

MPT in a Parallel Universe

Continued from page 13

Miccolis admits that we have not yet proven that all the fancy, complex, increasingly sophisticated analyses that grew out of MPT in the ERM space will produce better, sturdier, higher-returning portfolios for your clients. But he does think that ERM has taken the basic concepts of modern portfolio theory much further, and with fewer taboos, than you find in the advisor profession. Its tools are more sophisticated. And when you start to map the pillars of ERM into the asset management space, you suddenly see a new spin on a lot of the ancient debates that we've been tossing around in our profession for decades.

This represents some of the best thinking I've seen on how modern portfolio theory will evolve in light of 2008, and Miccolis assures me, after an hour and a half of fairly intense discussion, that he has only scratched the surface.

I should add that Miccolis will be a panelist at the Business and Wealth Management Forum (October 13-15 in Chicago), in a debate on emerging investing principles in the planning profession. I was the person who invited him to speak; the other participants in the debate are two gentlemen you might have heard of: Harold Evensky and Bill Bengen. I can hardly wait to see what, together, they come up with.

You, too, can watch it live; here's a link to see what other sessions might be worth attending: <http://www.signupforconference.com>. ■

Client Services

Healthy Choices

by Bob Veres

Synopsis: *Helping clients make good decisions about their health insurance and Medicare coverage can lead to substantial savings--and improved quality of life.*

Takeaways: *Income tax planning becomes more valuable now that Medicare Plan B and D are means-tested. Mapping a client's current health issues to Medicare coverage can save thousands of dollars in out-of-pocket expenses. For those under age 65, starting a business can lead to significant health insurance premium savings.*

Katy Votava, founder and president of [Goodcare, Inc.](http://www.goodcare.com) in Pittsford, NY and Washington, DC., believes that health insurance and Medicare advice can be one of the most important components of a client's financial plan. "If people can fully-fund their HSA and get the tax-free earnings," she says, "or if they pick the right Medicare option that minimizes their out-of-pocket expenses, we're looking at potential savings of thousands of dollars a year."

[Goodcare \(www.goodcare.com\)](http://www.goodcare.com) serves as a resource for advisors in this esoteric field; it specializes in the economics of healthcare, and offers consulting services for advisors whose clients have questions about things that are not part of the traditional CFP curriculum: health insurance, Medicare and Medicaid (and Medigap) policy options, COBRA continuing health coverage and a variety of long-term care issues. "We also do training and seminars

for advisor client groups," says Votava, "and help small business clients figure out their health care costs and needs."

Most advisors know that health care reform is slowly creeping into their clients' lives. But what do they need to know now? First, what is available. "Age 65 is the Great Divide in the U.S. when it comes to health care advice and health insurance issues," says Votava. "The rules of the game are very different when people are eligible for Medicare than they are for the under-65 crowd."

Under-65 Options

So let's start with the non-Medicare-eligible client. "The classic case that we're seeing a lot of today," says Votava, "is where somebody leaves their employment not-voluntarily, and they are trying to replot themselves. They already have a nest egg, but not enough to live until their 90s."

Typically, these clients have

been covered by employer-based insurance, and know very little about shopping the individual market for themselves and their families. "The very first thing you want to do is make sure they maintain their health coverage through COBRA while we look at other options," says Votava. "Even though they will be paying full price for the health insurance offered by their former employer, it may actually be the best and least expensive option, because there is risk pooling."

In a recent case, an advisor-referred couple, both age 52, were shocked at the price of individual coverage on the open market. "The best price we could find ran to \$1,900 a month," says Votava. What to do? "The advisor suggested that the clients start a business, even if it isn't going to be their full-time occupation," says Votava. "He helped them set up an S-Corp. The husband and wife will be officers, and we can buy them each individual coverage through the business."

How much can they save? "The plan we recommended recently cost \$390 a month for high-deductible coverage, which is what the clients wanted," says Votava. "Meanwhile," she adds, "the advisor is talking to them about fully-funding their HSA account, so if they can pay for their health costs out of other dollars, the tax-free earnings from age 52 until retirement can be significant."

Sometimes the choices are less pleasant. An advisor referred a couple to Votava at a time of maximum stress; the husband had

been medically disabled for years, and recently the working wife had been diagnosed with cancer. "The first thing you want to do is get the paperwork filled out to ensure that they can continue to maintain the coverage she had at work under COBRA," says Votava. "But once that expires, because they are in a medical underwriting situation, it can be quite problematic to get decent coverage at an affordable price."

Most of the provisions in the recent health care reform act will affect people under 65, Votava says; the law doesn't make significant changes in Medicare. Votava thinks the state pools that will go into effect in 2014 will be a big improvement over the current chaotic marketplace. "Because all insurance is based on risk pooling, all of today's individual policies have sky high premiums," she says. The coming health insurance environment will also get people accustomed to buying their own coverage, which will make health care consumers more sophisticated.

Over-65 options

How do you plan for the client who is approaching Medicare-eligibility? "Making the right choices is a big deal," says Votava. "The choices are very different from what they see in the under-65 market, which puts them in unfamiliar territory."

Votava and her staff will walk a client through the initial process of applying for Medicare, which can be handled online or on the phone. "It's a series of steps,"

she explains. "Three months before you turn 65, you apply for Part A [hospitalization] coverage, and Part B [outpatient, laboratory, doctor] coverage if you are going to take that. Then you have to decide if you're going to have Medigap coverage plus Part D [drug coverage], or take some form of Medicare Advantage coverage, which has Part D built into it."

Medicare Advantage, otherwise known as Part C, wraps in parts of coverage from Parts A, B and D, and has some features of a Medigap policy as well. Different combinations and choices will leave different types of costs exposed to out-of-pocket payments, so clients will want to buy coverage that addresses the costs they are more likely to incur. This may cost more per month, but ultimately saves them money as they receive treatment.

Consider, for example, a husband and wife that Votava has been working with at the request of their financial planner. Both are now in the hospital. "They had a Medicare Advantage plan that had no stop-loss amount," says Votava, "and they didn't know that going in. The plan was decent, and it had very low premiums, but it's definitely the wrong coverage for their circumstances."

Why? "Medicare only covers 80% of the costs, so 20% gets offloaded to the beneficiary," Votava explains. "A Medigap plan or a good Advantage plan will put a cap on the total amount they will have to pay out-of-pocket. If they had been in a better plan, instead

Continued on page 16

Healthy Choices

Continued from page 15

of spending \$20,000 a year out-of-pocket, they probably would have spent \$4,000 or \$6,000."

Unfortunately, you can only change Medicare coverages once a year. "We did our analysis and helped them find the right plan, but it was expensive for that one year," Votava concludes.

To make matters more confusing from a financial standpoint, the cost of Part B coverage is means-tested, based on a client's prior income. The basic premium is \$115 a month, but it can rise to more than \$300 a month for people in higher tax brackets. As of January of this year, higher income taxpayers pay more for their Part D coverage as well. "The cost of those premiums is based on the modified adjusted gross income (MAGI) for two years prior, which is the most current tax return that Social Security will have in their files," Votava explains. "MAGI is a specific calculation for Medicare, which is basically adjusted gross income with tax-exempt interest added back in."

As it happens, this calculation is negotiable. "Suppose your clients are retiring this year," says Votava. "Their tax return that is available for Social Security to look at--because you apply through Social Security, not Medicare--is from when the client was engaged in full-time work. If her income at that time was dramatically higher than what she expects to earn in retirement, you have the opportunity to tell Social Security, hey, I'm retiring; I no longer will

have that level of income. If you provide some documentation, like a letter from your former employer, and fill out the appeal form," she adds, "usually they'll accept it."

If clients are still working, then the advisor has another tax planning issue to consider. "If the client makes one dollar over \$170,000 in MAGI," says Votava, "then it will cost her over \$1,000 in additional Medicare premiums." She says that many advisors will look at these numbers and realize that it lends weight to the Roth conversion argument, since money coming out of the Roth account doesn't figure into the MAGI calculation. "It gives people a chance to bring their income down to a bracket below where they would otherwise be," says Votava, "and they save real money on their Medicare B and D premiums."

Mapping coverage to health issues

When they work with Goodcare, each client will have his or her circumstances put on a spreadsheet, and the advice can be very different for different people. "The cost and benefit analysis is not always clear-cut," Votava explains. "For people under 65 who are retiring, or if they lost their job, we want to get their corporate paperwork done so their coverage doesn't lapse. For people who are about to apply for Medicare coverage, we need to understand their health issues. Is their most likely expense going to be prescription drugs or hospitalization? What is the history

of dementia in their family?"

And for clients who are already paying for Medicare coverage, is it still appropriate for their current health expenditures? "We see a lot of people who are paying more for their coverage than they need to," says Votava. "The advisor should never assume their client cannot do better."

Sometimes this evaluation takes place in the context of an emergency, like the retired couple who saw the husband get sick and go into the nursing home, and the wife was so stressed out that she stopped looking at her bills. "By the time the children found out, neither parent had Medicare Advantage or a Medigap plan," says Votava, "and dad was running up some significant medical costs. We had to scramble around to see what we could put in place in a hurry. Fortunately, in their case we got them better coverage than they had before."

Point of Contact

What's the advisor's role in all this? Because of the way health care and financial planning are increasingly intertwined, and because the client is accustomed to receiving advice from the advisor, Votava believes that in many cases you're the point of contact for people who are sorting out their healthcare options.

You might think that the family doctor would be a more logical choice, but advisors have a better understanding of the financial issues (and constraints),

they are usually more willing to spend time helping the client sort through these questions, and they are regarded as a less biased source of information. "The advisor becomes the information referral center," says Votava. "Most of the advisors we talk to would rather refer this work out rather than try to stay up on all the ins and outs. So they supervise the process and stay as involved as they need to be."

Can't advisors simply go through some of the Goodcare coursework and learn the options to recommend. "The only problem," Votava says, "is that this is a highly-specialized area that changes quite frequently. Advisors have a lot to keep up with on tax and estate planning and all the other issues, so it's hard to stay current in this field as well." Her recommended solution is to build a team of outside experts, similar to the way advisors refer to their local CPA and estate attorney on complex tax and estate planning issues. Goodcare, or a local firm with similar expertise, can serve as the resource for sorting through policy options. A local case manager will be able to provide advice on the local caregiver scene and long-term care facilities. Meanwhile, advisors can contact their local Office on Aging (www.eldercare.gov), which operates somewhat like the county agent in the farming community. Healthcare.gov, a government-supported web site, provides answers to frequently-asked questions.

In addition to serving as

a conduit to more information, Votava would like to see advisors budget for health insurance in the financial plans they draw up. "Most retirement plans don't have a specific line item for health insurance," she says. "Ideally, advisors would plan realistically for future health care costs, and put something in the retirement plan budget that starts when their clients retire."

How much? "If they have the Medicare Advantage Plan without the copay, the total cost can be \$10,000 or more for clients earning more than \$170,000," says Votava. "At the lower end, you might plan to pay \$6,500--and this doesn't include the normal expenses to stay healthy, plus dental costs, since Medicare doesn't cover dentistry." Whatever you budget today, she says, inflate it by 8% a year in the future.

Beyond that, Votava believes that health insurance should be discussed in the client's annual meeting, as one more opportunity to streamline a client's financial life. "We had a client recently who was spending \$24,000 a year in premiums for his family," says Votava. "He is a sole proprietor. We got him a high-deductible health plan for \$7,000 in premiums, and he can fully-fund his HSA for about \$13,000. He is putting away about \$11,000 a year for his own retirement."

Terminal Planning

You hear a lot of talk and debate these days about end-of-life

issues, and what Elizabeth Jetton has called the "4th Stage of Life"--the terminal years of retirement when medical issues and costs tend to dominate the budget and lifestyle. But Votava isn't seeing that in the planning clients referred in her direction. "Our typical clientele is generally around 50 to 70," she says, "and they are concerned about their own needs or the needs of their small business, or they are the caregivers for their elderly parents."

In the end-of-life cases that Votava has seen, the biggest issue is the last person to die in a family. "In the older population, you will see a husband and wife who have been hanging in there, and then one member crashes," she says. "The other one is left to cope, and it quickly becomes too much."

Votava recalls a situation where the advisor referred a client in her 80s, who was already living in an assisted living facility. "She had no long-term care insurance," says Votava, "but the facility was offering extra services for around \$15,000 a year. I said to the advisor that it seemed like a good value, because it was going to cost at least that much to take care of her."

In another case, an elderly husband and wife, whose daughter was the caregiver, were managing just fine until the husband died. "Mom was the one with dementia, and she was not able to cope," says Votava. "Assisted living is not designed for people who can't function. The daughter is trying to figure out how to get the

Continued on page 18

benefits in place, they don't have long-term care insurance, and the nearest facility is two hours away, four hours roundtrip to visit. The daughter wouldn't be able to go on her lunch hour to visit Mom."

For advisors who are thinking about whether they want to become a conduit for health care planning advice, the point is that this is an opportunity to save real money, either as tax-advantaged growth in the HSA account, or income tax planning to lower the Medicare premiums, or finding the coverage that minimizes out-of-pocket costs for existing (or projected) health conditions. Future health costs, meanwhile, represent a real bite out of income. If they are not factored in, you might be projecting a far more sumptuous lifestyle than the client will be able to afford in retirement.

And finally, whenever you talk about health care, you are fundamentally talking about the most basic quality-of-life issues: the best care, a good assisted living facility or assisted living services in the home, a good long-term care facility, and coverage of the costs that clients rely on to stay healthy and alive.

"The difference in quality of life between a person who gets great healthcare and coverage advice, and somebody who is left to find it on their own, can be enormous," says Votava. "This is really an area where advisors, if they will take it on, can make a huge difference in the lives of their clients." ■

THE *REAL* MEDIA BIAS

As you might have noticed, our elected representatives in Washington very nearly blew up the best credit history in, well, history by squabbling over the debt ceiling right up to the white-knuckled edge of the default deadline. The "debate" had all the elements of a sordid drama: representatives signing pledges and answering to bosses who are not part of their electorate constituency, finger-pointing, posturing, exaggerating the other side's positions, a stunning lack of emotional maturity and (how else can I put this?) patriotism, in the sense that the participants never quite found a way to put aside their personal interests and figure out how to do what's best for the country.

We are absolutely right to condemn this behavior.

But I think it's also helpful to step back and ask ourselves: how do we know all these political implications of every proposal? That is, how do we know so much about the politics, the squabbling, the exaggerations, the bosses who tell our representatives in Washington what they can and cannot do--and why have we seen so little detailed analysis of the actual of the actual merits of the proposals?

Every time I pick up any of the news sources--online, print, broadcast--I see the same thing: rigorous, deep, thoughtful, breathless up-to-the-minute analysis of the political consequences of this or that position on the debt ceiling, and virtually nothing about consequences on the country, the debt, the budget and the economy. Obviously, we need to fix Social Security and Medicare, and eventually stop spending so much money fighting these Middle Eastern wars. Our tax structure is a mess. Ditto the economy. But whenever somebody in Congress offers a proposal, well-meaning or not, to address any of these issues, the American Public is told, by the Fourth Estate, how this latest political ploy relates to the 2012 elections and the future balance of power in Congress.

The future of our country is at stake, and the reporting is all about who might or might not get elected.

I find myself wondering if Congress is capable of having a substantive debate if the reports about its deliberations are always framed purely in political terms. Put another way, if some functioning adult in Congress were to sit down and create a realistic set of proposals that shares the pain across the full spectrum of citizenry, in a way that is bearable and sustainable, and shows us a way out of the debt crisis without sacrificing the fragile economic recovery at the same time, would the voters ever learn about the merits of the proposal? My guess is that several of