

VIRGINIA CHAPTER OF IPMA

**GASB 45 and Medicare Part D:
Understanding Your Liability
and Potential Cash Subsidy**

August 16, 2005



**WACHOVIA
INSURANCE SERVICES**



PALMER & CAY

Established 1868



Agenda

- » Government Accounting Standards Board Statement No. 45 (GASB 45)
- » Medicare Part D
- » Questions

GASB 45



**WACHOVIA
INSURANCE SERVICES**



PALMER & CAY

Established 1868



GASB 45 – Useful Terminology

GASB = Government Accounting Standards Board

OPEB = Other Postemployment Benefits other than Pensions

SLG = State and Local Government

ARC = Annual Required Contribution



GASB 45 – Current Accounting Approach

- » Many OPEB plans have never had an actuarial valuation performed
- » Most SLGs finance OPEB on a pay-as-you-go basis
- » SLG financial statements generally:
 - Disclose that OPEB are provided
 - Report only the amount paid



GASB 45 – Current Accounting Approach

- » SLG financial reporting fails to:
 - Recognize the cost of benefits in periods when employee services are rendered
 - Provide information about the actuarial accrued liabilities for promised benefits
 - Provide information useful in assessing potential demands on future cash flows



GASB 45 – Purpose of Accounting for OPEB

- » Treat OPEB in a manner similar to pension benefits
- » Recognize that OPEB constitute compensation for employee service
- » Recognize the cost of benefits during the periods when employee service is rendered



GASB 45 – Purpose of Accounting for OPEB

- » Accounting for OPEB will:
 - Improve the relevance and usefulness of financial reporting
 - Provide for the systematic accrual of OPEB over the employee service period
 - Provide information about the size of the liabilities and the extent to which they are funded



GASB 45 – What Benefits are Valued?

- » Postemployment healthcare benefits
 - Medical (including Rx)
 - Dental
 - Vision
 - Hearing



GASB 45 – What Benefits are Valued?

- » Other postemployment benefits:
 - Life insurance
 - Disability
 - Long-term care
 - “Other” benefits
- » Only when provided separately from a defined benefit pension plan



GASB 45 – What Benefits are NOT Valued?

- » Other postemployment benefits not valued:
 - Vacation benefits
 - Sick leave conversion benefits
 - Special termination offers and benefits
 - Incentives to terminate service rather than compensation for services
 - Valued under GASB 47, issued June 27, 2005



GASB 45 – Effective Date

» Effective date depends on the size of the SLG:

<u>Total Revenues</u>	Effective for fiscal year <u>Beginning after:</u>
\$100 million or more	December 15, 2006
\$10 million to \$100 million	December 15, 2007
Less than \$10 million	December 15, 2008



GASB 45 – Measurement Frequency

- » Plan sponsors with over 200 members
 - At least biennially
- » Plan sponsors with less than 200 members
 - At least triennially



GASB 45 – Why is this Important?

- » Most SLGs provide some level of retiree welfare benefits
 - Medical
 - Life insurance
- » Most SLGs subsidize the retiree cost for these benefits
 - Cost sharing based on service
 - Implicit (hidden) cost subsidies



GASB 45 – Why is this Important?

- » GASB 45 will significantly increase the annual expense for SLGs to provide these benefits
 - Amortization of unfunded liabilities
 - Recognition of future retiree accruals
- » Many SLGs will struggle to afford this



GASB 45 – What You Should Do Now!

- » Begin planning now, it's not too early
- » Identify the benefits promised
- » Derive actuarial estimates of the OPEB Obligation (liability)
- » Determine accounting impact
- » Evaluate cost containment strategies
- » Consider funding alternatives

Medicare Part D



**WACHOVIA
INSURANCE SERVICES**



PALMER & CAY

Established 1868



Medicare Part D - Terminology

- » **TrOOP** – True out of pocket cost
- » **Creditable Coverage** – Measures plan design only. Applies to any plan sponsor with Medicare eligible participants (active or retired).
- » **Actuarial Equivalence** – Measures plan design and contributions. Applies to employers with retiree Rx coverage.
- » **Part D Eligible Participants** – Those who are enrolled in Medicare Part A or Part B and live in a service area of a Part D plan.
- » **CMS** – The Centers for Medicare and Medicaid Services
- » **PDP** – Prescription Drug Plan approved by or contracted with CMS.

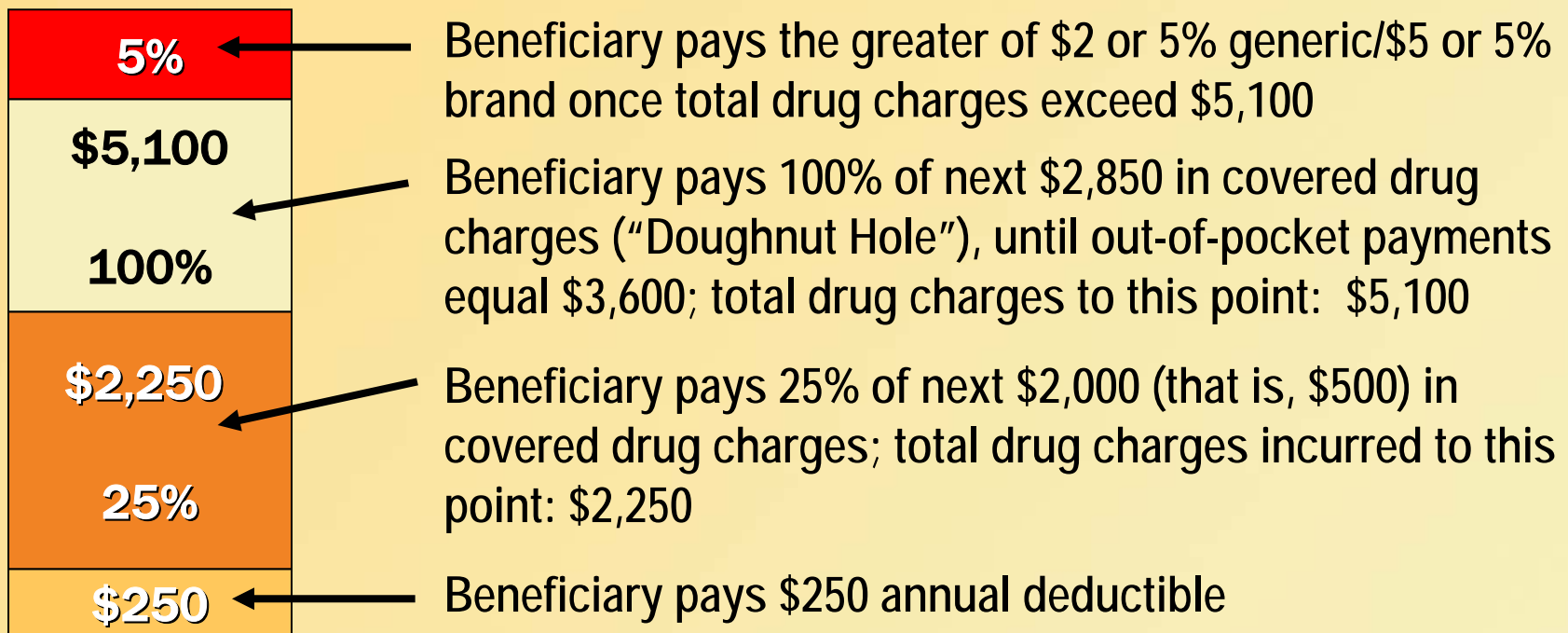


Medicare Part D - Highlights

- » Medicare Part D provides prescription drug coverage to beneficiaries eligible for Medicare
- » Effective 1/1/2006
- » Open enrollment begins 11/15/2005 for 2006
- » Voluntary program
- » Annual enrollment period
- » Average premium is estimated to be \$37/month for 2006, but may vary (late enrollment penalties apply)
- » PDP plan design and premium are not available yet

Medicare Part D - 2006 Plan Design

Medicare Rx Benefit – Cost Sharing



- » \$3,600 is the true out-of-pocket (TrOOP)
- » Dollar limits are indexed annually



Medicare Part D - Creditable Coverage Notification Requirements

- » Which plan sponsors need to comply?
 - Any plan sponsor who has Part D eligible participants (*active, retired, disabled or dependents of any covered by your plan*)

- » What are plan sponsors required to do?
 - Determine if their plan qualifies as creditable coverage (separately for each plan option)
 - Notify Part D eligible individuals
 - Notify CMS



Medicare Part D - Creditable Coverage Notification Requirements

» What is creditable coverage?

- Creditable coverage occurs if the plan sponsor's plan design would pay at least as much as Part D
- CMS has issued simplified rules for determining creditable coverage
- Plans with low annual maximums or integrated medical/Rx deductibles would need further testing



Medicare Part D - Creditable Coverage Notification Requirements

- » Plan sponsors must communicate results to all Part D eligible participants who are covered or who apply for coverage
- » Can be stand alone communication piece or with other plan materials
- » Must contain standard information elements (CMS has provided model language)



Medicare Part D - Creditable Coverage Notification Requirements

- » Timeline for disclosure to participants:
 - Prior to the initial enrollment period for Part D (11/15/05 for those eligible 1/1/06),
 - Prior to effective date of coverage under plan sponsor's plan,
 - Upon any change that affects whether coverage is creditable, and
 - Upon request



Medicare Part D - Creditable Coverage Notification Requirements

» Notification to CMS

- Plan sponsors must notify CMS whether or not their plan provides creditable coverage
- CMS will provide further guidance on the timing, format, etc.
- Annually or when status changes



Medicare Part D - Options for Employers

- » Maintain existing plan and receive the subsidy (if plan passes two prong actuarially equivalent test)
- » Provide a wrap around plan
- » Contract with a licensed PDP (Prescription Drug Plan)
- » Drop coverage for Medicare eligible beneficiaries



Medicare Part D - Determining Actuarial Equivalence for Subsidy

- » Actuarial equivalence takes into account both plan design and contributions
- » Two-prong test
 - ***Gross actuarial value test:*** The plan passes if the plan would pay at least as much as Part D
 - ***Net actuarial value test:*** The plan passes if the plan's paid claims for Rx less premiums paid by retirees for Rx is at least as much as the standard Part D's paid claims less Part D premiums



Medicare Part D - Determining Actuarial Equivalence for Subsidy

- » Actuary has reasonable discretion on how to allocate premium between medical and Rx
- » If there are multiple retiree plans, actuarial equivalence may be determined separately for each plan or in the aggregate



Medicare Part D - Determining Actuarial Equivalence for Subsidy

Development using Plan Sponsor's Actual Pharmacy Claims Data	Part D (Annual)
Value for Standard Part D Coverage	\$1,550
Retiree Premium (\$35 x 12)	\$420
Value for Standard Part D Plan	\$1,130

Medicare Part D - Determining Actuarial Equivalence for Subsidy

	Retirees	Spouses	Combined
Head Count	200	120	320
Total Plan Cost	\$2,800	\$2,800	
Medical Plan Cost	\$1,120	\$1,120	
Rx Plan Cost	\$1,680	\$1,680	
Total Retiree Premium	\$800	\$1,800	
Retiree Medical Premium	\$800	\$1,120	
Retiree Rx Premium	\$0	\$680	
Employer Rx Value (cost minus premium)	\$1,680	\$1,000	\$456,000
Standard Part D Value	\$1,130	\$1,130	\$361,600
Net Value Test	PASS	FAIL	PASS




Medicare Part D - Determining Actuarial Equivalence for Subsidy

- » Determine eligible plan costs
 - Include Rx costs for Medicare eligible retirees and Medicare eligible spouses and dependents of a retiree
 - Exclude beneficiaries enrolled in individual Part D plans
 - Exclude drugs not covered by Part D
 - Eligible plan costs are allowable charges incurred under the plan between \$250 and \$5,000 per person
 - Include the portion paid by the employer and the claimants
 - Include ingredient costs + dispensing fee
 - Subtract value of rebates (how to determine?)
 - Exclude administrative cost
- » Subsidy equals 28% of the eligible plan costs for the year



Medicare Part D - Employer Subsidy Comments

- » Tax free
- » Direct payment to the employer
- » Will result in reduction in GASB 45 liability
- » Does not reduce the employer's deduction for retiree medical
- » CMS estimates average subsidy of \$668 per Medicare eligible participant
- » Plan sponsor must apply by 9/30/05 for a 2006 subsidy



Medicare Part D – Other Options

- » Wrap around drug plan
 - Plan sponsor's plan supplements the beneficiary's out of pocket expenses under Part D
 - Retiree/spouse enrolls in Part D **and** the employer's wrap around plan
- » Contract with a licensed PDP
 - Could offer standard Part D benefits or one of the enhanced benefit designs offered by the PDP
- » Drop Retiree Prescription Drug Coverage




Medicare Part D - To Do List for Employers

- » Educate yourself and your retirees regarding Part D options
- » Determine creditable coverage and communicate to Medicare eligible participants and CMS
- » Evaluate options for the retiree prescription drug plan (subsidy, wrap, contract with PDP, or drop coverage)
- » Request a claims extract and exposures from the PBM for the actuary to determine actuarial equivalence




Medicare Part D - To Do List for Employers

- » Determine what PBM will provide and applicable charges
- » Upcoming Deadlines:
 - September 30, 2005 – Subsidy application due for 2006 (includes actuarial attestation and list of eligible beneficiaries due to CMS)
 - November 15, 2005 – Deadline for communicating creditable coverage to all Medicare eligible beneficiaries
 - November 15, 2005 to May 15, 2006 – Open enrollment for Medicare Part D (subsequent years, September to December)



Medicare Part D – What Should You do Now!

- » Determine whether your plan provides creditable coverage
- » Use model language for creditable coverage notices
- » Determine if your plan passes the two pronged actuarial equivalent test and provide a certified attestation for employers seeking the subsidy
- » Calculate subsidy effect on GASB 45 liabilities
- » Evaluate plan design and funding issues



Medicare Part D – What Should You do Now!

- » Training of your HR staff
- » Developing communication strategy for retirees

Questions?



**WACHOVIA
INSURANCE SERVICES**



PALMER & CAY

Established 1868