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Advisers Help Clients Brace for Health Care Surprises in Retirement

By: Darla Mercado | September 19, 2014

Health care expenses are the ultimate moving target when it comes to retirement planning, and advisers can use distinct strategies to help provide clients with some certainty around those costs.

It's no secret that investors preparing for retirement are already concerned about the looming expenses that await them in old age, particularly as their health begins to decline. But few people really have a handle on the unexpected nature of surprise health care crises that can completely derail even the best intentions in retirement planning.

A recent Merrill Lynch survey found that less than a quarter of early retirees stopped working because they had “sufficient financial resources” for retirement. Rather, 37% of those who left early did so because they had a health problem, and 27% left because they lost their job.

The survey examined 2,121 affluent individuals age 50 and over. Of the participants who were already retired, 55% had left the workplace earlier than they intended. In contrast, 38% retired when they wanted to and 7% left later than expected.

While an adviser can't necessarily anticipate a client's health crisis long before it comes, he or she can help the client sketch out a plan, just in case.

“Just because we don't know what might befall us and how long we might live, doesn't mean we can't create some straw-man models,” said Ken Dychtwald, gerontologist and CEO of AgeWave.

That preliminary planning can begin while the client is still at work, with disability insurance.

“It's not only about planning for out-of-pocket expenses and long-term-care insurance, but what if you're forced to retire early,” said Cyndi Hutchins, director of financial gerontology at Bank of America Merrill Lynch. “You wanted to work until 70 and you retire at 63. Make sure you have a backup plan for the years you lose because of illness.”

Disability coverage, in addition to long-term-care insurance for retirement, are a must for clients at Lenox Advisors, noted Greg Olsen, a partner at the firm. Clients need to make a move on that disability coverage while they're still in the workplace.

“If you're able to work, you build a nice retirement nest egg and you're in a position where you can draw income for the rest of your life,” Mr. Olsen said. “What can derail that? Disability during the working years or in your retirement years that can make you unable to perform the activities of daily living.”

Meanwhile, advisers use various tactics when considering the amount of money clients will require for health care expenses in retirement.

For instance, Carolyn McClanahan, a physician and founder of Life Planning Partners, suggests advisers consider a client's health risk factors and weigh their use of care services.

“As we target how much to save for health care, there are three different parts,” she said. “Are you a high health care user? How well do you care for your health? What are your potential long-term-care expenses?”

The frequency with which someone uses health care services makes a huge difference in the cost estimates.

A 2010 EBRI study showed that men and women in the 90th percentile in drug spending would need $187,000 and $213,000, respectively, in order to have a 90% chance of covering their health care costs in retirement. In comparison, men and women with median drug expenditures would require $124,000 and $152,000, respectively.

In addition, measuring how a client looks after his health is important because of the role it plays in determining longevity, Dr. McClanahan noted.

“Say you have high blood pressure and it's genetic,” she said. “If you take your medicine, you'll probably live as long as other people. But if you don't take care of it, you're at risk for other conditions.”

Finally, estimating potential long-term-care expenses should take into account how well a person takes care of his or her health. Someone who has a chronic condition and lives an unhealthy lifestyle could probably expect to be in a long-term-care facility for about two years, but Dr. McClanahan uses a five-year estimate for healthier retirees whose greater risk might be dementia.

“Make sure you can get insured as quickly as possible,” she said. “If you can't get insurance, then minimize debt and put away as much as possible to save for your needs. That's how we prepare everyone: You never know when it's going to hit.”

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