Student Debt Putting Retirement Planning on Hold?

Near-retirees and midcareer workers are feeling similar stress as recent college grads.

There’s no doubt that the rising cost of college is putting lots of financial stress on American workers. Frequently, the cost of attending a four-year private university is more than the average cost of a home in most areas of the country. Here is a snapshot of the student loan landscape, along with some suggestions for what to do if you’re feeling the pinch.

Student debt by the numbers

Student loan debt in the United States now totals $1.56 trillion.¹ This drag on household finances not only can delay plans to get married, have children, or buy a house, but also defer retirement savings, which is by far the largest single expense you will have to fund. Did you know that:

- The average student in the class of 2017 has $28,650 in outstanding student loans;² and the average loan payment for borrowers age 20 to 30 is $351/month.³
- Notably, roughly eight million Americans age 50 and above owe $20,000 more than new graduates and are still paying off loans.⁴
- Women shoulder almost two-thirds of outstanding student loans — about $929 billion — even though they account for just 57 percent of students enrolled in colleges and universities.⁵

Options for managing student loan debt

The rules governing how private student loans are repaid are some of the strictest around. Younger borrowers often do not have any credit history, and lenders, who are mindful of the added risk of lending to borrowers with no track record, can make it difficult to restructure a loan repayment plan. Still, here are some available options:

Loan consolidation — If you are carrying high balances on your student loans, car loans, or credit cards, it may be more cost-effective to put all of your outstanding debt under one consolidated payment plan with a single lender. Generally, this is a viable option if you have a steady employment history, reliable monthly income, and a strong history of making payments on time.

Graduated payment plans — Some federal student loan options let you pay less in the beginning of the term, and then pay more later. Graduated plans usually are limited to 10 years, unless you opt for loan consolidation.

Extended repayment plans — These plans let you lengthen your repayment time line for up to 25 years, securing a lower monthly payment in the process. You’ll ultimately pay more on your loans for a longer time period, but your monthly savings can be significant.

Private loan company refinancing — Private student loan companies could be a viable option if you have a good credit rating. But you may lose some of the borrower protections that come with federally guaranteed loans.

DID YOU KNOW?

Government student loan programs generally offer more protection options and flexibility than those offered by private lenders.

The Lowdown on Health Savings Accounts

With longer life spans come extended health-care needs — and significantly more dollars required to pay for them

It's more likely today that you'll live longer than your grandparents did. The flip side is that you may spend far more on doctors' bills and treatment for chronic illnesses than previous generations. With health-care costs continuing to rise along with life expectancies, health savings accounts (HSAs) are an increasingly popular way to bridge the retirement and health savings gap.

Most retirees are underfunding their future health-care needs

It's very difficult to visualize a future unknown such as health-care expenses — let alone set aside money to pay for them. But according to a 2019 research report, a 65-year-old couple retiring today will need $360,000 to cover their total lifetime health-care costs. Plus, while 70 percent of Americans age 65 or older will need some form of long-term care during their lives, only 17 percent are very or extremely confident that they'll have the resources to pay for it. And the numbers suggest a growing funding crisis: according to HSA Bank, 40 percent of consumers never set aside money specifically for future health-care costs.

An HSA complements your retirement plan

The key with any large expense is to break it down into manageable chunks. Just as your retirement plan takes manageable amounts out of your paycheck each month, you can use an HSA to pay for future health-care expenses by making small, regular deposits. An HSA is a hybrid savings and investment account that lets you set aside funds in a tax-advantaged way, and allows you to:

1. Pay for Medicare premiums on a tax-qualified basis, meaning your contributions are taken from your paycheck before taxes are taken out
2. Pay for qualified long-term care insurance premiums tax-free
3. Reimburse yourself for qualified medical expenses at any time, with tax-free withdrawals
4. Avoid taking required minimum distributions at age 70½
5. Set aside funds that are not factored into income for Medicare means testing.

How HSAs work

An HSA allows you to lower your federal income tax bill by making tax-free deposits each year. In order to contribute to an HSA, you must be enrolled in a high-deductible health insurance policy (HDHP), either through your employer or on your own. In 2020, the Internal Revenue Service has set minimum deductibility limits for HDHPs of $1,400 for individuals and $2,800 for families. You can't be covered by another person's health plan, and your income isn’t a factor in your eligibility.

The amount you contribute to your account can be invested in basic interest-bearing accounts or funds, and the amounts deposited along with any earnings can be withdrawn tax-free at any time to pay for qualified medical expenses not covered by your HDHP. (Qualified expenses include items such as dental and vision costs, as well as preventive medications, such as sunscreen, bandages, and lip balm, among other things.)

You must stop contributing to an HSA once you enroll in Medicare.

An average of $245 per day to cover a semiprivate room in a nursing home in 2018.

You can also use your HSA to pay for medical expenses of a spouse or other family member — even if they are not covered by your health insurance. If your employer offers an HSA, you can take your account with you when you retire or change jobs.

If you're healthy and don't anticipate having much in the way of medical expenses as you get older, an HSA can be an excellent long-term tax-advantaged investment. But if you wind up needing long-term care not covered by Medicare, a well-funded HSA may be able to fill any short-term funding gap — giving you and your loved ones peace of mind.
How an HSA Works

Funds go into an individual account that is **TAX-DEDUCTIBLE**

Funds **ACCUMULATE** and carry over from year to year

### PHARMACEUTICAL

- Take your prescription to the pharmacy and present your insurance ID card.
- The pharmacy will confirm your insurance coverage and charge you only the discounted rate.

### MEDICAL

- Choose a doctor either in or out of network.
- Visit the hospital, lab, doctor’s office, or imaging area. No copay is required (before deductible — some plans require a copay after the deductible).

**PAY THE PROVIDER BY EITHER:**

- Using your HSA FUNDS (debit card or transferring investment funds to your personal account).
- Paying OUT OF POCKET and keeping money in your HSA investments. (You must save your receipts to REIMBURSE yourself tax-free in the future.)

* Refer to IRS Publication 502 for a complete list of eligible expenses.

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Three HSA Mistakes to Avoid

There are lots of advantages to an HSA. But you should keep these three potential pitfalls in mind before you decide to open an account:

- **Contributing when you are no longer eligible** – In 2020, you can participate in an HSA if you have a high-deductible health insurance policy with an annual deductible of $1,400 or more for single coverage or $2,800 or more for family coverage. At the same time, your maximum annual out-of-pocket costs must be $6,900 as an individual and $13,800 as a family. If you do not meet these requirements, you are not eligible to contribute to an HSA.

- **Using HSA funds for nonqualified medical expenses** – Although the definition of qualified medical expenses is fairly liberal (including vision, dental, and sunscreen products, for example), you generally can’t use this money to pay for elective procedures or cosmetic surgeries. Be careful of the rules before you spend any funds.

- **Spending down your account balance each year** – Unlike Flexible Spending Accounts, in which you have to use the funds in the account or lose them, you can carry over a balance in an HSA each year. This makes them a good complement to your retirement savings account — and a good reason to fund them each year.

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Money conversations

When you are in a close relationship, it can be easy to put off talking about money with your partner. Even if you’re anxious about your financial situation, it’s important to be open to discussing it. It is possible to work toward multiple goals at once, such as saving for retirement and paying down student debt, but both partners need to be on the same page. Just because the conversation may be uncomfortable, it doesn’t mean it shouldn’t happen.

Q&A

When does it make sense to work with an accountant?

Some only contact a CPA once a year, when preparing a tax return. But checking in with a knowledgeable CPA before taking money from your retirement account — or a traditional or inherited IRA — may help you avoid poorly timed withdrawals that may increase your taxable income, or the taxes you pay on your Social Security benefits. Hiring a tax advisor can ultimately save you a lot of money over the course of a retirement that can last 30 years or more.

Quarterly Reminder

Are you getting good value from your fund investments?

When there are three months left in the year, it could be a great time to revisit the progress you’ve made toward your financial goals. These may include creating an emergency fund, debt management, planning a first car or home purchase (or refinancing), considering long-term care needs for yourself or other loved ones, or setting up a college savings plan, among others.

Tools & Techniques

Life has unexpected expenses: car or appliance repairs, for example. It may be helpful to create a rainy-day fund in a separate checking account for small financial shocks like these, and an emergency fund, which should have enough to cover an unexpected job loss or serious family health issue. Many financial experts recommend setting aside as much as nine months of living expenses to keep you afloat during emergencies, but you can certainly start smaller, with a goal of socking away two months of salary.

Corner on the Market

Basic financial terms to know

Bond – A bond is a security, generally issued for a period of more than one year, that is used to raise capital by borrowing from a lender. The United States and foreign governments, states, cities, corporations, and many other entities sell bonds. Bonds generally pay a stated rate of interest over a specific period of time, and issuers promise to pay that interest along with a return of the investors’ principal when the bond matures.

If you have questions about your current 401(k) Plan with ADP, you may contact your Plan Administrator or Financial Advisor.

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