



AFL-CIO

December 10, 2009

The Honorable Harry Reid
Majority Leader
United States Senate
Washington, D.C. 20510

RE: Proposed Change to the Tax Treatment of Retiree Drug Subsidies

Dear Mr. Leader:

We are writing to express our serious concerns regarding Section 9012 included in the Patient Protection and Affordable Care Act and urge that it be deleted from the version of the legislation brought to the full Senate for consideration.

Including such a provision would only compound the enormous problems that would be posed for workers and employers by the provision that applies an excise tax on health benefits, a provision that both our organizations have protested strongly on multiple occasions.

Section 9012 would cease the current tax excludability of the 28 percent subsidy provided to employers who continue to provide prescription drug coverage to their retirees. If this provision becomes law, it will be highly destabilizing for retirees who rely upon employer sponsored drug coverage, it will impose a dramatic and immediate impact on company financial statements, and it will not raise the estimated federal revenue attributed to this change in tax law.

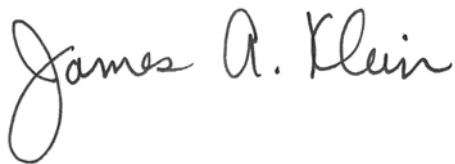
The current tax treatment of the subsidy was included in the Medicare Modernization Act of 2003 precisely to encourage employers to continue sponsoring drug coverage for retirees – not only helping to preserve this important benefit, but also resulting in savings to the federal government by avoiding the necessity of many retirees to obtain Medicare Part D coverage.

It is clear that in drafting Section 9012, the Senate was not aware of, and therefore not able to take into consideration, the significant negative impact, required under Financial Account Standard No. 109, on the financial statements of companies currently providing retiree drug coverage. Regardless of the effective date of the provision, accounting rules dictate that *immediately* upon being signed into law, this deferred tax liability would have to be reflected on company financial statements. This would substantially increase liabilities 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. Moreover, it would compel many employers to cease offering the coverage and require their retirees to obtain coverage through Medicare Part D, at considerably greater cost to the government.

The immediate impact on financial statements, and resulting shift of retirees from employer-sponsored plans to Medicare, is just one reason the \$5.4 billion in federal tax revenue estimated to be raised from this provision is highly unlikely to be realized and, in fact, this proposal is likely to be a revenue *losing* provision. If the tax revenue to be collected is calculated, but the federal outlays to provide the comparable benefit are not appropriately taken into account, then the actual cost to the government is not being accurately considered. Independent calculations show that if as few as 24 percent of retirees are dropped from employer plans and obtain coverage through Medicare Part D, then Section 9012 will be a net revenue losing provision.

Health care reform must be about stabilizing and expanding the employer-sponsored health benefits system. Taxing the drug subsidy will have the opposite effect. Whatever differences the undersigned organizations may have on other aspects of the Patient Protection and Affordable Care Act, on this matter both labor and management are in full agreement. We respectfully urge that Section 9012 be deleted from the legislation under consideration.

Sincerely,



James A. Klein
President
American Benefits Council



William Samuel
Director, Department of Legislation
AFL-CIO