



WHAT HAPPENS TO HEALTH BENEFITS AFTER RETIREMENT?

By Richard W. Johnson*

INTRODUCTION

Because most workers receive health benefits from their employers, retirement often disrupts health insurance coverage. Some employers offer health insurance to retirees, but many firms are cutting retiree health benefits by passing more costs to retirees or eliminating benefits altogether. Few alternatives exist. Private nongroup coverage is generally quite expensive, and few people in their 50s and early 60s qualify for publicly financed benefits. Many workers who cannot obtain retiree benefits from their own employers or their spouses' employers delay retirement to age 65, when Medicare coverage begins.

This *brief* examines the availability and cost of health insurance coverage at ages 55 to 64 and changes in coverage after retirement. Today most workers with employer health benefits retain their coverage when they retire early, although their required premium contributions have increased sharply over the past ten years. In the future, however, steady declines in the share of younger workers with access to retiree health benefits may jeopardize income security for the next generations of retirees.

SOURCES OF HEALTH INSURANCE COVERAGE

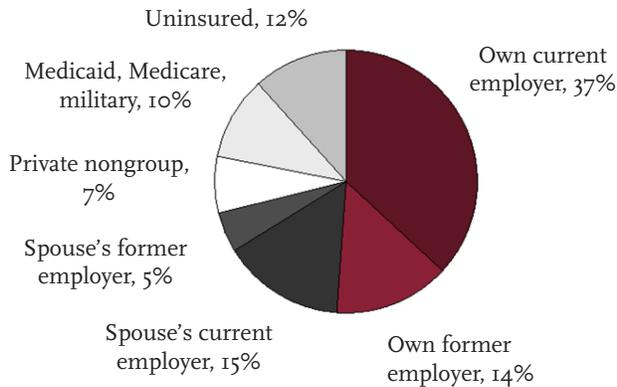
In 2004 employers provided health insurance coverage for about seven of every ten adults near traditional retirement ages. Among adults aged 55 to 64, 37 percent received insurance coverage from their own current employers and 15 percent received coverage from their spouses' current employers (see Figure 1).¹ Another 14 percent received benefits from their own former employers and 5 percent received coverage from their spouses' former employers. Most people with coverage from former employers received retiree health benefits, which continue until age 65 and sometimes supplement Medicare benefits at older ages. A few people, however, received only federally mandated continuation coverage from their former employers. The Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) requires employers with health plans and 20 or more employees to offer coverage to separating workers for up to 18 months (or 29 months for disabled workers), but these workers must pay up to 102 percent of the group rate.

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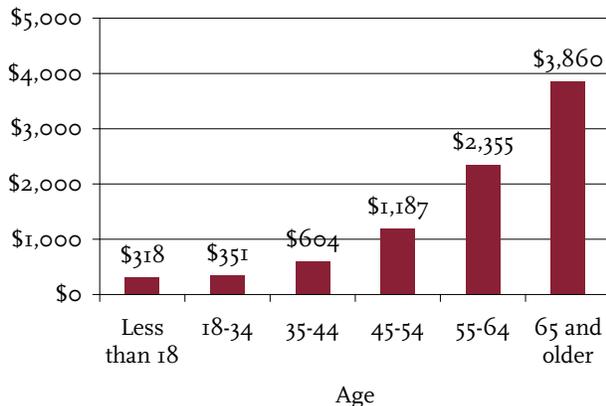
FIGURE 1. HEALTH INSURANCE COVERAGE FOR ADULTS AGED 55 TO 64, BY SOURCE, 2004



Source: Author's estimates from University of Michigan (2005). See endnote 2 for more details.

Some older people without employer health benefits who are too young for Medicare turn to the private nongroup market or government for coverage. About 7 percent of adults aged 55 to 64 purchased private nongroup insurance in 2004 and did not receive employment-based benefits. Relying upon the private nongroup market at older ages has drawbacks, including the high price of coverage (especially for those in less-than-perfect health), the limited benefits provided by many plans, and the possibility that coverage may be denied. Before age 65, adults without dependent children (and those who are not pregnant) can qualify for Medicare or Medicaid only if they are blind or

FIGURE 2. MEDIAN ANNUAL HEALTH CARE COSTS, BY AGE, 2004

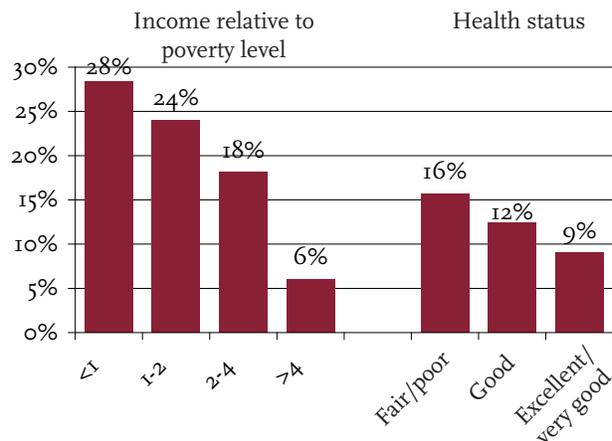


Source: Author's estimates from Agency for Health Care Research and Quality (2007).

disabled. Medicaid benefits are also subject to strict income and asset tests. In 2004, about 8 percent of adults aged 55 to 64 received Medicaid or Medicare coverage and another 2 percent received military health benefits.

The overall uninsured rate is not particularly high at older ages. About 12 percent of adults aged 55 to 64 lacked health insurance in 2004. By contrast, about 15 percent of adults aged 45 to 54 and 19 percent of adults aged 35 to 44 lacked coverage.³ However, lack of coverage creates special difficulties at older ages, because older adults are more likely than younger adults to develop health problems and need expensive medical care. In fact, median health care expenditures in 2004 were almost four times as high at ages 55 to 64 than at ages 35 to 44 (see Figure 2).⁴

FIGURE 3. PERCENT OF ADULTS AGED 55 TO 64 WITHOUT HEALTH INSURANCE, BY INCOME AND HEALTH STATUS, 2004



Source: Author's estimates from University of Michigan (2005).

Uninsured rates are relatively steep among older people with limited incomes and health problems, groups arguably in greatest need of health insurance. For example, 28 percent of adults aged 55 to 64 with incomes below the federal poverty level lacked insurance in 2004, compared with 6 percent of those with incomes in excess of four times the poverty level (see Figure 3). Whereas 16 percent of those in fair or poor health were uninsured, only 9 percent of those in excellent or very good health lacked coverage.

RETIREE COVERAGE

Health insurance coverage at older ages varies by work status. In 2004, 49 percent of adults aged 55 to 64 worked full time (35 or more hours per week) and 13 percent worked part time. The remaining 38 percent that did not work were fairly evenly split between those who described themselves as retired, disabled, or homemakers. About 2 percent were unemployed in 2004.

The vast majority of full-time workers aged 55 to 64 received health benefits through the workplace, with nearly three-quarters receiving benefits from their own employers (see Table 1). Most early retirees also received employer health benefits. Nearly half received coverage from their own former employers, and another 21 percent received spousal coverage. There is no evidence that employer coverage has declined among retirees or older workers over the past ten years. In 1994, 66 percent of full-time workers aged 55 to 64 received health benefits from their own employers and 46 percent of retirees received benefits from their own former employers.⁵

TABLE 1. HEALTH INSURANCE COVERAGE BY WORK STATUS FOR ADULTS AGED 55 TO 64, 2004

Coverage source	Workers		Nonworkers		
	Full-time	Part-time	Retired	Disabled	Other
Own employer	72%	40%	49%	13%	9%
Spouse's employer	13	29	21	15	45
Private nongroup	4	10	9	7	11
Medicaid, Medicare, military	2	6	11	59	9
Uninsured	9	15	10	7	25

Note: Retired and disabled status is based on how respondents describe themselves. Columns do not always sum to 100 due to rounding. See endnote 2 for more details. Source: Author's estimates from University of Michigan (2005).

The 2004 uninsured rate was nearly identical for retirees and full-time workers aged 55 to 64. The uninsured rate was higher for part-time workers and nonworkers who were neither retired or disabled.

Relatively few workers lose employer health benefits when they retire early. About two-thirds of full-time workers aged 53 to 63 in 1994 with employer health benefits who later retired before age 65 re-

tained their employer coverage when they retired (see Table 2). Another 11 percent obtained coverage from their spouse's employer, 8 percent purchased private non-group insurance, and 5 percent obtained public benefits. Only one in ten became uninsured.

TABLE 2. HEALTH INSURANCE COVERAGE IN FIRST YEAR OF RETIREMENT FOR ADULTS WHO HAD EMPLOYER HEALTH BENEFITS WHEN WORKING

Coverage source	Age at retirement	
	Under 65 ^a	65 and over ^b
Own employer	66%	34%
Spouse's employer	11	5
Private nongroup	8	27
Medicaid or military	3	4
Medicare only	2	29
Uninsured	10	1
	100	100

^a The estimates were restricted to adults aged 53 to 63 who were working full-time in 1994 and who retired by 2004. See endnote 2 for more details.

^b Except for the uninsured, nearly all retirees ages 65 and older have Medicare coverage in addition to the supplemental coverage listed in the table.

Source: Author's estimates from University of Michigan (1995-2005).

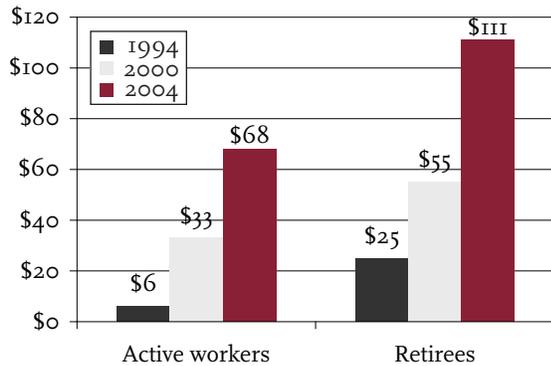
However, people who did not retire until after age 65 were more likely than early retirees to lose their employer coverage, because people without access to retiree health benefits tend to delay retirement until they qualify for Medicare.⁶ Among late retirees who received employer health benefits, 34 percent received employer benefits that supplemented their Medicare benefits, 5 percent received supplemental benefits from their spouses' employers, and 27 percent purchased supplemental Medigap coverage from private insurers.

PARTICIPANTS' COSTS FOR RETIREE COVERAGE

Most employers force retirees to shoulder some of the increased cost of providing health benefits. The premium contributions that most firms now require from both employed and retired health plan participants have been rising rapidly in recent years.

Between 1994 and 2004, median contributions more than quadrupled — after adjusting for inflation — for adults aged 55 to 63 enrolled in health plans offered by their former employers (see Figure 4). The

FIGURE 4. MEDIAN MONTHLY CONTRIBUTIONS FOR EMPLOYER HEALTH INSURANCE BY ADULTS AGED 55-63, BY WORK STATUS, 1994, 2000, AND 2004 (2004 DOLLARS)



Note: The University of Michigan's *Health and Retirement Study* did not interview 64-year-old respondents in 1994. Source: Author's estimates from University of Michigan (1995-2005).

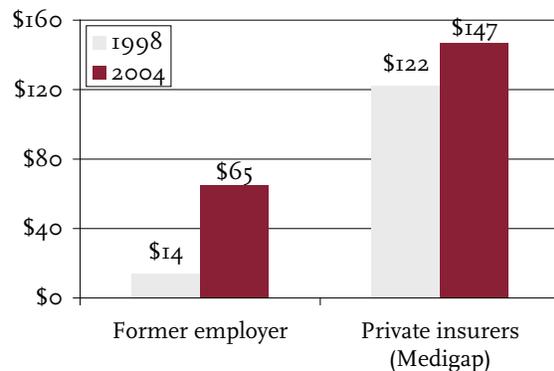
median monthly contribution was \$111 in 2004, up from \$25 in 1994 (expressed in constant 2004 dollars). Over the course of an entire year, the increase in required contributions between 1994 and 2004 for the median retiree too young to qualify for Medicare exceeded \$1,000 in inflation-adjusted dollars. Nonetheless, most people with retiree health benefits continue to pay much less for their coverage than those who purchase insurance in the private nongroup market, where employer subsidies are unavailable. The median monthly premium paid in 2004 by adults aged 55 to 63 with private nongroup insurance totaled \$278.

Required contributions for active workers aged 55 to 63 in employer health plans have also been rising rapidly, but active workers contribute only about half as much as retirees toward their health plans. In 2004, the median active worker with employer coverage paid \$68 per month for benefits, up from \$6 in 1994 (in constant 2004 dollars).

Retiree health benefits after age 65 supplement Medicare, covering part of Medicare's deductibles and copayments and filling some of the gaps in the Medicare benefits package. For example, before Medicare began covering prescription drugs in 2006, virtually all employer-sponsored retiree health plans offered drug benefits.⁷ Medicare-eligible retirees generally pay much less for their employer health benefits than younger retirees, because Medicare covers many of their medical expenses.

However, premium contributions for retirees older than 65 with employer coverage have been soaring in recent years. Between 1998 and 2004, median monthly premium contributions to employer health plans by Medicare beneficiaries ages 65 and older more than quadrupled in inflation-adjusted dollars, increasing from \$14 to \$65 (see Figure 5). On an annual basis, after adjusting for inflation, the median-aged Medicare beneficiary paid about \$600 more for health benefits from their own former employers in 2004 than they did in 1998. Nonetheless, the premium contributions by Medicare-eligible retirees with employer benefits lagged well behind those paid by their peers who bought Medigap coverage from private insurers to supplement Medicare. In 2004, the median monthly Medigap premium totaled \$147 for covered adults aged 65 and older.

FIGURE 5. MEDIAN MONTHLY CONTRIBUTIONS FOR SUPPLEMENTAL HEALTH INSURANCE BY ADULTS AGED 65 AND OLDER, BY COVERAGE SOURCE, 1998 AND 2004 (2004 DOLLARS)

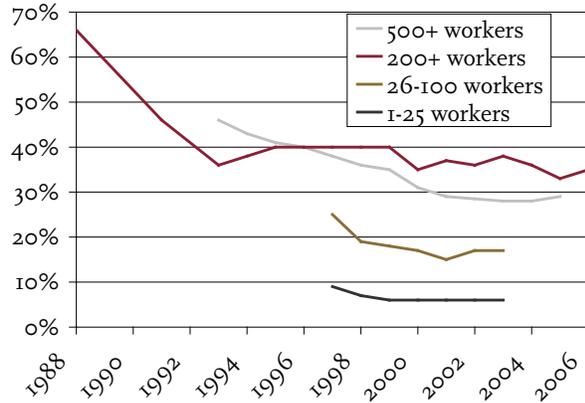


Source: Author's estimates from University of Michigan (1999-2005).

TRENDS IN EMPLOYERS OFFERING RETIREE BENEFITS

Retiree health insurance offers dropped sharply about fifteen years ago. The share of private firms with 200 or more employees providing retiree health insurance fell from 66 percent in 1988 to 36 percent in 1993 (see Figure 6). Most analysts attribute this decline to a 1993 accounting rule requiring employers to recognize expected future retiree health care costs as liabilities on their balance sheets.⁸

FIGURE 6. PERCENT OF PRIVATE SECTOR EMPLOYERS OFFERING RETIREE HEALTH BENEFITS, BY FIRM SIZE, 1988 TO 2006



Note: The estimates for 500 or more workers refer only to offers for early retirees.
 Source: Mercer (2006) for 500 or more workers; Kaiser Family Foundation and Health Research and Educational Trust (2006) for 200 or more workers; Buchmueller, Johnson, and Lo Sasso (2006) for 1 to 100 workers.

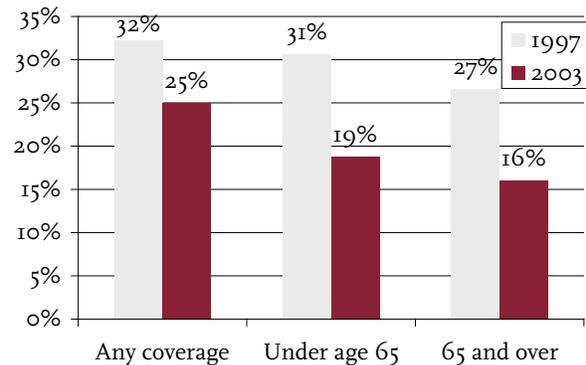
Observed trends since 1993 in the share of private employers offering retiree health insurance vary by firm size and the data source. Data from Mercer Human Resources Consulting indicate that the share of employers with 500 or more workers offering health benefits to early retirees declined from 46 percent in 1993 to 29 percent in 2001 but remained roughly constant through 2005. Employer surveys by firms KPMG and then the Health Research and Educational Trust, in partnership with the Henry J. Kaiser Family Foundation, show that between 1993 and 2006, the share of private firms with 200 or more employees providing retiree health insurance fluctuated between 40 percent and 35 percent (except for a dip in 2005). Offer rates are much lower among smaller firms. Between 1997 and 2003, the share of private firms employing between 26 and 100 workers that offered retiree health benefits declined from 25 percent to 17 percent. Over the same period, offer rates among private firms employing fewer than 26 workers remained fairly constant, with about 6 percent offering coverage in 2003.

The share of employers offering benefits does not shed much light on workers' future retirement security, because these estimates give as much weight to an establishment employing a handful of workers as to one employing thousands. The variation in retiree health insurance offers by firm size makes simple establishment-level estimates especially problematic.

Figure 7 shows the share of private sector workers at firms offering retiree health benefits, based on estimates from a large survey of employers weighted by number of employees.⁹ In 1997 about 32 percent of private sector workers were employed at establishments offering retiree health benefits. By 2003 this figure was down to 25 percent. Expressed in levels, this change means that the number of private sector workers with access to retiree health benefits fell by about 6.4 million. Employers are slightly more likely to offer coverage for retirees younger than age 65 than for those who qualify for Medicare.

Evidence of substantial declines in retiree health benefits in the private sector stand in sharp contrast to the situation in the public sector, which employs about 16 percent of the workforce.¹⁰ The federal government continues to offer health benefits to its retirees, as do 82 percent of state and local governments employing 200 or more workers in 2006.¹¹ However, retiree health benefits for public sector workers are also under pressure. Like private employers, public employers face rising health care costs and an aging workforce. Although a recent study found no re-trenchment in retiree health benefits for government workers in the early 2000s,¹² a change in government accounting rules, to take effect in 2006 and 2007, will require state and local governments to recognize the expected future health care costs promised to current and future retirees as a long-term liability. It is impossible to predict the impact of this change on public sector retiree health benefits, but government failure to address these liabilities could reduce state and municipal credit ratings, raising borrowing costs.

FIGURE 7. PERCENT OF PRIVATE SECTOR WORKERS AT FIRMS OFFERING RETIREE HEALTH BENEFITS, BY COVERED AGE GROUP, 1997 AND 2003



Source: Buchmueller, Johnson, and Lo Sasso (2006).

CONCLUSION

Although millions of older Americans still rely on retiree health benefits from former employers to help pay their medical expenses, coverage appears to be slowly disappearing, possibly jeopardizing retirement security for future generations. As health care costs rise, the workforce ages, and global competition intensifies, many employers seem to be concluding that they can no longer afford to offer subsidized health insurance to retirees. In just the past year, several large companies, including GM, Ford, Chrysler, Nissan, Verizon, and Sears, announced cuts in retiree health benefits for future retirees. Employers who continue to offer retiree health benefits have been sharply raising the premium contributions they require from plan participants.

The creation of a Medicare drug benefit adds to uncertainty over the future course of retiree health benefits. Medicare provides an incentive to employers to continue retiree drug coverage, by paying 28 percent of the annual drug costs incurred per retiree between \$250 and \$5,000. Only 8 percent of large employers that offered retiree drug benefits and responded to a recent survey dropped coverage in 2006, although more employers may choose to do so in later years.¹³ A recent Congressional Budget Office analysis predicted that many employers would drop their retiree health plans following the introduction of the Medicare drug benefit, causing 17 percent of all Medicare beneficiaries to lose retiree health benefits.¹⁴

The erosion in retiree health benefits among private sector workers is part of a larger trend that threatens retirement security. In addition to cutting retiree health benefits, many employers have replaced traditional defined benefit pension plans, which promise a federally guaranteed lifetime benefit based on earnings and years of service, with defined contribution retirement plans. Retirement benefits from defined contribution plans typically depend on uncertain investment returns, and participants must generally make regular contributions throughout their careers. Additionally, Social Security is scheduled to replace a smaller share of pre-retirement earnings for future retirees as the retirement age for full benefits rises. And long-term fiscal imbalances may soon lead to Medicare cutbacks and further cutbacks in Social Security. Even if these programs are not cut, and retiree health plans continue at their current levels of generosity, rising health care costs will force future generations of retirees to devote ever increasing shares of their incomes to health care.¹⁵

ENDNOTES

1 These estimates were based on data from the 2004 *Health and Retirement Study* (HRS), a nationally representative survey of adults ages 51 and older. The survey was conducted by the University of Michigan with primary funding from the National Institute on Aging.

2 Coverage was determined by the following hierarchy: own current employer, own former employer, spouse's current employer, spouse's former employer, military benefits, private nongroup, Medicaid, and Medicare.

3 U.S. Census Bureau (2006). These estimates were based on data from the Census Bureau's *Current Population Survey*.

4 Author's estimates from the *Medical Expenditure Panel Survey*. For more information, see Agency for Healthcare Research and Quality (2006).

5 Johnson (2006).

6 See, for example, Johnson, Davidoff, and Perese (2003) and Rogowski and Karoly (2000).

7 Laschober (2004).

8 General Accounting Office (1998).

9 Data came from the *Medical Expenditure Panel Survey* Instrument Component (MEPC-IC), a nationally representative annual survey of about 25,000 establishments.

10 Bureau of Labor Statistics (2006).

11 Kaiser Family Foundation and Health Research and Educational Trust (2006).

12 Hurley et al. (2006).

13 Kaiser Family Foundation and Hewitt Associates (2006).

14 Congressional Budget Office (2004).

15 Johnson and Penner (2004).

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