MEDICARE ACT GIVES EMPLOYERS NEW RETIREE MEDICAL OPTIONS

The Medicare Modernization Act of 2003 (MMA) brings welcome relief to employers reeling from the increasing impact of retiree medical programs on their bottom line. This new legislation — which includes optional prescription drug coverage for Medicare-eligible individuals beginning in 2006, along with a tax-free subsidy to employers that continue to provide actuarial equivalent drug coverage to their retirees — will be phased in over time. But employers have little time to waste in addressing critical MMA accounting deadlines and communication issues.

Equally important, since the new legislation will significantly change the retiree medical landscape, employers need to reevaluate their commitments to current and future retirees, understand the impact of various plan design and delivery options, and determine which actions, if any, they will take in the future.

WHAT EMPLOYERS NEED TO DO RIGHT NOW

- First, employers need to determine the FAS 106 impact of the MMA on their current substantive plan (i.e., the current and future benefits as defined for FAS 106 accounting). If the impact is significant, which it will be for most employers, the MMA must be recognized in employers' financial statements no later than the third quarter of 2004.

- Next, employers need to decide whether or not to restate earnings for previous quarters in 2004 or account for the change on a prospective basis.

- Finally, to help retirees sort through the barrage of information and misinformation about the new legislation, particularly Medicare discount cards and Medicare Advantage plans, employers need to clearly explain what it all means to their retirees and what actions they should and should not take. (For instance, retirees who have employer-provided prescription drug coverage generally should not purchase Medicare discount cards.) Furthermore, for many employers it will be important to use this opportunity to influence retirees' views and expectations about the company's commitment to retiree medical benefits.

PLAN DESIGN AND DELIVERY OPTIONS/IMPLICATIONS

Although regulations under the MMA are not expected until sometime in early 2005, employers need to reevaluate their retiree medical goals and commitments. When determining their future actions, employers should consider the following plan design and delivery options and their implications:

- Provide primary prescription drug coverage that is at least as rich as the Standard Medicare Part D benefit and accept the federal subsidy payment.

Implications: Companies looking to reduce costs and minimize the impact on retirees may prefer this option, which will not require any changes to existing plans for most employers. However, this approach may pose significant communication and administrative challenges.

- Provide secondary drug coverage, similar to how employer plans typically integrate with Medicare Parts A and B.

Implications: This strategy allows employers to deliver a consistent message regarding how they coordinate benefits across all parts of Medicare. Retirees will need to enroll in Part D and should be given limited plan choices to avoid significant administrative complexities.

- Negotiate or sponsor an employer-specific Part D plan including supplemental benefits.

Implications: Employers who wish to maintain coverage similar to their current plans and reduce costs through a mechanism other than the federal subsidy are likely to favor this approach, which will minimize administration and allow plan design flexibility. Retirees will need to enroll in the employer plan by enrolling in Medicare Part D.

- Eliminate the employer plan and provide retirees with an employer contribution that can be used toward the cost of purchasing private coverage.

Implications: This strategy provides retirees with flexibility in choosing the right plan for them. However, available options may be limited in certain markets and overwhelming in others. In addition, publicly available plans may not be as rich as the current employer plan. This approach may be especially attractive to employers who wish to transition toward exiting retiree medical altogether.

- Encourage enrollment in Medicare Advantage Plans as an alternative to the employer-sponsored Medicare supplemental prescription drug and medical/surgical plans.

Implications: A 10.6% average increase in payments to Medicare Advantage Plans (formerly known as Medicare+ Choice Plans), effective March 2004, has already generated lower premiums and enhanced benefits for many plans. With an additional 6.6% average payment increase scheduled for 2005, health plan sponsors are returning to this marketplace in large numbers, which will result in attractive plans that may reduce costs for both the employer and retirees.

- Eliminate the employer subsidy for retiree prescription drug and possibly medical/surgical benefits.

Implications: With Medicare now paying a portion of retiree prescription drug costs, some employers may choose to eliminate these benefits altogether, especially for future retirees. This approach may be most attractive to employers who are under significant pressure to reduce benefit costs.

LOOKING AHEAD

Although the MMA is being phased in over time, in the short term, employers will need to address impending accounting deadlines and communicate with retirees. Moreover, employers who take the time now to consider how the MMA will affect their current and future commitment to retirees will have more time for transition, implementation and communication if and when they do make significant changes to their retiree medical programs for 2006 or anytime thereafter.

FOR FURTHER INFORMATION

If you have questions about this subject or other health care issues, please contact your Towers Perrin consultant.

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