



Health Care Reform and Walmart

What the Free Rider Provision Means to the Country's Largest Employer

Executive Summary

This memo discusses the impact of “free rider” provision on America’s largest private sector employer, Walmart.

As written, this bill will:

- Incentivize the hiring of a largely part-time workforce, and encourage reducing workers’ hours as a way to reduce health care costs.
- Force low-income Walmart employees into high-deductible company-provided insurance.
- Make few, if any, Walmart employees eligible for tax credits to purchase better insurance through the health insurance exchange.
- Continuing dependence of tens of thousands of Walmart workers on federal and state subsidies for Medicaid and Medicare, and encourage Walmart to have even more employees dependent on Medicaid and Medicare.
- Provide little or no incentive for Walmart to provide better care to their employees.

In order for health care reform to be effective for the thousands of Walmart employees across the country, it must include the choice of a public option *and* strong employer responsibility provisions that ensure that large employers like Walmart pay their fair share for their employees’ health insurance.

Background

Walmart Stores, Inc. (Walmart) is the world’s second largest private sector corporation. In the fiscal year ending January 31, 2009 it had annual sales of \$406 billion. It is also the world’s largest private sector employer, with around 2.1 million employees. It operates more than 8,100 stores worldwide, with 4,300 of them in the United States. Walmart employs 1.4 million people in the U.S., making it the second biggest U.S. employer after the federal government.

Summary of Free Rider Provision

The “free rider” provision requires that, if an employer with more than 50 employees has employees who receive a subsidy (i.e., tax credit) for insurance through an exchange, the employer has to pay a penalty that is the *lesser* of:

- The average national tax credit for insurance through exchanges multiplied by the number of *full-time* employees receiving the tax credit; OR
- \$750 times the total number of *full-time* employees of the company.

This means that if an employer has only *part-time* employees receiving tax credits for insurance purchased through the exchange, *the employer pays no penalty*.

To qualify for the tax credit for insurance purchased through the exchange:

- If the employee's income is below 133 percent of the Federal Poverty Level (FPL), the employee qualifies for Medicaid and is ineligible to receive a tax credit for insurance purchased through the exchange. *Hence, if an employer has employees on Medicaid, the company will not pay any penalty for these employees.*
- If the employer offers health insurance that meets the minimum qualification of having an actuarial value of 65%¹, and the employee opts out of it and purchases insurance through the exchange instead, the employee is eligible for the tax credit *only if the lowest-premium plan offered by the employer is unaffordable*. Affordability is based on percentage of income required to be paid in *premiums alone* (not including other forms of cost-sharing such as deductibles and co-pays). The threshold percentage of income that must be paid in premiums for a plan to be deemed unaffordable is 10%.
- If an employee can obtain coverage through a spouse or (for a young employee) a parent, or if the employee is over 65 and therefore qualifies for Medicare, or if the employee has more than one job and can obtain coverage through another job, the employee is ineligible for tax credits and therefore *the employer pays no penalty*.

Flawed Incentives in Free Rider Provision

The free rider provision as described above has several serious flaws, i.e. it creates incentives for employers to institute hiring, scheduling, and pay practices that hurt low income workers. In particular:

- The employer pays a penalty only for *full-time* employees who qualify for tax credits. The definition of full-time employment in the bill is 30 hours per week. This gives an employer the incentive to cut the hours for low income workers who would qualify for credits down to part-time to avoid paying the penalties, instead of offering affordable coverage.
- The employer pays no penalties for employees who are on Medicaid. This gives employers the incentive to cut back employees' wages so that more of them qualify for Medicaid, instead of offering affordable coverage.
 - This provision gives employers the incentive to preferentially hire employees who would be covered under another health care plan. For example, those over 65 who qualify for Medicare, teenagers who are on their parents' health plans, and workers with coverage through a spouse or a second job. It also encourages

¹ Actuarial value is defined as the percentage of health care charges that a plan pays on average. For example, if the average participant in a plan pays 10% of health care charges and the plan pays 90%, the plan has an actuarial value of 90%. For further details see McDevitt, Roland, "Actuarial Value: A Method for Comparing Health Plan Benefits," prepared by Watson Wyatt Worldwide for California Health Care Foundation, October 2008, available at: <http://www.chcf.org/documents/insurance/HealthPlanActuarialValue.pdf>

companies to discriminate against those who would create a health care burden.

For example, a single mother with two children and without any other job.

- Employees do not qualify for tax credits if the employer offers coverage deemed to be affordable based on premiums as a share of income. The employer then has the incentive to offer bare-bones, high deductible, high co-pay coverage with low premiums (as long as the coverage meets the 65% actuarial value threshold). Employees are then forced to choose to accept this coverage, purchase coverage through the exchange without receiving any tax credits, or pay a penalty for being uninsured.

Impact of the Free Rider Provision on Walmart Employees

Walmart currently offers a range of health plans. According to the company, 51.8 percent of employees are insured through company plans.²

The lowest-premium plans offered by Walmart in 2009 are affordable in terms of the premium, but have high deductibles. For example, the lowest-premium family plan has a premium per pay period (two weeks) of \$6.80 and an annual deductible of \$4,000. This amounts to an annual premium expenditure of \$176.80.³

Walmart discloses its average wage for full-time employees as \$11.24 per hour.⁴ The obvious caveat regarding this number is that it is an average, and the lowest (i.e. starting) wage is significantly lower.

An internal memo by a Wal-Mart Vice President⁵ states that full-time Walmart workers in 2005 worked an average of 34 hours a week. While the memo argued for increasing the average hours to spread the fixed cost of health benefits across more hours to enhance cost-efficiency, we do not know if those practices have been implemented. Since we have no way of determining if the average hours of a Walmart employee has changed since 2005, we assume that the average hours have remained at the 34 hours per week level.

We come to the conclusion then that a full-time Walmart worker making the average wage of \$11.24 an hour has a gross annual income of:

$$(\$11.24/\text{hour}) \times (34 \text{ hours/week}) \times (52 \text{ weeks}) = \$19,872.30$$

The calculation assumes that the employee works the full 52 weeks in the year. This assumption has the effect of increasing the annual earnings, and therefore increasing the amount of Federal Poverty Level that the employee's income constitutes, unlike an assumption of fewer than 52 weeks worked.

² "Walmart Health Care Benefits Enrollment Rises, Uninsured Rate Declines," Walmart press release, February 13, 2009, available at: <http://walmartstores.com/FactsNews/NewsRoom/8970.aspx>

³ This information is taken from the guide to annual enrollment that Walmart distributed its employees in September-October 2008 for benefit year 2009. We have just received a copy of the corresponding guide for benefit year 2010, and will repeat our calculations based on the new numbers in the near future.

⁴ "Corporate Facts: Walmart By the Numbers," Walmart fact sheet available for download at: <http://walmartstores.com/FactsNews/FactSheets/>

⁵ "Supplemental Benefits Documentation," confidential internal memo by Susan Chambers (Executive Vice President, People Division), presented at Board of Directors retreat for fiscal year 2006, leaked to the New York Times, available for download at: <http://www.nytimes.com/packages/pdf/business/26walmart.pdf>

Now, assume two different family configurations:

1. A family consisting of two adults with two children, with one or more of the adults a Walmart employee, with annual family income that places the family at *exactly* 133% of the Federal Poverty Level. If a health plan meets the premium affordability criterion of 10% for this family, it will meet the criterion for all other 4-person families with income greater than or equal to 133% of Federal Poverty Level. It is realistic to assume that a family of 4 with 2 earning adults, one of whom is a Walmart employee, could be at 133% of FPL, as discussed below.
2. A family consisting of a single Walmart employee earning the average Walmart wage, with two children. The family income is, therefore, \$19,872.30.

Federal Poverty Level thresholds for the different family configurations were obtained from the Centers for Medicare and Medicaid Services, Department of Health and Human Services website:⁶

1. For the first family configuration, the FPL threshold is \$22,050. The family income under our assumption is 133% of \$22,050, which amounts to \$29,326.50 a year.
2. For the second family configuration, the FPL threshold is \$18,310. The family income of \$19,872.30 is 108.5 percent of the threshold. Note that this is less than 133% of FPL, and that therefore this employee qualifies for Medicaid, and is ineligible to purchase insurance through the exchange. Walmart is therefore not liable to make any “free rider” payments on account of this employee.

The analysis of affordability of coverage obtained through the exchange is therefore performed only for the first family configuration.

The assumption that a family of 4 with 2 earning members, one of whom is a Walmart worker, could be at 133% of FPL is realistic, as stated earlier. Consider a family with a male Walmart worker, and his spouse who does not have a high school degree and has earnings that place her in the bottom decile of full-time women workers without a high school degree. Her weekly income is therefore at most \$252⁷. Assuming 52 weeks worked in a year, her annual income is \$13,104. If the family income is assumed to be 133% of FPL, , which amounts to \$29,326.50 a year for a family of 4, her spouse (who is a Walmart worker) has an annual income of \$16,222.50. Assuming 34 hours worked in a week and 52 weeks worked in a year, this translates into \$9.18 per hour. A detailed analysis of Walmart’s wage distribution for the year 2006 estimated that more than 27% of Walmart workers earned less than \$8/hour⁸. Walmart reported a 2006 average wage of \$10.11/hour, while current average wage is \$11.24/hour – an 11% increase. Assuming that Walmart’s entire wage scale grew by approximately the same percentage, the 2006 wage level of \$8/hour corresponds to a 2009 wage of \$8.89/hour. Hence it is highly plausible that a Walmart worker today could earn wages of \$9.18/hour or lower.

The free rider provision requires that, if an employee is offered health coverage by their employer that meets the 65% actuarial value threshold, but opts out of the coverage and obtains insurance through the exchange instead, the employee is not eligible for tax credits unless the

⁶ <http://www.cms.hhs.gov/MedicaidEligibility/Downloads/POV09Combo.pdf>

⁷ “Highlights of Women’s Earnings in 2008,” Bureau of Labor Statistics, U.S. Department of Labor, Report 1017, July 2009, Table 6, p. 42, available at: <http://www.bls.gov/cps/cpswom2008.pdf>

⁸ Dube, Arindrajit, Dave Graham-Squire, Ken Jacobs, and Stephanie Luce, “Living Wage Policies and Wal-Mart: How a Higher Wage Standard Would Impact Wal-Mart Workers and Shoppers,” UC Berkeley Center for Labor Research and Education Research Brief, December 2007, Table A1.

cheapest employer health care offering has premium expenses of at least 10% of the employee's income.⁹

The actuarial value of three specific Walmart health plan offerings, including the cheapest plan discussed above, were estimated by Segal Co., a consultant for the UFCW health and welfare and pension funds¹⁰. The estimates used the known deductibles, co-insurance, and out-of-pocket maximums of the plans.

The calculations by Segal Co. showed that all three plans analyzed, including the cheapest Walmart plan, met the actuarial value floor of 65%. Therefore, the affordability comparison can be made using this plan.

For a family of four, the FPL is \$22,050. The Medicaid threshold of 133% of FPL is therefore \$29,326.50. Applying the premium expense cap of 10 percent of income, we obtain a maximum annual premium expenditure of \$2,932.65, which is well above the actual employee premium expenditure for Walmart's lowest premium plan (\$176.80/year). Therefore, Walmart is not liable for any penalty payments if this family chooses to reject the coverage offered by Walmart and obtain health insurance through the exchange instead.

However, if we examine the total health care expenditures incurred by this family before Walmart's plan starts making payments (not including a "health care credit" of \$100 which effectively means that the first \$100 worth of care for the family is covered), they have to pay \$4,000, plus \$176.80 in annual premium, after which the plan will pay 80 percent of costs for doctor visits, hospital inpatient services, and preventive care (for in-network providers). Thus, the family has to pay a minimum of \$4,176.80 before Walmart's plan pays anything beyond the first \$100 of services.

For a family of four with family income at 133% of FPL, \$4,176.80 amounts to 14% of income. Thus, a Walmart worker's family could pay as much as 14% of their income in health care costs before the Walmart health care plan pays anything towards their expenses.

Therefore, Walmart workers who earn too much to qualify for Medicaid but are eligible (on the basis of income alone) for tax credits for insurance purchased through the exchange, will either have to accept Walmart's current high deductible health coverage or purchase insurance through the exchange without being able to use any affordability tax credits. Under this assumption, the company appears to be unlikely to have to pay any penalties under the free rider provision, since employees earning as little as 133 percent of FPL will still pay premiums considered affordable on the basis of the 10% cap on premium expenses, and therefore will not qualify for tax credits, while employees earning less than 133 percent of FPL would qualify for Medicaid.

Zero Impact on Walmart is a Problem

⁹ America's Healthy Future Act of 2009, TITLE I—HEALTH CARE COVERAGE, SUBTITLE D—SHARED RESPONSIBILITY, Employer-Provided Health Insurance Coverage, Chairman's Mark, page 38, available at: http://www.finance.senate.gov/sitepages/leg/LEG%202009/100209_Americas_Healthy_Future_Act_AMENDED.pdf.

¹⁰ "Re: Projected Health Plan Relative Values -Select Wal-Mart Health Plan options," memorandum from Segal Co. dated 10/29/2009, available at: www.wakeupwalmart.com

Based on data disclosed by a number of states, Walmart appears to follow a pattern of having a large number of workers qualifying for Medicaid and other publicly subsidized care.¹¹ Two examples follow.

Ohio. A September 2009 report issued by the Ohio Department of Jobs and Family Services¹² identifies Walmart as the company with the greatest number of employees and their dependents on Medicaid (15,246 in August 2009). As of June 2009, the state spends an average of \$245 per month on each recipient. Extrapolating this number to one year, medical coverage for Walmart workers in Ohio will cost taxpayers \$44.8 million for 2009.

Massachusetts. An April 2009 report issued by the Massachusetts Division of Health Care Finance and Policy¹³ identifies Walmart as the one employer in the state with the greatest number of employees using publicly subsidized health care (4,796). Walmart has held this dubious distinction every year for the three years for which this report has been published. In 2009, this amounts to 40.4 percent of Walmart's total workforce in Massachusetts of 11,881 (as of September 2009). The discrepancy in time periods between the data on number of employees on subsidized care and on the total number of employees adds some uncertainty to the results. The cost to taxpayers of publicly subsidized coverage in 2008 was \$9.3 million for Walmart employees in Massachusetts, and \$15.5 million for employees and dependents.

Ultimately, the "free rider" provision is constructed such that Walmart, a company with a proven track record of failing to insure a large percentage of its workforce and of offloading a large number of its workers onto the public rolls, is likely to end up paying nothing to provide enhanced coverage or to compensate the government for subsidies paid to its employees.

¹¹ According to data compiled by Good Jobs First, in 21 of 23 states which have disclosed information, Walmart has the largest number of employees on the public rolls of any employer. The list of states with summarized disclosure data is available at: http://www.goodjobsfirst.org/corporate_subsidy/hidden_taxpayer_costs.cfm

¹² The report is not available on the Ohio Department of Jobs and Family Services website, but has been made available for download by Progress Ohio at: http://pnohio.3cdn.net/5ddd17f44b6d3a8a58_sjm6bx1ew.pdf

¹³ "Employers Who Had Fifty or More Employees Using MassHealth, Commonwealth Care, or the Uncompensated Care Pool/Health Safety Net in State FY08," report by the Executive Office of Health and Human Services Division of Health Care Finance and Policy, Commonwealth of Massachusetts, April 2009, available for download at: http://www.mass.gov/Eeohhs2/docs/dhcfp/r/pubs/09/50_plus_employees_04-09.pdf