Transcript

Better conversations. Better outcomes.

Episode 64 – Health savings accounts: A strategic retirement tool?

Peter Stahl - Retirement healthcare will be your clients' most expensive item.

Ben Jones - Welcome to *Better conversations. Better outcomes*. presented by BMO Global Asset Management. I'm Ben Jones.

Emily Larsen - And I'm Emily Larsen. In each episode, we'll explore topics relevant to today's trusted financial advisors, interviewing experts and investigating the world of wealth advising from every angle. We'll also provide you with actionable ideas designed to improve outcomes for advisors and their clients.

Ben Jones - To access the resources we discuss in today's show, or just to learn more about our guests, visit bmogam.com/betterconversations. Again, that's bmogam.com/betterconversations. Thanks for joining us.

Emily Larsen - Before we get started, one quick request. If you have enjoyed the show and found them of value, please take a moment to leave us a rating or review on iTunes. It would really mean a lot to us.

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Emily Larsen - HSAs, or health savings accounts, have been in the market since 2003, but recently, they've seen a huge increase in use as the cost of healthcare has become an increasing concern for Americans. Many people think of them as a spending vehicle, rather than a savings vehicle. Today, we're here to discuss how advisors can help their clients reframe the use of HSAs as a retirement tool.

Ben Jones - Our guest today is Peter Stahl, and he's brought some actionable and practical advice for you. Peter is the president of Bedrock Business Results, as well as the author of *Top of the First: The Convergence of Healthcare and Financial Planning*. Peter speaks to advisors and firms across the country on the convergence of these two fields.

Emily Larsen - As Peter sat down with Ben in Chicago, he said there is so much that advisors don't know and need to know, which means their clients don't know and need to know about this topic. We aim to fix that by the end of this episode.

Peter Stahl - A health savings account, better known as an HSA, is a tax advantage saving and investment account that can be used for healthcare expenses.

Ben Jones - Can anyone participate in these?

Peter Stahl - No. I wish that were the case, many people wish that was the situation, but it is tied to the type of health insurance that you have. So it's commonly called a high-deductible health insurance plan, but that's actually not the only stipulation. It needs to be a high-deductible health insurance plan, but it has a few other stipulations it has to meet, both at the federal and even at the state level to get approved as an HSA-eligible health insurance plan.

Ben Jones - If someone's in a health plan is it obvious if they're in a qualified plan or not? Or is that a non-obvious thing?

Peter Stahl - It should be obvious, but if there's any doubt, I always tell folks go right to the insurance company, or to your employee benefits person, and ask them, is this basically HSA insurance? In fact, some of the healthcare reforms that were proposed by the last couple of sessions of Congress that did not get passed were going to change the name to just HSA Insurance, just so it's blatant and obvious, this is an insurance plan that allows you open up an HSA.

Ben Jones - Oh, that would make a lot of sense.

Peter Stahl - That would help.

Ben Jones - One question I always have is like I've always had the good fortune of working for employers that had HSA plans and high-deductible plans, but is always come through an employer or can you get an HSA individually and have an individual high-deductible plan?

Peter Stahl - Well, it's not always through the employer. That's pretty common, because you think about it, where do you get your health insurance during your working years? Typically it's coming through your employer. So that's a pretty common scenario. But if you're unemployed or if you've taken an early retirement so you're not on to Medicare yet and you're getting your insurance either through the federal health insurance exchange or if your state's adopted a health insurance program, getting it through the state exchange, you can also find HSA eligible insurances on those exchanges.

Ben Jones - Now, let's talk specifically about the HSA account. What types of expenses can an HSA, money inside of an HSA be used for?

Peter Stahl - It's a pretty broad range. The most similarity you'll find is the list that the IRS publishes for what qualifies for a deduction if your health expenses exceed a certain percentage of AGI. So to speak more generally to it, it's really health expenditures. So copayments, deductibles, uncovered items. But it even broadens out from there. If you want to make a home improvement during retirement, to put a ramp on the front of your house to make it wheelchair accessible, that's health-related, so that would be a tax free distribution from your HSA. Medicare premiums are a great example. Not a Medigap policy, but the Medicare premiums that people will pay. That's a justifiable tax free distribution from an HSA.

Ben Jones - Oh, so a lot broader than the old traditional FSAs. Some people do get FSAs and HSAs confused a bit. What are the primary differences there?

Peter Stahl - The primary difference I like to say is the second letter. It's the S. Flexible spending account is an account that was designed for you to spend. So the concept is, I think anyone who has one knows, you got to size it up at the start of the year, how much do I think I'll spend on these approved items, and then you put that amount into the FSA, and if you don't use it, you lose it. HSA is a health savings account, or as I like to say, a health savings and investment account, but let's just call it a health savings account. You certainly can put money into the HSA and spend it on approved healthcare distributions right away, but you're not forced to. The idea is you can let the thing grow and accumulate, and it's real money. It's always your money.

Ben Jones - That's a big advantage, and I remember like back in the day my parents trying to figure out how much they were going to spend on orthodontia and healthcare bills. You can never really precisely come up with that amount in the FSA, so this is a much more user friendly, human experience.

Peter Stahl - Yeah, anytime you have a real account that's a real asset. There's a custodian, there's money there, what happens if I die? Well, it goes to the beneficiary. It's a real asset, it's always there for you. It carries over year to year. What if I leave my employer? Well, it goes with you. So this is a real asset.

Ben Jones - I want to talk a little bit about the current limits. So what is the limit for what someone can put into an HSA if they're an individual and does it change if they're a family?

Peter Stahl - Yeah, so, insurance looks at it in two ways, whether you have family coverage or individual coverage. If you have a family coverage insurance plan, in 2018 the contribution limit is $6,900, and then for individual insurance, it's $3,450. And then you also get a catch-up provision when you're age 55 where you can put another $1,000 in.

Emily Larsen - So why is it so important for financial advisors to understand the convergence of healthcare, HSAs, and financial planning?

Peter Stahl - Retirement healthcare will be your clients' most expensive item. It's their biggest expenditure when you really add it up, and when I go through my training on retirement healthcare, I tell folks think about $220,000 per person over the course of a 25-year retirement, and that's routine healthcare. That's not a nickel for any custodial care, long-term care. That's a big number. That's a lot bigger number than the common press coverage would give it. But I break that down to $6,700 per person today. Medicare premiums, out-of-pocket. So, where I'm going with that is if you consider the enormity of the cost and recognize that most Americans will have their largest healthcare expenditure during retirement it's critical to start to build sources of tax free income for retirement, and an HSA is an extremely efficient way to do that. When I named the title of my book, I named it *Top of the First*, because we are very early on, as a nation and as a financial services industry, in addressing it. But there are clear -- there's four or five clear points of convergence as it relates to retirement healthcare and financial planning that have a direct impact on wealth accumulation strategies and wealth distribution and wealth preservation strategies. If you're a financial advisor, you have to understand them to do comprehensive wealth management. It's written actually for consumers, so advisors like to have it for themselves, but also to provide for their people transitioning and accumulating wealth for retirement, but it really goes through retirement healthcare in the financial planning consideration. So, Medicare, an overview and understanding it, costs, we're estimating retirement healthcare costs, understanding how higher income drives higher costs, looking at health savings accounts, Roths. Tax deferred annuities can even play a role. Looking at custodial care and how do we approach and effectively have conversations with clients on that front?

Ben Jones - Wonderful. And we'll put a link to that in the show notes so people can easily access it and buy a copy.

Peter Stahl - Thank you.

Ben Jones - I know that there's the primary or intended kind of use for HSAs, at least in my mind, was kind of this idea that they were used for healthcare management, and then I know that I've recently, especially over the last four or five years, you hear a lot about as kind of an alternative savings vehicle for these retirement healthcare costs. Are those the two primary uses?

Peter Stahl - Yes. When the HSAs first came out, people had that FSA mindset. So they put the money in, you get a nice little debit card, right? And then you can use it for these qualified expenditures and you put the money in, you get a nice income tax deduction, and we haven't really covered that, but this goes in pre-federal, pre-state, in most states, and pre-FICA. That's a better deduction, actually, than you get on your 401(k) contribution. That's a pretty nice deduction. And you put the money in there and then they're using for current expenses. So it's kind of going in the front door and out the backdoor in the same year. I would say that's the wrong use for most people of an HSA. What we really need to recognize is healthcare costs will be enormous in retirement. If you're generating a lot of taxable income in retirement, they're going to be even bigger for you, because Medicare is means tested, so we need to be using the health savings account as a retirement investment vehicle.

Ben Jones - And so walk me through how that works. So obviously you've already mentioned that you can put money in and it can stay in.

Peter Stahl - Mmm-hmm.

Ben Jones - But walk me through how one should start thinking about -- especially if there's a lot of advisors listening, how should they be counseling their clients to start thinking about money into this HSA account then as it gets to some certain point, I got to imagine, they need to maybe even start investing it or can start investing it. So just kind of maybe some practical steps here.

Peter Stahl - Right. So the concept is you make a decision to fully fund your HSA. So let's say you have a family plan. You can put that $6,900 in. Then you make decision number two, which is not to take a nickel out of the HSA. Think of it like your IRA, your 401(k). You kind of get this retirement mindset with the asset. It takes some financial planning, that means you got enough disposable income to pay out-of-pocket high-deductible costs without touching the HSA. But now, you're sitting down with your financial advisor, let's say you're 50 years old and you're targeting 67 for retirement. We now have an asset that we're going to fund for 17 years. To me, that spells getting fully invested. Now of course, your risk profiles and risk tolerances all come into plan, just like it would with a 401(k) or an IRA, but I'm going to get that fully invested. There's plenty of HSA custodians that will allow you to fully invest that asset from dollar one.

Ben Jones - That's a great point. I guess one of the things I didn't really think through is like at what time would an advisor using it as a traditional health care augmentation plan? I don't know what you'd call that, but using it for healthcare versus the point at which an advisor might say for you, you might want to start thinking about this as an alternative savings vehicle.

Peter Stahl - Right, I mean the practicality of it is it's almost a barbell, it's interesting. Very young employees who don't have -- they're very healthy, they don't have a lot of healthcare expenses, they are starting to fund their HSAs and saying I don't need to pull on this right now, so they're getting it invested. Then you kind of get into those years where you're having the kids and you've got the mortgage and you've got college payments and being able to have enough disposable income to fully fund an HSA and not touch it gets pretty challenging. Then you start to move out of that phase. So I would say kind of that age 50+, that's when I want to push hard on folks to say, let's fully fund that HSA, get it fully invested, and find disposable income elsewhere in your financial plan in order to pay that high deductible.

Ben Jones - That's a great tip. You know, it's funny. I've lived an accident-prone life myself and spent many trips to the hospital and ER and clinic, but I have not even rivaled what happened when we had kids. It feels like monthly there's a visit to some doctor for something.

Peter Stahl - Right. I can give you a great example that I use, I have twin boys. I have five children, but I have twin boys. Last summer, they had to have their wisdom teeth out. As you're going through this, you're thinking oh boy, what's it going to cost to get four teeth pulled? No, it's eight teeth, right? Everything is doubled with twins, right? I'm a small business owner, I don't have dental insurance. So the eight teeth get extracted, the bill shows up. It's $5,200. So I've got a choice to make. Do I pull that out of my HSA or do I find the funds elsewhere in my cash flow? So I did the latter, I paid the 5,200 out-of-pocket. What's interesting, Ben, is I now can take $5,200 out of my HSA at any point, income tax free. Next month, next year, or 15 years from now when I'm in my upper 60s and retired and looking for tax free income. So there's some nice financial planning that can go on with that.

Ben Jones - Now I didn't realize that. So you can actually defer the spending, so you've spent money out of your own pocket, later you can take that money to recoup your expense at some point down the road, if I'm understanding that correctly. What's required practically to be able to pull that off?

Peter Stahl - I always tell folks keep your big receipts, not because you're necessarily going to need those to get the distribution, right? You can call you HSA custodian, please send me $5,200. Well, Mr. Stahl, is that a qualified disbursement? Yes it is. Have a great day, your money is on the way. Now, if the IRS comes in and audits me --

Ben Jones - You're going to want the receipt.

Peter Stahl - Then I want that receipt. It's funny, the HSA custodians and there's different people developing apps, right? To help you track your out-of-pocket healthcare expenditures. But as you can see, if you keep track of those expenditures, pretty nice planning going on.

Ben Jones - Yeah. That's a really great and real practical tip. It's easy to just scan those into Evernote or put them into your file and save them forever.

Peter Stahl - Right, mmm-hmm, exactly.

Ben Jones - And just dust one off when you need some money in retirement, I like it.

Peter Stahl - Exactly.

Ben Jones - Now, how should kind of a new user think about kind of managing their HSA in the beginning? Maybe where I'm going with this is I think of it as like most people, when they're getting new into a high deductible plan, the first thing they're thinking about is well, what if I break my leg and I have to spend $1,000? And maybe like you said, they're younger, they're just new to this HSA concept. Are there any strategies that you should think about as to keeping some of that money into cash or do you immediately start investing dollar one?

Peter Stahl - What I do is I actually take it a step back and I go to some basic financial planning. Before you invest a dollar anywhere, I want to make sure you have that emergency fund in place, liquid, available. Now some financial planners will tell you that's six months of living expenses, some would tell you it's three months, some would tell you it's 12 months. But work that out with your advisor. Have that emergency fund in place. That's where I'm going if I break a leg. That's where I'm going if I have an emergency, unforeseen health expense, is to that emergency fund. That enables me to invest the HSA from dollar one. Now having said that, if there's a comfort level there that boy, I'd like to at least get a few thousand dollars built into this money market in the HSA and keep it there, I'm not going to argue with that. But think it through in terms of what the exposure is, and then after you cross that line, let's get invested.

Ben Jones - Now, let's say someone doesn't have the ability to fund their 401(k) to $18,000 and their HSA to $6,900, I mean that's a lot of money, they don't have that, but they say they can put $10,000 towards these accounts. Do you recommend one over the other or splitting it? How would you think through that budgeting exercise?

Peter Stahl - I like to say if you're getting a company match on your 401(k), I want to see that fully funded all the way up to the match, right? It's free money. And then once I hit that amount, fully fund my HSA, and then if I have additional disposable income, go back and continue to fund my 401(k).

Ben Jones - And the reason for that is that the HSA dollars can come out tax free, correct? Versus your retirement dollars that are going to be taxed as income in retirement.

Peter Stahl - Yeah, there's actually -- in some ways, the HSAs are more liquid because the way the HSA works, number one, the deduction, if it's coming through a payroll, like an employer, that's where you get the federal, the state, and the FICA. You get the tax free growth. If you pull it out for non-medical, you've got a 20% penalty, plus it's taxable, but the 20% penalty goes away in retirement. So you get all the way to retirement, I always tell people you should never have to make a taxable distribution from your HSA. When you consider in retirement all your current medical expenses, your Medicare premiums - justify. When you consider that, and you consider all those expenses you had over the years where you'd saved those receipts. You should be able to get a tax withdrawal but in the event there's something major that changes and you have to pull it out in retirement and you're doing is paying taxes on it. Not a 20% penalty. So in some ways, it's more liquid.

Ben Jones - Now, you mentioned some people get them through their employers, some people work in a corporate job where they have these and then they go self-employed, or maybe they switch jobs. How does the HSA, does this end up being that you have five different HSA accounts or how does it work about keeping track of those and keeping them consolidated.

Peter Stahl - It's similar to the 401k, right. You have a custodian, any time you have an HSA, it has to have an HSA custodian. So couple of things to realize. First off, it's your money so you choose your custodian. And if you leave your employer, if you like the custodian, you can leave it right there, just like you like your 401k from your previous employer, you keep it right there. Or, you can do a transfer and move it to a new custodian. You can keep a number of HSA accounts out there, or you can consolidate them all under one umbrella, one custodian. The thing to realize is is you don't have to separate employment. If you're with an employer, and their HSA is a dinosaur, and they're looking at you cross-eyed, when you say investment options and they're saying we offer you a money market account and that is it. I'm moving my money tomorrow. Right, now the ongoing payroll deductions will continue to go into whoever my employer has tied with the group health insurance plan. But the existing balance can be transferred. Now, you want to be aware of fees, as well. Be sensitive to that. Maybe it's a once a year transfer, not every month.

Ben Jones - When it comes to fees on HSAs, I'm assuming all custodians have different fees and different schedules. Are they straight forward; are they a bit confusing at times, kind of like the old 401ks?

Peter Stahl - Yeah, it can be a little confusing. You'll typically have a custodial fee. So that might be, pick a number, $4 a month, $3 a month, so kind of that $36 to $48 a year type custodial fee. Then, if you're going to invest the assets, you'll have underlying costs, so it's just like selecting a mutual fund, you want to look at expense ratios and those type things to make sure that your fees are competitive.

Ben Jones - Are there any disadvantages to using this as a saving and investment vehicle versus kind of more like an FSA.

Peter Stahl - Boy, I mean I guess the only disadvantage would be you get this fully invested and the markets go down, and you say, I have to have this money, right. Bad planning. If you're going to get fully invested, you need to have a timeframe, right, where you can let that money grow and work and not sweat it when the market goes down. This is built-in dollar cost averaging, right, because you're making that contribution each and every year so you ought to be rooting for the down years. You want to get some of those pullbacks so you're buying in to those funds or ETFs or whatever you're investing this HSA in, during the downside. So that's the only, you really got to make sure you can commit to an appropriate timeframe.

Ben Jones - As I said, Peter has some amazingly practical ideas, for you to take to your clients so they can better harness the benefits of HSA accounts. Now you want to check out the show notes page at bmogam.com/betterconversations for links to his web site, his book and you can even hire him to speak for client events. As advisors thinking about the subject, I asked Peter what questions he most often gets about HSAs and financial planning.

Peter Stahl - The HSAs are growing in popularity. So the next logical question that you get from an advisor is can I offer an HSA to my clients, and basically help them choose the investments, maybe even be compensated on that HSA. And now the answer is generally-speaking yes. If advisors want to contact me and work through that, I can explain that in more detail, but the concept really is, if you're working through a broker/dealer, your broker/dealer needs to approve an HSA product for your broker/dealer in order for you to offer it, advise on it and be compensated on it. We're really not there yet. I'm having some pretty interesting conversations with broker/dealers about this. But we're getting close, 2018 you'll start to see some of these break through, but generally-speaking not there. But if you're let's say an RIA and you want to offer an HSA solution to your clients, maybe you want to private label it, or maybe you just want to use a custodian-branded solution, you can do that. You can charge an asset-based fee on that, you can charge a flat dollar amount, so I can help advisors work through that. And the more interesting conversation even gets if you're working with a business on their defined contribution plan, what I love to see is an advisor step in there and say let's mirror what you're doing on your defined contribution plan with the HSA. We'll take the same mutual fund choices, or ETF platform you have and we'll setup model portfolios. Some people are going to use a money market account or maybe even a stable value fund. But other people are going to say sure, it's the same timeframe, it's retirement, it's the same risk profile, let's setup these model portfolios and do in my HSA what I'm doing in my 401k.

Ben Jones - Boy, the simplicity of that creates for an employee, just to not have to understand a separate set of investments, and have someone who's overseeing and monitoring them.

Peter Stahl - But the only way that happens, Ben, is if an advisor steps forward, right, and says I have a solution. This is how it would look, I can put this in place for you, so those are the interesting conversations, really even over the last six months. That I'm having with RIAs in particular and then to some extent the broker/dealers about how do we make this happen.

Emily Larsen - As you can see, we are in the early days of the convergence of healthcare, HSAs and financial planning. We want to extend a big thank you to Peter Stahl for enlightening us and providing you with actionable ideas you can use for better conversations with your clients. For additional training on HSAs including CFP® continuing education check out his resources at yourwealthwatch.com. We'll leave you with Peter's last piece of advice on the topic.

Peter Stahl - If you fail to address these issues in the financial plan, I mean let's face it, most financial advisors, myself included, did not get into this industry to do this type of planning. But if we fail to recognize the enormity of healthcare costs, of custodial care, of the means testings. If we fail to do this, we are really not acting in the best interest of our clients and there's all this chatter, fiduciary standards and best interests and doing what's right for the client. Wherever that lands, if that's the path we want to follow, we have to at least have some proficiency on the convergence of healthcare and financial planning.

Ben Jones - Thanks for listening to *Better conversations. Better outcomes*. This podcast is presented by BMO Global Asset Management. To learn more about what BMO can do for you, visit us at www.bmogam.com/betterconversations.

Emily Larsen - We value listener feedback and would love to hear what you have thought about today's episode. Or, if you're willing to share your own experiences or insights related to today's topic, please e-mail us at betterconversations@bmo.com. Of course, the greatest compliment of all is if you tell your friends and coworkers to subscribe to the show. You can subscribe to our show on iTunes, Google Play, the Stitcher app, or your favorite podcast platform. Until next time, I'm Emily Larsen.

Ben Jones - And I'm Ben Jones. From all of us at BMO Global Asset Management, hoping you have a productive and wonderful week.

Emily Larsen - This show and resources are supported by a talented team of dedicated professionals at BMO, including Pat Bordak, Gayle Gipson, Matt Perry, and Derek Devereaux. This show is edited and produced by Jonah Geil-Neufeld and Annie Fassler of Puddle Creative.

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