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Saving Retiree Health Plans

By ELLEN E. SCHULTZ

More companies in dire financial straits are pulling the plug on retiree health-care benefits—dealing a blow to everyone from hourly union employees to upper management.

Eastman Kodak and Hostess Brands, both of which filed for Chapter 11 bankruptcy this month, are expected to ask the courts to let them kill their plans, following in the footsteps of bankruptcies at American Airlines parent AMR Corp., Harry & David, the mail-order food retailer owned by private-equity firm Wasserstein & Co., and scores of auto-parts companies, steelmakers and others.


Keith Negley

Bankruptcy judges usually let companies terminate such plans, figuring the move will make it more likely that creditors will be paid and that the company's chances of turning itself around will be enhanced if it can shed millions or even billions of dollars in retiree obligations at the stroke of a pen. Retirees, who are unsecured creditors, always are vulnerable.

But loss of coverage can devastate retirees who might not be able to obtain, or afford, coverage in the open market, especially involuntary early retirees who are years away from collecting Medicare benefits and might be one heart attack or bout of cancer away from financial ruin.

Still, retirees of companies in bankruptcy protection have an option unavailable to retirees of companies that are healthy but eliminate retiree health coverage anyway: the Health Coverage Tax Credit, or HCTC, a federally funded program administered by the Internal Revenue Service.

The credit pays a portion—currently 72.5%—of health-insurance premiums for retirees whose benefits have been reduced or eliminated in bankruptcy proceedings and whose pensions are taken over by the Pension Benefit Guaranty Corp., the federal insurer that assumes control of failed plans and pays the benefits.

The program will pay for comprehensive major medical coverage, including prescription drugs and dental and vision care, if they are included in that coverage.

People can elect to pay 27.5% of their monthly premium to the HCTC program, which will then send the full payment to the insurer. Or they can pay their health insurer directly each month and claim a credit on their federal tax return for the 72.5%.

To be eligible for the subsidy, you must be receiving a pension from the Pension Benefit Guaranty Corp. You also must be 55 to 64 years old and enrolled in a qualified health plan (provided you are paying more than 50% of the costs). That includes Cobra, which requires your former employer to continue offering job-based health coverage to you if you lose your job.

In 2009, Congress expanded HCTC coverage to include benefits sponsored by Voluntary Employee Benefits Associations, or VEBAs, which are trust funds established during the bankruptcy process to provide retiree health benefits. Such large-scale associations have since been set up to cover retirees of some bankrupt companies, including Delta Air Lines and General Motors' floundering auto-parts spinoff, Delphi. These post-bankruptcy arrangements cover both union and salaried retirees, including management.

Roughly 7,000 participants in the Delphi VEBA pay $150 to $200 a month in premiums per person, for example, with a $250 deductible and total out-of-pocket expenses capped at $1,200. American Airlines retirees have recently formed a committee that will likely explore setting up a VEBA if their coverage is terminated, and retirees of another major airline is in the planning stages of setting up such a plan.

In a little-noticed move last October, a New York bankruptcy court judge approved the creation of the first industrywide VEBA, which will provide benefits to retirees of failed auto-parts manufacturers based in Ohio, Michigan and Wisconsin.

Retirees in the auto and steel industries are planning to roll out VEBAs in March and April, says Cathy Cone, managing partner of Cone Insurance Group, a Houston-based insurance broker that helps set up the plans.

The Health Care Tax Credit was set to expire at the end of 2010, but it was extended and expanded from 65% to 72.5%, with the increase retroactive to Feb. 13, 2011, after retiree groups and unions lobbied vigorously.

The tax credit is authorized through 2013, but there is likely to be strong pressure to reauthorize it—and not just from retirees and unions. Insurers, which have been developing products and services financed by the taxpayer subsidy, will push vigorously to keep it alive, though there isn't a guarantee it will happen.

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