An Update of the Health Care and Health Insurance Market in the U.S.

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As health insurance companies continue to deliver double-digit premium increases, employers become more desperate for solutions to control health insurance costs. In an effort to add perspective to this ongoing crisis, I have compiled some interesting facts and suggestions for employers who are interested in controlling their health care and health insurance costs. It is my hope that this summary will help employers to better understand the health insurance market so they can implement appropriate tools to improve their company's health insurance program and minimize their company's future health insurance costs.

<u>Alarming Health Care Trends</u>:

- Health care costs are rising at 12%+ per year. These are the highest cost increases since 1990.
- Prescription drug costs are increasing at 18-20% per year.
- Rising uninsured levels. (Currently more than 41,000,000 Americans lack health insurance.)
- Employee participation in health benefit costs is increasing (*e.g.* increased employee contribution, decreased benefits, dropped coverage, etc.).
- Rising popularity of Defined Contribution plans. (A basic Defined Contribution plan combines high deductible insurance policy with employer-funded health reimbursement accounts. Participants use the health reimbursement accounts to pay for lower-cost care and the high deductible policies to pay for catastrophic care.)

According to a 2002 PriceWaterhouseCoopers survey, there are 7 major cost drivers that have caused health care and health insurance costs to outpace general inflation in past years. These factors are expected to result in a 13.7% premium increase in 2003.

1. 3% - Medical advances, including drugs, medical devices, treatments, and testing.
2. 2.5% - Rising provider expenses.
3. 2.5% - General inflation.
4. 2% - Government mandates and regulation.
5. 2% - Increased demand.
6. 1% - Litigation.
7. 1% - Fraud and abuse and other cost drivers.

<u>Advantages of a Good Employee Benefits Program</u>:

- Eliminate potential for financially devastating catastrophic health care claim or loss for employees and their families.
- Increase employee quality, attendance and loyalty.
- Attract and retain good employees.
- Maintain healthier and happier workforce.
- Reduce employer and employee taxes.

<u>Cost Principles</u>:

- Health care inflation is rising at 3-4 times the rate of general inflation.
- Health care is not a free market commodity. The laws of supply and demand don't effectively work in a health care system. This is particularly true in a third-party payer system where the user is insulated from the actual cost of the care.
- 80/20 rule – 1% of insureds use 30% of health care dollars; 10% use 72%; 18% use $0.

- Insurance only works when the "risk pool principles" work correctly. This means selection must be random and adverse selection must be removed to the extent possible at employer and insurer levels.

Employer Tools:

1. Tools to Eliminate Adverse Selection
   a. Increase employee and dependant participation in the plan.
   b. Increase employer contribution toward employee and dependant premium.
   c. Require insured individuals to contribute to cost of care rather than to the cost of premium. It avoids adverse selection and it is a more equitable way to apportion the cost of the insurance. It will also result in lower premium increases over time.
   d. Use individual "age-rated" premium instead of "class composite" rates. Age-based premium eliminates subsidization of the cost of older employees on the backs of younger employees.
   e. Make selection into benefit program random – not adverse to insurance company and ultimately to the employer.

2. Plan Design
   a. Instead of increasing employee contribution to premium, decrease benefits through higher deductibles and higher cost sharing percentages. This controls utilization and costs without adverse selection.
   b. Develop a more "catastrophic" plan design. Move more toward a plan that has a more meaningful deductible and higher co-insurance levels. Avoid co-payment plans.
   c. Develop a cost-effective prescription drug plan. Mandate generics, avoid flat co-pay plans, use a percentage co-insurance that will remain indexed to inflation, consider a front-end Rx deductible, consider 3-tiered drug benefit (generic, preferred, brand).
   d. Encourage utilization of PPO providers where available.
   e. If appropriate, distinguish classes of employees for benefit levels, contribution levels, and waiting periods. Ensure that classifications are not based on a prohibited criteria or classification (e.g. age, gender, race, etc.)

3. Other Tools
   a. Education of employees – academically and financially.
   b. Defined contribution plans – will they control costs? The jury is still out.
   c. Consider true partial self-funding of employee benefits (if company size and financial position allow):
      (1) Increases control of plan and benefits;
      (2) Allows employer to ignore state mandates and premium tax;
      (3) Can develop strong benefit fund;
      (4) Be careful of excess risk;
      (5) Requires long-term commitment.

If you would like to discuss your company's health insurance plan or options to help control health insurance costs, even if your company is not currently insured with WMI, please feel free to contact me at (801) 263-8000 or via e-mail at davidleo@wpma.com.