# CARVING

**WHEN THE BUSINESS CYCLE HITS THE BRAKES, COMPANIES SCRAMBLE TO FIND WAYS TO CUT COSTS.** The best, most aggressive benefit consultants are there to help with long-term sustainable strategies. That's when expertise and creativity can turn a benefit broker into a valued partner for customers. By showing employers how the health benefits game has changed and outlining a menu of proven strategies, independent producers can offer insight that deepens relationships with existing customers and wins referrals to new ones.

## THE BOTTOM LINE

In the past, the promise of retiree health benefits was a way to attract and retain the best employees. Covered by the same plan as current workers, the retirees represented an incremental cost and a short-term obligation. Today, workers are retiring earlier, living longer and requiring far more costly care at the end of their lives.

At the same time, overall health care costs are skyrocketing, presenting businesses with an all-but-intractable problem that makes it difficult for them to compete in today's global marketplace.

The drag on the corporate bottom line is huge. In 2006, Standard & Poor's estimate for the unfunded liability for retiree health benefits at 300 of the largest companies in the country was almost $300 billion. Some of the most visible examples of this problem have been in the automobile industry. Before winning concessions from unions in 2006, General Motors calculated that the cost of health care was adding more than $1,500 to the price of a car — and that

# OUT RETIREES

## to Reduce Health Care Costs as the Economy Worsens

BY SAMUEL H. FLEET

70% of that cost was attributable to retirees. Carmakers are not alone. Kellogg Co. is shifting the Medicare-eligible retirees in its Keebler unit to a lower-cost approach to coverage.

In today's economy, it's more necessary then ever before for companies to reduce the huge unfunded liabilities on their balance sheet created by large numbers of retirees. Brokers should be aware that companies must use the best strategy to bring these current retiree health care costs under control, while still meeting legal and ethical obligations to their former workers. Brokers can walk in and tell employers that they can help them improve their borrowing power by reducing the large, unfunded liability on their balance sheet. That is a big business solution, not just a health care solution.

### THE CARVE OUT STRATEGY

Benefit brokers can present their customers with a number of options that flow from a time-tested, proven strategy: Carve out retirees from the existing company health care plan and address their needs separately. This frees the health care plan for the current workforce from the costly burden of covering older and usually sicker individuals, while also improving balance sheet liabilities. By following one of the options below, a company is able to convert an uncertain future obligation into a reliable annual cost.

- **CONTRACT OUT** — Using a third-party administrator with access to a national pool of retirees, companies can create a separate plan for their retirees. This approach can eliminate uncertainty in annual costs, spread the risk to a broader base, reduce administrative costs and offload customer service responsibility. Contracting out for coverage gives the company the flexibility to make choices that are different from those for their worker base while creating a plan that meets the needs of their retirees.

- **EMPLOY A PDP** — The new Medicare Part D prescription drug benefit has complicated the retiree health benefits picture by forcing employers to understand the ins and outs of accepting a federal subsidy to continue their own plans. A compelling case can be made that by contracting with a Prescription Drug Plan (PDP) a company can avoid the costly strings attached to the subsidy, shift risk to the PDP and federal government, eliminate the most costly and volatile component of their retiree health care coverage, outsource customer service and education, and convert an unfunded liability to a current, quantifiable cost.

- **TERMINAL FUNDING** — Terminal funding is a fixed-annuity contract that a company purchases to provide guaranteed payments to a designated group of participants under a defined benefit plan. It's an efficient, lump-sum method of retiring long-term liabilities from the corporate books. At the same time, it provides retirees a guaranteed benefit into the future. For companies that have capped their obligation to retirees, terminal funding allows them to take care of the future uncertain expense with a one-time payment.

- **HRA NATIONAL ACCOUNTS** — Health reimbursement arrangements (sometimes known as retiree reimbursement arrangements) allow companies to deposit an annual contribution for each retiree into a tax-free personal account. The funds can then be used as the retiree sees fit — purchasing Medicare Advantage, supplemental insurance or paying out-of-pocket medical costs. This approach returns control of health care choices to the retiree and streamlines administrative processes and costs.

Companies will always struggle to cut costs while offering benefits that attract talented employees. As demographics change and health care costs continue to soar, companies should know that what worked in the past will not necessarily be the best guide for coping with the future. By approaching retiree obligations with creativity and a choice of cutting-edge products, the benefit broker can help customers revamp their benefit strategies to address current challenges.

*Samuel Fleet is president and CEO of AmWINS Group Benefits, a leading developer, distributor and administrator of various group insurance programs. Fleet founded NEBCO, the AmWINS Group Benefits predecessor, in 1991. AmWINS Group Benefits is a division of AmWINS Group, Inc., the largest wholesale insurance broker in the country.*