T. Rowe Price

The Real Costs of Retiree Health Care

Key Takeaways

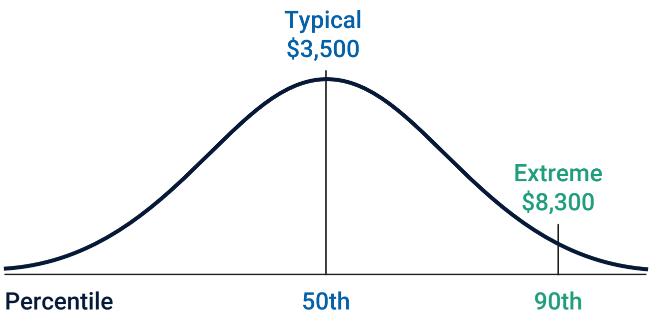
Historically, retiree health care costs have been a scary subject and a challenging financial puzzle. Our research and analysis helps take the guesswork out of planning. The following **three-step** approach provides a structure for taking action.

1. Understand and plan for the costs

Lost in the retiree health care discussion are key facts that bring the challenge down to size.

Costs are predictable: Projections for retiree health care expenses are often presented as lump-sum, lifetime figures. But actual costs are typically more modest and predictable, and best viewed as annual expenses. Half of retirees will pay less than $3,500 annually, and only 10% will pay more than $8,300 annually.

Total annual health care spending



Source: T. Rowe Price estimates based on 2024 Medicare premiums (for Medicare Parts A, B, and D) and data from the Health and Retirement Study (2020). All costs are rounded to the nearest hundred.

2. Focus on the typical; be aware of the extreme

In addition to total annual health care spending, retirees may experience health care "shocks"—an increase in out-of-pocket health care expenses over a two-year period. Understanding what these look like, as well as end-of-life expenses (the amount spent over the last two years of life at the age of death), can help with planning.

The typical and the extreme

	50th percentile	90th percentile
Health care "shocks"	$2,000	>$5,000
End-of-life spending	$3,400	$85,200

Source: T. Rowe Price estimates from Health and Retirement Study (2012–2018). Expenses are measured in 2022 dollars.

3. Take action

Preretirement: Evaluate retiree health care funding vehicles. When it comes to planning and paying for retirement health care expenses, investors have multiple options to complement insurance coverage and help manage ongoing costs.

Choose what account to use

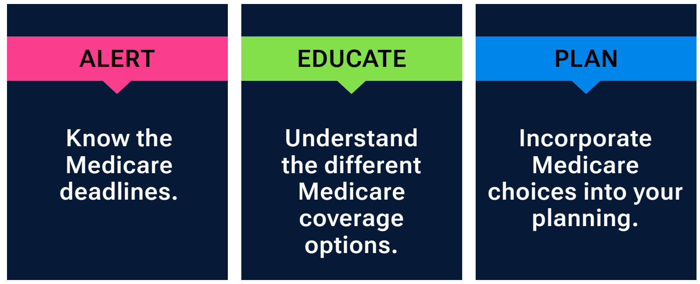
Tax benefits	Pretax account	Roth account	Health Savings Account
Contributions[1]	Excluded from taxable income	Not excluded from taxable income	Excluded from taxable income
Earnings growth	Tax-deferred	Tax-deferred	Tax-deferred
Taxes on distributions	Ordinary rate	Tax-free if qualified[2]	Tax-free if qualified[3]

■ = Tax Advantage

The chart reflects Roth and pretax employer-sponsored plans (as opposed to IRAs). Advantages of account type (relative to the others) shown in blue. These are not the only options when it comes to saving for health care and/or medical-related expenses in retirement. Note that while Health Savings Accounts (HSA) are structured for the individual to save or invest for health costs, this is not the intended primary purpose of a defined contribution plan or an IRA. Individuals should evaluate their health coverage needs and other factors before seeking tax benefits of an HSA. HSAs are only available if you are covered by a high-deductible health care plan. Chart is for illustrative purposes only. Source: IRS documents.

At retirement: Account for Medicare. Medicare will be a key cost input.

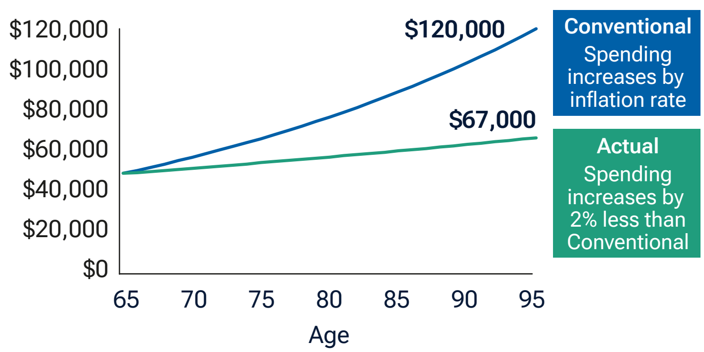
Medicare selection and enrollment



In retirement: Implement insights. Incorporate retiree health care costs and the nuances of retirement spending into your planning process (overall spending declines over the course of retirement when adjusted for inflation).

Retiree spending in retirement

Retirees increase their spending by 2% less than "conventional wisdom" each year



Source: Banerjee, Sudipto, Decoding Retiree Spending, T. Rowe Price Insights on Retirement, T. Rowe Price Group, Inc., March 2021 analysis of Health and Retirement Study, public use dataset. Produced and distributed by the University of Michigan with funding from the National Institute on Aging (grant number NIA U01AG009740). Ann Arbor, MI.

Next Steps

Talk with your T. Rowe Price representative or financial professional to learn more about the real costs of retiree health care.

[1] Federal income taxes. State laws vary. HSA contributions through an employer may be excluded from FICA taxes.
[2] Once you reach age 59½ with an account that has been opened for at least 5 years, you may qualify for tax-free withdrawals of both Roth contributions and any accumulated earnings.
[3] HSA distributions are considered qualified if they are used to pay for Qualified Medical Expenses.

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