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Joan Claybrook, President

AARP's Financial Stake in the Medicare Drug Bill

In many ways, AARP has become a business deriving a large portion—about 60 percent—of its annual revenue from selling insurance products, such as Medigap supplemental drug insurance policies; selling mail-order prescription drugs; and offering prescription drug discount cards. It also sells its membership list to corporations, such as health insurers, and sells advertising space in its magazine to customers that include pharmaceutical and insurance companies. It also temporarily invests insurance premiums paid by its members before they are due to the insurer. At this point in time membership dues represent only 29 percent of AARP's total revenues.¹

The insurance-related portion of the non-member income streams totals at least \$161.6 million a year. Much of this income is derived from health insurance-related activities, from which AARP would stand to gain many millions of dollars in new income under the Republican Medicare bill. Maximizing corporate-related income and profits poses a significant conflict of interest for an organization trying to represent the best interests of its members.

An examination of AARP's financial statements and other public documents reveals the following conflicts of interest:

- **Royalty Income from Health Insurance Policies: \$107.8 million in 2002; 17% of operating revenues**

AARP endorses and lends its logo and name to products, namely insurance and investment plans, in return for royalties. The royalties, which are based on how much AARP members have invested in various plans, totaled \$217.7 million in 2002. Royalty income from insurance policies alone was \$123.3 million in 2002. Health insurance royalties, unreported in 2002, accounted for an average of 87.4 percent of AARP's total royalty income in both 2000 and 2001. Assuming the same percentage in 2002, AARP's health insurance royalty income for that year would be \$107.8 million – 17 percent of AARP's \$635.8 in total operating revenues.

A large portion of this royalty income likely was derived from insurance policies administered by the UnitedHealth Group, the principle health care plan approved by AARP. In 1997, AARP signed a ten-year deal to sell managed-care services of UnitedHealth Group to its members.² Ovation—a subsidiary of UnitedHealth Group—offers AARP members Medicare supplement, hospital indemnity, and supplemental hospital insurance, as well as prescription drugs and health products.

Effect of the Republican Medicare Bill: The legislation will result in most Medicare beneficiaries getting their drug coverage either by signing up for drug-only plans or by joining managed care organizations that provide a full range of services. UnitedHealth Group, one of the nation's leading health plans, can be expected to make a major push for a share of this new market. UnitedHealth Group's AARP-approved plans already are marketed to AARP's 35 million members through member lists and its 22 million-circulation magazine. This arrangement should dramatically accelerate AARP's future royalty income, which is based on how much AARP members pay in AARP-affiliated program premiums.

Assuming that AARP, with 35 million members, captured just 5 percent of the new \$400 billion Medicare prescription drug market over the next 10 years, it would collect an additional \$20 billion in insurance premiums. At AARP's average royalty rate of 2.9% (over the past three years),³ its royalties would raise \$58.4 million a year from the Medicare drug entitlement alone.

- **Investment Income from Insurance Products: \$26.7 million in 2002; 4.2% of operating revenues**

AARP earned \$26.7 million in 2002 by temporarily investing the \$4.2 billion in insurance premiums that it collected from its members before forwarding those premiums to UnitedHealth Group and other insurers.

Effect of the Republican Medicare Bill: Assuming that AARP, with 35 million members, captured just 5 percent of the new \$400 billion Medicare prescription drug market over the next 10 years, it would collect an additional \$20 billion in insurance premiums. At AARP's average return rate of 0.83 percent on member premiums (2000-2002), it would make \$167 million over the next ten years (or \$17 million a year) off the new market alone.⁴

- **List Access Fees: \$10.8 million from insurance companies in 2002; 1.7% of operating revenues.**

In 2002, AARP earned \$10.8 million, 1.7 percent of its income, from selling its membership lists to insurance companies alone. Essentially, insurance companies rent AARP's membership list to promote products. AARP earned an additional \$7.1 million selling their list to other industries.

Effect of the Republican Medicare Bill: This income should increase significantly as new drug insurance products would be marketed to seniors who would be subsidized by the federal government to purchase these products.

- **Drug Discount Cards: N/A**

In 2001 Ovation began managing the AARP Pharmacy Services program. Ovation negotiates discounts with drug makers and pharmacies, and then passes on a portion of the savings to clients. AARP licenses its name to Ovation so that the company can provide discount cards to members. AARP members who choose to purchase discount cards can use them to shop at local pharmacies and through mail order services. More than two years ago, a UnitedHealth Group press release to business editors stated that "[Ovation] and AARP are evaluating opportunities to expand older Americans' access to health and wellbeing products

with this program, as well as the potential to participate in the senior discount card program for pharmaceuticals proposed by President George W. Bush.”⁵

Based on AARP’s current financial statement, the percent of AARP’s revenue coming from these drug discount cards cannot be calculated. However, it is likely that the discount card revenues are accounted for under the “Royalties” category in AARP’s financial statement, since AARP licenses its name for UnitedHealth Group’s use in selling drug discount cards. Still, it is unclear whether this licensing is included under the “Insurance Royalties” or “Other Royalties” category. Insurance Royalties generated 19.4% of AARP’s revenue in 2002, and Other Royalties generated another 14.8% of AARP’s revenues.

Effect of the Republican Medicare Bill: The legislation would introduce a major drug discount card program for 2004 and 2005 before Medicare drug coverage begins in 2006. For an annual fee of about \$30, anyone enrolled in Medicare can receive a federal drug discount card worth an estimated 15 percent off medications. AARP directly, or indirectly through Oventions, will be eligible to compete for marketing rights of drug discount cards. Approval will be made by the federal government’s Centers for Medicare and Medicaid Services. Given AARP’s close working relationship with the Bush Administration in promoting this legislation, an AARP-related application could be given favorable consideration by CMS.

- **Advertising: \$76.4 million in 2002; 12% of operating revenues**

AARP derives considerable income from advertising sales. A major source of advertising is *AARP—The Magazine*, which is sent to 21.5 million households six times a year. Advertising also is sold on its Web site. Drug companies are major advertisers with AARP. A review of the November/December 2003 issue of the magazine found that of the 24 full-page ads, five pages advertised prescription drug products, two pages advertised over-the-counter drugs, and one page was for an AARP-sponsored Medigap health insurance plan.

Effect of the Republican Medicare Bill: Advertising revenue should increase significantly as drug discount cards get promoted, private plans competing for the new entitlement program seek new business, and prescription drug companies promote their products to a growing market as a result of the discount cards and expanded prescription drug coverage.

- **Mail Order Pharmacy Business**

It has not been possible to determine whether or not AARP receives additional benefits when members with AARP drug discount cards purchase medications through its mail order pharmacy. In these cases customers order drugs through AARP, but it is undeterminable what kind of compensation AARP gains or where it is accounted.

Effect of the Republican Medicare Bill: If it is true that AARP receives more than licensing fees but also fees for the use of its direct mail order services, AARP will receive even more benefits from the drug discount card program created by the bill.

November 20, 2003



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Public Citizen Fact Sheet: AARP Revenues 2000-2002

AARP Revenue Breakdown (in thousands)								
	2002			2001			2000%	2000 \$
	percent	subtotals	totals	percent	subtotals	totals		
Membership Dues	29.3%		\$186,312	31.5%		\$163,711	28.8%	\$144,554
Health Care Ins Royalties				19.4%	\$101,026		19.5%	\$97,745
Other Insurance Royalties				2.8%	\$14,470		2.8%	\$14,034
Total Ins Royalties	19.4%	\$123,283		22.2%	\$115,496		22.3%	\$111,779
Other Royalties	14.8%	\$94,373		12.8%	66,342		10.4%	\$52,135
Total Royalties	34.2%		\$217,656	35.0%		\$181,838	32.6%	\$163,914
Ins "Quality Control" Fees	0.1%	\$893		0.1%	\$680		0.2%	\$822
Other Ins Income	0.0%	\$0		0.6%	\$3,000		0.0%	\$0
Total Member Servies and Program	3.3%		\$20,955	3.0%		\$15,648	5.1%	\$25,668
Publication Advertising	12.0%		\$76,444	15.3%		\$79,685	14.8%	\$74,175
Ins Member List Access Fees	1.7%	\$10,794		1.8%	\$9,286		1.8%	\$8,947
Other Member List Access Fees	1.1%	\$7,150		1.1%	\$5,571		1.1%	\$5,418
Total Member List Access Fees	2.8%		\$17,944	2.9%		\$14,857	2.9%	\$14,365
Insurance Investment Income	4.2%	\$26,708		6.4%	\$33,133		8.0%	\$40,292
Other Investment Income	3.1%	\$19,562		4.7%	\$24,677		7.6%	\$38,017
Total Investment Income	7.3%		\$46,270	11.1%		\$57,810	15.6%	\$78,309
Other Income	1.5%		\$9,294	1.2%		\$6,445	0.2%	\$1,066
Grant Revenues	9.6%		\$60,899	0.0%		\$0		\$0
Total Insurance Income	25.4%		\$161,678	0.0%		\$0	32.2%	\$161,840
Total Commercial Income	59.7%		\$379,269	67.3%		\$349,838	71.0%	\$356,431
Total Member/Grant/Other Income	40.3%		\$256,505	32.7%		\$170,156	29.0%	\$145,620
Total Income			\$635,774			\$519,994		\$502,051



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AARP's Insurance Investments (in thousands)				
	2002	2001	2000	Total
Premiums	\$4,162,000	\$3,996,000	\$3,854,000	\$12,012,000
Return	\$26,708	\$33,133	\$40,292	\$100,133
Percent	0.64%	0.83%	1.05%	0.83%
Projected return on \$20 billion@ 0.83%	\$166,722			

AARP's Insurance Royalties (in thousands)				
	2002	2001	2000	Averages
All Insurance Premiums	\$4,162,000	\$3,996,000	\$3,854,000	
Health Insurance Royalties		\$101,026	\$97,745	
All Insurance Royalties	\$123,283	\$115,496	\$111,779	
Health royalties per Ins Royalties		87.47%	87.44%	87.46%
Rate of Return on All Insurance Royalties	2.96%	2.89%	2.90%	2.92%
Projected 2002 Health Royalties@ 87.46%	\$107,821			
Projected Return on \$20 billion@ 2.92%	\$583,516			

Endnotes

¹ All of these figures are calculated from AARP's 2002 Consolidated Financial Report, *available at*: www.aarp.org.

² David Stires, Fortune, "The HMO (Almost) Nobody Hates; UnitedHealth Can't Really Be This Good--Can It?," September 15, 2003.

³ Calculation based on data in AARP's, "Consolidated Financial Statement," 2001 and 2002.

⁴ Calculation based on data in AARP's, "Consolidated Financial Statement," 2001 and 2002.

⁵ Business Wire, "UnitedHealth Group Reports Record Second Quarter Net Earnings of \$0.68 Per Share," July 27, 2001.