PROSPECTS FOR RETIREE HEALTH BENEFITS AS MEDICARE PRESCRIPTION DRUG COVERAGE BEGINS

Findings from the Kaiser/Hewitt 2005 Survey on Retiree Health Benefits

SECTION 2

RETIREE HEALTH BENEFIT DESIGN AND PRESCRIPTION DRUG BENEFITS

Retiree Health Benefit Design and Prescription Drug Benefits

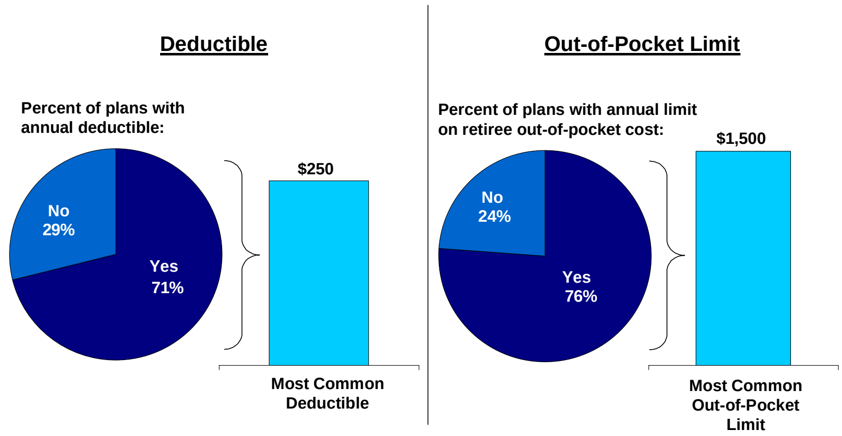
Employers typically require retirees to contribute to the cost of their medical coverage through cost sharing for incurred medical services, in addition to retiree contributions to premiums. Employer-sponsored plans often include a deductible and generally require a copayment or coinsurance for many covered health care services, while simultaneously limiting the retiree's financial exposure through annual limits on retirees' out-of-pocket costs. To understand common benefit design features of retiree plans, the survey asked employers about cost-sharing requirements for their retiree health plans with the largest age 65+ retiree enrollment. The survey also asked detailed questions about prescription drug benefit design to facilitate a comparison between employer plans and new Medicare drug plans.

Deductibles

- 71 percent of surveyed employers say their largest age 65+ retiree health plan has an annual deductible that must be satisfied before the plan begins to pay benefits (Exhibit 3).
  - The annual in-network deductible ranges from $50 to $2,000, and the most commonly reported deductible is $250.

Exhibit 3

Large Private-Sector Employers' Benefit Design Features for Age 65+ Retirees in the Largest Plan



Note: Applies to overall retiree health plan with the largest number of Medicare-eligible retirees. Based on responses from private-sector firms with 1,000 or more employees offering retiree health benefits.
SOURCE: Kaiser/Hewitt 2005 Survey on Retiree Health Benefits, December 2005.

Out-of-Pocket Limits

- 76 percent of surveyed employers report that the largest age 65+ plan has an annual limit on retiree out-of-pocket costs (Exhibit 3).
  - The most commonly reported annual out-of-pocket limit is $1,500.

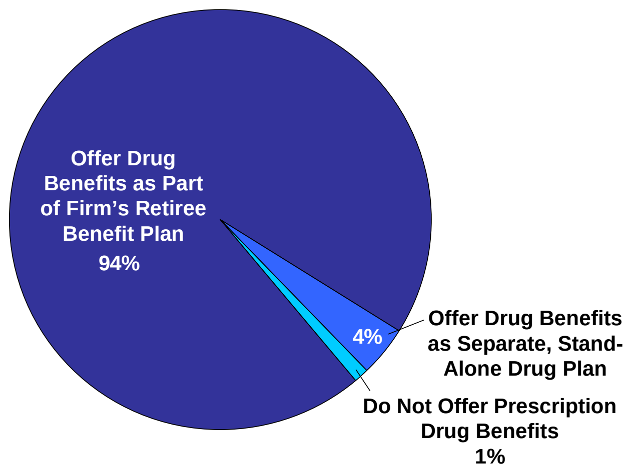
Prescription Drug Benefits

Prescription drug coverage is a critical component of retiree health benefits. For a baseline of the scope and structure of prescription drug benefits prior to the implementation of the Medicare drug benefit, the survey asked employers to describe features of prescription drug coverage for the benefit plan with the largest number of age 65+ retirees in 2005.

- The vast majority of employers that offer retiree health benefits provide coverage for prescription drugs. Most (94 percent) offer drug benefits as part of the firm's retiree health benefit plan, while a small share (4 percent) do so as a separate, employer-subsidized stand-alone drug plan. One percent of surveyed employers does not offer prescription drug benefits to age 65+ retirees (Exhibit 4).

Exhibit 4

Percentage of Large Private-Sector Employers Offering Prescription Drug Benefits to Age 65+ Retirees



Note: Numbers may not total 100% due to rounding. Based on responses from private-sector firms with 1,000 or more employees offering retiree health benefits.
SOURCE: Kaiser/Hewitt 2005 Survey on Retiree Health Benefits, December 2005.

- Among plans with the largest number of age 65+ retirees, 58 percent of surveyed employers report that drug benefits are subject to the overall plan design, meaning the plan does not impose deductibles and out-of-pocket limits for drug benefits separate from other covered benefits (Exhibit 5).

- 19 percent have a separate annual drug deductible. For retail and mail order pharmacy claims combined, prescription drug deductibles range from $25 to $250, and the most common deductible is $100.

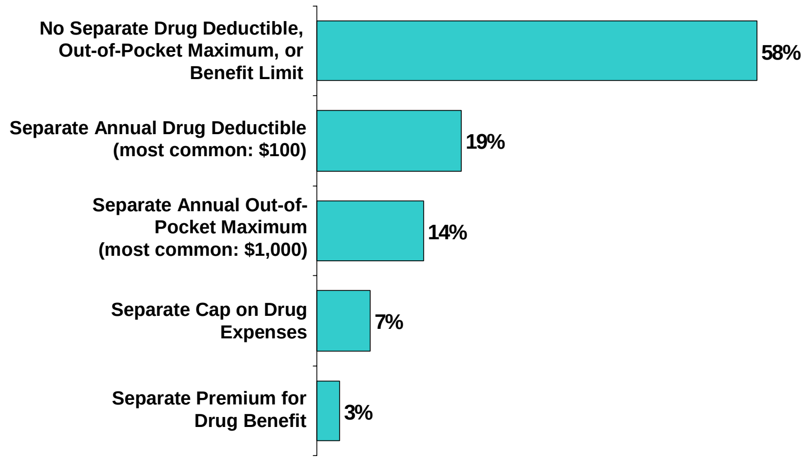
- 14 percent have a separate annual out-of-pocket maximum (or stop-loss coverage) for pharmacy claims. Out-of-pocket-maximum amounts range from $200 to $3,350, and the most common out-of-pocket limit is $1,000.

- Benefit limits for drugs are fairly uncommon with 7 percent of the largest plans reporting a separate cap on total covered drug expenses. Under these arrangements, the plan would cover costs up to the benefit limit but not beyond that point.

- Only 3 percent have separate premiums for prescription drug benefits.

Exhibit 5

Prescription Drug Benefit Design Features for Age 65+ Retirees



Note: Based on responses from private-sector firms with 1,000 or more employees offering retiree health benefits.
SOURCE: Kaiser/Hewitt 2005 Survey on Retiree Health Benefits, December 2005.

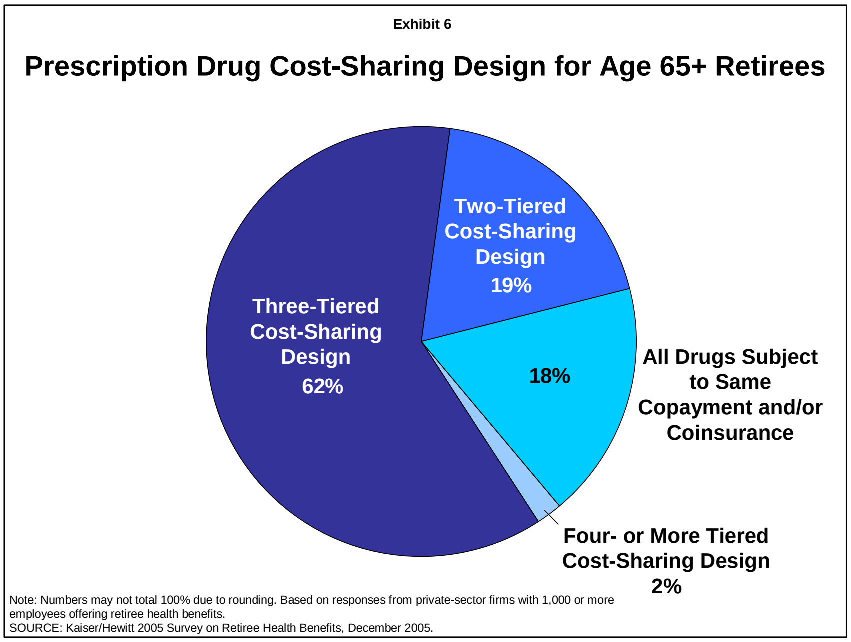
Employers use a variety of cost-sharing strategies for prescription drug benefits, with three-tiered arrangements being the most common in the largest age 65+ plan (Exhibit 6).

- 62 percent have a three-tiered plan design in which generic drugs, formulary/preferred drugs, and non-formulary/non-preferred drugs are each subject to different copayments/coinsurance rates.

- 19 percent have two tiers for prescriptions with generic drugs subject to a different copayment and/or coinsurance rate than all other drugs.

- Only 2 percent have a drug cost-sharing design with four or more tiers.

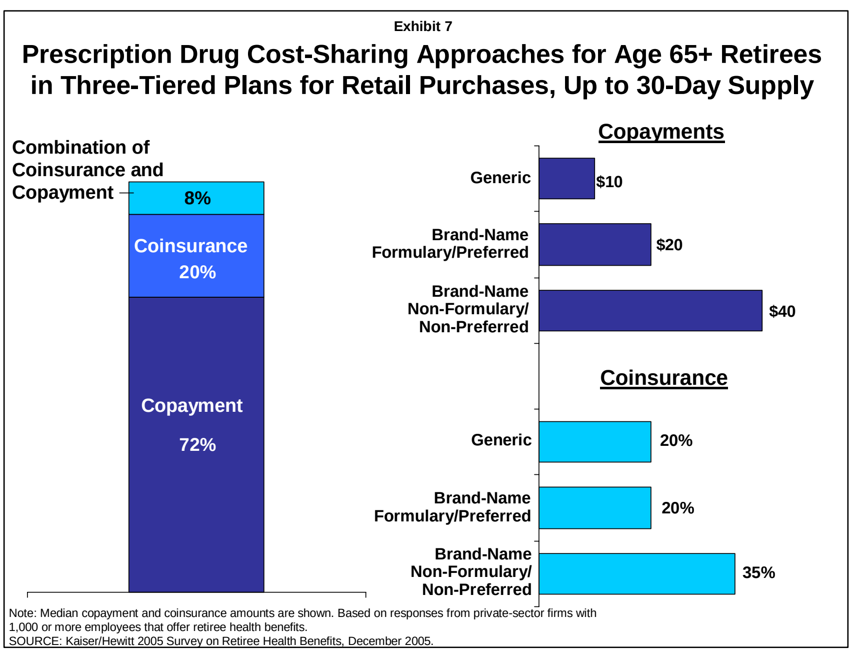
- 18 percent apply the same copayment and/or coinsurance rate for all prescription drugs.



Three-Tiered Drug Cost-Sharing Design

Prescriptions Filled at Retail Pharmacies

- Among the majority of employer plans with a three-tiered drug design for their largest age 65+ plan, more than two-thirds (72 percent) require flat-dollar copayments for pharmaceuticals purchased at retail pharmacies; one-fifth (20 percent) require coinsurance payments (retiree pays a specified percent of the cost of each prescription); and only 8 percent use a combination approach of copayments plus coinsurance (Exhibit 7).



– For drugs purchased at retail pharmacies, median copayment amounts are $10 for generics, $20 for brand-name drugs on the formulary/preferred list, and $40 for brand-name drugs on the non-formulary/non-preferred list. Typically, retiree cost sharing at retail pharmacies covers a 30-day supply or a lesser quantity, as prescribed.

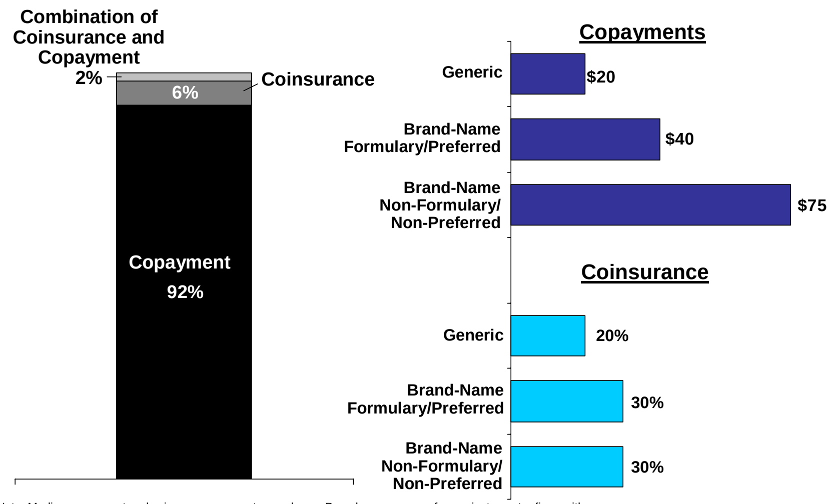
– Among the minority of plans that use a coinsurance approach for prescriptions filled at retail pharmacies, the median coinsurance rates are 20 percent for generics and brand-name formulary/preferred drugs, and 35 percent for non-formulary/non-preferred drugs.

Prescriptions Filled at Mail-Order Pharmacies

- Among employers whose largest age 65+ plan offers a mail-order option with a three-tiered drug design, 92 percent require retirees to pay fixed-dollar copayments, 6 percent impose coinsurance payments, and 2 percent use a combination of copayments and coinsurance (Exhibit 8).

Exhibit 8

Prescription Drug Cost-Sharing Approaches for Age 65+ Retirees in Three-Tiered Plans for Mail-Order Purchases, 90-Day Supply



Note: Median copayment and coinsurance amounts are shown. Based on responses from private-sector firms with 1,000 or more employees that offer retiree health benefits.
SOURCE: Kaiser/Hewitt 2005 Survey on Retiree Health Benefits, December 2005.

– For drugs purchased through mail-order pharmacies, median copayment amounts are $20 for generics, $40 for brand-name drugs on the formulary/preferred list, and $75 for brand-name drugs on the non-formulary/non-preferred list. Typically, the mail-order copayment covers a 90-day supply of medication.

– For the relatively few employer plans in this survey where coinsurance is used for mail-order claims, median coinsurance is 20 percent for generics, and 30 percent for brand-name formulary/preferred drugs and for non-formulary/non-preferred drugs.

Comparison with Standard Medicare Drug Benefit

The majority of employers (94 percent) say their 2005 prescription drug benefit is of equal or greater value than the standard Medicare drug benefit in 2006. The typical prescription drug coverage offered by large employers in 2005 is unlike the standard Medicare Part D benefit in several ways.

- Most employer plans do not charge a separate premium or deductible for prescription drugs.
- The typical large employer plan does not suspend coverage at a given level of prescription drug spending until the retiree's drug spending reaches a specified out-of-pocket threshold.
- As it stands today, most plans require retirees to make flat-dollar copayments rather than pay a coinsurance percentage.[11]

11 Some experts expect there to be more movement toward coinsurance in coming years, perhaps following Medicare's example.