Healthcare Costs in Retirement: Medicare Overview and Important Dates

No retirement income plan is complete without addressing healthcare expenses in retirement. Afterall, for the average American healthcare expenses are the second largest expense in retirement, totaling only less than housing costs.[1] However, these essential expenses tend to be overlooked by many, as it's a common misconception that Medicare will cover 100% of costs. This unfortunately is a gross misunderstanding. According to the Employee Benefit Research Institute, it is estimated that Medicare only covers about 59% of healthcare expenses in retirement.[2]

As you look to help clients plan to cover their healthcare expenses in retirement, many clients may find it helpful to think of these costs as an ongoing annual expense of approximately $5,000 to $8,000 per year, on average, for a typical healthy 65-year-old (or $10,000 to $16,000 per 65-year-old healthy couple). These estimates are dependent on a client's type of coverage but at minimum can provide a good starting point. It's important to keep in mind that healthcare costs have historically increased at a higher level of inflation than other industries. It's been estimated that healthcare expenses will continue to inflate at a rate of 2-2.5 times faster than overall U.S. inflation.[3] Additionally, the relative amount spent on healthcare typically increases significantly at older ages. If you combine this with the longer life expectancy of the average American, this can lead to a significant tail end risk in retirement. Ultimately, a retirement plan that doesn't address these issues would be incomplete and could put clients at risk.

Medicare Overview

Medicare is the default government healthcare insurance system typically for Americans over the age of 65. Medicare has multiple parts and methods for obtaining insurance coverage. The traditional method of coverage would generally involve enrolling in Medicare Part A (Hospital Insurance) for inpatient services, Medicare Part B (Medical Insurance) for outpatient services, and Medicare Part D (Prescription Coverage) for drug coverage. Many individuals also elect to enroll in a Medicare Supplement Plan (Medigap Plan) to provide them with additional insurance that helps fill in some of the gaps in coverage.

An alternative to this traditional method is for individuals to choose to enroll in Medicare Part C or Medicare Advantage Plans. This alternative approach has grown in popularity over the past 15 years, as enrollment in Medicare Advantage Plans has jumped from about 19% in 2007 to over 50% in 2023.[4] Medicare Advantage Plans are offered by private insurance companies and include Hospital Insurance, Medical Insurance, and typically Prescription Coverage. These plans may offer some extra benefits that original Medicare doesn't cover, such as vision, hearing, and dental services. They also might may have lower out-of-pocket costs (e.g., deductibles, co-insurance, and copayments). In 2023, the out-of-pocket limit for Hospital and Medical coverage under a Medicare Advantage Plans is $8,300 for in-network services. The 2023 out-of-pocket limit for Prescription Coverage is $7,400, and after reaching that amount, a client generally would only pay 5% of the cost. However, Medicare Advantage Plans do require that individuals see providers that are in their network and may require approval before covering certain drugs or services. Clients are also likely to still have to pay a monthly Medicare Part B premium, often in addition to the premium they pay for the Medicare Advantage Plan.

Important Dates

Most Americans can't enroll into Medicare until they approach the age of 65. The Initial Enrollment Period is generally a seven-month period, including:

- the three months prior to the month an individual turns 65,
- the month an individual turns 65, and
- the three months after the month the individual turns 65.

For clients who are still working and covered under a comprehensive healthcare plan through work, those that fall into this situation may want to evaluate whether enrolling in Medicare during their initial enrollment period is the best option. Afterall, there are premium costs associated with Medicare Part B, Medicare Part D, a Medicare Supplement Plan, and a Medicare Advantage Plan. If a workplace healthcare plan is comprehensive enough to meet a client's needs, it likely wouldn't make sense to pay these additional costs.

Another factor to for clients to consider as they determine when to enroll in Medicare is that once they enroll in Medicare Part A, they are no longer able to continue investing in a Health Savings Account (HSA). This may be especially important for clients who are deciding when to claim Social Security, as they may be automatically enrolled in Medicare and thus lose the ability to continue investing in a HSA.

If a client decides to enroll in Medicare after their initial enrollment period due to having a robust healthcare plan through work, they will be provided a Special Enrollment Period upon losing their employer sponsored healthcare coverage. The special enrollment period allows an individual to enroll in Medicare during an eight-month period, which begins the month after employment ends. It's critical to note that if a client fails to enroll during the Special Enrollment Period, they will not be able to enroll into Medicare until the next General Enrollment Period, which occurs annually from January 1 to March 31. If an individual has a 12-month gap in coverage, Medicare will charge a 10% Late Enrollment Penalty, which will last for the rest of their life.

For clients interested in applying for a Medicare Supplement Plan, a six-month initial enrollment period called Medigap Open Enrollment starts the first month they have Medicare Part B and are at least age 65. During this specific period, a client can buy any plan sold in their state, as they cannot be denied due to pre-existing conditions or charged more for coverage. It's critical to note that this benefit only applies during the Medigap Open Enrollment Period, as after this period, a client can be denied coverage or be subject to increased premium costs.

Every fall there is an Annual Enrollment Period, which stretches from October 15 to December 7. During this time clients can change their coverage for the next year from Traditional Medicare to Medicare Advantage (or vice versa), change from one Medicare Advantage plan to another, and elect or switch between Medicare Part D prescription drug plans.

Prudential is Here to Support You

No retirement plan can be complete without addressing healthcare expenses in retirement. By educating clients on the importance of planning for these essential expenses, you can help prevent their plans from potentially being derailed. Prudential's Advanced Planning Team stands by ready to support you as you build and refine retirement income plans designed to address the spectrum of client needs. For further discussion of Medicare, healthcare costs, or any advanced strategy, contact the team at 888-425-1022.

[1] Bureau of Labor Statistics, Consumer Expenditure Survey 2020; Table 1300 Mean annual expenditures by age; Age 75+

[2] EBRI.org Issue Brief, January 13 2022

[3] Healthview Insights 2021 Retirement Health Care Costs Data Report

[4] KFF analysis of CMS Medicare Advantage Enrollment Files, 2010-2023; Medicare Chronic Conditions (CCW) Data Warehouse from 5 percent of beneficiaries, 2010-2016; CCW data from 20 percent of beneficiaries, 2017-2020; and Medicare Enrollment Dashboard 2021-2023

This Advanced Planning Insights and Ideas bulletin was published October 2023.

Prudential