THE COMMITTEE ON ENERGY AND COMMERCE
INTERNAL MEMORANDUM

April 27, 2010

To: Ranking Members Joe Barton and Michael Burgess

Fr: Committee on Energy and Commerce Minority Staff

Re: Investigation of AT&T, Caterpillar, Deere & Company, and Verizon By Majority

On April 14, 2010 the Chairman of the House Committee on Energy and Commerce and Chairman of the Subcommittee on Oversight and Investigations cancelled an investigation of large employers after a preliminary investigation by the Majority Committee staff indicated that AT&T, Caterpillar, Deere & Company, and Verizon had "acted properly and in accordance with accounting standards" in reporting substantial cost increases to their retiree prescription drug coverage programs. The April 14, 2010 Majority Committee staff memorandum concluded that the impact of the health care law on large employers "could be beneficial" and "will require continued oversight." The Minority Committee staff has reviewed the documents provided by these companies in response to the March 26, 2010 document request from the Chairman and Subcommittee Chairman.

The preliminary Minority Committee staff investigation indicates:

(1) Each of the large employers under investigation warned that the health care legislation under consideration would trigger reporting requirements months before passage of the bill.

(2) Internal company documents from each large employer under investigation reflect concerns over the health care legislation's new taxes and effect on costs.

(3) Internal company documents indicate that there will be an incentive to drop employer health care coverage because the cost of providing coverage will be much larger than the penalty imposed by the health care legislation.

I. Company Filings Were Not Only Proper But Had Been Forecast

The April 14, 2010 Majority Committee staff memorandum indicated that the filings were proper. Documents provided by the investigated companies show that both the companies and other groups anticipated these filings if the health care legislation became law.

On November 2, 2009 the American Benefits Council and the AFL-CIO wrote a letter to House Speaker Nancy Pelosi, warning that ending the tax exclusion provided "to employers who continue to provide prescription drug coverage to their retirees…could well lead to an unintended and precipitous decline in some of the most comprehensive health coverage protection for retirees available today."[1] The letter went on to state:

> Finally, Congress has not considered at all the negative impact, required under Financial Accounting Standard 106, on the financial statements of companies that currently provide retiree health coverage...[A]ccounting rules dictate that immediately upon being signed into law, these provisions would substantially increase the FAS 106 liability for the very companies providing the most comprehensive coverage to current and future retirees. In the current economic environment, this would be particularly ill-advised and disruptive.[2]

As required, after the health care bill became law, AT&T, Caterpillar, Deere & Company, and Verizon all issued notifications about the negative impact the law would have on their retiree prescription drug programs.

All four investigated companies had signed letters stating this would happen*:*

> -Executives from Caterpillar, Deere & Company, and Verizon wrote "this change would result in large earnings statements reductions due to U.S. GAAP income tax accounting rules, which would require employers to immediately account for the present value of this tax increase."[3]
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> -The Chairmen and CEOs of AT&T and Verizon wrote "[A]ccounting rules dictate that, immediately upon the signing of the health reform legislation, employers would have to recognize, on their books, the long-term impact of the new tax liability."[4]

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[1] Letter from Diann Howland, Vice President of Legislative Affairs for the American Benefits Council, and William Samuel, Director of the Department of Legislation for AFL-CIO, to the Honorable Nancy Pelosi, Speaker of the United States House of Representatives (Nov. 2, 2009) (AT&T-EC-00010).
[2] *Id.*
[3] Letter from Business Executives to the Honorable Harry Reid, Majority Leader of the United States Senate, and the Honorable Nancy Pelosi, Speaker of the United States House of Representatives (Dec. 11, 2009) (VZ-HEC 00113).
[4] Letter from Larry Cohen, President of the Communications Workers of America, Ivan Seidenberg, Chairman and CEO of Verizon, Edwin Hill, President of the International Brotherhood of Electrical Workers, and Randall Stephenson, Chairman and CEO of AT&T to the Honorable Harry Reid, Majority Leader of the United States Senate (Dec. 15, 2009) (VZ-HEC 00110).

-Shortly before passage, Caterpillar wrote again warning about the taxation of “the Medicare Part D subsidy.”[5]

II. Large Employer Documents Show Concerns About Health Care Legislation Increasing Taxes Or The Cost Of Providing Health Care To Employees

The documents provided by AT&T, Caterpillar, Deere & Company, and Verizon demonstrate concerns within each company about the health care legislation raising the cost of providing employees health care.

A Verizon document states that large employers could end up paying for health care legislation changes, as new requirements raise costs, while new taxes and fees are passed through to the employer. Health care coverage expenses “may go up in cost due to shifting of increased taxes/fees from the provider and insurance industries to employers/employees.”[6] Large employers, like Verizon, that offer health care coverage would be required to pay for the “cost of general reform through increased employer taxes…”[7]

Days before the health care bill became law, the Vice President and Chief Human Resources Officer of Caterpillar warned leaders of both parties in the House of Representatives that “if passed the legislation will drive up Caterpillar’s healthcare costs by more than 20 percent (over $100 million) in the first year alone and put at risk the coverage our current employees and retirees receive.”[8] After passage of the bill, this individual would note in an e-mail that the company needed to “modify our plans” and “figure out what this will cost us and collect that in increased premiums which we will attribute to the legislation.”[9] He also noted that “with these additional mandates we will likely have to revisit those premium levels for 2011.”[10] Finally, the health care legislation will both “impact our ability to provide affordable health insurance coverage to our retirees” and will impact the paychecks of some employees where “incentive pay is based on profitability.”[11]

Internal company documents reflect concerns that retiree drug programs will become scarce in the future once the effects of the new tax are felt. Taxing the Medicare Part D Retiree drug subsidy “will cause employers to re-assess their decision to continue

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[5] Letter from Gregory Folley, Chief Human Resources Officer, to the Honorable Nancy Pelosi, Speaker of the United States House of Representatives, and the Honorable John Boehner, Minority Leader of the United States House of Representatives (Mar. 18, 2010) (CAT_WAXMAN_000286).
[6] “Health Care Reform Employer Impact” (Mar. 3, 2010) (VZ-HEC 0006).
[7] “Health Care Reform Employer Impact” (Mar. 3, 2010) (VZ-HEC 0006).
[8] Letter from Gregory Folley, Chief Human Resources Officer, to the Honorable Nancy Pelosi, Speaker of the United States House of Representatives, and the Honorable John Boehner, Minority Leader of the United States House of Representatives (Mar. 18, 2010) (CAT_WAXMAN_000286).
[9] Email from Gregory Folley to Paul Gaeto, (Mar. 23, 2010) (CAT_WAXMAN_000300).
[10] Email from Gregory Folley to Clay Thompson (Mar. 24, 2010) (CAT_WAXMAN_000444).
[11] Email from Greg Folley, Chief Human Resources Officer to Doug Oberhelman (Mar. 3, 2010) (CAT_WAXMAN_00325).

providing prescription drug coverage for Medicare eligible retirees."[12] A Caterpillar document noted that if just one quarter of current retirees receiving prescription drugs from former employers shifted to the government program, then the cost to the government would exceed the savings obtained by removing the tax deduction.[13] An AT&T document noted that while the subsidy they receive is 23% on Medicare retiree drug costs, adding an income tax to the subsidy ultimately reduces it by 38%, or $44 million a year.[14]

The employer documents also indicate there are concerns about increased taxes on high cost plans as well. A Deere & Company document noted that the tax on high cost plans "will have a disparate impact on retirees and bargained employees and will raise the cost of providing health insurance to these groups" before concluding that the tax "will increase our costs and potentially result in lower benefits to retirees and others."[15] An AT&T document estimated that the 10-year cost of an excise tax on plans above benchmark levels could cost the company as much as $125 million.[16]

III. **Large Employer Documents Reflect Awareness It May Be Cheaper To Pay A Penalty**

The documents provided by AT&T, Caterpillar, Deere & Company, and Verizon contain varying examples in which the cost of paying for employee health care is weighed against the cost of paying a government penalty. A Verizon document states that "[t]o avoid additional costs and regulations, employers may consider exiting the employer health market and send employees to the Exchanges."[17] This same document indicates that the penalty assessed employers will not be a deterrent: "Companies that do not offer coverage to their employees…would be required to pay an assessment. Even though the proposed assessments are material, they are modest when compared to the average cost of health care."[18]

The companies involved in this investigation appear aware that ultimately it may become more profitable to pay a penalty as opposed to paying for increasing health care costs. In November of 2009 when the penalty was thought to be a percentage of wages, one Caterpillar employee in the Human Services Division noted that the penalty would be $280 million, while the "current healthcare spend for active employees is $305m." The employee concluded that the company "would need to give serious consideration to this option."[19] Deere & Company even considered this for a shorter time period. Faced with either following their collectively bargained agreement to provide health care after seven months, or the government requirement to provide it sooner, the Vice President of Labor

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[12] Memorandum on "U.S. National Health Care Reform" (Jan. 5, 2010) (DC 00000065).
[13] Caterpillar Slide "Medicare Part D Impact on Cat" (CAT_WAXMAN_000247).
[14] Presentation to the AT&T Board of Directors (Mar. 25, 2010) (AT&T-EC-00008).
[15] Deere & Company Memorandum "U.S. National Health Care Reform" (Jan. 5, 2010) (DC00000065).
[16] AT&T Policy Review of Health Care Reform (AT&T-EC-0001).
[17] "Health Care Reform Employer Impact" (Mar. 3, 2010) (VZ-HEC 0008).
[18] *Id.*
[19] Email from Jerry W. Dugan to Kathryn Himes and Valerie Johnson (Nov. 19, 2009) (CAT_WAXMAN_000360-61).

Relations stated: "…We ought to take a look at an alternative which would amount to denying coverage and just paying the penalty. In this case we would need to figure out which one was more expensive."[20]

These statements indicate that companies will consider dropping their health coverage if costs do not fall and the penalty owed the government is a cheaper alternative. A central issue debated during consideration of the health care bill was whether individuals happy with their health care coverage would be able could keep it. The documents provided by these employers raise questions about the potential for a different health care market in the future for the American worker: "From an employer market perspective, the longer term implications depend on how employers respond to the employer health insurance mandate or paying a penalty…some are predicting the future state is individual coverage on an after-tax basis without employer coverage."[21]

AT&T did not provide any documents showing discussions about pursuing the least expensive option.[22] Yet, the documents AT&T did provide show that the company stands to profit enormously by paying the penalty as opposed to providing health care. In 2009 AT&T paid $4.7 billion in medical costs for active ($2.4 billion) and retired employees ($2.3 billion).[23] If AT&T were to end coverage for active employees and pay the penalty, they would only spend $0.6 billion dollars, a savings of $1.8 billion dollars.[24]

Conclusion

The Majority Committee staff memorandum stated that "continued oversight" is needed as the health care legislation is implemented, and that the impact in the future "could be beneficial" to large employers.[25]

The small number of documents produced raises questions about the future for employer-based health care. Concerns have been raised about whether the health care legislation would change or end workplace insurance benefits, but this is based on a small number of documents from only four major companies. Further investigation is needed on the impact of the health care law on the future of employer-based health plans.

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[20] Email from Kenneth C. Huhn, Vice President of Labor Relations to Carol A. Lewis (Mar. 25, 2010) (DC00000172); Minority staff is aware that there are unique circumstances relating to their collectively bargained union contracts. We highlight this exchange only to show that companies are having a discussion about what is cheaper: paying the government penalty or providing employer based health care.
[21] Deere & Company Document "Healthcare Reform Update" (DC00000060).
[22] AT&T was the only company investigated that did not provide internal e-mail communications.
[23] Presentation to the AT&T Board of Directors (Mar. 25, 2010) (AT&T-EC-00009).
[24] *Id.*
[25] Memorandum to Chairmen Henry A. Waxman and Bart Stupak, "Investigation of the Impact of the Health Care Reform Law on Large Employers" (Apr. 14, 2010).