Client Alert

Medicare Prescription Drug Benefit Subsidiary Application Deadline Extended to October 31; Creditable Coverage Notice Deadline Remains November 15

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Executive Compensation & Benefits

Medicare Part D prescription drug coverage will become available to individuals enrolled in Medicare on January 1, 2006. If any of the participants or applicants to an employer-provided health plan that covers 20 or more participants are eligible for Medicare Part D coverage, the employer must determine whether the prescription drug coverage it provides is "creditable" or not, and notify all Medicare Part D-eligible plan participants and plan applicants of that fact before November 15, 2005. Coverage is creditable if it is equivalent to the prescription drug coverage offered under Medicare Part D. Employers who continue to provide creditable coverage to Medicare Part D-eligible participants may be eligible to receive a 28% subsidy from the government. The subsidy application deadline for plan years ending in 2006 was previously set at September 30, 2005 but has been extended to October 31, 2005. Employers do not have to take any action to apply for the extension.

The creditable coverage notice must be provided regardless of whether the recipient intends to enroll for Medicare Part D benefits, and regardless of whether the employer intends to take advantage of the subsidy. As a result, most health plan sponsors will be required to provide this notice.

Background

Medicare Part D prescription drug coverage (Part D) was added to Medicare by the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (MMA). The Part D benefit covers outpatient prescription drugs, including insulin and associated medical supplies and certain biological products, but does not include over-the-counter drugs. Part D also excludes prescription drugs covered under Medicare Part A (hospital charges) and Part B (physician charges).

Under the MMA, employers providing health coverage have several options for offering prescription drug coverage to their Part D-eligible participants, including dropping health coverage completely in light of the availability of Medicare Part D coverage; providing coverage that "wraps around" the Medicare benefit; contracting with a national or regional prescription drug plan or creating their own;

Pillsbury Winthrop Shaw Pittman LLP

Vol. 1100, No. 1113

Client Alert

or continuing their current health coverage plans. Employers who choose to continue providing creditable coverage may apply for a federal subsidy for each Part D-eligible participant who does not enroll in a Part D plan but elects instead to receive equivalent benefits under an employer-provided plan. The benefit of this arrangement is that employers may retain flexibility in structuring their benefits packages without financing the prescription drug coverage portion that is equivalent to the Medicare Part D benefit, and participants who become Part D-eligible may keep the drug coverage that they already have.

Medicare Eligibility and Enrollment

Individuals are eligible for Medicare if they are age 65 or older, disabled or have end-stage renal disease. To be eligible for Part D benefits, individuals must be entitled to Medicare Part A and/or enrolled in Part B as of the effective date of coverage under the Part D plan, and they must reside within the service areas of a participating plan. Entitlement to Part A means more than eligibility: an application for benefits under Part A must have been filed by an individual, or the individual must be receiving social security benefits, for him or her to be deemed entitled.

As with Medicare Part B, there is an enrollment deadline for individuals who whish to apply for coverage under Part D. The initial enrollment period for Part D benefits is from November 15, 2005, through May 15, 2006. Individuals who enroll within this period will pay the lowest premium for the Medicare prescription drug plan of their choosing. If an individual's initial enrollment period for Part B benefits extends beyond May 15, 2006, his or her Part D initial enrollment period runs concurrently. (The Part B initial enrollment period is the period beginning 3 months before an individual first becomes eligible for Part B benefits and extends for 3 months after the month in which eligibility occurs, for a total of 7 months.)

If an individual enrolls in Part D after the initial open enrollment period, and has had a gap in creditable coverage for a continuous period of 63 days or more thereafter (i.e., the individual had no coverage or had non-creditable coverage for at least a 63-day period following the expiration of the Part D initial enrollment period), he or she may incur a late enrollment penalty of a 1% premium increase for each month spent without creditable coverage that has elapsed since the close of the initial enrollment period. Thus, Part D-eligible individuals who are covered under a plan that provides no prescription drug coverage or non-creditable prescription drug coverage will need to enroll in a Part D plan during the initial enrollment period to avoid paying a late enrollment penalty for enrollment for Part D benefits subsequent to the expiration of the initial enrollment period. Part D-eligible individuals who are covered under a plan offering creditable coverage, however, will not pay a penalty if they choose to enroll in Part D at a later date.

"Creditable Coverage" for Purposes of Providing Notice

Employer-provided retiree health coverage is considered creditable coverage if it is at least equal to the value of coverage that the same participants would receive under Part D. This is determined under a gross value test which measures the expected amount of paid claims under a plan's prescription drug benefit and compares it with the expected amount of paid claims under the standard Medicare prescription drug benefit.

Pillsbury Winthrop Shaw Pittman LLP

Vol. 1100, No. 1113

Client Alert

A determination that prescription drug coverage under an employer health plan qualifies as creditable coverage can also be made if the plan in question provides coverage for brand and generic prescriptions; provides reasonable access to retail providers and, optionally, for mail order coverage; is designed to pay on average at least 60% of participants' prescription drug expenses; and (i) has no annual benefit maximum or a maximum annual benefit of at least $25,000 and an actuarial expectation that the play will pay at least $2,000 per Medicare-eligible individual in 2006, if the prescription drug coverage is not integrated with other benefits, or (ii) has no more than a $250 deductible per year with no annual benefit maximum or a maximum annual benefit payable by the plan of at least $25,000 and no less than a $1,000,000 lifetime combined benefit maximum, if the prescription drug coverage is provided under an integrated plan.

According to the Centers for Medicare & Medicaid Services (CMS), coverage under a health flexible spending account (FSA), health savings account (HSA) or Archer medical savings account (MSA) generally is not taken into account in determining whether an individual is receiving creditable coverage and plan sponsors are not required to send creditable coverage notices regarding these arrangements.

"Creditable Coverage" for Subsidy Application

With respect to applying for the subsidy, however, a two-prong analysis of the prescription drug coverage provided under each benefit option of an employer health plan is necessary; this analysis is referred to as the "actuarial equivalence" test. A qualified actuary must perform the analysis and sign an attestation to actuarial equivalence which is to be submitted with the subsidy application materials.

The first prong of the test is the gross value test, which is performed by comparing the expected amount of paid claims under a plan's prescription drug benefit with the expected amount of paid claims under the standard Medicare prescription drug benefit. The second prong measures net value by taking into account the employer's actual contribution toward the plan's provided prescription drug benefit. The net value is the expected amount of paid claims under the plan's coverage minus the expected premium paid by participants. This net value must be at least equal to the net value of the Part D standard drug benefit for a sponsoring employer to qualify for the subsidy.

Employers who do not qualify for the subsidy may choose to make changes to their benefit in order to qualify for the subsidy.

According to the CMS, coverage under a health FSA, HSA or Archer MSA generally is not taken into account in determining whether an individual is receiving creditable coverage for purposes of the employer subsidy.

Subsidy Benefit

The government subsidy is equal to 28% of each qualifying participant's actually incurred gross prescription drug costs (including dispensing fees but not including administrative costs) between $250 and $5,000. Qualifying participants are those who are eligible for the Part D benefit but choose to receive creditable coverage under an employer-provided plan instead. The subsidy payments are tax-exempt,

Pillsbury Winthrop Shaw Pittman LLP

Vol. 1100, No. 1113

Client Alert

and, according to the CMS, the subsidy benefit is valued at $668 per beneficiary. Thus, the pre-tax value of $668 equals to about $891 of taxable income for employers with a marginal tax rate of 25% and about $1,028 of taxable income for employers with a marginal tax rate of 35%.

Applying for the Subsidy

Employers who wish to receive the subsidy in 2006 must submit an application to CMS by October 31, 2005. Applications may only be made on-line, at the Retiree Drug Subsidy Program site. Employers will be required to submit the actuarial attestations of equivalence mentioned above, in addition to information for each qualifying participant for whom the employer will claim the subsidy. Employers will not be eligible for a subsidy for participants whose information is not included with the subsidy application. Participant information required to be submitted includes the participant's Social Security number or Health Insurance Claim number, full name, gender, date of birth, and relationship to the retiree/disabled participant. Beginning in 2006, participant files must be updated monthly to CMS. CMS compares this information to identify people who are enrolled in both a Part D plan and an employer-provided health plan; employers will not be able to receive a subsidy for such participants.

Because most employers administer their prescription drug benefit through outside contractors, these vendors may be best positioned to provide this data. Therefore, employers should investigate whether their vendors have the capacity to perform this function and whether additional fees will apply.

Employers may file for and subsequently receive the subsidy in monthly, quarterly or annual installments, but applications must be submitted at least annually in order for the subsidy benefit to apply.

Content of Notice

Employers with at least 20 participants in a health plan must provide notice of creditable coverage to Part D-eligible participants and Part D-eligible plan applicants before November 15, 2005. An annual notice of creditable coverage is also required to be provided to CMS, but CMS has not yet released guidance on this notice.

Model notices for creditable coverage and non-creditable coverage are available at Centers for Medicare & Medicaid Services These sample notices are for use with the initial enrollment period only: CMS will provide model notices for new plan enrollees at a later date.

Employers drafting their own notices to Part D-eligible participants are required to state whether the prescription drug coverage they provide is creditable or non-creditable and define what creditable coverage or non-creditable coverage means. They must include a statement describing the ramifications of non-creditable coverage with respect to incurring premium penalties after the initial enrollment period of November 15, 2005, through May 15, 2006, and explain that, even though coverage may be creditable, a late enrollment penalty may still be imposed if there is a subsequent break in creditable coverage of 63 days or more before enrolling in a Part D plan.

Pillsbury Winthrop Shaw Pittman LLP

Vol. 1100, No. 1113

Client Alert

Information should also be included on a Part D-eligible participant's rights to receive notice of creditable coverage, the coverage options available to a Part D-eligible participant, integrated benefits, if any, that they will still be eligible to receive under the plan even if they enroll in Part D, and information on how to obtain financial assistance for a Medicare prescription drug plan, including the contact information for the Social Security Administration.

Form of Notice

Employers have some flexibility in the form and manner of giving notice to Part D-eligible participants. Notice may be sent by a third party. Notice need not be sent in a separate mailing from other plan participant materials, including enrollment materials, but if it is included with other participant information, it must be prominent and conspicuous. This means that notice statements must be in at least 14-point font in a separate box, bolded or offset on the first page of the plan participant information being provided.

For example:

If you have Medicare or will become eligible for Medicare in the next 12 months, a new Federal law gives you more choices about your prescription drug coverage, starting in 2006. Please see page __ for more details.

A single notice may be provided to the covered Part D-eligible participant and the participant's covered dependents, unless it is known that any covered Part D-eligible spouse or dependent resides at a different address. Notice may be provided electronically if a Part D- eligible participant has indicated that he or she has adequate access to electronic media and sends his or her consent electronically (participants must also be informed of their rights to obtain a hard copy and to withdraw consent). If notice is sent electronically, it must also be posted on the home page of the employer's website, if one exists.

Timing of Notice

Notice must be given to Part D-eligible individuals at the following times:

1. Prior to the Part D Annual Coordinated Election Period (November 15 through December 31 of each year);
2. Prior to an individual's initial enrollment period for Part D;
3. Prior to the effective date of coverage for any Part D-eligible individual that joins the plan;
4. Whenever prescription drug coverage ends or changed so that it is no longer creditable or it becomes creditable; and
5. Upon a Part D-eligible participant's request.

Employers will meet the notice timing requirements under 1. and 2. if notice is distributed to all plan participants. The timing requirement under 3. will be met if notice is included with new hire and enrollment materials.

Pillsbury Winthrop Shaw Pittman LLP

Vol. 1100, No. 1113

Client Alert

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Live Links

Retiree Drug Subsidy Program

Centers for Medicare & Medicaid Services, Model Notice for Creditable Coverage

Centers for Medicare & Medicaid Services, Model Notice for Non-Creditable Coverage

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Vol. 1100, No. 1113