Employer Premium Contribution --- An Important Cost Controlling Mechanism

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Using the term "contribution" in the same sentence as "cost controlling" when talking about health insurance might appear to be an oxymoron, but it's not. In fact, there is a very close relationship between the amount an employer contributes to the health insurance premium of his employees and the long-term strength of his health insurance program. This is because of the simple principle known as "Adverse Selection" and its inverse relationship to employer contribution.

Insurance models operate best in the absence of adverse selection. This is what happens when individuals are forced to pay a portion of the cost of obtaining health insurance and they only elect to participate in the insurance program when they decide it is in their best financial interest to do so. Employer contribution to the insurance premium helps eliminate the detrimental phenomenon of adverse selection and, ultimately, produces a healthier insurance program overall. This is because as employer contribution increases, adverse selection decreases and as employer contribution decreases, adverse selection increases. Indeed this is why WMI requires employers to pay 100% of the employee premium (or an equivalent amount of the employee and dependent premium combined) if they wish to insure their group with WMI.

To illustrate this important phenomenon, let's assume the following scenarios:

Scenario 1: An employer with 10 employees pays 100% of the employee health insurance premium. In this scenario, all 10 employees, healthy and unhealthy alike, would participate in the plan and there would be no adverse selection. The result would be a healthier group as a whole with annual premium increases that closely track medical trend in an average year.

Scenario 2: The same employer decides she can only afford to pay 50% of the employee premium and the employees must pay the additional 50% of the premium if they want health insurance coverage. In this scenario, employees will calculate whether it is in their best financial interest to pay the remaining 50% of the premium. Inevitably, the unhealthy employees will decide it is and will find a way to come up with their 50% portion. The remaining healthy employees may or may not participate in the plan and at the end of the day, we may end up with a group of 7 or 8 employees that consists of all of the unhealthy employees and some of the healthy employees. The result is a group with less than average health which will produce annual premium increases that exceed medical trend in an average year.

Scenario 3: The employer decides she can't afford to pay any of the premium and the employees must pay all the premium themselves if they want coverage. In this scenario, the most unhealthy employees will take up the coverage and will drive up the cost of the benefits so dramatically that the healthy employees will drop the group coverage and find coverage elsewhere. Ultimately, this "group" health plan will collapse.

As you can see, while it might be tempting in the short term for an employer to reduce contribution to the group health insurance premium and push more of the cost of the insurance off onto the employees, this solution is very shortsighted and ineffective. An employer is far better off increasing the plan deductible or adopting other benefit concessions that make insurance more affordable on the front end and enable the employer to continue paying the employee's share of the premium. This approach encourages cost sharing and utilization control on the back end, and eliminates adverse selection in the plan.

If you have any questions about your company insurance program or would like to learn how WMI might be a service to your company, feel free to contact me at davidleo@wpma.com or at (801) 263-8000.