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This Just In...

State legislators are trying to help small businesses cope with rising health care costs. Michigan legislators have proposed legislation to control group health premiums for small businesses, those with fewer than 100 employees. Bills under consideration in the Legislature and Senate would prohibit insurers from charging small businesses 25 percent more or less than their average rate. This may make insuring small groups unaffordable for insurers.

Meanwhile, *Washington* state legislators have proposed allowing "bare bones" health plans for employers with 50 or fewer employees. The bill would exempt small businesses from having to provide certain mandated services, including mental health, chiropractic, chemical dependency care and mammograms.

Since the war in Iraq began, more companies have begun to pay reservists the difference between their military compensation and their civilian pay when they go on active duty. No law requires them to do this.

EMPLOYEE BENEFITS REPORT

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HEALTH BENEFITS

Consumer-Driven Healthcare: Can It Fix a Broken System?

Consumer-driven health plans (CDH) represent a shift in health care philosophy as much as a new type of health plan. These plans, also known as consumer-directed health plans or defined contribution health plans, shift responsibility for controlling costs from insurance companies and health care providers to health care consumers. They work on the principle that giving employees the incentive and ability to manage their own health care expenses will cut unnecessary costs.

Most plans combine a health reimbursement account with an employer-paid high-deductible insurance plan. The employer makes an annual contribution to a health reimbursement account (HRA) for each employee. Employers determine the amount of the contribution, which IRS-approved health expenses the HRA will cover, and whether employees can roll over unused funds into the next plan year. Employees can use HRA funds for regular health care expenses, such as office visits and preventive treatments. HRA participants receive these amounts tax-free.

Most CDH plans back up the HRA with employer-paid health insurance. Most of these policies are generous indemnity plans, paying 80 to 100 percent of inpatient and outpatient costs for network providers and 60 to 80 percent for out-of-network providers. However, the policies have very high deductibles—generally not less than $2,000 for single coverage and $4,000 for family coverage. This high deductible reduces the premium anywhere from 25 to 40 percent, making the CDH plan

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Presidential Candidates Unveil Universal Health Proposals

Ten years after President Clinton pushed universal health insurance, a new crop of Democratic politicians is proposing universal health insurance plans. Rep. Richard Gephardt has unveiled the more detailed of the two plans; former Vermont Governor Howard Dean has sketched a plan loosely based on Vermont's health insurance system.

1. The Gephardt plan

Gephardt's plan builds upon current employer-based health care by requiring all employers to provide health insurance for employees. Currently, employers can deduct premiums from their federal taxes—which equals about 30 percent of premium costs. Gephardt's plan would replace the deduction with a tax credit, which would reimburse employers for 60 percent of health insurance premiums.

Who would pay the remaining 40 percent? If an employer didn't previously offer health insurance, employees would. Gephardt's plan would make federal subsidies available for some low-income workers. The plan would also prohibit employers that currently offer health insurance from requiring employees to pay a larger share of premiums than they currently pay. These employers would pay any difference between the federal subsidy and the employee portion of premiums.

How the plan stacks up for employers

An employer currently paying 80 percent of health premiums for its workers saves approximately 30 percent of this amount with the federal tax deduction. The employer's final cost ends up being roughly 56 percent of premium. Under the Gephardt plan, the same employer would pay 80 percent of premium; after the 60 percent tax credit, its final tab would be 32 percent of premium. The government would pay 48 percent and the employee would continue contributing 20 percent.

A firm that currently does not offer health insurance would have to buy insurance for its employees. But the government would pick up 60 percent of the cost through the tax credit. Employees would pay the remaining 40 percent.

How employees would fare under the plan

Employees who currently have employer-provided health insurance would see no difference in their coverage. Low-income workers who currently lack employer-provided coverage may feel the pinch, however. Under the Gephardt plan, they would have to buy employer-provided insurance. Subsidies would help some lower-income workers pay for coverage, but some young, healthy workers who currently do not have insurance coverage would be forced to pay for it.

What about the unemployed?

Any employment-based health insurance scheme faces the problem of how to cover the unemployed, children and the elderly. The Gephardt plan would include a Medicare buy-in for uninsured Americans between the ages of 55 to 64, an extension of SCHIP (State Children's Health Insurance Plan) coverage to the parents of children currently covered and a federal contribution to COBRA coverage for the unemployed.

Gephardt would fund his plan by repealing any income tax cuts passed this year and repealing those passed in 2002.

2. The Dean plan

Former Vermont Governor Howard Dean was the first contender for the Democratic presidential nomination to talk about universal health coverage. Dean has provided fewer specifics than Gephardt, but he proposes providing near-universal coverage by: 1) guaranteeing Medicaid coverage to everyone under age 22, 2) expanding Medicare by providing prescription drug benefits to the elderly and 3) expanding the current employer-based health insurance system to provide coverage for all working people between age 23 and 65.

As governor of Vermont, Dean achieved near-universal health coverage for children age 18 and under through a program called "Dr. Dynosaur," which basically expanded Medicaid. Dean wants to require states to guarantee insurance coverage to children and young adults under age 23.

To cover working adults, Dean would rely on the existing employer-based health care system. He would expand employer-provided health insurance by offering subsidies to employers and to employees to purchase insurance. His health insurance program would provide catastrophic coverage, including "first dollar coverage for things like colonoscopies and mammograms that nobody would get if they had to pay for them. But after that, there's a big deductible." The insurance would likely be structured as it is in Vermont: insurers would price policies using community-rating rather than the insured's age to avoid "rate discrimination" against older insureds, and insurers would not be able to exclude applicants

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very attractive to employers and allowing them to afford the HRA.

Carriers consider the HRA part of the high deductible, so when insureds exhaust their HRA, their out-of-pocket amount equals the balance of the deductible less whatever amount was in the HRA. This creates incentives for employees to keep their annual health care spending within the limits of their HRA.

CDH plan participants need access to information to make wise healthcare decisions. A good CDH plan should offer Internet-based information to plan participants, including general references on health conditions and treatments, prescription drug information, directories of providers and quality of care statistics on providers.

The early results

CDH plans are catching on, at least among larger employers. Last year, only 4 percent of large employers gave employees a CDH option. Cambridge, Mass.-based Forrester Research estimates that number will increase to 16 percent in 2003 and reach 24 percent by 2004. Forrester Research predicts that 5 percent of smaller employers will offer a CDH option this year.

Employee response so far has been positive, found consulting firm Mercer. Companies that offer a CDH plan get about 15 percent of eligible employees to sign on, Mercer found. Forty-five percent of these employers said employees have had a "strongly positive" response to the plans; no employers reported "strongly negative" feedback. Not surprising, since a CDH plan was the lowest-cost health plan for 85 percent of employers in the Mercer survey.

Benefits

In addition to lower costs, a CDH offers the following benefits:

Reduced health care utilization: Families enrolled in a CDH decreased health plan utilization by 11 percent in 2002, according to a study by Synhrgy HR Technologies.

Greater predictability of health care costs: CDH plans might not lower costs for all employers, but they should provide greater predictability. Employers select the amounts to contribute to the health reimbursement accounts and deductible amounts for insurance coverage.

Flexibility: Employers tailor benefits to their needs and the needs of employees. They determine what types of IRS-approved benefits health reimbursement accounts can cover; they also determine rollover provisions. Employers can also select what benefits the high-deductible plan will provide, subject to applicable laws.

Increased retention: Permitting rollovers of unused HRA amounts allows employees to build a fund to pay for large medical expenses in the future or for post-retirement health expenses. This may encourage employee retention.

Employee awareness of medical service costs: Current managed care plans, with low co-payments and 100 percent coverage, have insulated employees from knowing or even caring about the real cost of their medical care. CDH plans increase employee awareness of the true cost of health care by giving them greater control over their medical service expenditures.

Challenges

Although CDH plans may encourage employees to make wiser healthcare spending decisions, discretionary spending only accounts for about one-third of health care expenses. CDH plans have no impact on other factors driving group health care costs, including costly technology, Medicare and Medicaid reimbursement shortfalls and an aging population.

Critics of CDH plans say that they encourage consumers to postpone preventive treatments, which can lead to more serious health problems…and higher costs. Critics also say that CDH plans cost-shift by attracting younger, healthier employees. Leaving older, less healthy employees in managed care or indemnity plans will further drive up costs for these plans. Jack Lord, MD, senior vice president at Humana, says employers can avoid that problem by completely replacing their health plans with a CDH plan, instead of offering a CDH as an option.

Employers offering a CDH plan may have to do a lot of education. California Health Decisions recently surveyed 800 Californians on CDHs. After hearing a description, only one in seven respondents reported hearing of CDHs. Half found the plans appealing; the other half did not.

Employees who have more direct control of their healthcare need to be informed about their options. Training employees to find and use this information might take work. A recent study by CIGNA Corp. found people are more likely to use the Internet to plan a vacation or to research buying a car than to obtain health information. Another study by the Center for Studying Health System Change found that of the people who do use the Internet for health research, most are white, well-educated and higher-paid.

CDH plans make most sense for employers who:

- Have above-average health costs, particularly where employees currently contribute to health premiums. CDH plans will be more appealing if employees can save money.
- Have a majority of employees who are computer-literate, with easy Internet access, at home or at work, to enable informed health care decision-making.
- Have few employees living paycheck to paycheck. These employees might not have the financial resources to cover health costs that fall between the limits of the HSA account and the deductible of the employer-provided health insurance.
- Have a management team committed to CDH plans and communicating plan goals.

If you decide to switch to a consumer-directed health plan, stress its positive features. Consumers surveyed in the California Health Decisions ranked the most attractive features of CDH plans as: 1) the ability to roll unused funds over into another year, 2) being able to use HSA balances after leaving a job, 3) having money for uncovered dental and vision care expenses, 4) getting to choose health care providers and 5) being able to compare quality and cost of providers and hospitals.

For more information on CDH plans, please call us. ❑

SEP IRAs: Simple Retirement Plans for Small Businesses

A Simplified Employee Pension (SEP) IRA plan is one of the easiest retirement plans to set up and administer. Here's how to do it:

1. Complete IRS FORM 5205-SEP. You do not have to file this form with the IRS; simply keep it on file.
2. Set up a SEP IRA account for each eligible employee. Either the employer or employee can open the account; however, the employee owns and controls the account. All employees who are at least 21 years old and have worked for you for any three of the past five years—including the current year—are eligible and must have an account.
3. Give a copy of the plan agreement to each participant.
4. Make contributions to each employee's SEP IRA account—for 2003, up to a maximum of 25 percent of an employee's eligible compensation or $40,000, whichever is less. You do not have to make a contribution every year; however, if you do contribute, you must contribute the same percentage of salary to every employee's account.
5. Make sure each employee receives an annual report of contributions made to their account for the year, if any. The financial institution where the accounts are set up may handle this for you.

That's it! For employers, the advantages include:

- ✔ No set-up fees.
- ✔ Flexibility—you can forego contributions in any year if the company doesn't meet its financial goals.
- ✔ You can make contributions for a particular tax year until the employer's tax filing date, including any extensions.
- ✔ Contributions are not included in the participant's taxable income.
- ✔ Self-employed business owners can set up SEP IRAs for themselves, as long as they have earned income from their business. If they don't have employees, they do not have to complete Form 5205-SEP—they simply apply for an IRA account and designate it as a SEP IRA. This type of SEP has no annual reporting requirement.

Disadvantages

- ✔ SEP IRAs do not permit employee contributions.
- ✔ SEP IRAs vest immediately and are completely portable. Other types of retirement plans may better suit the needs of employers who want to use a pension plan to encourage retention of valued employees.
- ✔ No catch-up contributions for older employees.

For more information on your retirement plan options, please contact us.

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with pre-existing conditions. (Gephardt's plan does not address this issue, which may result in very high premiums for small groups that have members with pre-existing conditions.)

Under Dean, we'd likely see incremental rather than dramatic change to the existing employer-based system. He acknowledges the current system has faults, but says it's more important to "get everyone in the system first and then we can argue about how to reform the system." Dean, a physician, likes managed care. He says, "I think it's very important to have gatekeepers. Too many people can go to their specialists in fee for service when a specialist is not appropriate. In a health plan, there's not just one person involved in looking after a patient's health care. Secondly, (managed care) does definitely decrease use of the emergency room. Thirdly, it has the potential to continue to improve patient satisfaction and physician practices."

Dean would pay for his program by repealing the portion of President Bush's tax cut that affects people earning more than $300,000 a year.

The bottom line

Making health insurance more accessible is a noble goal. However, both the Gephardt plan and the Dean plan would increase administrative burdens on small employers. By expanding government insurance programs, they would also increase taxes.

A nonpartisan analyst estimated the Gephardt plan would cost about $213 billion the first year. If the plan provides coverage to 40 million currently uninsured people (a very generous estimate), that would average more than $5,000 per person. The Health Insurance Association of America (HIAA) found that the average cost of health insurance purchased in the individual market was $173 a month for singles and $334 a month for families in April of 2002. (These figures show only part of the picture—people with pre-existing health conditions either cannot buy insurance on the individual market or pay extremely high rates for limited coverage.)

Too few details exist about the Dean proposal to make cost estimates. However, it's fair to say that the Dean proposal would also be costly. We'll keep you posted on any significant developments in this area. ❑