



BENEFITS PERSPECTIVES

Current Issues in Employee Benefits

Health insurance exchanges and early retiree health coverage

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Rising healthcare costs and changes to financial accounting rules have put pressure on private and public sector employers to control or reduce retiree healthcare costs. An increasing number of employers have capped the subsidies for coverage of early retirees (those aged 55 to 64) or provided only access to coverage without cash subsidies. Early retirees who do not have access to employer-sponsored health coverage and who purchase insurance in the private insurance market often face high premiums and, possibly, exclusions from coverage for preexisting conditions.

This article examines how the Patient Protection and Affordable Care Act (PPACA) may change the landscape of retiree health coverage. While the PPACA affects all demographic groups, including employees and Medicare-eligible retirees, this article focuses on early retirees. In general, employers that provide early retiree healthcare coverage will have options to consider and should weigh the advantages and disadvantages of maintaining the benefits for this group of former employees. In addition, the outcome of the U.S. Supreme Court's still-pending decision in the legal cases challenging the PPACA could present additional challenges.

The creation of health insurance exchanges

The PPACA will make significant changes to the way employers think about providing healthcare benefits to early retirees. The law also will likely alter the way early retirees view accessing such benefits. The PPACA will allow for the creation of state-based "health insurance exchanges" in 2014, where insurance carriers will not be allowed to deny individuals coverage because of preexisting conditions or charge them a higher premium because

of their health status. This provision is particularly significant for early retirees, given that they are more likely to have chronic health conditions, which insurers currently can specify as a reason to charge higher premiums (or to possibly deny coverage if "portability" rules do not apply). Age-rating also will be limited so that premiums for an older individual cannot be more than three times higher than for a younger one, which will benefit early retirees. The federal government will provide subsidies for individuals with household incomes below 400% of federal poverty level (FPL), and early retirees with incomes below 138% of the FPL will be eligible for Medicaid coverage.

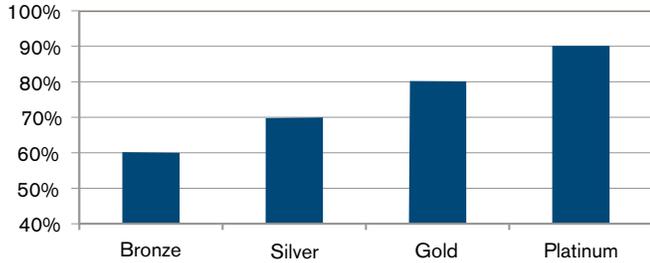
Features of health insurance exchanges

The insurance exchanges will be a centralized marketplace where individuals and qualified groups can purchase health insurance. States that set up exchanges will have some discretion about their administration and operation but will have to meet minimum federal requirements. If a state does not set up an exchange by 2014, the federal government will step in.

In general, insurance carriers will offer health insurance plans that satisfy federal requirements through the exchange. The plans will offer four levels of coverage (bronze, silver, gold, and platinum), based on how much a plan will cover and how much the patient pays for coinsurance, deductibles, and copayments. For example, someone covered by a silver plan would have to pay on average 30% out of pocket while the plan covers 70% of healthcare costs. Most Americans will be required to get at least a bronze-level plan. The exchanges will provide a method for consumers to compare benefits and prices among the plans.

The following chart shows the “actuarial values” of health insurance plans to be offered on the exchanges.

CHART 1



Individuals and employers with no more than 50 employees can start purchasing health insurance plans on the exchanges starting on January 1, 2014. The size of employers that are eligible to purchase insurance on the exchange will be expanded to cover groups of up to 100 employees on January 1, 2016. Beginning in 2017, states are permitted to open their exchanges to larger employers.

Covering early retirees under the health insurance exchanges

While employers with more than 50 full-time employees may face a federal penalty if they send their employees to the exchange, employers can allow retirees under the Medicare-eligible age of 65 to purchase health insurance through the exchange without a federal penalty. Once a retiree becomes eligible for Medicare, he or she may no longer purchase coverage through the exchange. The employer can continue to provide subsidies for the Medicare-covered retiree.

For some early retirees, purchasing health insurance from the exchange that provides comparable coverage could potentially come at a lower cost to them. The federal government might pick up part of the cost for some low-income retirees. Retirees might qualify for the federal subsidies based on the likelihood of having reduced income as compared with when they were working. There are limits on the amount that health insurers and health maintenance organizations (HMOs) can charge for older insureds relative to younger ones. The competition among private insurance plans on the exchange may offer the retirees a wider variety of health insurance plans to choose from, instead of being limited to the plans offered by their former employer.

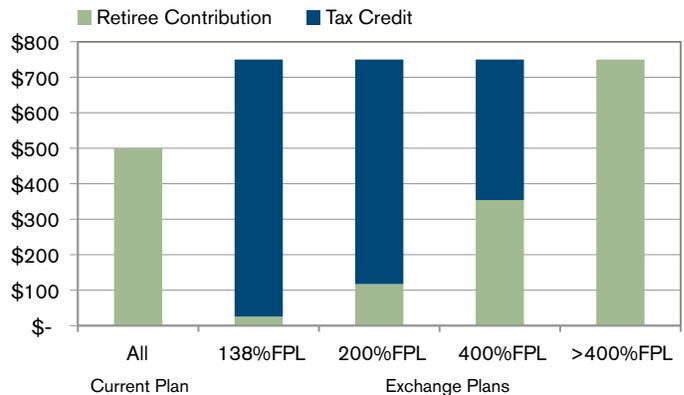
The federal government will provide individuals a tax credit for insurance purchased in the exchange if their insurance premiums are more than 9.5% of their household income and their household income is below 400% of the FPL (see the table for the applicable income levels). For example, assuming that the FPL remains at the 2012 level in 2014, an early retiree in a family of two with income of \$30,260 annually would be eligible for a federal tax credit if health premiums cost more than \$1,906. Hence, some early retirees may pay less to obtain coverage through the exchange, even if the employer does not subsidize the coverage.

HOUSEHOLD INCOME AT DIFFERENT FEDERAL POVERTY LEVELS (2012)

PERSONS IN FAMILY	ONE	FOUR
100% FPL	\$11,170	\$23,050
138% FPL	15,415	31,809
400% FPL	44,680	92,200

Chart 2 illustrates an early retiree’s premium cost, assuming the premium for comparable benefits through the exchange is 50% higher than that of the employer’s plan. By staying in the employer’s plan, early retirees may receive implicit subsidies from the employer by being part of a pool that includes younger (and healthier) workers if they are included in the active employee plan. The level of implicit subsidy depends on the demographics of employees and early retirees in the group. A subsidy of 50% is common. In this example, an early retiree pays \$500 per month to obtain coverage through his former employer, which provides access, but not a cash subsidy, to its retirees. If the household income of this retiree is \$44,680 (using 2012 FPL), he can purchase insurance coverage for himself on the exchange by paying only \$354 per month, with the remaining \$396 of the premium paid via the federal tax credit.

CHART 2



If the employer provides a cash subsidy by limiting the amount retirees pay to a certain percentage of total premiums, the change in retirees’ cost for health insurance purchased from the exchange will depend on the current level of subsidy, the employer subsidy after the change, and the federal subsidy on the exchange. Depending on the level of implicit and cash subsidies the employer currently offers, the early retiree may or may not be better off by going to the exchange. For example, if the employer in the previous example offers a 50% cash subsidy (in addition to the 50% implicit subsidy)—that is, the early retiree only pays \$250 per month for coverage through the employer’s insurance plan—he will have to pay \$104 more per month when he goes to the exchange. A holistic approach to costs and benefits is necessary before the employer makes any change to the way it provides health insurance benefits to its early retirees.

For a fully insured employer insurance plan, early retirees who purchase insurance through the exchange will no longer be part of the employer's rating pool, resulting in lower average premiums for the employer and remaining employees. Accounting costs will also be reduced by eliminating subsidies provided to retirees. For a self-insured plan, the savings will come in lower claims and expenses because early retirees are receiving medical coverage through the exchange.

Thus, if the employer requires retirees to purchase health insurance coverage through the exchange, the employer can:

- Coordinate (explicit/cash) subsidies for retirees with premium credits on the exchange
- Eliminate implicit subsidies (by removing retirees from the health insurance rating pool)
- Lower total premiums and possibly employee portion of the premiums for employees
- Take advantage of federal subsidies that may be available to the employer's eligible early retirees

Some employers, however, may choose to maintain early retirees under their health plan despite the potential advantages of encouraging use of a state health exchange. Their reasons could include:

- A desire to ensure that no retirees will need to pay more for coverage than under the current employer-sponsored arrangement
- Avoiding potential healthcare service and provider disruption for retirees
- Uncertainty about the financial sustainability of the exchanges and the subsidies over time
- Concerns about greater administrative complexities such as educating retirees about the exchanges and the various plan options, rather than just keeping retirees under the existing plan
- The effort that would be required for a low volume of current and future retirees, in cases where the employer's plan is not open to employees hired after a certain date
- Existing legally binding written commitments or union contract to offer health coverage to retirees
- A paternal corporate culture
- Competitive issues such as employee attraction or retention needs

Track the development of the health insurance exchange

While health insurance exchanges will not become operational until 2014, now is the time to start thinking about how to utilize this new system to address healthcare benefit needs for your current and future early retirees. The following is a timeline for you to keep track of the development of the exchange.

2012

- Understand benefits and costs of using the exchange for employees and retirees
- Track the progress of state's (or federal) exchange implementation
- Benchmark coverage level against exchange coverage levels
- Estimate benefits and costs of offering employee coverage through the exchange
- Estimate benefits and costs of offering retiree coverage through the exchange
- Await decision by U.S. Supreme Court on cases challenging the PPACA

2013

- Track the insurance carriers and HMOs that will offer plans through the exchange
- Complete financial analysis of offering coverage through the exchange
- Educate future early retirees about the exchange and enable them to compare plans from different carriers
- Communicate changes (if any) to employees and retirees
- Provide enrollment assistance (open enrollment for plans in the exchanges is expected to occur in the fall)
- Plan health reimbursement arrangement (HRA) contribution levels if offering such program to early retirees

2014

- Exchanges effective for individuals and small businesses with up to 50 employees

2016

- Exchanges effective for groups up to 100

2017

- Exchanges possibly expanded to larger employer groups

With the creation of exchanges still in its infancy, the U.S. Supreme Court's decision still pending, and political disagreements over PPACA still unsettled, employers and individuals face near-term uncertainties about the health insurance market in 2014.

Health reimbursement accounts under the health insurance exchanges

The health insurance exchanges may spur more employers to adopt health reimbursement arrangements (HRAs) for the early retiree group. This is because the exchanges are designed for individuals—such as early retirees—to purchase insurance that is suitable for their needs (e.g., different levels of coverage at various price points, but all of them providing “essential health benefits”). HRAs offer employers the means to continue or newly provide subsidies to the early retirees.

In general, an HRA is an employer-funded program that reimburses an individual for medical expenses (such as premiums, copays, coinsurance, deductibles, and services) up to a specified dollar amount for a coverage period. Contributions to the HRA are made solely by the employers (and are tax deductible), and are tax free (i.e., excluded from income) to the individual when used for qualified expenses. Under current regulations, some or all of the credit balances in a retiree’s (or an employee’s) HRA account may be rolled over from year to year, a design consideration determined by the plan sponsor.

For early retirees, an HRA allows them to use the employer subsidies to purchase health insurance from the exchange or to pay for other qualifying medical expenses. Unlike a health savings account (HSA), an HRA does not require coverage under a high-deductible health plan, and HRAs may be used to pay insurance premiums. From an employer’s perspective, an HRA can control healthcare costs by giving the employer the right to determine the subsidy amounts and to specify the covered medical expenses.

An HRA can be stand-alone or integrated with another group health plan. If the HRA is integrated with another group health plan, the HRA is not required to satisfy the annual limit restrictions imposed by the PPACA, as long as the other group health plan alone satisfies the PPACA’s annual limit restrictions. Note that a standalone HRA is permissible through January 1, 2014, if it was in effect prior to September 23, 2010, without having to obtain from the Department of Health and Human Services a waiver from the annual limit restrictions. Guidance for integrated HRAs in 2014 and later could limit HRA offerings for active workers. Standalone HRAs covering retirees only (or covering “excepted benefits” such as dental or vision benefits), however, will remain permissible after January 1, 2014.

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Other tax-advantaged programs such as a health savings account (HSA) may not offer effective financial support for early retirees as an HRA does in purchasing health insurance. Once an individual retires, he or she can spend down his/her HSA to pay for qualified medical expenses. However, premiums cannot be treated as qualified medical expenses under HSAs unless the premiums are for long-term care insurance, healthcare continuation coverage (such as COBRA), healthcare coverage while receiving unemployment compensation under federal or state law, or Medicare and other healthcare coverage (excluding Medicare supplemental policies) if an individual is aged 65 or older.

Conclusion

Starting in 2014, individuals and small businesses will have more options through the health insurance exchanges to purchase affordable and quality health insurance. Early retirees may be able to choose insurance plans that suit their needs from a variety of plans offered by private insurers on the exchange. To begin or continue subsidizing early retirees’ health insurance, employers may set up tax-advantaged programs such as a retiree-only HRA to help pay premiums, copays, deductibles, and other qualified out-of-pocket expenses. This may be the time for employers to start planning for changes in the health insurance landscape, and the possibility of no longer offering retiree health coverage given the new paradigm presented by the PPACA.



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