

New Strategy Manages Retiree Benefit Costs

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The high cost of retiree benefits is a factor in rising employer expenses for group benefits.

For years, insurance benefit brokers and consultants have encouraged decision-makers to keep retiree medical benefits combined with active employee populations in corporations' self-funded plans.

When retirees comprised a much smaller portion of the overall employee benefit pie and lived only a few years past 65, combining populations and self-insuring made good economic sense.

Today, however, with increases in retiree health care costs ranging from 12 to 18% a year, year after year — thanks primarily to escalating prescription drug costs — we need to rethink this strategy.

As more baby boomers head into retirement and new accounting rules kick in, the financial burden on employers is only going to get worse — much worse.

In addition to skyrocketing costs in retiree health care premiums and prescription drug expenditures, companies also face a growing administrative burden caused by the use of multiple vendors and the complex, time-intensive nature of serving an aging population.

Throw in the typical year-end claims shortfalls experienced by self-funded plans and the escalating plan administration expenses caused by balance sheet liabilities, and it's not surprising that runaway retiree health care costs are considered a financial time bomb.

Insurance benefit brokers and consultants need to offer chief executive officers, chief financial officers, and other top executives a better solution by segregating retirees from their active employee populations.

Solution Saves Time, Money

By insuring retirees separately, employers can pool this group with a larger population, thus spreading the risk and stabilizing premium increases. Without the higher risk factors and higher claim levels the elderly bring, costs for active employees can drop significantly.

I also recommend outsourcing plan administration. Developing and underwriting programs, negotiating with carriers, educating and enrolling retirees, providing one-on-one customer care, maintaining benefit Web sites, and handling policy administration, billing, and premium collection all cost time and money.

Factor in the administrative burden caused by having to deal with multiple vendors and large numbers of senior citizens with varied and challenging medical needs, retirees' time-intensive demands for customer service, and the heavy costs associated with claim shortfalls, and outsourcing makes even better financial sense.

In addition to lowering costs, companies gain increased productivity as human resource personnel now may devote more time to supporting the active employees who make the products, provide services, and generate revenue.

For example, a Fortune 500 automotive manufacturer with under \$10 million in health care-related costs in 2000 expected to spend more than \$20 million by 2007 with no changes in its current benefit plan. Including accounting amortization and interest expenses, the total costs would rise to close to \$35 million.

By segregating retirees and insuring them as a separate group, that company can develop a defined contribution plan that capped costs at \$10 million the first year, with an additional \$4 million in savings forecast for 2006 and 2007. By holding down FASB 106 and interest expenses, the company will save an additional \$20 million by 2007.

Because the contribution amount is fixed, it's easy to calculate balance sheet liabilities. The contribution also is carried as fixed cost rather than an actuarial estimate, creating additional tax benefits.

Called "carve outs," segregating retirees as a separate group also can serve as a powerful legacy liability reduction tool. By locking in corporate retiree medical expenses, CEOs and CFOs gain the flexibility they need to meet corporate financial goals, now and in the future. With their financial futures more secure, leaders can create more opportunities for their employees.

While each plan is tailor-made, I've been able to use this same basic strategy effectively with a wide variety of clients, including a national retailer that needed a new voluntary plan for 40,000 retirees, a steel manufacturer that faced the termination of its retiree health care benefits as part of a bankruptcy restructuring plan, a Fortune 500 automotive supplier that wanted to reduce its FASB-related expenses, and a health care organization that wanted to reduce its administrative burden.

In addition to claims administration, other outsource services and potential cost savings include fund accounting, actuarial calculations and study costs, fund legal expenses, PPO network leasing, stop loss premiums, utilization review expenses, and prescription expenses.

Outsourcing Benefits Retirees

Businesses aren't the only ones hard hit by the changing landscape of employee and retiree benefits, however.

According to the 2000 U.S. Census, the nation's 35 million retirees aged 65 and older now make up 12% of our total population. The percentage of people living to age 85 and beyond also is growing steadily, increasing the likelihood that more retirees will experience significant health issues — and major claims — during the last years of their lives.

Many of these retirees face an uncertain future, as promised medical benefits fail to materialize, premiums rise exponentially, and Medicare payments dwindle. Rapidly rising costs for prescription drugs are particularly problematic.

By participating in a group medical plan sponsored by their former employers, retirees usually enjoy more stable benefit packages and costs, as well as the increased attention that comes from companies that specialize in providing customer care for the elderly.

High quality customer care centers for senior citizens don't set time limits on each call. As a result, retirees are happier and receive better service, and company personnel can focus more time and attention on keeping active employees healthy and productive.

Unlike Medicare supplements, which are sold individually, employer-sponsored group insurance plans don't require health screenings and a lengthy application process as long as the retiree has been insured for at least six months prior to the start of the new plan.

Additionally, unlike standard Medicare supplements, these plans can be customized to meet the needs of the employer and retirees. My company, for example, has preferred carrier arrangements, allowing the pooling of retirees and the customization of benefits.

It's a Solution, Not Products or Services

By solving a major business problem for clients, and by making it easier to manage their retiree programs, insurance brokers and consultants will achieve better results and will grow their businesses more effectively.

While this approach doesn't fit all scenarios — why insure this group separately if retirees' claim expenditures are less than those of the active population? — focusing on solutions rather than specific products or services starts moving brokers and consultants from a vendor-type relationship driven by cost to serving as a true business partner.

Before the new Medicare rules kick in in 2006, CEOs, CFOs, and human resource directors will need new, effective solutions to hold down retiree benefit costs.

The coming pain represents a huge marketing opportunity. By offering proven solutions and a turnkey program, savvy insurance benefit brokers and consultants can improve everyone's bottom line, including their own.

Data Analysis and Detailed Planning Are Critical

The keys to success in developing this kind of solution lie in accurate and thorough data collection and analysis.

To begin the planning process, clients will need to provide an accurate census of all covered lives, including date of birth, gender, and ZIP codes. We analyze the current plan designs, both pre- and post-age 65, and the claims history with pharmacy-related expenses pulled out separately. The program's effective date(s) and a two- to three-year rate and administrative history are thoroughly examined.

The most important conversation, however, is going to be about the client's retiree benefit philosophy, and goals and objectives for the program. We can't design an effective solution without a clear understanding of what's driving the initiative. Financial goals (both short- and long-term) and the corporation's value system must align.

For many employees and other key stakeholders, benefits represent decades-long promises. Carving out retiree medical benefits, including prescription drug programs, helps business leaders keep their promises without breaking the bank.