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# Decoding the Costs of the Health Care Reform for Mid-Size Employers:

## What will it cost and how can this expense be better spent?

As legislators debate coverage options for the uninsured, employers around the country have one simple question: What will it cost my business?

This is an excerpt of a presentation given to CEOs, CFOs, and Board members of Milestone Partners Portfolio group October 27, 2009 by Mary Kate Scott. The presentation outlined the legislation and provided employers with both an estimate of likely costs and options to spend their health care budgets in smarter ways. The focus was on mid-size employers with 20-500 employers, with different types of health plans.

While important philosophical debates ensue about increasing coverage, and managing the multi-trillion dollar health care bill, employers are becoming increasingly aware that government-mandated health coverage for (nearly) all employees is highly likely. It will be a new, large, and fast-growing cost that will impact the bottom line for the majority of businesses.

Here is an overview of how a likely version of the pending legislation will affect business[1]:

- If your payroll is $500K or more, you *will* be obligated to provide coverage and (as a quick estimate) it may cost you around 10% of your payroll
- If you already provide coverage for *all* your employees, continue on to learn if you need to increase your contributions to employee premiums. You will also learn new ways to spend your money wisely
- If you provide it for only some of your employees now, you are likely to increase your coverage (for all full-time and some part-time employees)
- If you don't provide any coverage at all – there are new costs for your company on the way, with a $10k-$50k minimum (the alternative being penalties that may be likely to be greater than coverage costs)

### Breakdown of Proposed Legislation

The Senate and House are debating which employers will be mandated to participate in health insurance reform. There are three main factors that will drive employer coverage: total number of employees; total payroll; and what percentage of premiums the employer must pay (from 60% to 75%). Overall, under any of the proposed bills, about 30 million additional people will be

[1] This presentation was delivered October 27, 2009; legislation is still in progress and these impacts may change as the final health care bills are presented and passed.

covered, with around 20 million of those to be covered by employers.

**The Senate version**[2] would require companies with more than 25 employees to pay at least 60% of their workers' premiums or face annual penalties of $750 per full-time worker and $375 per part-time employee (beyond the first 25 employees). Companies with fewer than 25 employees are exempt from these requirements, with subsidies offered to companies that choose to pay 60% or more of premiums for their 50 or fewer employees.

**The House version**[2] focuses more on payroll size, requiring employers with at least $250K in payroll to provide coverage for all employees, and pay up to 72.5% of their workers' premiums. The penalty for those who do not pay is a payroll tax on a sliding scale from 2-8%. The bill calls for companies with payrolls higher than $400K to pay a minimum of 72.5% of worker premiums or be hit with an 8% penalty.

**Other bills under debate**: Federal subsidies for families at 300% income of the federal poverty scale (400% also being debated). Another separate piece of legislation would apply a federal tax to employers that self-insure their health plans. Yet another bill would require all employers to spend 7.5% of their payroll on health care. The Small Business Health Tax Credit would grant a refundable credit of up to 50% on premiums paid by employers on behalf of their employees. Qualifying businesses would need to offer a quality health plan to all employees and cover a "meaningful share" of the cost of employee health premiums (although it is unclear on qualifying business size).

## Impact on Your Business

Whether you currently offer insurance or not, there are new costs coming to your business, significant enough to potentially change your cost structure. The essence of health reform today is **health insurance reform** – meaning more people will have coverage who don't have coverage now:

Of the four main groups of uninsured, employers will likely be tasked with covering at least some individuals in two of the groups:

1. Working poor currently not offered employer coverage – employers will be impacted as the mandates require employers to offer insurance.
2. Young healthy employed who in the past have elected not to pay the premium – this would no longer be an option.
3. Self-employed who choose not to be insured.
4. Unemployed – some discussion that post employment employers may need to contribute to coverage benefits via COBRA payments.

**The following cases are illustrations of how insurance reform may play out for various sized companies.**

**Owner-Operated Small Business:** A company consisting of an owner and 5 full time employers has a $500K payroll. Only the owner currently has health insurance.

**Potential Coverage Costs Under the House Bill[3]:** Given the size of the payroll this company is likely to be asked to provide coverage for the 5 full time employees with approximately 70% of their premiums. The total new

[2] As of October 27, 2009

[3] These estimates use national averages of employer costs (from the Kaiser Family Foundation 2009 cost estimates), and assumes 3 of these employees will require family coverage at an employer cost of $9,800 per year for 3-year employees and $3,800 for 2 single employees, or $36,400 total.

**The following cases are illustrations of how insurance reform may play out for various sized companies,** continued

cost might be ~$36,000. This figure can easily be ± 20% depending on the state, type of coverage, premium paid, what's included in the plan and the health and dependent status of employees. Under the Senate bill no additional coverage would apply for the 5 employees.

There may be federal subsidies for this business given its small size (number of employees), however these would be temporary and likely for 2-3 years.

**Paying the fine:** The alternative to providing the coverage is to pay a fine; early estimates put this at 2-7% of the payroll or $10,000 to $35,000.

**50 Employee Firm Offering Coverage:** A business with a $3M payroll currently provides coverage to all its 50 employees, paying 70% of the premium.

**Potential Coverage Costs:** Likely no new costs to this employer. However it's probable that the cost of health coverage will increase as insurance carriers grapple with new regulations that will increase their costs and will be passed on to employers. This employer might consider plan options such as HDHPs or other cost-saving measures if costs increase beyond the value of the expenditure.

**100 Employee Company with Basic Health Plans:** A company with a $10M payroll provides basic coverage and pays 50% of the premium to half of its 100 employees

**Potential Coverage Costs**: Given the size of the payroll this company is likely to be asked to provide coverage for the uncovered 50 full time employees with approximately 70% of their premiums. The total new cost might be ~$360,000. This figure can easily be ± 20% depending on the state, type of coverage, premium paid, what's included in the plan and the health and dependent status of employees. The other 50 employees currently covered will have ~70% of their premiums covered (from the current 50%) for an increase of ~$150,000 in costs; for a total of $510,000.

**Paying the fine:** The alternative to providing the coverage is to pay a fine; early estimates put this at 8% of the payroll or $800,000.

## Managing the Challenge of Providing Health Coverage

As you review your options and costs to provide health coverage consider these elements: The type of plan (the extent of care in your plan(s) (preventive, prescription drugs, catastrophic, etc.); the use of alternative delivery models such as urgent care or retail clinics, the deductible for your employee and the type and amount of co-payments. Each of these elements can change the type of coverage and the cost for you and your employees.

## Strategies for spending your health care dollars most prudently

### *Negotiating for Lower Cost Plans in 2010 for 2011*

If you offer coverage, it's likely your plan will be set for 2010; early in 2010 your firm negotiates options for 2011. Usually small businesses select a single plan; in fact 86% of small businesses with fewer than 200 employees have only one plan option, usually because adding additional plan options adds costs. Negotiating plans can be tricky, but here are some options to look into that may lower the overall plan premium.

***"Regardless of which direction employers choose to go, this may be the ideal time to renegotiate expectations with employees."***

- Higher deductibles: A large deductible (which translates to larger risk) means a lower premium for employer and employee. If a deductible is large enough, you can opt into a "HDHP" or High Deductible Health Plan that can be coupled with a Health Saving Account
- Higher co-payments for visits and prescriptions
- Use of co-insurance vs. co-payment to pay the required percentage of every medical bill and primary care provider visit. This often means a higher payment for the employee but smaller premium for the employer.
- Use of emergency care alternatives including urgent care and/or retail clinics
- Negotiate with local health care providers; larger employers in a smaller town may have some negotiating power with local providers and hospitals for large costs items such as surgery
- Consider out of state plans if your state has higher coverage mandates; there may be more plan options next year, possibly including the option to purchase out of state (currently in state is sole option). Different states have different mandates for coverage.

### High Deductible Health Plan with H.S.A.'s and H.R.A.s

1. High Deductible Health Plans (HDHPs) feature higher deductibles, lower premiums and employees take on more of the risk. It is predicted that 60% of employers will offer HDHPs in 2010. Participants are able to put pre-taxed money aside to pay for health expenses, making it a savings vehicle similar to a 401K. Health Reimbursement Arrangements (HRAs) are employer-owned plans. Health Savings Accounts (HSAs) are employee-owned plans.

**2. Negotiating for Lower Cost Prescription Drug Plans**

Employers may choose to do this as part of their health plan, or they can negotiate it separately with a pharmacy benefit manager (PBM). For employers with more than 200 employees this could be valuable.

**3. Healthier Employees Reduce Overall Health Costs**

Employers can also engage in strategies to improve the health and productivity of their employees and therefore encouraging smarter spending of health care dollars.

- Flu shots
- Healthier meeting food
- Weight loss and stop smoking campaigns onsite
- Screen savers with health tips and encouragement
- Avoid costly and time consuming ER visits with urgent care and retail clinics
- Offer health assessments that include a generic switching component
- Education to ensure employees use in-network providers and use the medical cost estimators (only 11% currently use them)
- Choose the stairs vs. the elevator the choice with employers and senior managers setting a positive example

## Is this health coverage cost issue worth your attention?

***Self-Assessment Tasks***

The following tasks will help CEOs and CFOs determine how much time they might invest to considering health care costs on their business and who the best person within the organization is to handle this task. If companies have coverage in place and costs are well managed this may not be a high priority. For companies facing new costs and trying to determine the nature of the challenge, here are three tasks:

**Task 1:** Ask your HR person how much you spent on health care this year and last year and check the growth rate. It is interesting to see the magnitude of the costs, how long this takes to do, as well as a good indication of who is watching these costs. During this process, take a moment and assess this person's financial skills. They are working within a significant budget and you should be seeing the skill sets of the HR manager include quantitative financial skills.

**Task 2:** Change just one company meeting food to healthy food (ex. from cookies to carrots and apples; from BBQ lunch to healthy Subway sandwiches). This is an excellent way to assess your employees' readiness and willingness to engage in healthy lifestyle options. See if they notice and how they respond to the changes. Their response may be a good indicator of how challenging it will be to change the health mindset within your organization.

**Task 3:** Finally, take five minutes and ask yourself a few questions. When is the last time you had a physical? How is your weight, blood pressure, cholesterol? This is not to suggest a complete clinical check-up, but asking these questions will help you figure out how willing you are to personally engage on health issues. If you are not in great health and embracing a healthy lifestyle, it's tougher to communicate the message on health to your employees.

## Conclusion

If you provide good coverage for all of your employees already, and pay 75% of the premiums – you likely have less to worry about in regards to the coming changes. It would be appropriate to delegate tasks and research related to health care reform to your HR manager, while ensuring they pay attention to good plan design and encourage healthy behaviors.

But if you are a mid-size company and are only providing some coverage to some employees – the pending legislation *will* impact your bottom line and it could get pretty expensive. This is the time to estimate the health insurance costs on your business and to develop solutions to manage the change.

### AUTHOR

Scott & Company, Inc. is a management consultancy working with health care stakeholders for over twenty years. Focusing at the nexus of health care, business and technology, projects focus on: scenario, strategic and business planning, financial and technology forecasting. Our firm works with many segments of the health care industry including health care systems, technology and medical device companies; employers; educational institutions; pharmaceutical firms; payers and plans; consumer products companies; retailers; non-profits; and, financial services firms.

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