000	$50,000
Average annual total return	6%	6%
Monthly amount contributed from age 40 to 65	$100	$250
Account value at age 65	$292,548	$396,497

1 Source: DST Systems, Inc. This is a hypothetical example used for illustrative purposes only. It is not representative of any investment vehicle. It assumes monthly compounding. Your investment results will be different. Tax-deferred amounts accumulated in the plan are taxable on withdrawal, unless they represent qualified Roth distributions.

2 Investing in stocks involves risks, including loss of principal.

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What to do

Despite the prospective costs and the variables that may come into play, you can take certain steps that may help you control and manage health care costs during your retirement years.

Focus on prevention

During your working years, focus on improving your overall health by exercising, eating carefully and healthfully, and avoiding smoking and drinking alcohol to excess. Doing so helps reduce the risk of disease and aids your body in fighting off infection. It's also important to seek out preventative health services and stay up to date on vaccinations.

Look into long-term care insurance

A long-term care insurance policy provides money to pay for home health aides, nursing home care, and assisted living facilities. You will pay lower premiums for a policy if you buy it when you are young and healthy. The size of the daily benefit amount you select and the length of time you are willing to wait to receive benefits will also have a big impact on the cost of the policy. Long-term care policies vary in the range of benefits they offer so you should work with a professional to compare different policies to find one that meets your needs.

Maximize your savings

Make an effort to save at higher rates during your working years to account for potential future increases in health care costs. If you are at a higher risk of chronic conditions because of your current health or your family's medical history, you should aim to maximize your savings. Likewise if your employer is unlikely to provide health care benefits in retirement.

Look into health savings accounts

A health savings account (HSA) can be used to pay for a variety of retirement-related health expenses. An HSA is essentially a medical savings account available to those enrolled in a high-deductible health plan (HDHP). Typically, HDHPs are less expensive than traditional medical insurance plans but have higher deductibles and out-of-pocket maximums. HSAs offer several tax-saving features that can help defray these higher costs. For example, contributions are deductible, interest (or earnings) on contributions is tax deferred, and, as long as the medical expenses paid with HSA savings are "qualified" expenses for the individual, spouse, or dependents, HSA withdrawals are tax free.

Contributions can be kept as cash or invested in other options that may be available, such as stock or bond funds. Any money not spent during the year is rolled over for subsequent years. A relatively healthy individual could accrue a sizable HSA balance over a number of years. Consult with a tax professional before investing.

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*Source: Estimates from the U.S. Bureau of Labor Statistics, Current Population Survey (1962-2017); and U.S. Social Security Administration, Social Security Trustees Report (2017).

**Source: The Lifetime Medical Spending of Retirees, John Bailey Jones, Mariacristina De Nardi, Eric French, Rory McGee, and Justin Kirschner, National Bureau of Economic Research Working Paper No. 24599, May 2018.

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