

Your Retiree Health Care Costs May Top \$1 Million

Last week, one of the nation's largest insurance companies, [MetLife](#), [abruptly stopped selling new long term care insurance policies](#). Although they didn't cite the exact reasons, it's a pretty fair bet that it had something to do with skyrocketing health care costs, rising utilization and increasing life expectancies.

When a big insurance company exits a market, you can be pretty sure that whatever risk they were insuring is getting awfully expensive. So we all better start planning for bigger health care bills in retirement.

When you look at the MetLife decision in the broader context of health care and ageing, what this is really telling us is that health care costs are becoming less of an insurance cost and more of a cost of living. Let me explain the difference.

Insurance works best when the event you're insuring is unlikely to happen. For example, you insure your house against fire, and the vast majority of houses never burn down. That means for a small premium each year, an insurance company can offer to insure your house against fire. Since most houses don't burn down, the insurance company uses all those small premiums to cover the costs of the few houses that do burn down, and it pockets the difference as profit. Because it's an unlikely event, lots of people can afford to insure their houses against fires.

But what if you lived in an area where every single home burned down every 20 years. That means the insurance company has to basically charge you a premium equal to the cost of rebuilding your house, plus a profit, spread out over 20 years. Otherwise, they'd be out of business.

When the occurrence of a "loss event" is highly likely, the policy starts to look more like a pre-payment plan. Basically, you know you're going to incur the costs, and you're just prepaying the cost of rebuilding your home through the insurance premiums. The premiums are expensive because it's a loss the insurance company knows it has to pay at some point.

That is sort of where we're headed with retiree health care costs. More and more of us will need a substantial amount of health care as we age. If most of us are going to consume a lot of health care, then you can assume that the insurance premiums we pay to cover those costs will go up as well. This is just like the house fire example. If insurers know we will incur these costs, then we will have to pre-pay those costs through our insurance premiums.

So how much should you allocate for health care in retirement? The reality is that no one knows, but I'll try to put a number on it.

Consider that you will at least have to pay your Medicare Part B premium, medigap coverage, and prescription drug coverage. Those insurance premiums can run \$5,000 to \$6,000 a year for you and a spouse in today's dollars. Let's say you're 55 today, with premiums going up every year, within 10 or so years, it's certainly possible those could be running \$10,000 per couple, per year. Consider you'll probably live about 25 years in retirement, and there's \$250,000, without even accounting for longer-term inflation in premiums or out of pocket costs.

Then you have the non-government insured costs of long term care, which encompass nursing home care, home care and some forms of assisted living. These are not covered by Medicare.

Think about this basic example for long term care. Today, it costs about \$80,000 a year for nursing home care. In 25 years (when you might need long term care) assuming a mild 3% inflation (we should be so lucky), the costs would at least double to \$160,000 per person, per year.

If you and your spouse, at some point, need 2 years of care each, that would be \$160,000 x 2 people x 2 years, for a grand total of \$640,000. Maybe only one of you will need care, or maybe you get really lucky and neither of you needs care, but on average, it's reasonable to expect that many of us will pay a healthy portion of that estimate.

When you add the \$250,000 to the \$640,000, my back of the napkin calculation gets you to \$890,000. Throw in \$100,000 for 25 years worth of deductibles, prescription drugs and other out of pocket expenses, and it puts you at a cool \$1 million for lifetime health care costs for you and a spouse.

Is my number accurate? At first blush, it looks outrageous. But at the pace we're going, I think it's in the ballpark. And if the insurance companies can't quite figure it out, I would err on the side of it costing more, as opposed to costing less. Eventually, we'll have to pay for all of this through higher premiums for insured care, and writing bigger checks for our uninsured care.

If you're thinking there's no way most people will have enough money to pay for all this, you're right. But that's not something I can do anything about. I'm just telling you where it's probably headed so you can plan accordingly if you like.

Bottom line. For many of us, it's not a question of if, but when we'll incur huge health care costs.