Understanding the True Cost of Benefits

Everybody's talking about the cost of benefits these days, and usually with alarm. Health insurance costs have been growing dramatically since the 1980s, with a period of particularly rapid growth from 1998 to 2005. Although managed care plans and utilization controls initially helped to contain costs, premiums have been escalating yet again.

Many people expected the Affordable Care Act (ACA) to reduce costs. In actuality, many employers will experience a significant cost increase as the impact of the ACA spreads across the market. According to the American Health Policy Institute, employers saw their health care costs grow by 3.8% in 2013—more than double the general rate of inflation.

New taxes and regulations will continue to put upward pressure on costs for years to come, forcing employers to find new ways to limit their expenses. This is challenging because many employers do not realize that premiums and claims are only part of the overall costs of benefits. There are other factors at play here, such as:

- Soft costs: Hidden expenditures and overlooked time costs that can be attributed to health benefits.
- Opportunity costs: The advantages lost when you choose one plan over another.
- Actual costs of health care: The price paid for health care services.

In this paper, we'll take a closer look at each factor contributing to the true cost of health care benefits—and what you can do to gain some measure of control over them.

Hard Costs: Know Your Options and Opportunities

Companies pay a tremendous amount of money to the insurance industry every month, every year. Post-ACA, many companies are receiving much higher renewal rates from their current insurance carriers. Some believe these rates are non-negotiable. Others insist they're negotiable. The reality is somewhere in between.

A lot depends upon the size of the company. Unfortunately, smaller companies don't have the bargaining power of a large enterprise. However, rates can be negotiated extensively even in mid-market companies (50+ employee groups).

Employers have always had the option to offer low-priced health coverage to their employees in the form of high-deductible insurance plans. Historically, employers have been hesitant to offer these high-deductible plans, but the 60% actuarial value plan threshold mandated by the ACA is causing many employers to rethink that position. Plans with a 60% actuarial value typically have the lowest premiums and the highest deductibles.

These plans can be a win-win for employers and employees alike:

- They allow employers to achieve ACA compliance.
- They are affordable for many employees who were previously priced out of health insurance, and employees can pay for them with pre-tax deductions from their paychecks.

Many employers are surprised to learn that they can offer these plans at a reasonable cost, as long as they make sure that employee contributions are not higher than 9.5% of their W-2 income.

That said, the desire to deliver "big time" benefits leads many smaller businesses to choose high-deductible plans in order to save on their contribution. But offering these plans might not be wise if employee goodwill suffers as a result.

Alternative methods of funding health plans are becoming increasingly popular. Many employers are considering switching to a defined contribution model or offering self-funded or partially self-funded plans.

- In the defined contribution model, employers set a dollar amount for each member and employees can choose the benefits they want. Younger populations are especially drawn to this approach. Millennials and members of Generation Y have a different perspective on purchasing decisions in general (and benefits in particular) than their baby boomer predecessors. Companies can take advantage of this fact by offering a menu of choices to their employees, managed via technology, and letting them decide. For example, companies can set up a private exchange that gives employees 4–5 plans to choose. A defined contribution approach can be a great way to stabilize cost while giving employees more choices.
- In a self-funded plan, the employer pays for benefits directly, rather than contracting with an insurance company. To mitigate some of the risks involved, some employers opt for partial self-funding—in which companies pay for fixed costs annually and cover claims as they go. One of the advantages of partial self-funding is that the employer is able to retain any funds set aside for claims that are not spent at the end of the plan year.

Soft Costs: Hidden or Overlooked Expenses, Real Impact

Administrative costs related to health care can directly affect profitability. That's not "soft" at all—it's a cold, hard fact that time is money.

It takes time to enroll employees and administer a health plan. Thanks to the ACA, benefits administration just got much more complex, and most HR departments are ill-equipped to manage the complexity.

Your human resources team now has to contend with:

- Trying to make the best plan decisions for the company and the employees
- Educating employees about the ACA and how it affects them
- Ensuring plan compliance with all state and federal guidelines
- Keeping the plans competitive with the benefits offerings of other similar companies

These complicated issues can lead to paralysis, reduced productivity and poor decisions.

Companies can also incur costs from compliance audits. Increasing numbers of audits by the Department of Labor and other governmental agencies eats up a tremendous about of HR time can result in hard costs like fines and penalties.
And of course, the ultimate soft cost is employee dissatisfaction. If you're spending enormously on your benefits, but employees are unsatisfied, what's the point? That's why benefits education and communication are so important—they help employees to understand, utilize, and appreciate their benefits. On the other hand, dissatisfied employees become unproductive, and may even leave the company.

Opportunity Costs: The Choices You Didn't Make

What did you give up in choosing the health plan you have now? That's what's known as an opportunity cost. Without comprehensive knowledge of the insurance landscape, you may well have missed out on a better plan option. Or you may have a plan that isn't the right fit, without knowing it. For example, if you are paying for the richest plan but your employees are never using the benefits, you've missed the opportunity to downsize and use the savings elsewhere.

If you're spending significant money on a low-deductible plan, you may be missing the chance to go for a high-deductible plan and put the cost difference into a Health Reimbursement Account (HRA) for each employee. Opportunity costs are hard to spot, but they can have a very real impact on your bottom line.

The Actual Cost of Health Care Services: What Nobody's Talking About

Despite our national discussion around the cost of health care, the price paid for health care services is under-discussed and under-reported.

The total cost for health care services is affected by utilization (the appropriate or inappropriate use of services) as well as the age and overall health of a population. These costs are rising exponentially—well in excess of overall inflation—and nothing in health care reform addresses that fact. Companies can affect these costs only indirectly, through wellness initiatives, and other proactive lifestyle incentives like smoking cessation assistance, weight loss programs, and mental health coverage.

From Understanding to Control

As we've shown, in order to control health care costs, you must first fully understand all of the factors that contribute to them. Hard and soft costs, opportunity costs and actual health care expenditures all contribute to the price tag for your business.

Many businesses are turning to external benefits experts for help. Because they focus exclusively on benefits, an outside expert has intimate knowledge of all the ways health care benefits can affect an organization's bottom line. These trusted partners know the appropriate actions to take to reduce or control health care costs, and the best of them have plans and strategies to support those actions.

Here's what to look for in a potential partner:

To help control hard costs	You need a partner experienced in the different product options to help you align your benefits program with your unique needs. You also need a partner with strong insurer relationships, plus the ability to muster competitive market data as leverage to negotiate rates or solicit competitive bids form multiple carriers.
To help decrease soft costs	You need a trusted partner who knows the regulatory requirements inside and out and can handle compliance issues, enrollment and administration, plan design and employee communications. By outsourcing these responsibilities, you can save tremendous time and hassle, and exchange uncertainty for a simple, predictable monthly fee.
To minimize opportunity costs	You need a partner who can bring you plenty of plan and funding options during the planning stages, and help you make strategic decisions.
To help reduce actual health care costs	You need a partner who can share best practices for ensuring appropriate utilization and encouraging overall wellness among your plan members.

By partnering with an expert in employee benefits, you'll gain a much better understanding of what you're paying for in terms of health care. Armed with those insights and the experience of industry veterans, you can take strategic steps to get those costs under control.

Johnson & Dugan acts as that trusted partner for employers, sharing experience and expertise to help stabilize health care costs. With our core competencies in plan design, benefits administration, competitive benchmarking and market review, Johnson & Dugan empowers employers to spend their benefits dollars wisely.

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1 The American Health Policy Institute, "The Cost of The Affordable Care Act to Large Employers," 2014 .

2 Centers for Medicare and Medicaid Services, "Report to Congress on the impact on premiums for individuals and families with employer-sponsored health insurance from the guaranteed issue, guaranteed renewal, and fair health insurance premiums provisions of the Affordable Care Act," February 21, 2014.

3 *Forbes Magazine*, "Obamacare Will Increase The Cost Of Employer-Sponsored Insurance," February 22, 2014.

4 IRS.gov, "Request for Comments on Health Coverage Affordability Safe Harbor for Employers" (Section 4980H), 2011.

Johnson & Dugan is a one-stop employee benefits and human resources consulting and support services company. For over twenty-nine years, Johnson & Dugan's highest priority has been to make it easy for companies of all sizes to expertly plan and administer employee benefits. A partnership with Johnson & Dugan will help you align your benefits strategy to broader initiatives, reduce your HR workload and improve efficiencies company-wide.

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