



Having Problems with Retiree Drug Subsidy Under Part D? Try EGWP

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Even before health reform crossed the finish line as the Patient Protection and Affordable Care Act, employers were beginning to have doubts about opting for the Retiree Drug Subsidy (RDS) under [Medicare Part D](#).

While the federal government writing a check for up to 28 percent of the costs for retiree pharmaceuticals sounded good at first, the choice wore thin as employers gained more experience with the bookkeeping mandates and other rigid requirements that came with the subsidy.

Then when the health reform law put in place provisions that reduce the value of the subsidy beginning in 2013, corporations who filed for the RDS were forced to immediately adjust their financial statements to the tune of billions of dollars in future tax costs. It may well be the final straw that drives companies away from the subsidy and into the arms of agents and brokers who can bring them a better strategy: an Employer Group Waiver Plan (EGWP), better known as "egg whip."

Understanding the basics

The details of Medicare Part D options for employers who provide benefits to retirees can be complex. But agents simply need to know the broad outlines of the challenges facing their customers and why an EGWP can reverse the negative effects created by health care reform changes.

The story begins with [the creation of Medicare Part D](#). To keep employers from dumping drug prescription coverage and flooding the new program with their retirees, the federal government invited companies to accept a subsidy to pay for 28 percent of approved costs. The subsidy is not only tax free, but companies can continue to write off 100 percent of their pharmaceutical costs as expenses (their 72 percent share, plus the government's 28 percent).

The average value of the subsidy has been estimated at around \$500 per Medicare beneficiary per year, a bargain for the government since its cost to provide coverage exceeds \$1,000 per year.

Under health reform, companies will no longer be able to write off the 28 percent of the costs covered by the subsidy, and the administrative costs associated with the retiree drug subsidy will no longer be deductible. These are significant reductions in the value

of the subsidy for employers – a value that under general accounting rules has been factored into future liabilities that are reflected in current financial reports.

As with all substantive changes in financial situations, companies were obligated to immediately report the change in their future tax liabilities. The amounts were stunning: \$1 billion for AT&T, \$150 million for John Deere, and \$90 million for 3M, to name a few. In fact, Towers Watson benefits consultants estimates that as many as 3,500 companies that accept the drug subsidies may write down as much as \$14 billion.

Whipping up eggs in place of subsidies

Although the new tax status for the 28 percent retiree drug subsidy does not kick in until 2013, many companies are already beginning to look for a way out. Employer Group Waiver Plans – EGWPs, pronounced "egg whips" – are increasingly attracting their attention.

At its most direct, an EGWP allows an employer to contract with the federal government as a prescription drug plan (PDP) sponsor to provide drug benefits to retirees. Using a nationally based formula, the government pays the company a capitation fee that can exceed the retiree drug subsidy by \$100 to \$200 per member per year. Experts estimate that under EGWP, the federal government covers 35 percent or more of the drug prescription costs incurred by an employer, far exceeding the 20 percent average yield of the drug subsidy.

A more appealing approach for many companies is what is known as an 800 Series EGWP. Under this strategy, a company can contract with a third party Part D sponsor, who interacts with the federal government. The sponsor retains a fee but passes through the bulk of government payments in the form of lower premiums or direct payments to the employer.

The 800 Series EGWP offers a number of benefits. The contracted PDP sponsor shoulders the expenses associated with verifying compliance each year. The plan can be customized to match an employer's current benefits, allowing the company to meet its obligations, whether thanks to collective bargaining or to commitments made to employees in a non-union environment. Overall, it maximizes the government contribution toward pharmaceutical expenses without imposing administrative burdens on the company.

Riding to the rescue

The change in the drug subsidy situation is undoubtedly just the beginning. As the ramifications and unforeseen consequences of the health reform act begin to unfold, many businesses will be looking for solutions to unexpected health benefit problems. Agents who partner with third-party experts can stay on top of the changes and bring creativity and innovation to their role as a trusted advisor to their customers. In many cases, an 800 Series EGWP may be just the solution a customer needs.

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