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Report to Congressional Requesters

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EMPLOYEE BENEFITS

Extent of Companies' Retiree Health Coverage

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The Honorable Edward R. Roybal
Chairman, Select Committee on Aging
House of Representatives

The Honorable J.J. Pickle
Chairman, Subcommittee on Oversight
Committee on Ways and Means
House of Representatives

This report is in response to your request for information on the extent to which companies provide retiree health benefits. We determined the (1) percentage of companies with retiree health plans, (2) number of workers enrolled in company health plans that extend coverage to retirees, (3) number of retirees enrolled in company health plans, and (4) percentage of companies that have terminated retiree health plans since 1984.

The data we obtained showed that companies provide health coverage to active workers much more often than they do to retirees. A very small percentage of companies provide retiree health coverage. However, because the companies providing retiree coverage tend to be larger, a relatively high percentage of people worked for firms with retiree health coverage. Specifically, in our study population:

- Over one-half of all companies provide health coverage to active workers, and nearly two-thirds of private sector workers are in company health plans.
- About 4 percent of companies have retiree health plans. Sixty-seven percent of those without plans said they had no retirees.
- Companies with retiree health benefits employed 40 percent of private sector workers. About 30 million workers are enrolled in company health plans that provide for continued coverage upon retirement.
- Over 5 million retirees are now in company-sponsored health plans. About 2 million, or 40 percent, of these retirees are under age 65.

Fewer than 1 percent of companies have terminated a health plan that resulted in retirees or active workers losing retiree health coverage since 1984. However, companies are taking measures short of termination to limit retiree health costs. Over one-third of companies with health plans for active workers or retirees required participants to help pay for coverage. A recent benefit survey, as well as previous GAO work, show that companies are increasingly requiring participants to share coverage costs or shifting more of the costs to participants.

The data we obtained do not include retiree health benefits that companies are providing indirectly, through multiemployer plans. We will provide information on these plans in a separate report to be issued in late 1990.

Background

Company group health plans play a major role in providing active and retired workers and their dependents with access to needed medical services. Through group health plans, workers and their dependents may obtain hospitalization, physician, and other health services at less cost than they could purchase them individually. Retiree health plans usually cover similar services. This health coverage is especially important to retirees under the age of 65, because most are not eligible for Medicare.

Although seen as a low-cost employee benefit decades ago, retiree health coverage has now become a major concern for companies because retiree health costs have risen and are expected to continue to increase dramatically in the future. Most companies fund these costs as they come due (pay as you go), rather than set aside funds to help pay for health coverage once workers retire (advance funding).

Companies currently recognize only the pay-as-you-go retiree health costs as expenses on their income statements. The Financial Accounting Standards Board (FASB),[1] however, has announced its intention to require companies to recognize on their financial statements retiree health liabilities for current and future retirees. Companies have expressed concerns about the impact that such disclosure could have on their operations since it will result in a less favorable picture of their financial position.[2] The increasing costs of retiree health benefits and potential adverse effects on businesses' financial statements from disclosing unfunded liabilities have raised questions about companies' ability and willingness to continue providing these benefits.

[1] An independent authority responsible for setting accounting standards for the private sector.

[2] Employee Benefits: Companies' Retiree Health Liabilities Large, Advance Funding Costly (GAO/HRD-89-51, June 14, 1989).

Current Law Provides Limited Benefit Protection

Under current law, retirees who are receiving benefits, as well as workers who expect to receive health coverage after they retire, have little protection from company actions to reduce or terminate benefits. Retiree health benefits are specifically excluded from many of the protections provided to pension benefits under the Employee Retirement Income Security Act of 1974 (ERISA). For example, companies are not required to advance fund retiree health benefits, and there are no standards to ensure that employees will not have to work an unreasonable number of years before having a nonforfeitable right to benefits accrued (vesting).

The Congress has taken some actions to protect retiree health benefits; however, these actions offer only limited protection. The Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) requires companies to offer retiring and other terminated employees the opportunity to continue to participate in a company's group health plan for a limited period of time, generally 18 months, at the former employees' expense. The Retiree Benefits Bankruptcy Protection Act, passed in June 1988, prohibits companies that file for chapter 11 bankruptcy from modifying or terminating retiree health benefits unless they can prove in court that modification is necessary to avoid liquidation.

The Congress has recently considered other legislative proposals designed to enhance the security of retiree health benefits and provide companies with tax incentives to encourage advance funding. Bills introduced during 1989 would have changed federal tax law to encourage advance funding; permitted tax deductions for employer contributions to retiree health trusts that meet certain requirements, including vesting, transfer, and distribution standards; and provided for federally guaranteed loans to certain distressed companies to provide retiree health benefits. While none of these proposals was enacted, some may be considered during the current congressional session.

Limited Data on the Extent of Benefits

Information on the extent to which retiree health benefits are offered is limited. Several private and public sector studies present data on company health plans, but they primarily cover medium and large companies.[3] Little is known about smaller companies' health benefits, especially companies with fewer than 100 employees.

Scope and Methodology

We collected data in response to your questions from March to August 1989. In doing so, we mailed questionnaires to a random sample of 5,550 companies, stratified by size and industry group. We developed the strata by grouping companies into four sizes and six industry categories. Our sampling frame of 6.9 million companies was developed from the Dun's Marketing Service database. We selected this database because it had the most complete and current information on companies of all sizes and industry types.

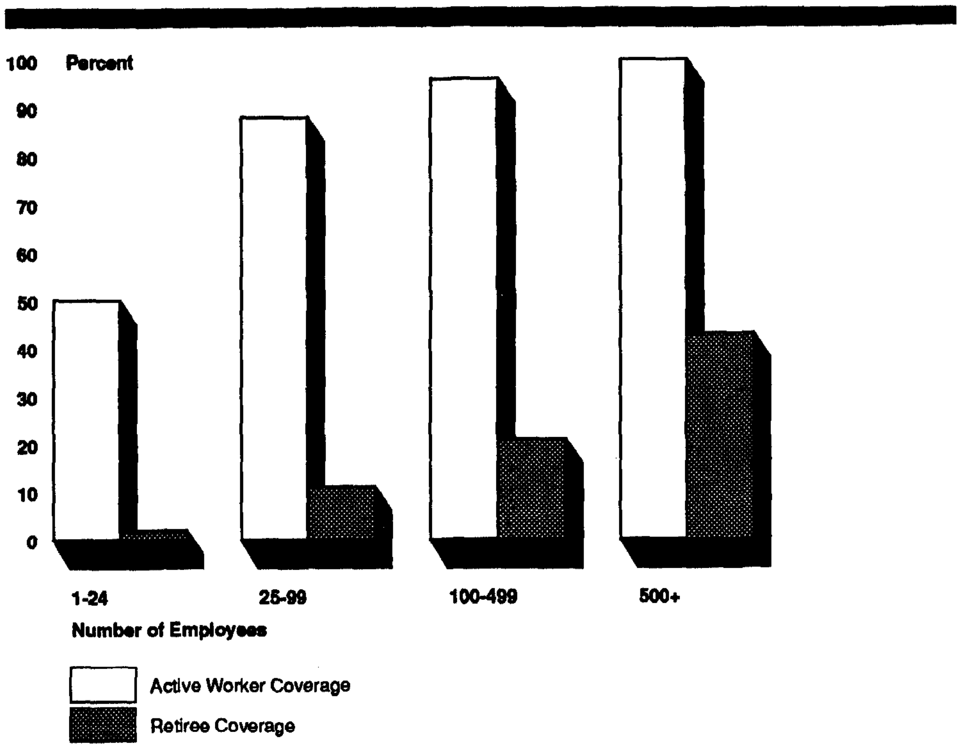
The responses we received to our survey allow us to generalize the results to a population of 2.5 million of the 6.9 million companies. We did not independently verify the data companies submitted. (For details of the sampling and survey procedures used, see app. I.)

Larger Companies More Likely to Have Retiree Health Benefits

Through our questionnaire, we examined the relationship between companies with group health plans for active workers and those with retiree health benefits. Overall, only about 105,000, or 4 percent of all companies, extend health coverage to retirees beyond the time required by COBRA. Larger companies extended coverage much more often than smaller ones. Nearly all companies with over 500 employees have health coverage for active workers and about 43 percent of these also offer retiree coverage. In contrast, only one-half of the companies with fewer than 25 employees offer health coverage to active workers; only 2 percent of these provide retiree coverage. (See fig. 1.) These small companies constitute 85 percent of all companies.

[3]Examples include: U.S. Department of Labor, Bureau of Labor Statistics, Employee Benefits in Medium and Large Firms, August 1989; Foster Higgins, Health Care Benefits Survey 1988, Report of Survey Findings, 1988; The Wyatt Company, A Survey of Health and Welfare Plans Covering Salaried Employees of U.S. Employers, 1988; and Equicor, Looking to the Future of Retiree Health Benefits, conducted June-August 1986.

Figure 1: Percentage of Companies With Health Benefits for Active and Retired Workers, by Company Size



Five Million Retirees Have Benefits; Millions More May Become Eligible

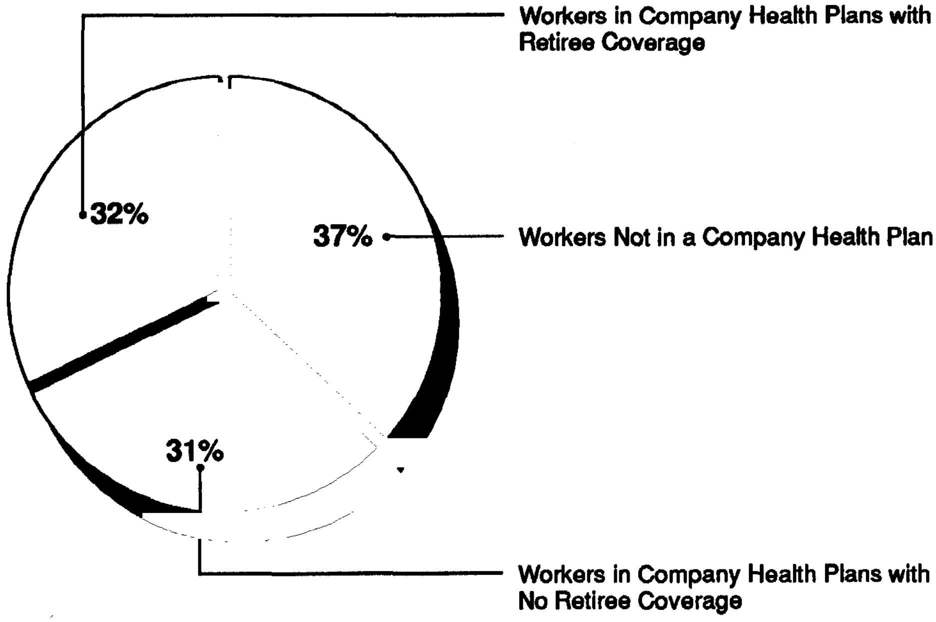
We estimate that over 5 million retirees are currently in company group health plans, including about 2 million, or 40 percent, who are under age 65.[4] Nearly 80 percent of companies with retiree health benefits cover retirees under age 65; over 60 percent of companies with retiree health benefits cover retirees regardless of age. As noted earlier, health coverage is especially important for retirees under age 65, because most are not eligible for Medicare.

Far more workers may become eligible for retiree health coverage than the number of companies with retiree coverage might suggest, because most workers are employed by larger companies. About 73 percent are employed by companies with 100 or more employees. Our work shows that companies with retiree health coverage employ 38 million workers—40 percent of an estimated 96 million private sector workers.

[4]For sampling errors associated with worker, retiree, and company characteristic estimates, see tables I.5 and I.6.

About 30 million of these workers,[5] or nearly one-third of all workers, are in company-sponsored plans that cover retirees (see fig. 2). Assuming company health plan provisions do not change, these are the workers companies must consider in calculating future retiree health liabilities, and who may expect to receive retiree health benefits in the future.

Figure 2: Breakdown of Workers' Participation in Company Health Plans



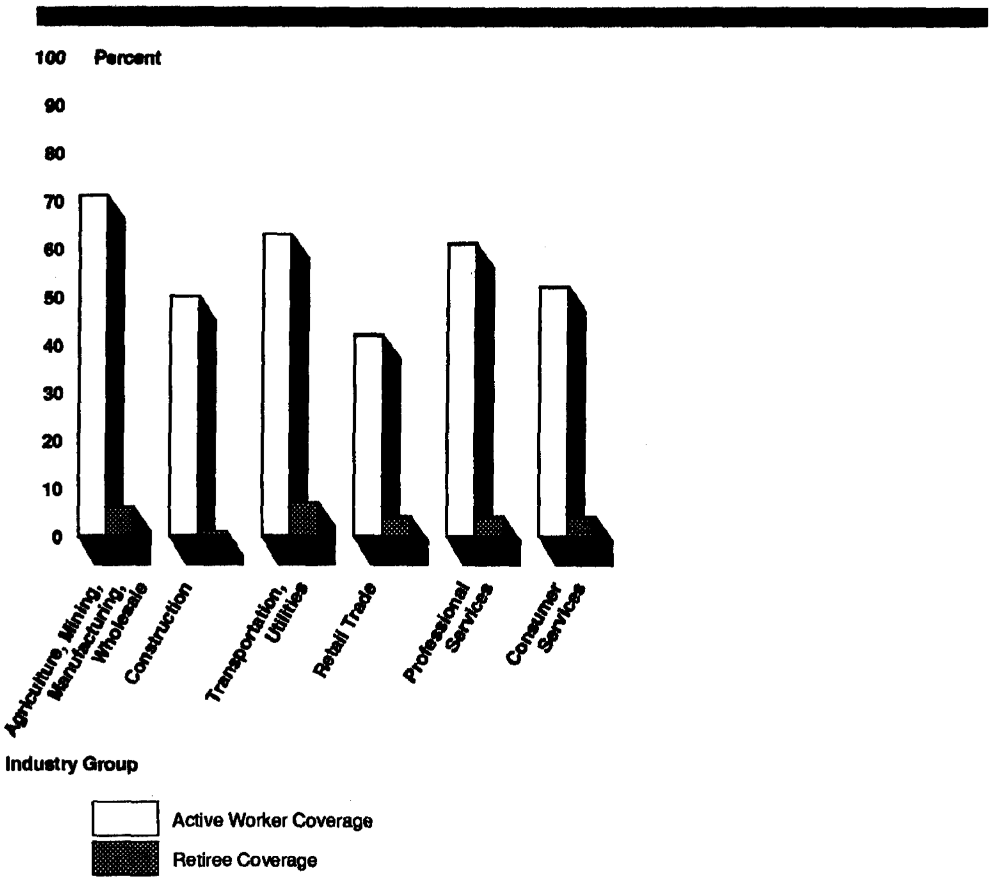
Note: For sampling errors, see table I.7.

Retiree Health Coverage Varies Little Among Industries

We compared health coverage for active workers and retirees by type of industry, to determine whether certain industries are more or less likely to provide these benefits. While differences were sizable for active worker coverage, we found little variation among companies with retiree health benefits when comparing companies by industry group. (See fig. 3.)

[5]Some workers are not enrolled in company plans because they either (1) do not meet eligibility requirements, (2) are covered through a multiemployer plan, or (3) choose not to participate.

Figure 3: Percentage of Companies With Health Benefits for Active and Retired Workers, by Industry Group



Note: For sampling errors, see table I.8.

All six of the industry groups shown in figure 3 are characterized by a high percentage (78 percent or more) of companies with fewer than 25 employees. Because few small companies offer retiree health benefits, the percentage of companies with these benefits is relatively low among all industry groups. The construction industry had relatively fewer companies with retiree health coverage; the construction and retail trades had fewer companies with health coverage for active workers.

Most Companies Cited "No Retirees" as a Reason for Not Having Retiree Health Benefits

We asked the companies in our survey that did not offer retiree health benefits to select the reasons, from those cited in several health surveys we reviewed, why they did not offer this benefit. Table 1 shows that 67 percent of these companies selected "no retirees" as the reason they do not have a retiree health plan. "Little or no demand by employees" was the second most selected reason at 29 percent.

Table 1: Reasons Companies Selected for Not Having Retiree Health Benefits

Reason	Percent[a]
No retirees	67
Little or no demand by employees	29
Not a normal practice within the industry	25
Retirees covered by Medicare	12
Cannot qualify for group coverage	10
Employees receive benefits through a multiemployer plan	2
No reason selected	2
Other	11

[a]Percentages do not add to 100 because respondents could select more than one reason.

Companies Are Making Changes to Limit Retiree Health Costs

Since 1984, fewer than 1 percent of companies have terminated a health plan that resulted in retirees losing their coverage, or active workers not being eligible for coverage upon retirement. A benefit survey[6] and a GAO study[7] both found, however, that companies are taking measures short of termination to limit retiree health costs. Companies have changed health plan provisions to shift costs to retirees or reduce benefits, and appear to be doing so at an increasing rate.

One way companies can limit their health costs is by requiring participants to share in the cost of coverage. Our survey shows that, as of 1987, over one-third of companies with health plans for active workers or retirees required contributions to help pay for the cost of coverage.[8] A 1988 survey of over 1,600 companies, by the consulting firm Foster Higgins, reported that 62 percent of survey respondents required contributions from retirees under age 65; 53 percent required those age 65 and over to contribute.

[6]Foster Higgins, Health Care Benefits Survey 1988, Report of Survey Findings, 1988.

[7]Employee Benefits: Company Actions to Limit Retiree Health Costs (GAO/HRD-89-31BR, Feb. 1, 1989).

[8]For sampling error, see table I.6.

Companies appear increasingly to be asking participants to share coverage costs, or are shifting more of the costs to participants. In the Foster Higgins survey, 21 percent of respondents offering retiree health coverage had increased the level of contributions in the last 2 years or planned to increase it by 1990.

In our February 1989 report, we reviewed the changes that a sample of 29 medium and large companies in the Chicago area had made to limit retiree health costs. All 29 companies had changed their plan provisions during 1984-88 to require retirees to pay more of the costs for coverage and services received. We concluded that future changes companies may make to help contain costs could be more substantial. Officials at 26 companies expressed uncertainty about their companies' ability to continue providing retiree health benefits in the face of rising costs and the FASB proposal to require companies to disclose future retiree health costs on their financial statements.

In June 1989, we recontacted these companies and found that 21 of the 29 had made additional changes in the last year.[9] While many of these changes were similar to those made in previous years, a few made even more significant changes to help limit retiree health costs. One company has decided to phase out this coverage altogether; current employees and retirees will not be affected, but new employees will not receive health benefits upon retirement. Officials at 21 companies said they were considering further changes to their retiree health plan structures; at 10 companies officials said they were studying the impact of FASB's proposed regulations before making changes.

Concluding Observations

Millions of workers and retirees have or may become eligible for company-sponsored retiree health benefits. The private sector's role in providing these benefits is changing, however. Companies are taking actions to limit rising retiree health costs. While few companies have terminated benefits, many are requiring retirees to pay more for their health care. Current and future retirees have limited protection under current law against company actions to reduce or terminate benefits. FASB's proposal that companies recognize retiree health liabilities on their financial statements has caused some companies to reconsider whether they will be able to continue providing these benefits.

[9] Employee Benefits: Companies' Retiree Health Liabilities Large, Even With Medicare Catastrophic Insurance Savings (GAO/T-HRD-89-29, June 24, 1989).