

PROSPECTS FOR RETIREE HEALTH BENEFITS AS MEDICARE PRESCRIPTION DRUG COVERAGE BEGINS

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

SECTION 6

MEDICARE PRESCRIPTION DRUG BENEFIT AND RETIREE HEALTH

on behalf of their Medicare-eligible retirees would not count toward the retirees' true out-of-pocket (TrOOP) limit. Supplementing the Medicare prescription drug benefit is considered administratively challenging in the first year, with the availability and the design of Medicare PDPs and MA-PD plans relatively unknown during the employers' benefits planning cycle for 2006.

- CMS estimates that these approaches toward supplementing Medicare drug coverage will achieve cost savings to employers of at least \$900 on average due to the federal government subsidizing a significant portion of the cost of standard Part D coverage.²⁴
- Become a Medicare PDP or MA-PD plan, receiving a CMS-estimated average payment of close to \$900 per participant in an employer-sponsored PDP or MA-PD plan.²⁵
- Terminate prescription drug coverage (and possibly make a contribution to Medicare prescription drug plan premiums).

A key concern remains which path(s) employers choose for 2006, and whether they contemplate changing their approach in subsequent years. This survey was conducted between June 21 and October 7, 2005, during the period that private-sector employers were making final decisions as to whether they would choose to take the retiree drug subsidy or pursue some other employer option for coordinating with Medicare drug coverage in 2006.

Strategies for 2006

The Kaiser/Hewitt 2005 survey asked employers to identify which strategies their firm would most likely pursue in response to the Medicare drug benefit. Overall, the majority of surveyed employers (82 percent) say they intend to maintain prescription drug coverage for their Medicare-eligible retirees in 2006 and take the 28 percent subsidy; 15 percent say they are likely to supplement the Medicare prescription drug benefit; and 2 percent say they intend to become a prescription drug plan. Eleven percent said they are likely to discontinue prescription drug coverage, of which 3 percent report they are likely to discontinue both drug and other medical coverage.²⁶

Employers were then asked which strategy they were most likely to pursue for their largest group of age 65+ retirees (Exhibit 17).

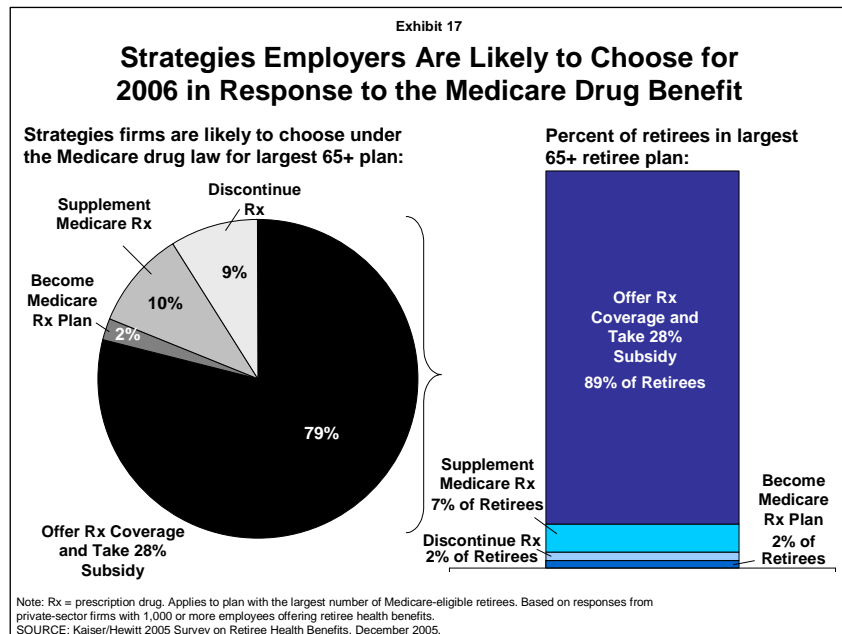
- 79 percent of surveyed employers – representing 89 percent of age 65+ retirees in the largest plans – expect to continue to offer prescription drug coverage and accept the tax-free subsidy for their largest group of age 65+ retirees.

²⁴ Centers for Medicare and Medicaid Services, *Overview of Plan Sponsor Supplemental Coverage Options and TrOOP*, <http://www.cms.hhs.gov/medicarereform/pdbma/OverviewofPlanSponsorSupplementalCoverageOptionsandTrOOP.pdf>.

²⁵ Centers for Medicare and Medicaid Services, *The Retiree Drug Subsidy: Why Employers and Union Plan Sponsors Should Consider It*, April 2005, <http://www.cms.hhs.gov/medicarereform/pdbma/RetireeDrugSubsidy4Emp04-06-05.pdf>.

²⁶ Some employers with multiple plans provided multiple responses to this question because they chose different strategies for their various plans. As a result, the total exceeds 100 percent.

- 10 percent of surveyed employers – representing 7 percent of age 65+ retirees in the largest plans – expect to offer prescription drugs as a supplement to the Medicare drug benefit for the plan with the largest group of age 65+ retirees.
- 9 percent of surveyed employers – representing 2 percent of age 65+ retirees in the largest plans – report that they are likely to discontinue drug and/or medical coverage for the plan with the largest group of age 65+ retirees.
- 2 percent of surveyed employers – representing 2 percent of age 65+ retirees in the largest plans – report that they are likely to become a Medicare prescription drug plan.



Expected Savings for Employers

Per Retiree Savings Due to Medicare Drug Benefit. As firms look toward 2006 and assess their preferred strategy, a key consideration is how much they expect to save as a result of the new Medicare prescription drug benefit.²⁷

- Across all surveyed employers – including employers that maintain drug benefits, supplement drug benefits, or even terminate drug coverage – the weighted average savings is estimated to be \$644 per individual retiree in 2006.²⁸

²⁷ The survey asked employers to indicate the average dollar savings per individual retiree that would result from the Medicare drug benefit in 2006. Employers reported their savings per individual retiree within pre-defined ranges (e.g., \$600 to \$649/year). Using the midpoint of these ranges, we calculated average savings across employers, weighted by firm size and the average number of age 65+ retirees. By doing so, the average savings per individual retiree of larger firms with a greater number of retirees are weighted more heavily than the relatively smaller firms that have fewer retirees. Employers that reported no savings attributable to their Medicare strategy were excluded from the analysis.

²⁸ In some instances, there are no savings to the employer because the retiree pays 100 percent of the premium. In other cases, employer savings may be lower because the employer contribution is capped and/or the employer pays a smaller percentage of the overall cost than other employers. Savings will also be lower if the employer intends to share a portion of the savings with retirees (a question not asked in the survey).

Estimated average savings per retiree varies by strategy. Looking at the two most common strategies identified by employers:

- The weighted average savings per individual retiree is \$626 among employers who intend to continue prescription drug benefits and accept the 28 percent subsidy.
- The weighted average savings per individual retiree is \$826 among employers who intend to supplement the Medicare drug benefit.

Savings as a Share of Total Retiree Health Costs. When the Medicare drug law was being debated, the hope was that the subsidy would provide employers with sufficient financial relief so they would maintain rather than terminate coverage for their Medicare-eligible retirees. While the subsidy provides a direct payment for drug costs associated with each eligible age 65+ retiree and Medicare-eligible dependent, employers incur costs associated with both their pre-65 retirees (for whom the employer is the primary payer) and for other medical and supplemental drug benefits provided to age 65+ retirees.

- The total employer savings attributable to their Medicare drug benefit responses represents a median 7 percent of the total cost of retiree health benefits for pre-65 and age 65+ retirees.²⁹

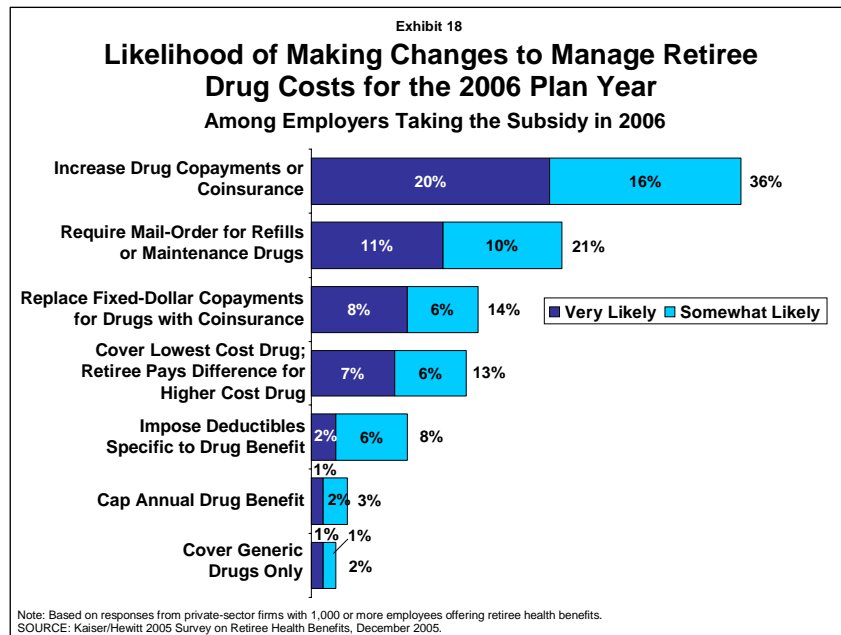
Other Strategies for Controlling Prescription Drug Costs in 2006

Among employers planning to continue drug coverage and take the retiree drug subsidy in 2006 (Exhibit 18):

- 36 percent say they are very (20 percent) or somewhat (16 percent) likely to increase retiree copayments or coinsurance for prescription drugs.
- 21 percent say they are very (11 percent) or somewhat likely (10 percent) to require use of mail-order for prescription refills or maintenance drugs.
- 14 percent of surveyed employers say they are very (8 percent) or somewhat (6 percent) likely to replace fixed dollar copayments with a coinsurance approach for prescription drugs.
- 13 percent of surveyed employers say they are very (7 percent) or somewhat (6 percent) likely to cover the lowest-cost drug for a given condition and make the retiree pay the difference for a higher-cost drug.

²⁹ This percentage savings was calculated by taking the total savings for each employer (i.e., savings per individual retiree multiplied by the total number of the company's age 65+ retirees) and dividing that sum by the employer's estimated 2005 total cost (employer and retiree share) of providing retiree health benefits to pre-65 and age 65+ retirees. We then calculated the median percentage savings among these companies.

- 8 percent of surveyed employers say they are very (2 percent) or somewhat (6 percent) likely to impose deductibles specific to the prescription drug benefit in 2006.
- 3 percent say they are very (1 percent) or somewhat (2 percent) likely to impose a cap on the annual drug benefit.
- 2 percent say they are very (1 percent) or somewhat (1 percent) likely to cover generic drugs only.



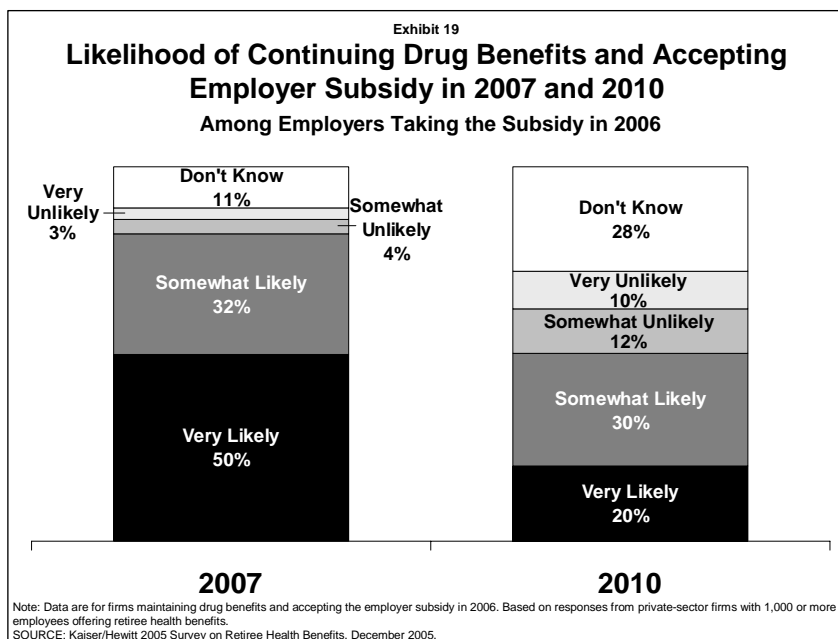
Likelihood of Continuing Medicare Strategy in Years Beyond 2006

The survey asked employers that intend to continue prescription drug coverage and accept the subsidy in 2006, how likely they are to continue the same strategy in later years (Exhibit 19).

Among the employers taking the retiree drug subsidy in 2006 for their largest group of age 65+ retirees in 2006 (79 percent):

- Looking to 2007, 82 percent say they are very (50 percent) or somewhat (32 percent) likely to continue offering these benefits and accept the 28 percent subsidy; 7 percent say they are very (3 percent) or somewhat (4 percent) unlikely to do so; and 11 percent report that they do not know what they will do.
- Looking to 2010, 50 percent say they are very (20 percent) or somewhat (30 percent) likely to continue offering these drug benefits and accept the 28 percent subsidy; 22 percent report that they are very (10 percent) or somewhat (12 percent) unlikely to do so, and 28 percent report that they do not know.

In other words, eight out of 10 employers that report they will take the subsidy in 2006 say they are likely to continue doing so in 2007, but that proportion drops to 5 out of 10 employers in 2010, and the uncertainty among these employers as to whether they will continue taking the 28 percent subsidy grows between 2006 and 2010. Employers may find other options to be more attractive in later years, such as supplementing Medicare drug plans as a secondary payer.



Whether employers maintain drug coverage for their age 65+ retirees over the long term will depend on a number of factors. A key consideration will likely be the financial burden of providing retiree health coverage over time, but other factors could include the administrative costs and challenges associated with any of the options, and the ease with which employers will be able to wrap around Medicare drug plans.

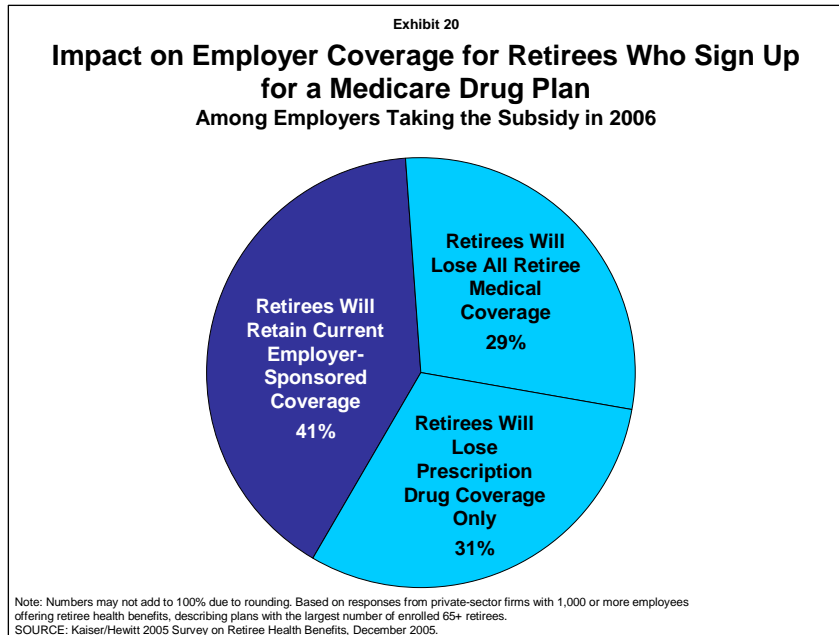
Other Employer Policies Affecting Retirees

Medicare beneficiaries with retiree health benefits from their former employer or union health plan generally have the option of retaining their employer/union benefits (assuming such coverage is offered and is at least as generous as the standard Medicare benefit) or enrolling in a Medicare prescription drug plan.

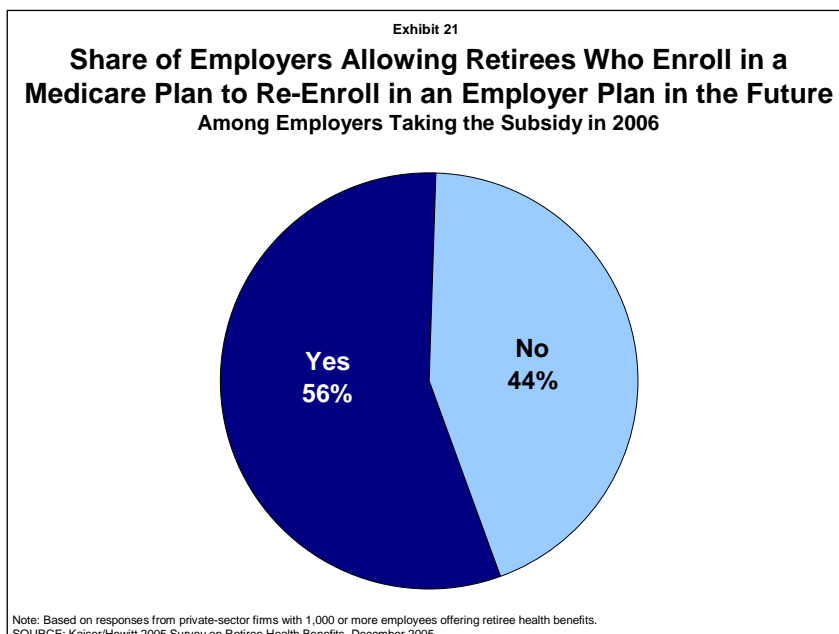
The 2005 survey asked employers taking the subsidy in 2006 for their largest age 65+ plan whether a retiree would have the option to maintain employer coverage if he or she enrolls in a Medicare prescription drug plan (Exhibit 20).

- 41 percent of employers said their retirees would be able to retain employer-sponsored coverage, which generally means both medical and prescription drug coverage, as a supplement to a Medicare drug plan.
- 31 percent said their retirees would lose prescription drug coverage only.

- 29 percent said their retirees would lose both employer-sponsored medical and prescription drug coverage if they elected to sign up for a Medicare prescription drug plan.



For retirees with employer coverage, informed decision-making is especially important. Many are concerned that some retirees – faced with a fairly significant change in their Medicare options – may sign up for a Medicare prescription drug plan without realizing the potential consequences in terms of forfeiting their employer-sponsored benefits. CMS and employers are taking steps to make retirees aware of the implications of dropping their employer coverage for a Medicare drug plan. They also have procedures in place to flag and address situations where retirees in employer plans taking the subsidy attempt to enroll in Medicare drug plans.



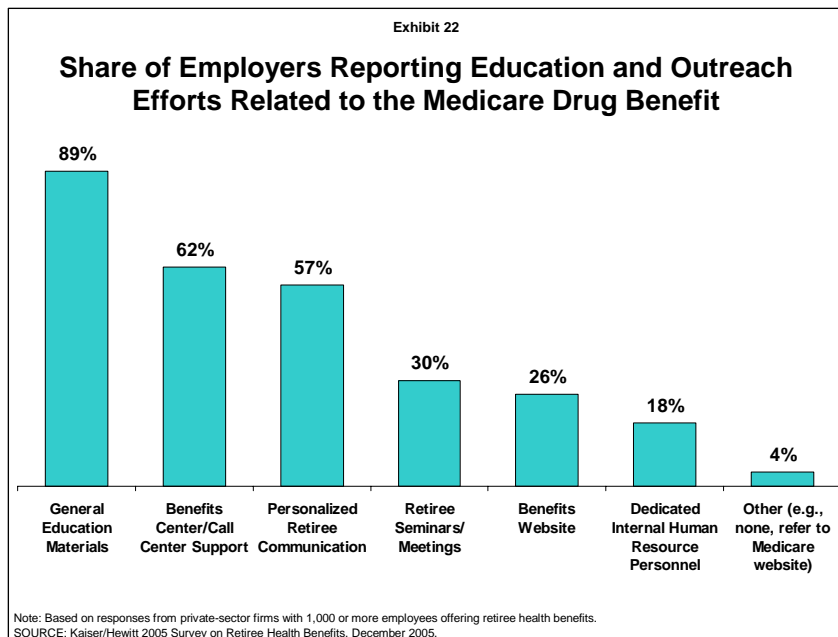
If Medicare-eligible retirees choose to enroll in Part D plans as they are entitled to do:

- More than half of employers taking the subsidy for their largest age 65+ plan in 2006 (56 percent) say retirees would be allowed to enroll or re-enroll in the employer plan at a future date if they sign up for a Medicare drug plan; however, 44 percent of employers say retirees would not be able to do so in the future (Exhibit 21).

This finding underscores the importance of safeguards to deter retirees from making an irrevocable decision with potentially adverse long-term financial implications.

Education Challenges

Employers are expected to be a key source of information for their age 65+ retirees as the Medicare prescription drug benefit is rolled out (Exhibit 22). Employers are required to provide their Medicare-eligible retirees with a notice indicating whether their employer coverage is “creditable” (i.e., at least as good as the Medicare prescription drug benefit) or “non-creditable” (i.e., less than the actuarial value of the Medicare drug benefit).



Many large employers report that they plan to provide additional support to their age 65+ retirees using multiple strategies, including:

- 89 percent will distribute general educational materials.
- 62 percent will maintain a benefits center or call center.
- 57 percent will provide personalized retiree communications (in addition to required notices).

Medicare Prescription Drug Benefit and Retiree Health

More than 12 million people on Medicare rely on employer-sponsored and/or union plans for their retiree health benefits.²² Retiree health plans are the largest single source of prescription drug coverage for Medicare beneficiaries prior to the implementation of the Medicare drug benefit.

The interaction between employer-sponsored retiree health benefits and the new Medicare prescription drug benefit received considerable attention during the long debate leading up to the enactment of the new drug benefit, and the future of retiree benefits continues to be a key issue for employers, retirees, and policymakers.

A central issue for retirees and their families is whether the new Medicare Part D prescription drug benefit will hasten the erosion of relatively generous and highly-valued employer-sponsored retiree health coverage. From the employer perspective, rising retiree health costs remain a pressing concern. Many are hopeful that the new Medicare drug benefit could help offset cumulative double-digit increases in retiree health costs.

Background

Looking toward 2006 for their age 65+ retirees, employers have four major options with respect to the new Medicare drug benefit:

- Maintain prescription drug benefits that are at least actuarially equivalent to the standard Medicare drug benefit defined in law. Medicare offers financial incentives for employers that choose this approach, in the form of tax-free payments equal to 28 percent of allowable drug costs between \$250 and \$5,000 for each covered retiree not enrolled in Part D in 2006. Taking the retiree drug subsidy is the least disruptive approach for employers and retirees. This strategy is a viable option because 94 percent of surveyed employers say their 2005 benefits have an actuarial value that is equal to or greater than the standard Medicare prescription drug benefit for 2006.
 - The Centers for Medicare and Medicaid Services (CMS) estimates an average tax-free retiree drug subsidy payment of \$668 per participant in 2006, equivalent to \$891 for plan sponsors with a 25 percent marginal tax rate and \$1,028 for plan sponsors with a 35 percent marginal tax rate.²³ Corporations owing no taxes obviously do not reap the additional tax benefits, just as not-for-profit employers and governmental plans do not.
- Supplement (or “wrap around”) Medicare Part D coverage or achieve a similar result by contracting directly with a Medicare prescription drug plan (PDP) or Medicare Advantage prescription drug (MA-PD) plan to provide more generous coverage to retirees for an additional premium. Payments for prescription drugs made by employers

²² Kaiser Family Foundation analysis of 2002 Medicare Current Beneficiary Survey Cost and Use File.

²³ Centers for Medicare and Medicaid Services, *The Retiree Drug Subsidy: Why Employers and Union Plan Sponsors Should Consider It*, April 2005, <http://www.cms.hhs.gov/medicarereform/pdbma/RetireeDrugSubsidy4Emp04-06-05.pdf>.

- 30 percent are planning on hosting retiree seminars or meetings.
- 26 percent will have a benefits website.
- 18 percent have dedicated human resources personnel.