

Improving Financial Literacy and Capability: What Works?

The George Washington University School of Business, June 21, 2012



UNDERSTANDING AND IMPROVING FINANCIAL LITERACY: HEALTHCARE EXPENDITURES IN RETIREMENT

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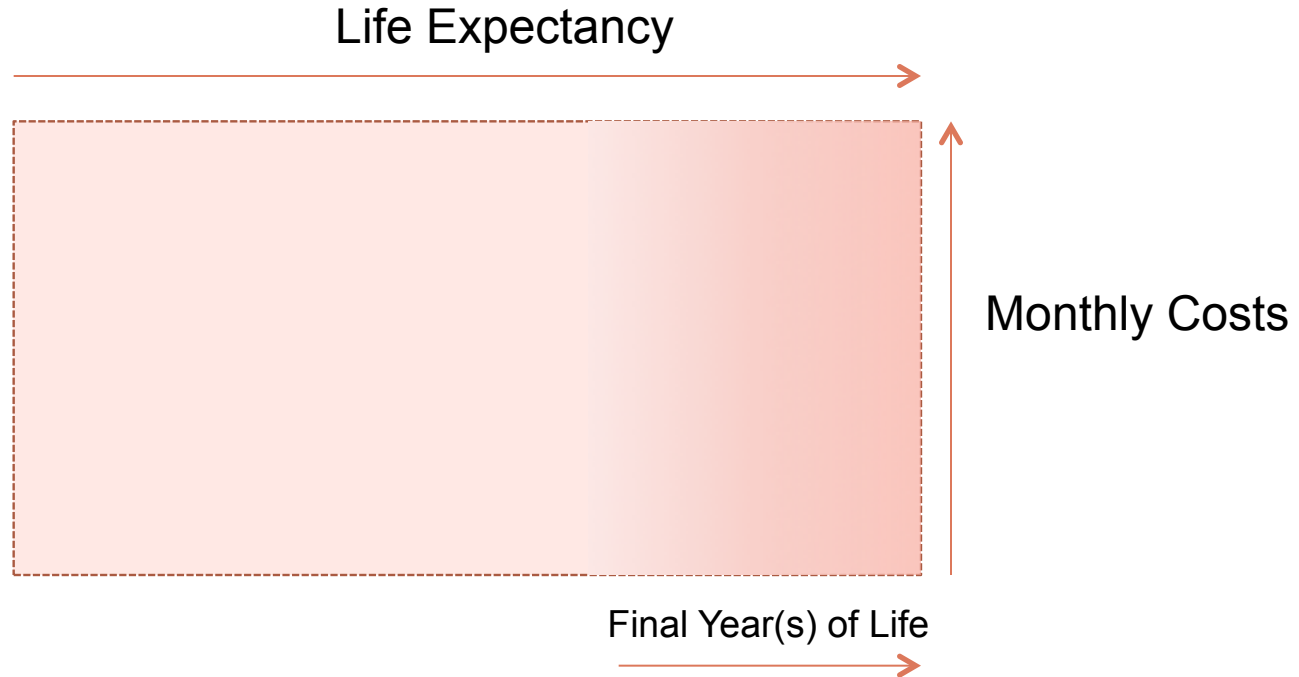


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Overview

- Financial Literacy Regarding a Complex Problem
 - “How much will you need to spend on out-of-pocket costs for health care during your retirement years.”
 - “Out-of-pocket costs are any expenses that you pay yourself. In addition to any direct payments, these costs include insurance premiums for government programs and other health insurance plans. Out-of-pocket costs also cover deductibles and co-pays. Out-of-pocket costs do not include payments made on your behalf or reimbursed by government programs or other insurance plans. In all cases, we are asking about your own personal health care costs in retirement. Do not include health care costs of other members of your household. Unless otherwise indicated, please do not include in your estimates the cost of long-term residential health-care services (such as extended stays in nursing homes) or premiums for long-term health care insurance. Some questions ask for estimates about costs in the future. Please do not attempt to adjust your estimates to reflect price increases from overall inflation. Just make your estimates using the value of money today.”

Estimating Retiree Health Care Costs



- Key Sources of Additional Uncertainty
 - Personal Health Experience and Medical Needs
 - Unanticipated Inflation in Medical Costs
 - Policy Changes with Respect to Medicare and other Programs

Structure of Paper

- Literature Review of Expert Views
- Survey from American Life Panel
 - 1700+ responses from Eight 5-year Age Cohorts: 40 to 80
 - Background Questions on Health, Financial Sophistication and Life Expectancies
 - Three Treatments
 - ✦ A. Three Simple Questions on Health Care Costs
 - ✦ B. + Segmented Questions on Expected Insurance Coverage, Expected Premiums. Costs at 65, 75, and 85.
 - ✦ C + Anchoring from Expert Views on Life Expectancies, Premiums, Ratios of Total Costs to Premiums
- Modules on Risk Assessments/[Long Term Care]

Summary of Findings

- Expectations About Insurance Coverage Vary

Table 2: Retiree Health Insurance Coverage Expectations by Cohort and Age

	N	Medicare		Medicaid		Employer Sponsored	
		Mean	SD	Mean	SD	Mean	SD
40-44	128	55.29	28.53	39.98	31.86	32.56	31.51
45-49	157	61.14	29.96	43.84	35.34	24.49	32.11
50-54	156	67.73	29.13	45.01	34.32	29.03	33.98
55-59	173	74.21	22.17	46.80	34.21	35.08	38.00
60-64	158	81.93	25.97	30.50	37.32	35.82	42.93
65-69	176	88.75	22.03	25.98	36.94	40.62	46.24
70-74	106	88.38	24.42	25.30	37.63	32.79	45.84
75-80	75	91.89	22.25	27.82	40.97	29.35	43.83
All Respondents	1154	72.86	29.10	37.84	36.36	32.05	38.49
Coverage from Literature Review		95 percent		15 percent*		33 percent *	

* Reflects Percentage of Coverage of Medicare Beneficiaries.

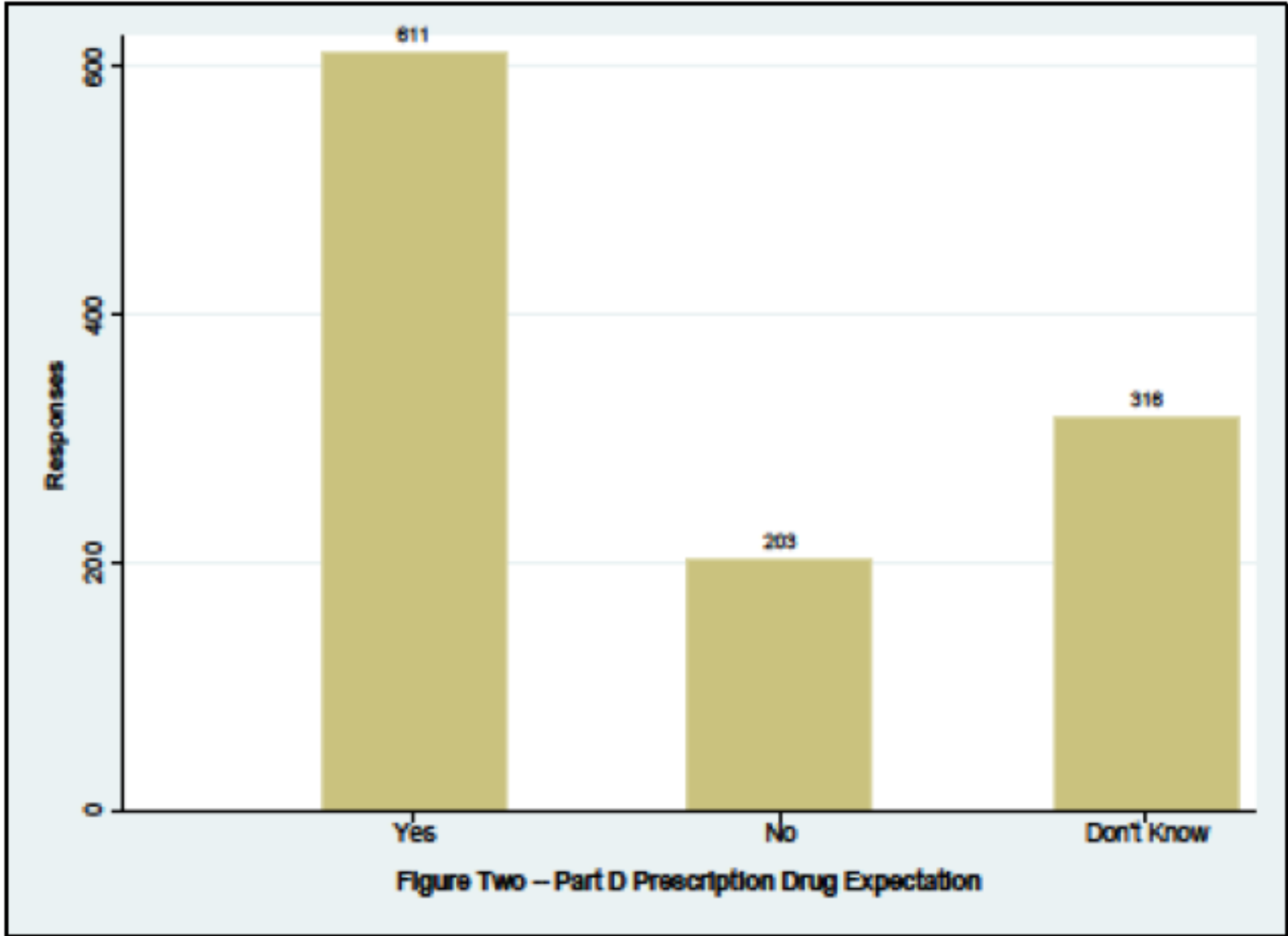


Figure Two – Part D Prescription Drug Expectation

Summary of Findings

- Expectations About Insurance Coverage Vary
- Expectations on Premiums Affected by Treatments and Narrows with Age

Table Three: Expectations as to Insurance Premiums for Respondents in Treatments B and Treatment C*

	N	p10	p25	Median	p75	p90	Mean	SD	Ranges Suggested in Anchoring for Treatment C**
Treatment B									
Total Medicare Premiums	573	30	98	120	250	500	210.8	252.6	<i>n.a.</i>
Medigap Premiums	568	0	0	50	150	206	105.7	173.3	<i>n.a.</i>
Employer Sponsored Premiums	566	0	0	55	200	450	149.1	254.8	<i>n.a.</i>
Treatment C									
Total Medicare Premiums	562	50	100	135	200	350	259.2	1018.7	<i>\$96 to \$115 for typical basic Medicare Premium plus an average of \$40 for typical Part D Prescription Drug Coverage</i> <i>Considerable variation in policy types, but majority of monthly medigap premiums range between \$50 and \$200</i> <i>Average Participant Costs for Those Over 65 roughly \$167</i>
Medigap Premiums	229	25	50	100	185	250	134.6	141.3	
Employer Sponsored Premiums	342	0	80	165	200	330	300.1	1579.0	
* Estimated Requested Only for Respondents Who Indicate Some Possibility of Maintaining Insurance Coverage at Some Point in Retirement.									
** See Appendix C for Additional Detail on Anchoring.									

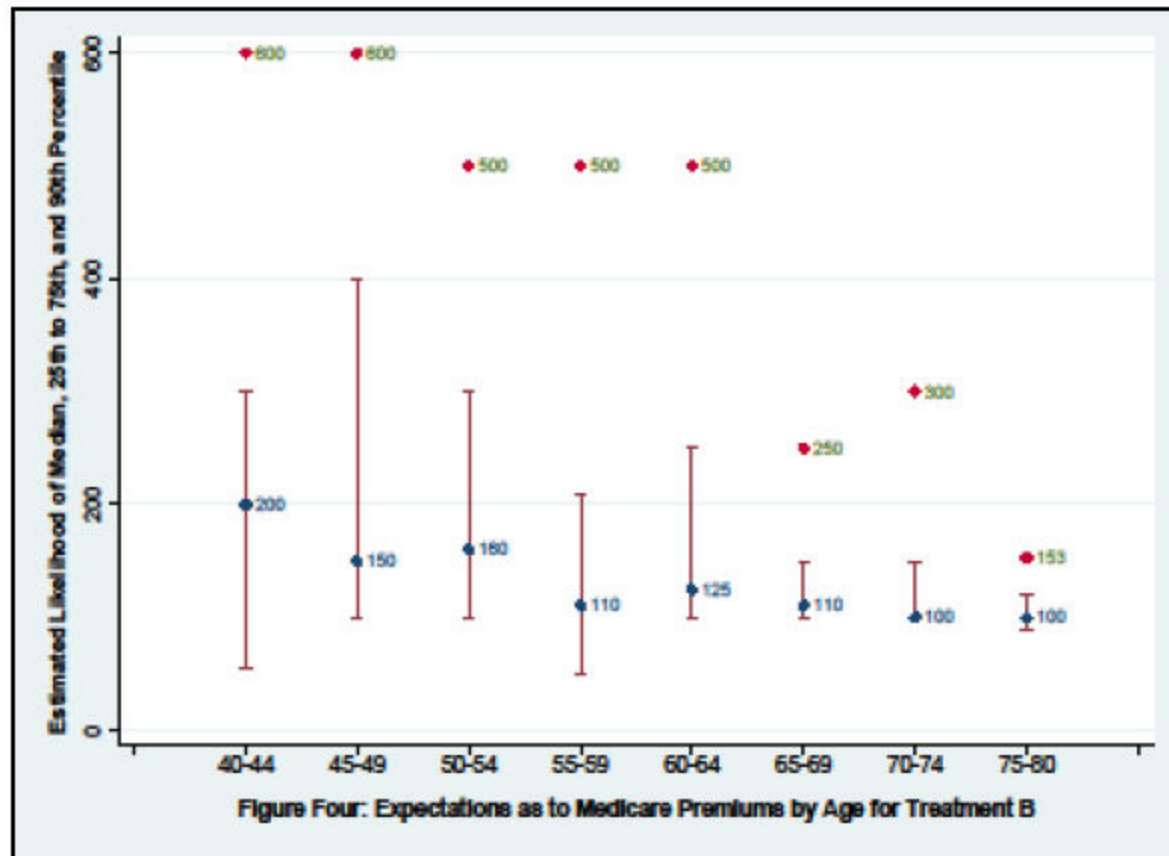
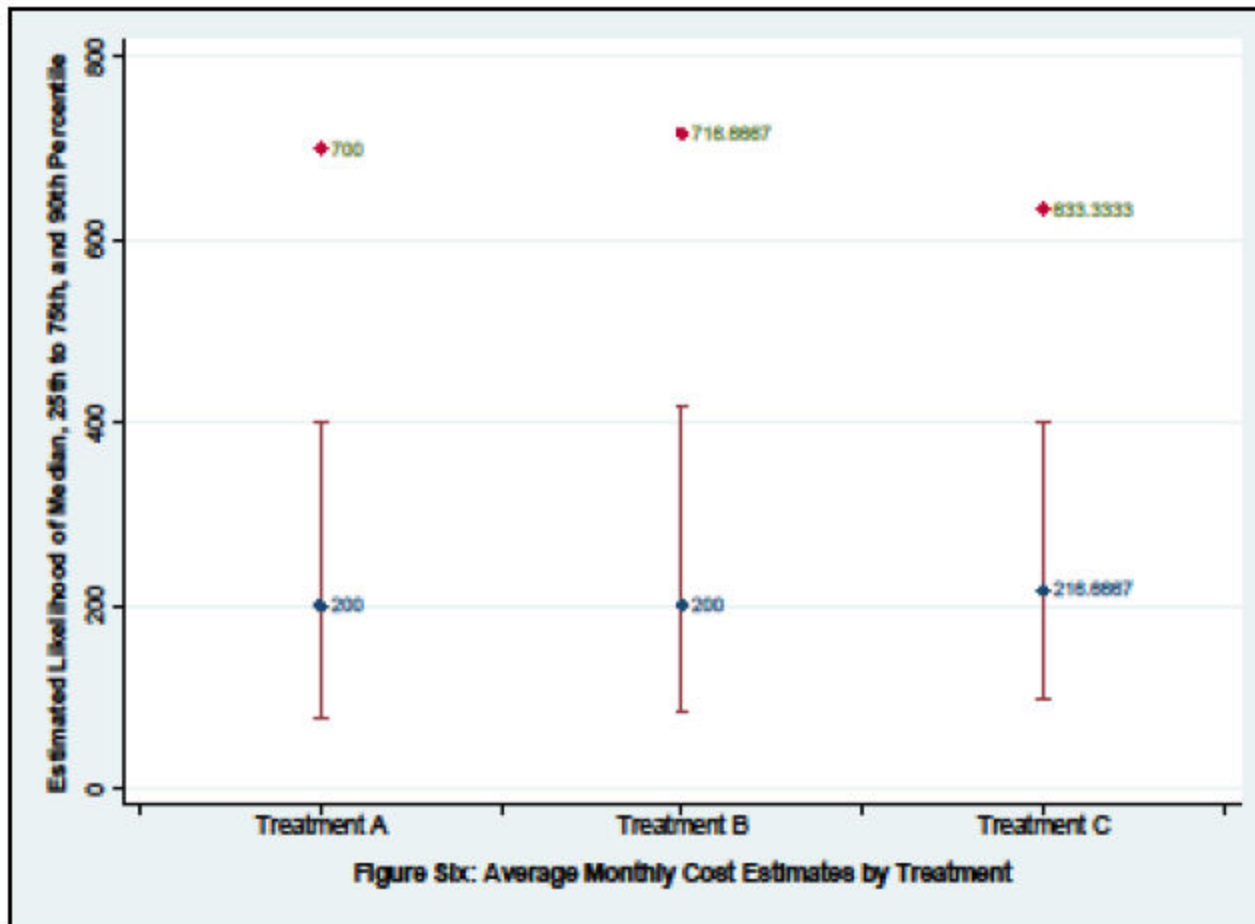


Figure Four: Expectations as to Medicare Premiums by Age for Treatment B

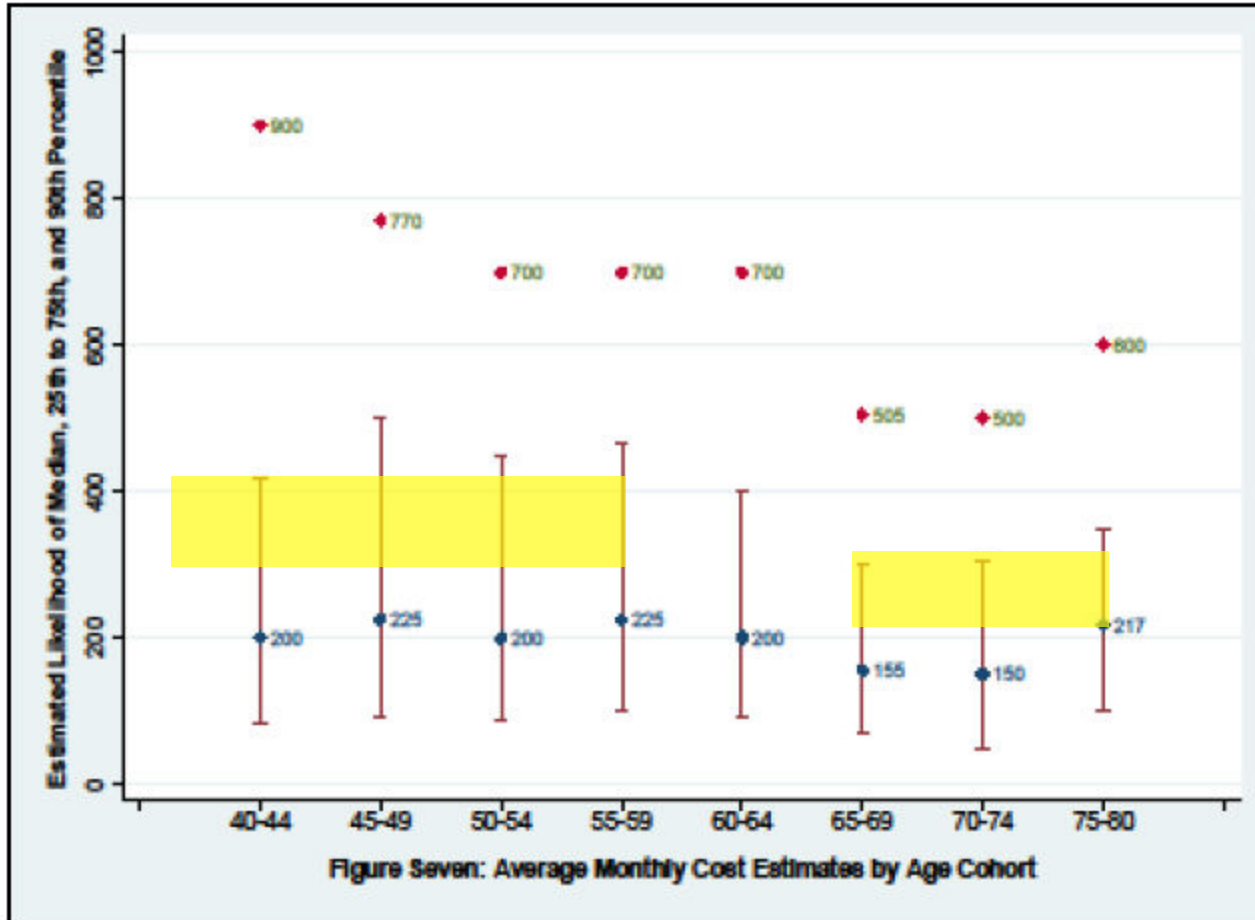
Summary of Findings

- Expectations About Insurance Coverage Vary
- Expectations on Premiums Affected by Treatments and Narrows with Age
- Expectations on Total Costs Less Affected by Treatments but Also Narrow with Age, Rise in time

Estimates Are Similar Across Treatments



Less Variation Across Age Groups



Sensitivity to Cost Growth with Aging

Table Five: Estimates of Changes in Monthly Costs During Retirement

	N	p10	p25	Median	p75	p90	Mean
Final Year Monthly Costs	1671	25	120	350	800	2000	1797.7
Ratio of Final Year Monthly Costs to Average Monthly Costs	1599	0.83	1.00	1.46	2.40	5.71	5.34
Ratio of Estimated Monthly Costs at 85 to Estimated Monthly Costs at 65	782	0.46	1.00	1.33	2.00	2.60	1.72

Summary of Findings

- Expectations About Insurance Coverage Vary
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- **Similar Results for Lump Sum Estimates**

Lump Sum Estimates by Treatment

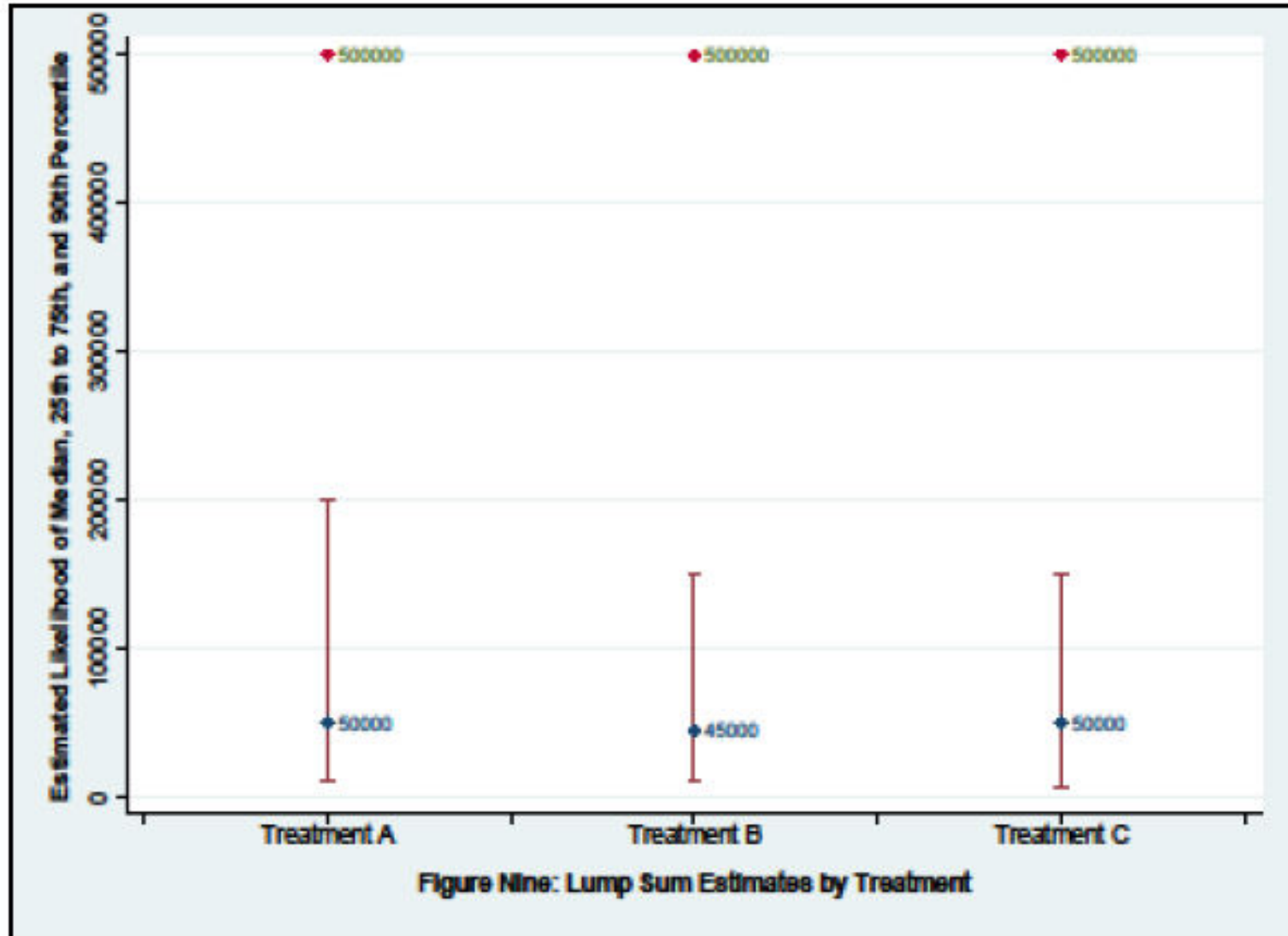


Figure Nine: Lump Sum Estimates by Treatment

Lump Sum Estimates by Age Cohort

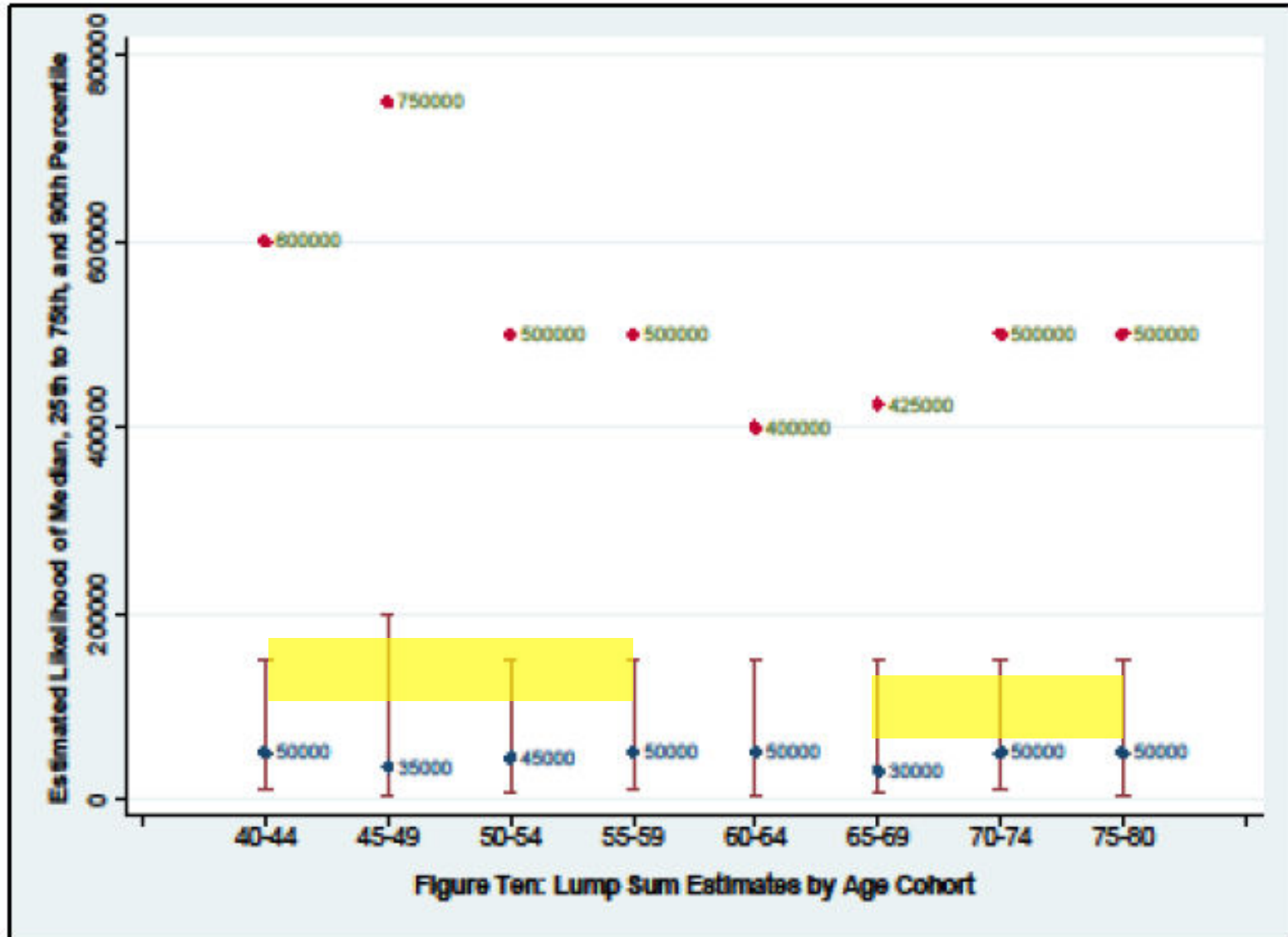
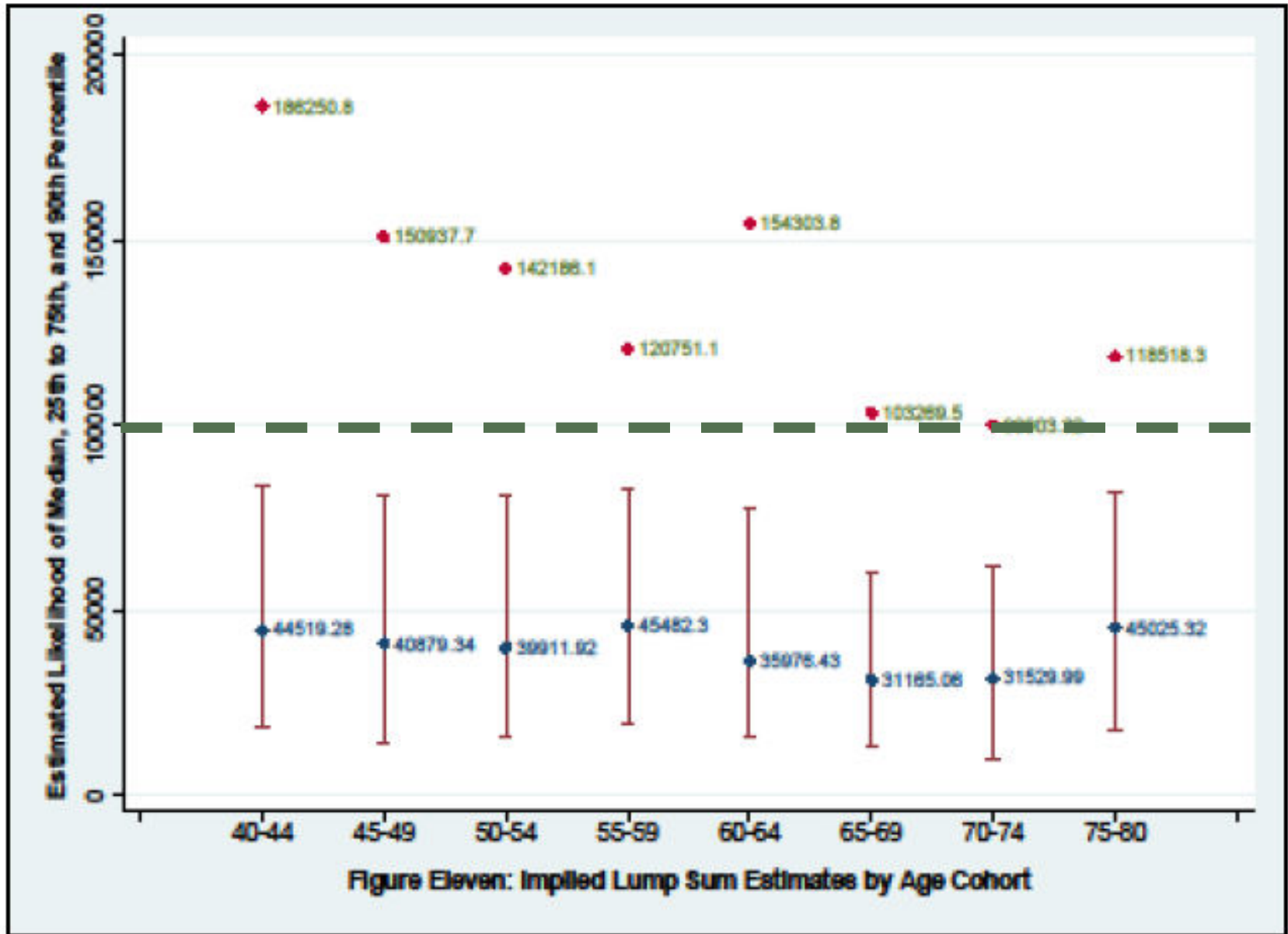


Figure Ten: Lump Sum Estimates by Age Cohort

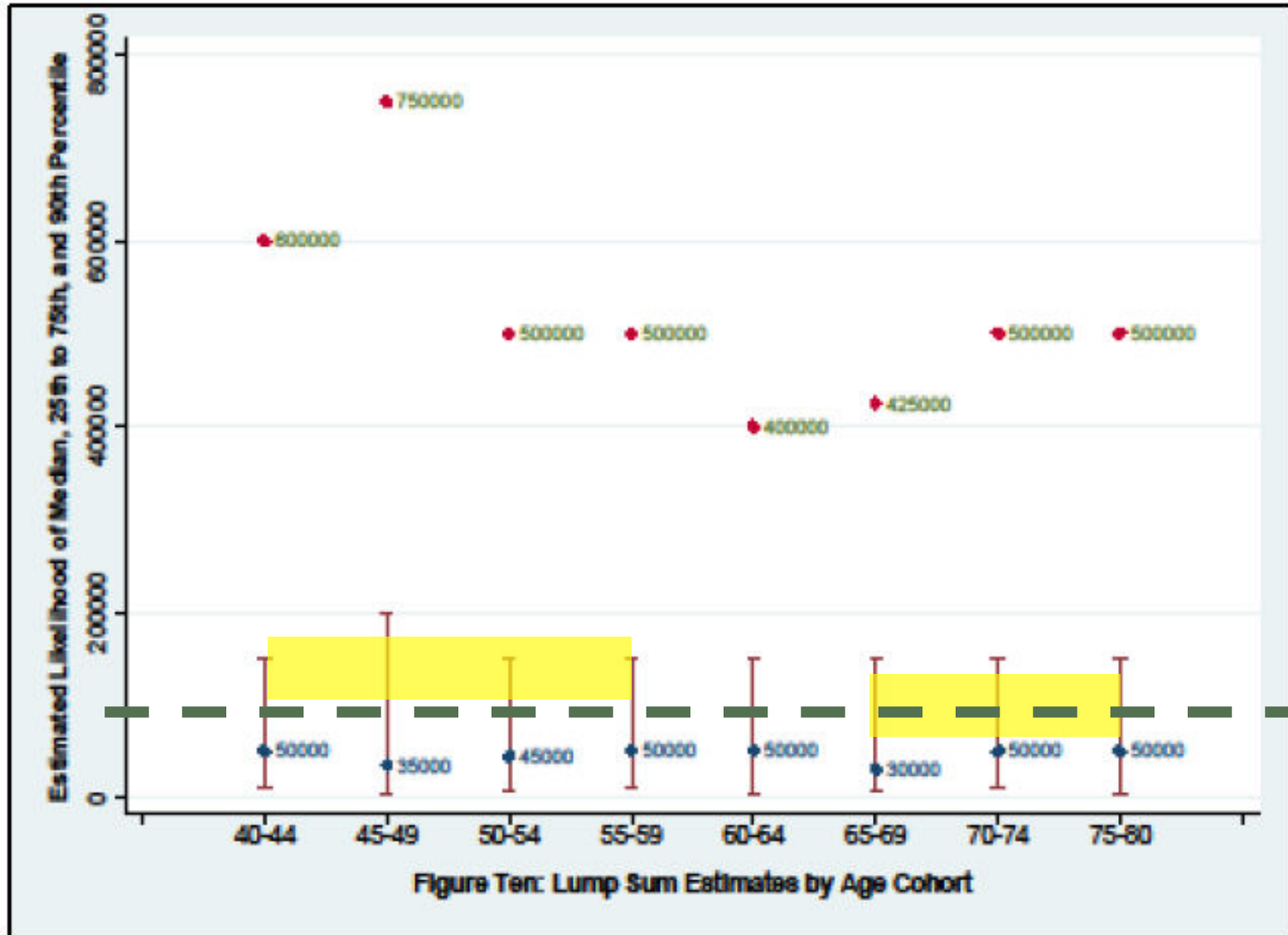
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- Expectations About Insurance Coverage Vary
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- Similar Results for Lump Sum Estimates
- **Lump Sum Estimates Not Hyperbolically Discounted**

Actual Lump Sum Versus “Implied Lump Sum”



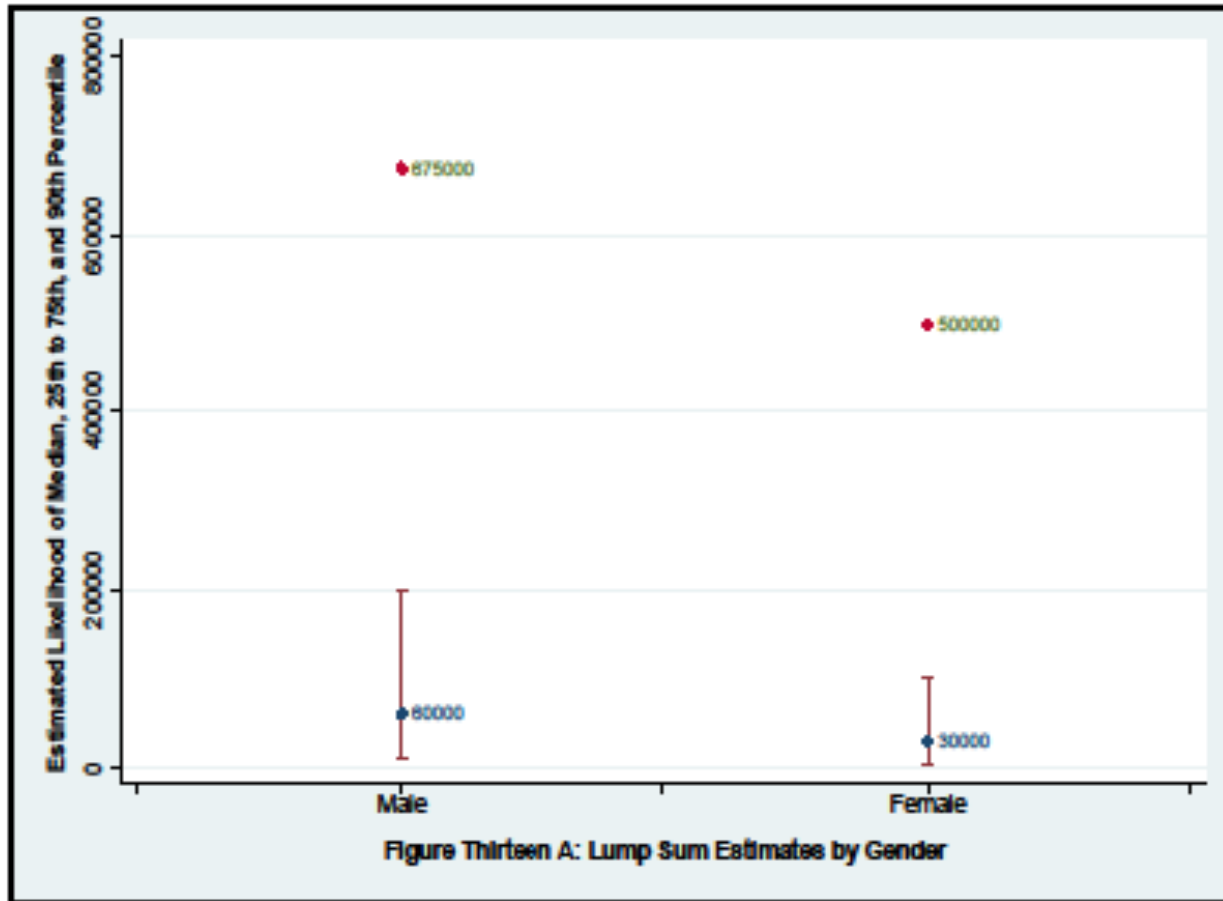
Lump Sum Estimates by Age Cohort



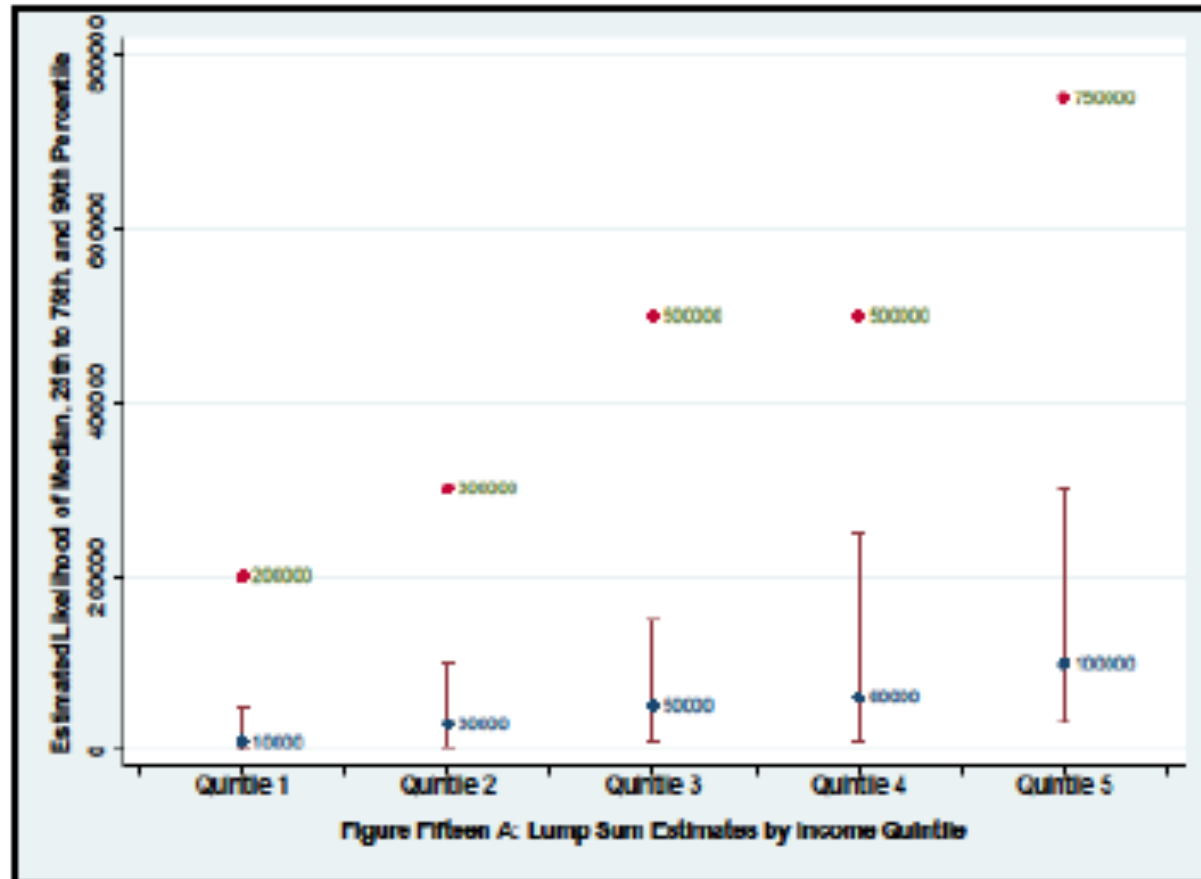
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- Expectations About Insurance Coverage Vary
- Expectations on Premiums Affected by Treatments and Narrows with Age
- Expectations on Total Costs Less Affected by Treatments but Also Narrow with Age , Rise in time
- Similar Results for Lump Sum Estimates
- Lump Sum Estimates Not Hyperbolically Discounted
- **Variation in Estimates Not Consistently Associated With Most Common Correlations**

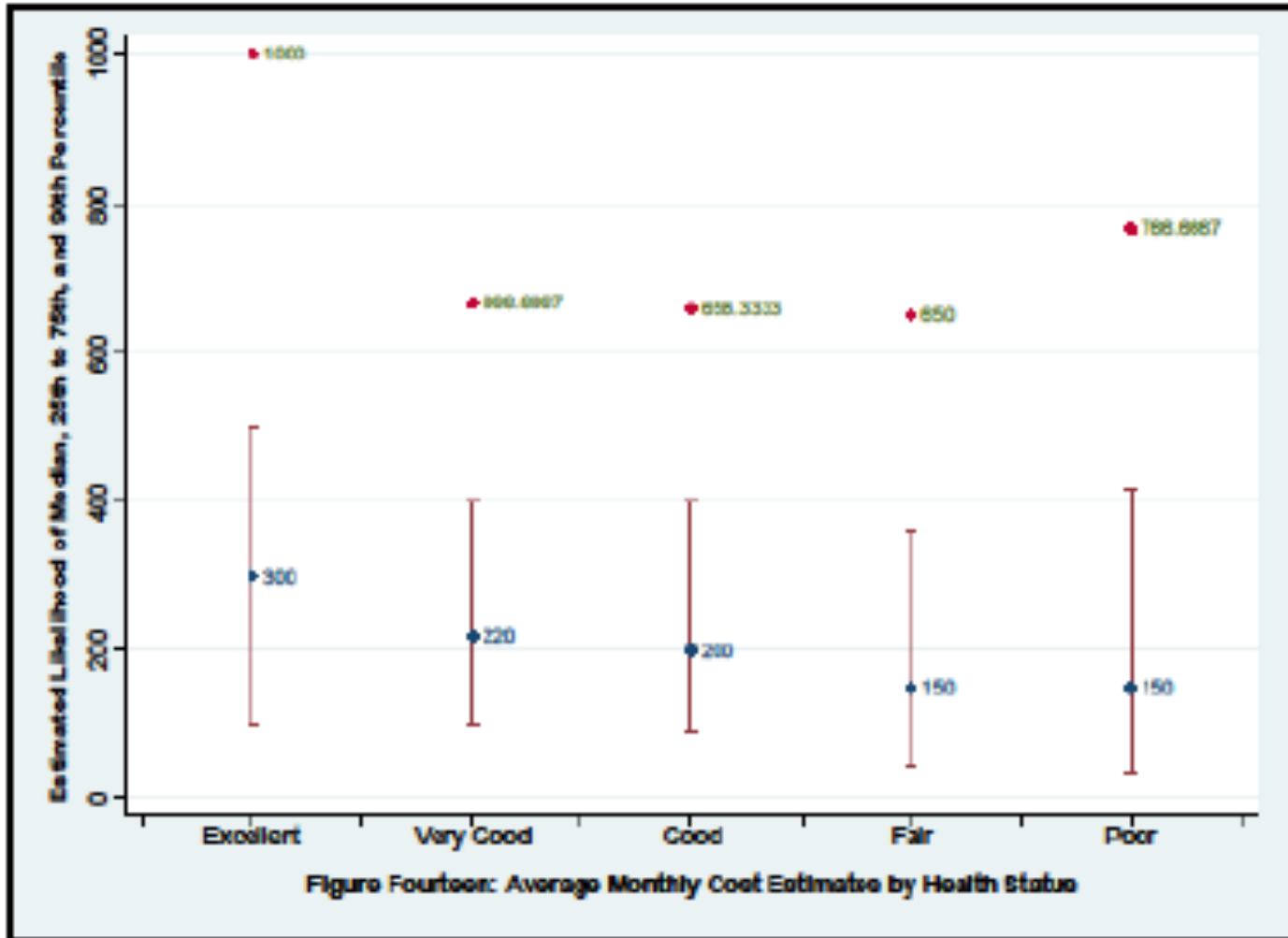
Lump Sum by Gender: $M > F$!



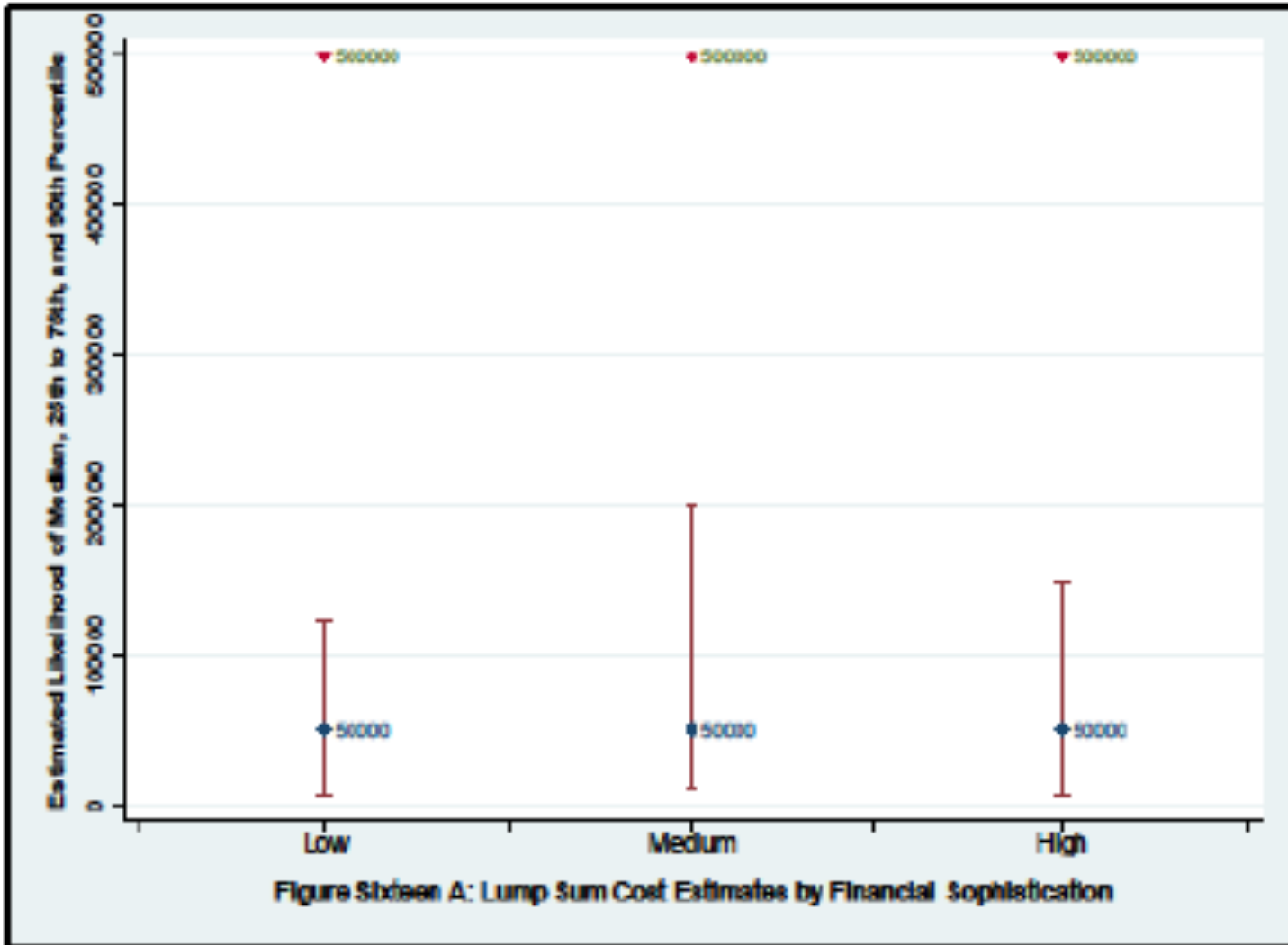
Lump Sum by Income: Wealth > Poor



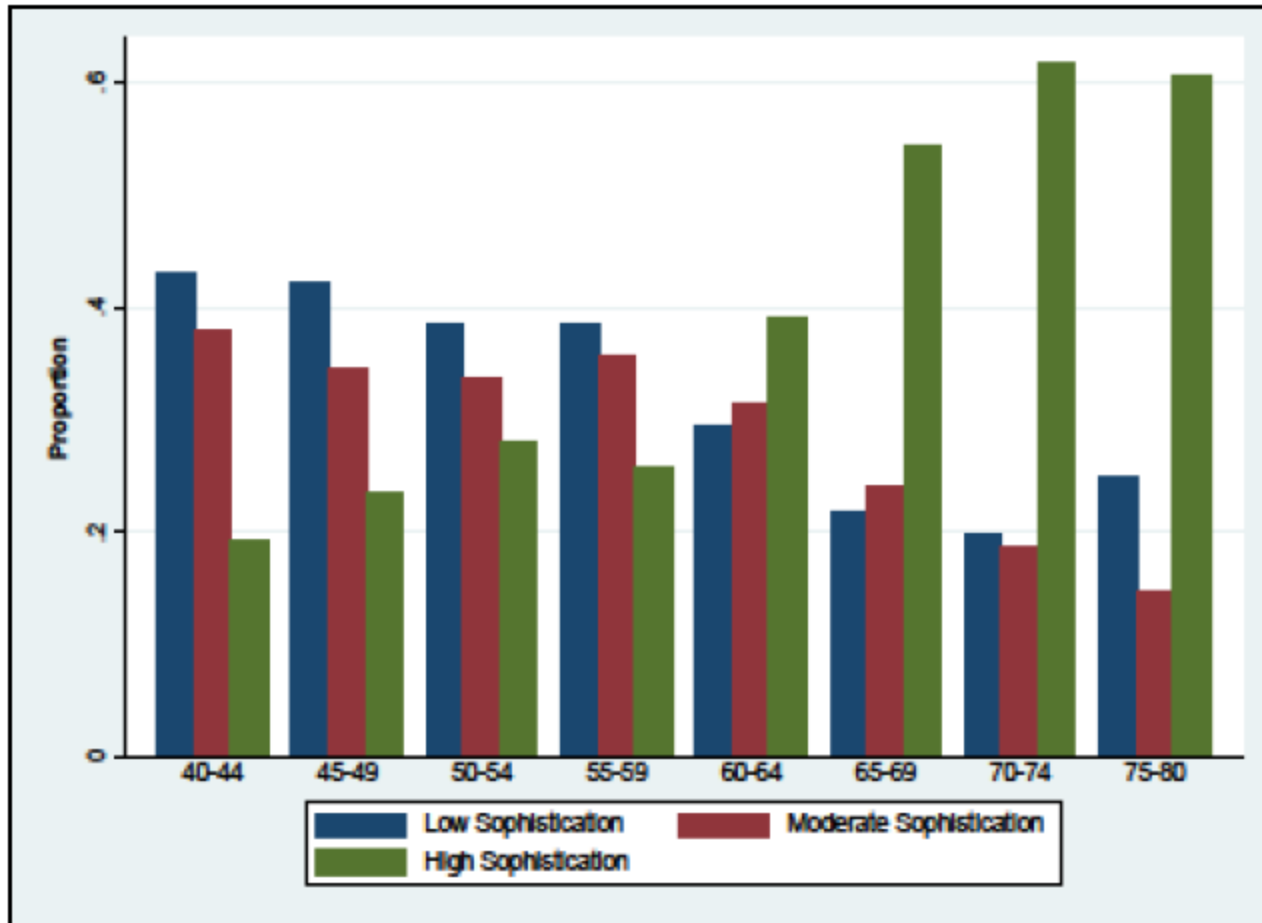
Lump Sum by Health: Excellent > Poor



Lump Sum by Financial Sophistication: +/-



Self-Reported Financial Sophistication



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- Expectations About Insurance Coverage Vary
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- Expectations on Total Costs Less Affected by Treatments but Also Narrow with Age , Rise in time
- Similar Results for Lump Sum Estimates
- Lump Sum Estimates Not Hyperbolically Discounted
- Variation in Estimates Not Consistently Associated With Most Common Correlations
- **Responses on Risk Assessments Mixed, Understated**

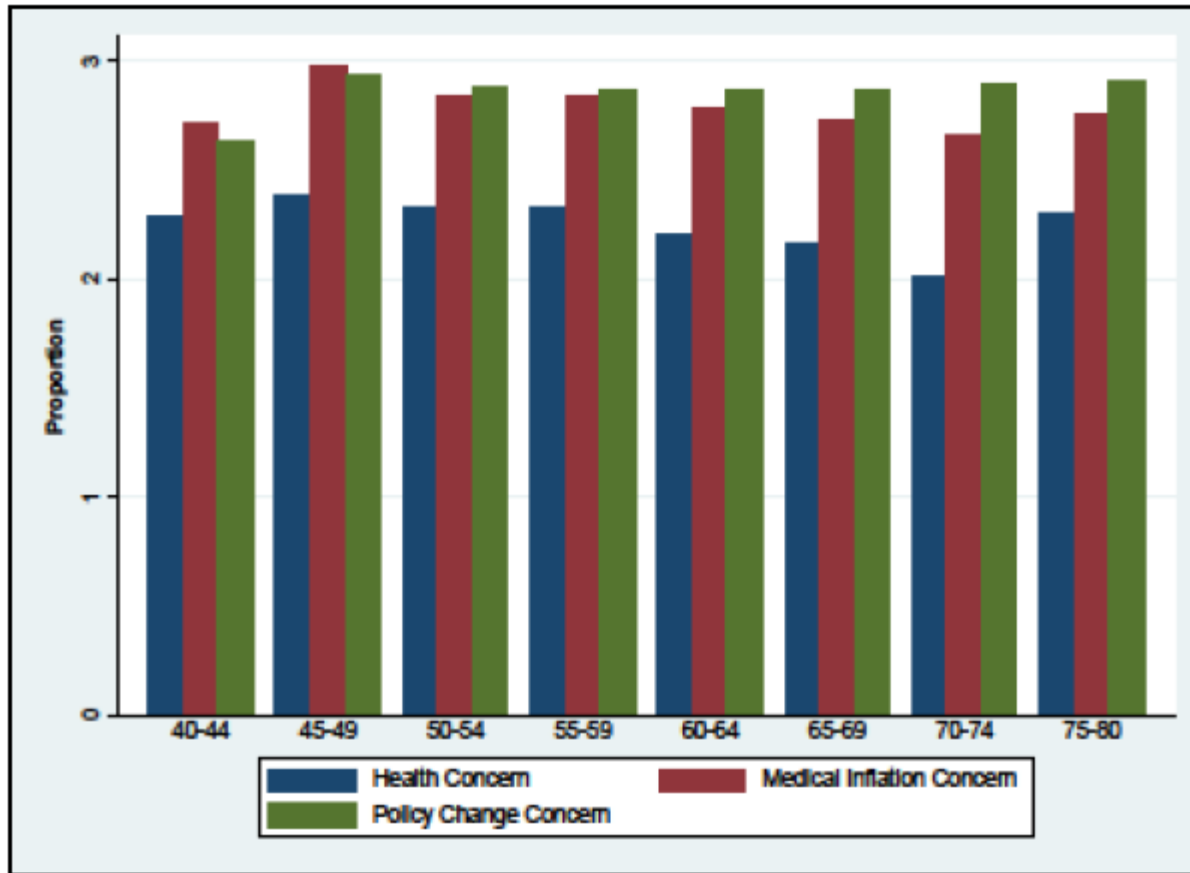
Ambiguous Results on Risk

- Summary Results on Module One: Willingness to Pay

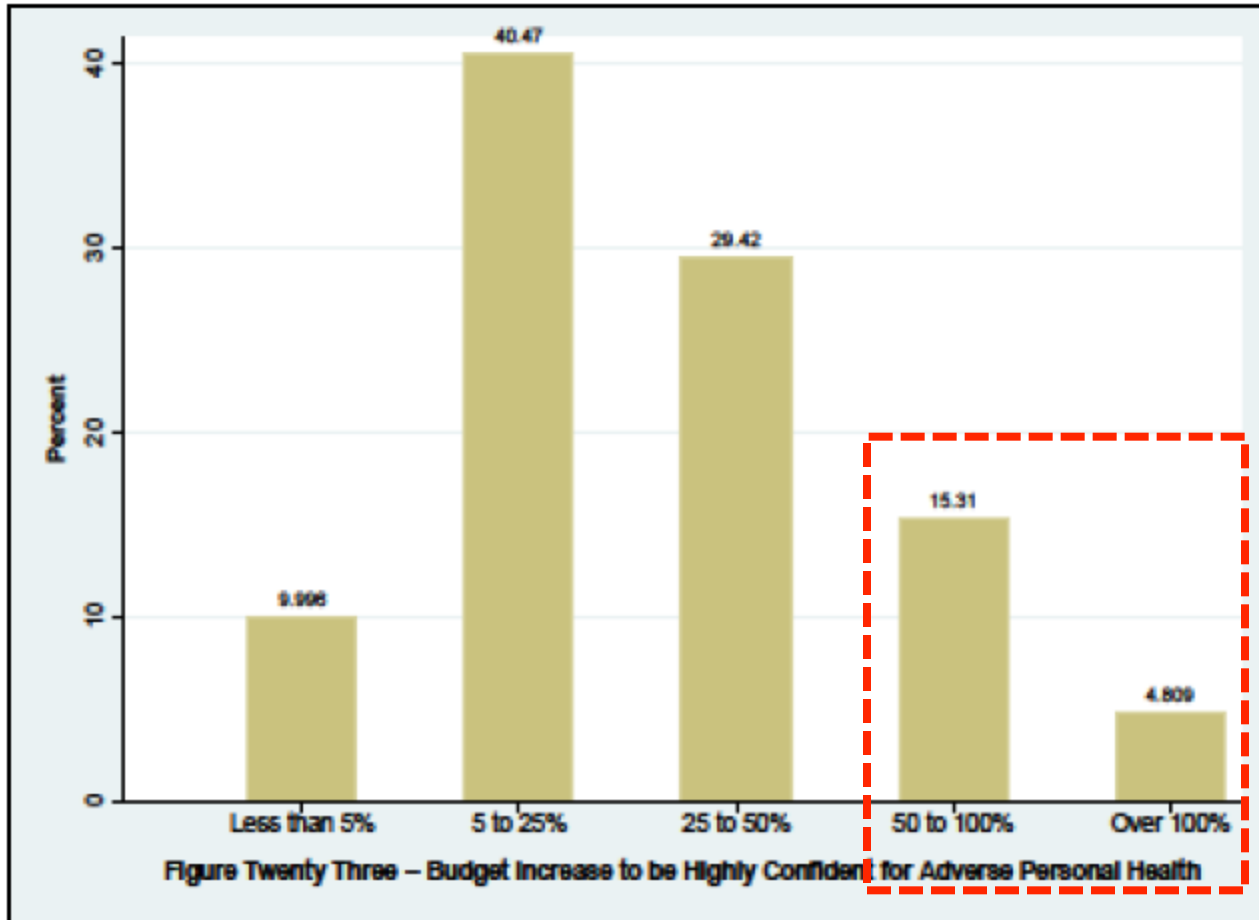
Table Nine: Willingness to Pay for Protection Against Three Risks

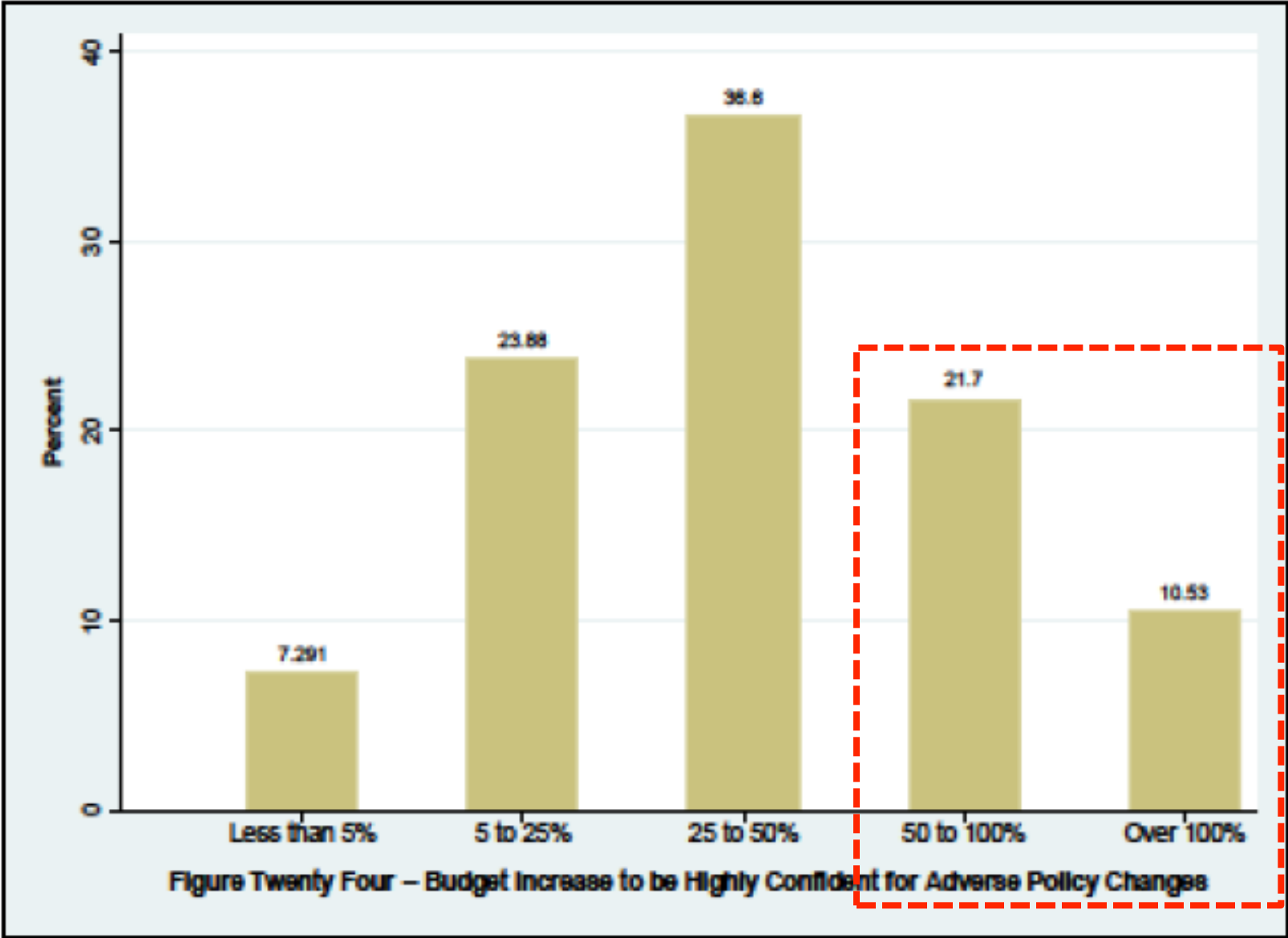
	N	p10	p25	Median	p75	p90	Mean	SD
Protection Against High Costs from Personal Health Experience	834	30	75	150	300	600	573.5	4510.7
Protection Against High Costs Unanticipated Inflation in Medical Costs	833	20	50	125	250	500	341.0	1364.6
Protection Against High Costs from Adverse Policy Changes	833	10	50	120	250	500	441.9	3434.2

Module Two: Concern About Risks



Module Two: Assessment of Severity





Further Research and Extensions

- Considerably More Work Can be Done in this Dataset
 - Controlling for different characteristics
 - Analyzing Long Term Care Estimates
 - Assessing Interactions with Insurance Coverage Expectations
- Better Coordination with Medical Cost Researchers
- Additional Work on Accuracy of Estimates on an Individual Basis; Mapping to Actual Savings Behavior
- Policy Implications from Apparent Misperceptions
 - Gender Differences
 - Implicit Negative Discount Rates on Many Lump Sum Estimates
 - Educational Efforts with Respect to Health, Policy Risks

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