
The Defined Contribution Health Plan:

What is it? What's in it for you?

**A Luncheon Briefing presented by
The American Academy of Actuaries**



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The Defined Contribution Health Plan

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Defined Contribution Health Plans – A Continuum

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Vice President, American Re Healthcare



Objective

- Define “Defined Contribution” plan designs
- Discuss its relationship to DC pension plans
- Describe the objectives of these plans
- Issues & challenges



Defined Contribution Health Plans

- DC name from the retirement analogy
- AKA
 - “Consumer-driven”
 - “E-health”
 - “Self-directed”
- Not a particular type of health plan
- A concept giving rise to alternative approaches to financing health care



DC Health & DC Pension

- Accounts
 - Health: immediate non-catastrophic health care needs
 - Pension: long term capital accumulation
- Benefits
 - Health: catastrophic insurance component
 - Pension: no catastrophic insurance component
- Benefits
 - Health: short term emphasis
 - Pension: long term emphasis



Common Characteristics

- Employer sets/controls their cost
- Participant choice
- Increased participant cost-sharing
- Participant education
- Internet enabled systems capability

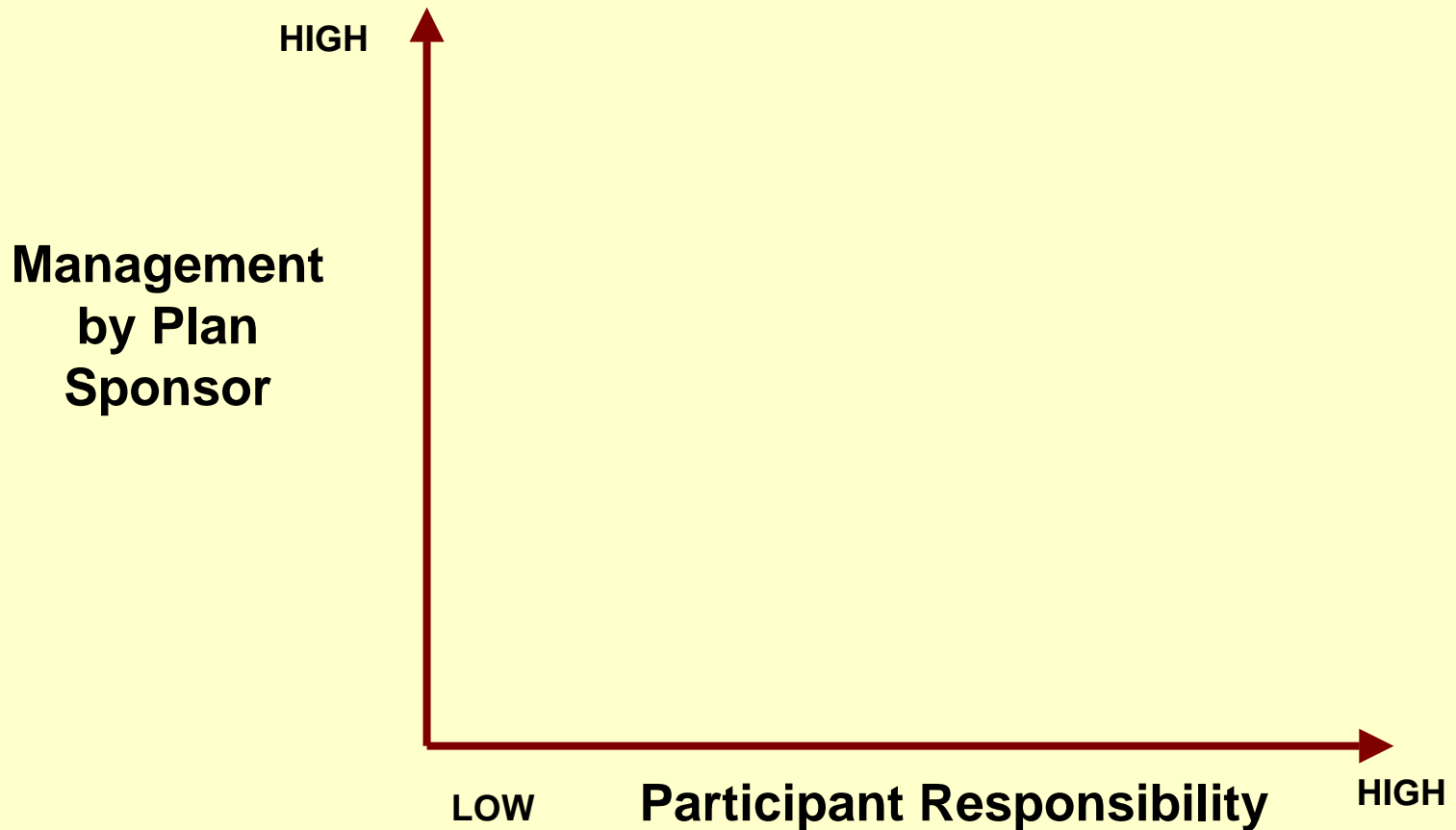


The DC Health Plan Continuum

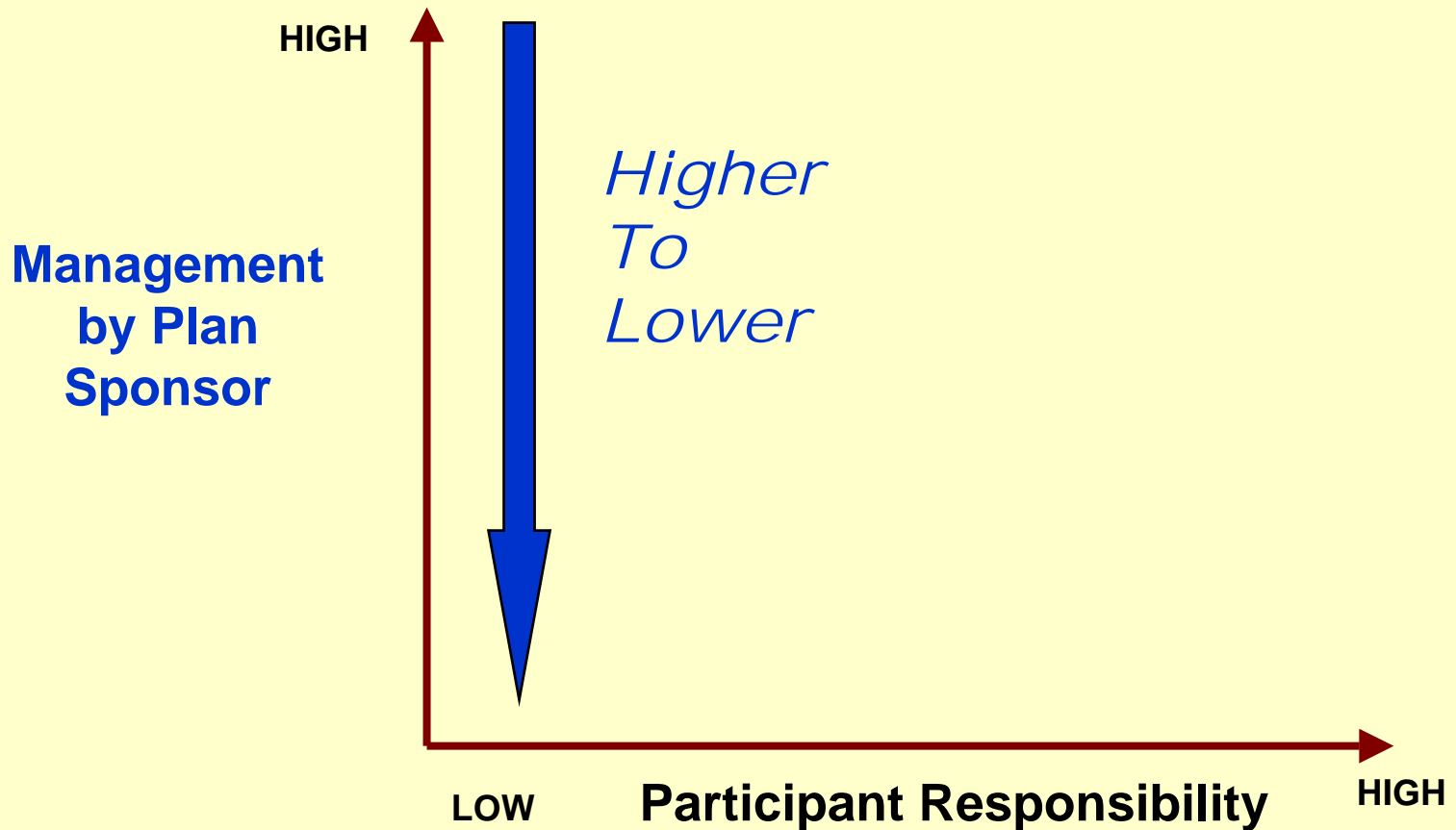
- Several ways to array range of DC plans
 - Level of employer management
 - Market in which coverage is purchased
 - Degree of financial risk born by employer
- Our continuum reflects the level of employer/sponsor management
 - And reflects the level of employee responsibility as well



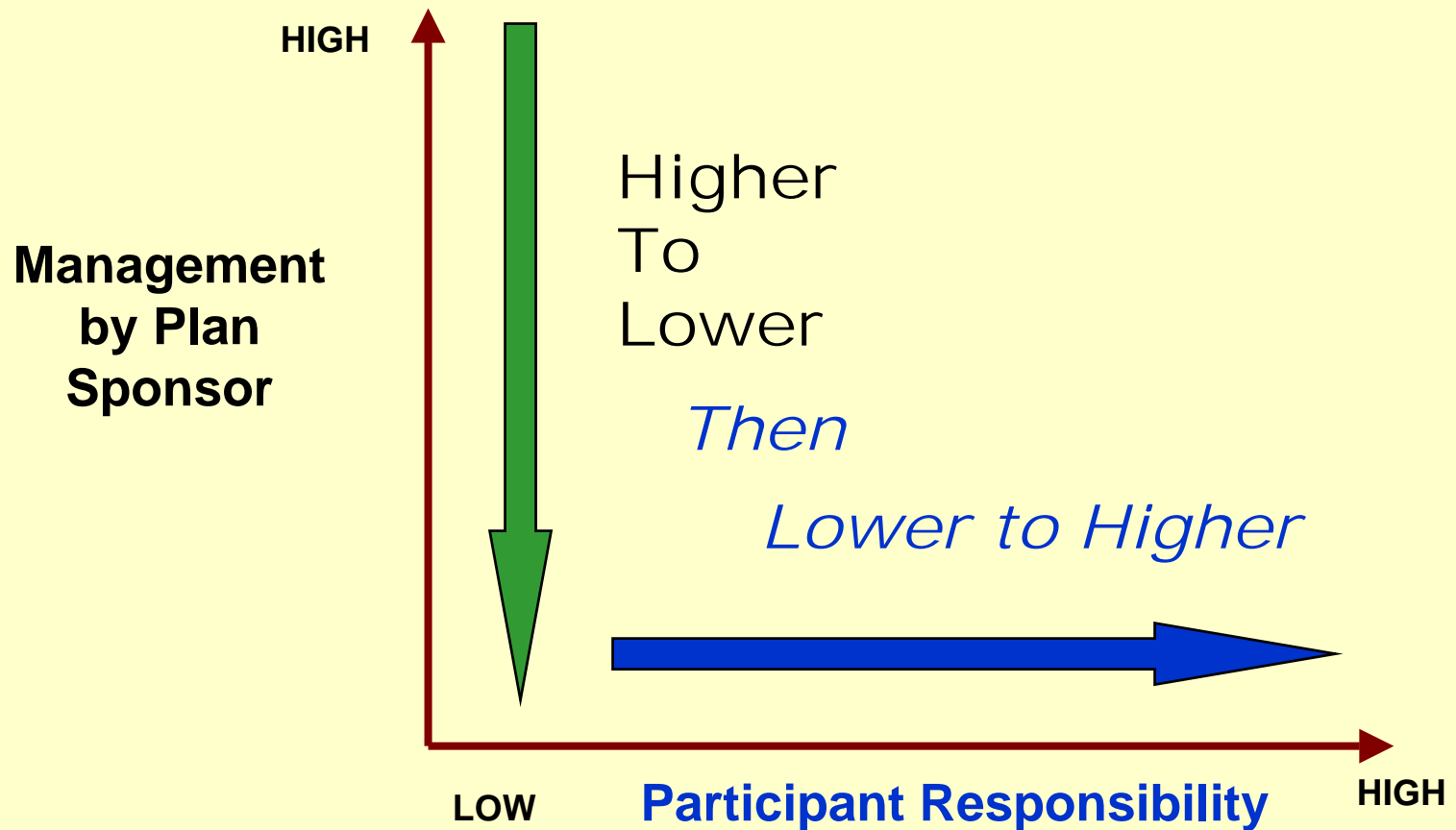
The DC Health Plan Continuum



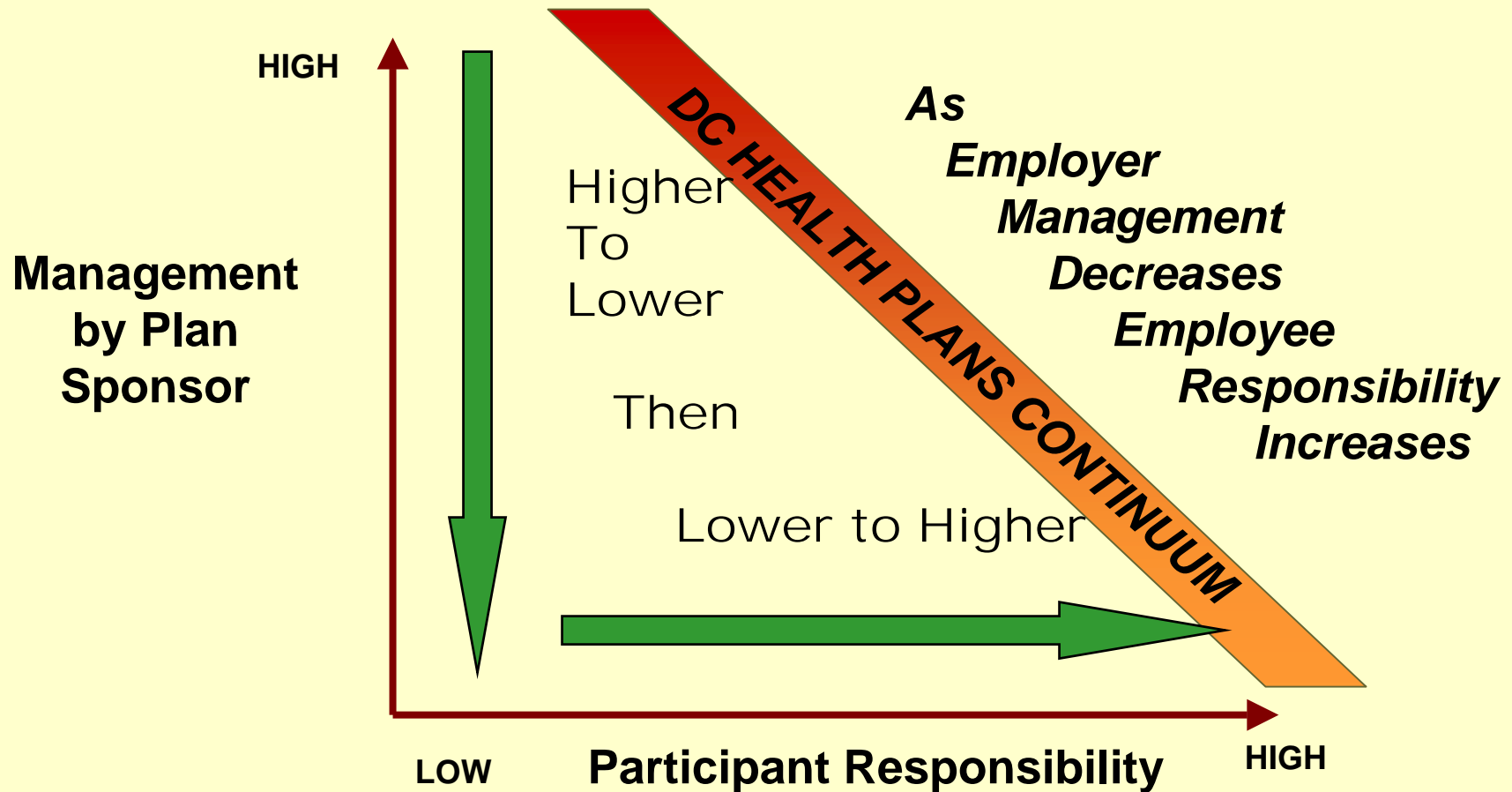
The DC Health Plan Continuum



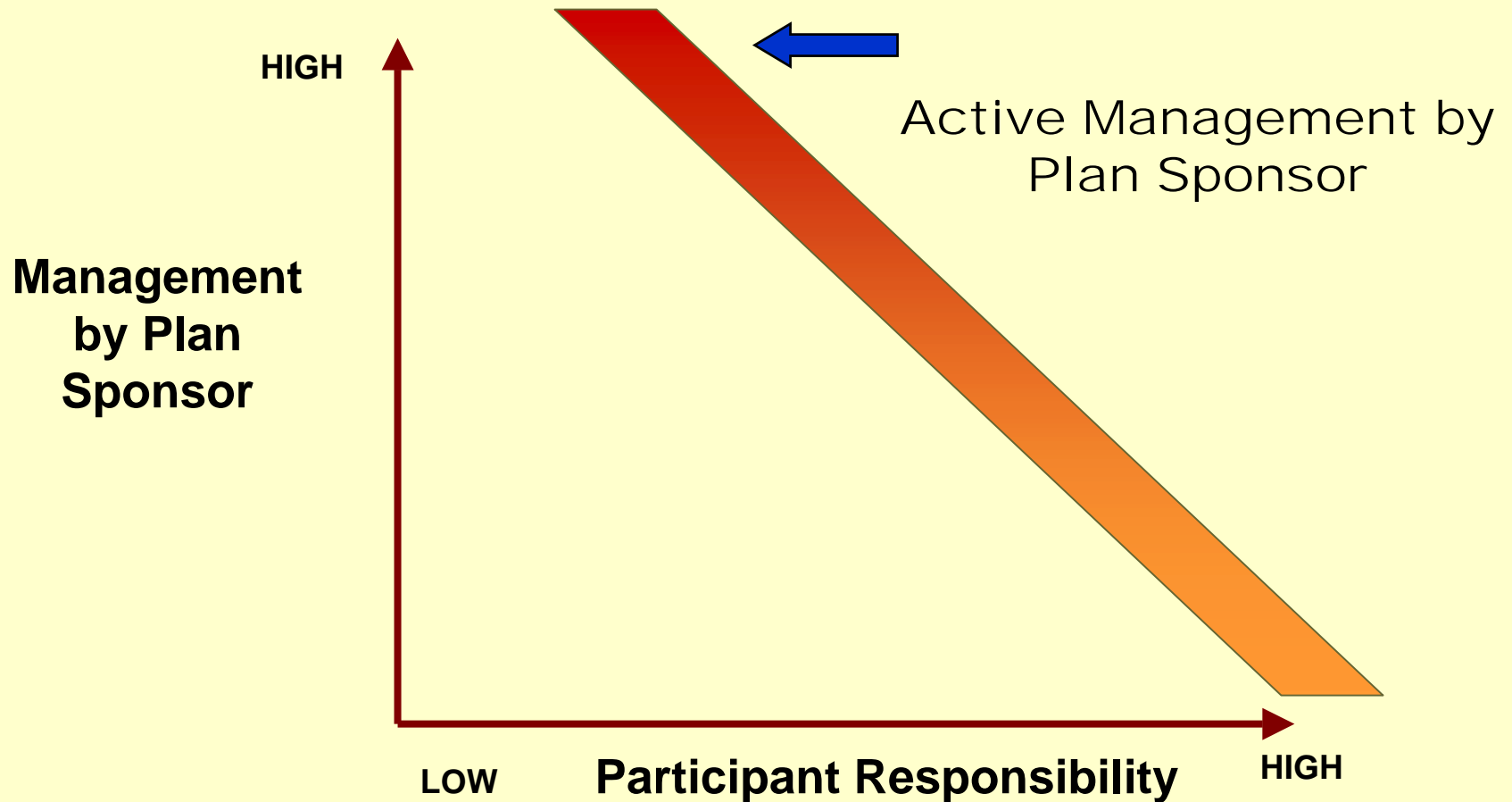
The DC Health Plan Continuum



The DC Health Plan Continuum



The DC Health Plan Continuum



Active Management by Plan Sponsor

- Similar in many ways to a DB health plan or perhaps a cafeteria plan
 - The sponsor
 - Determines and offers a limited number of benefit plan options
 - Sets maximum contribution
 - The participant
 - Chooses a plan option
 - Pays the difference between cost and sponsor contribution



Active Management by Plan Sponsor

- Sponsors' plan contributions can be...
 - Pre-determined budget
 - The cost of the lowest-cost plan
 - Vary contributions based on tenure, family status, or salary
 - To encourage the selection of certain plans



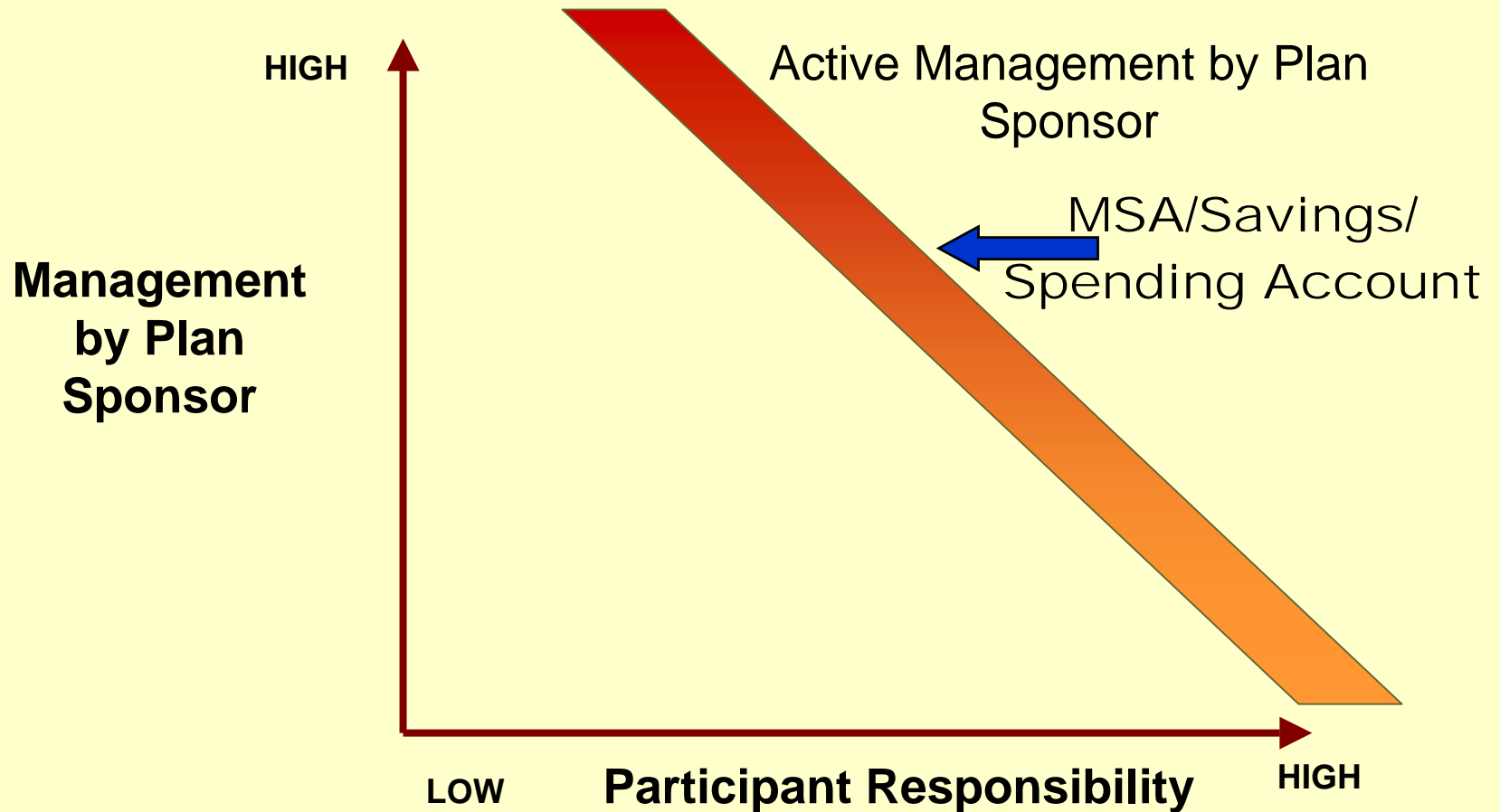
Active Management by Plan Sponsor

An alternative:

- Sponsor offers a list of recommended plans
 - The sponsor may have arranged for discounted premium rates
 - Recommendations may reflect plans' service, premium rates, or some quality measures



The DC Health Plan Continuum



MSA/Savings/Spending Account

- The participant has an “account” to use to purchase health care
 - High-incidence, low-severity health services
 - Year end balance usually can carry forward
- The plan includes an insurance component
 - High-severity, low-incidence health services
- Provide participants incentive to more actively participate in health care process
 - thereby leading to more efficient decisions



MSA/Savings/Spending Account

- The three types of accounts vary by whether cash or notional dollars are used, and whether they are tax advantaged:
 - MSA accounts use cash dollars and are tax advantaged
 - Savings accounts use cash dollars but are not currently tax advantaged
 - Spending accounts use notional dollars instead of cash dollars and are intended to result in tax treatment similar to traditional DB plans

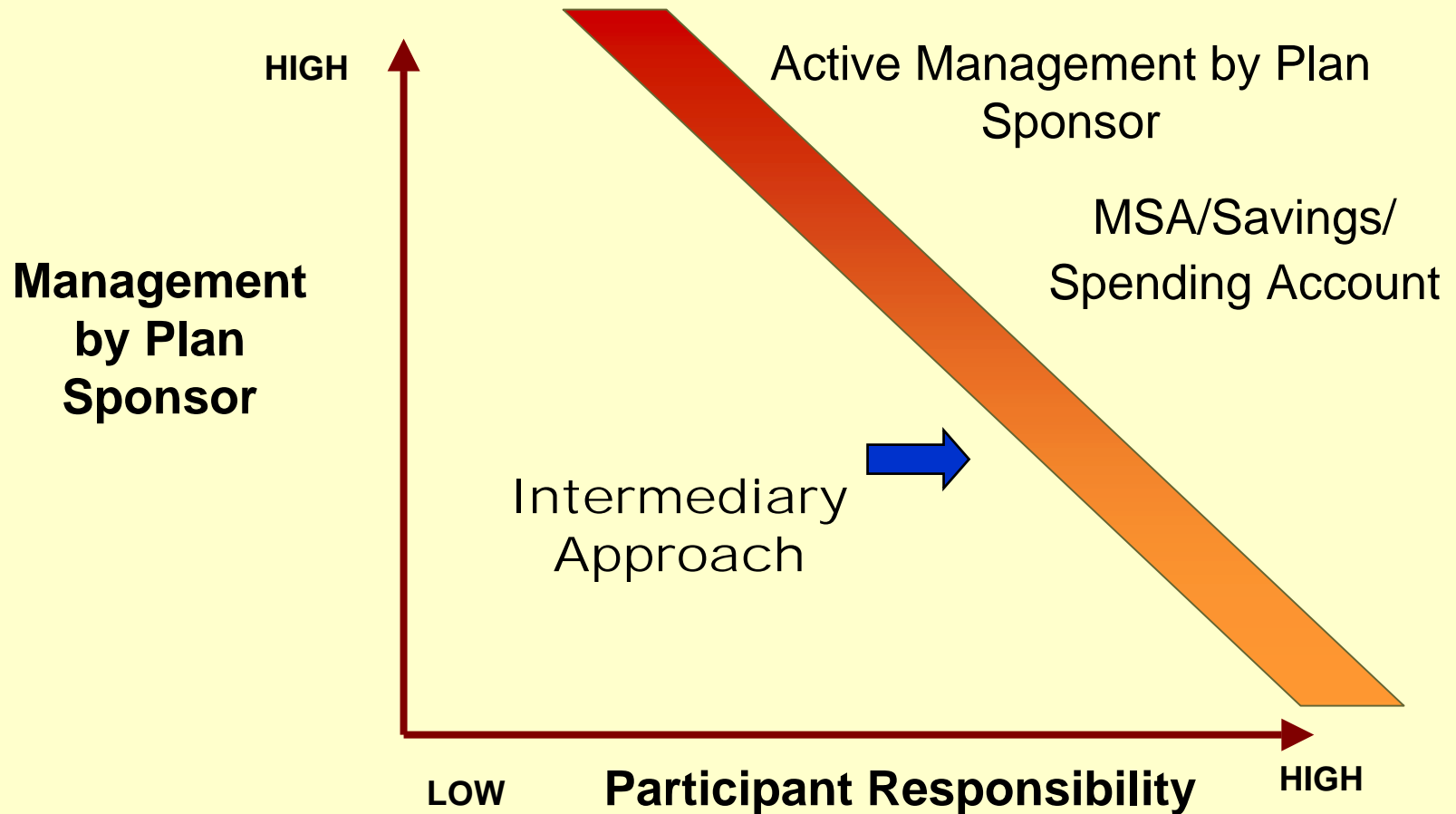


MSA/Savings/Spending Account

- Some issues to be addressed
 - Funded or notional account? If funded, who funds the account / Investment options?
 - Tax implications to the sponsor or participants
 - deposits, distributions or interest earned to and from the account?
 - Are tax advantages related to health care benefits portable beyond the year of coverage, and do they carry into new employment situations or into retirement?
 - What expenses are eligible for reimbursement from the account?



The DC Health Plan Continuum



Intermediary Approach

- Sponsor transfers its management role to an intermediary
 - Insurance carrier, employer coalition or independent organization
 - One or multiple sponsors may use same intermediary
 - Intermediary sets rules and offers choices

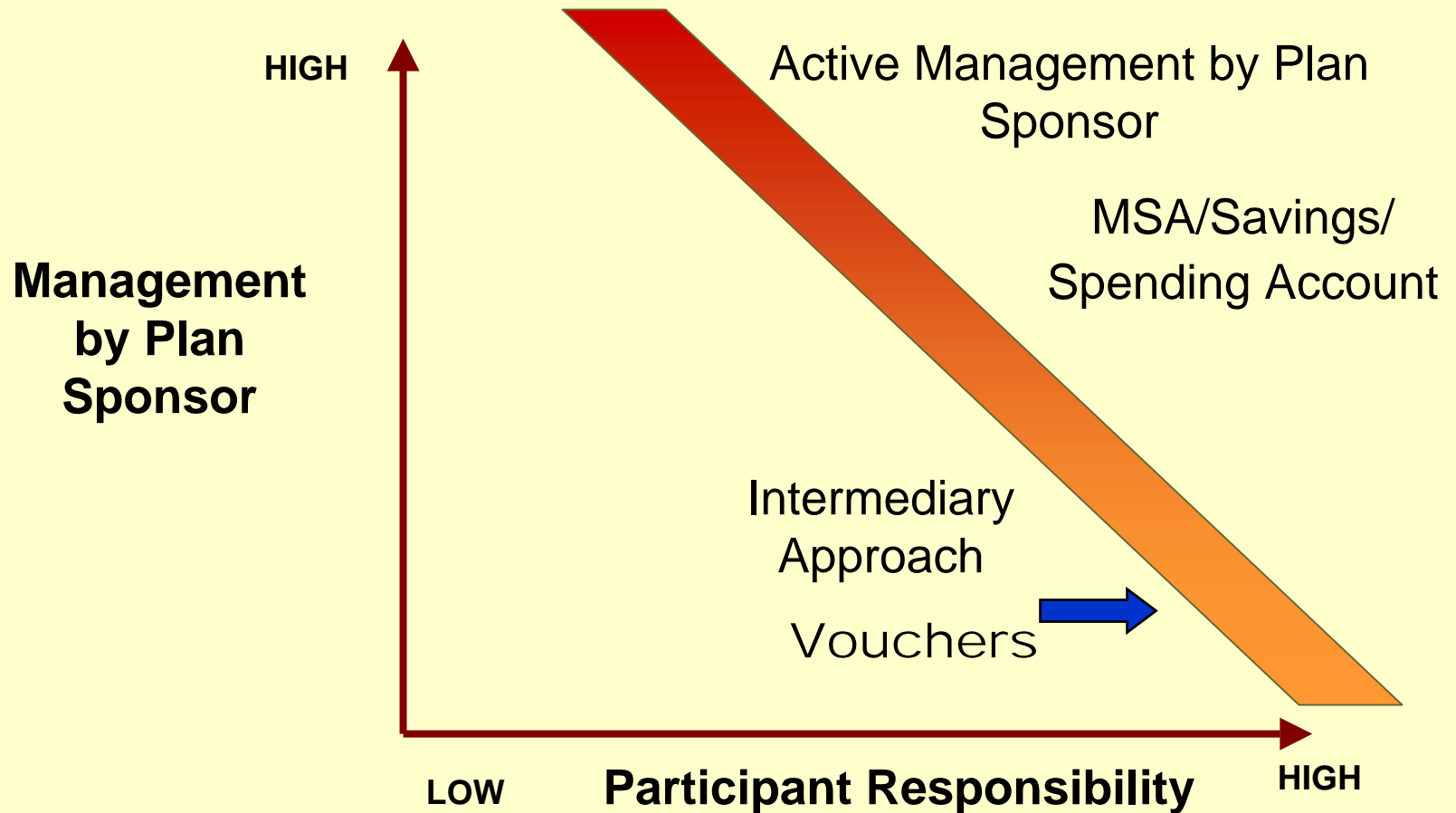


Intermediary Approach

- Intermediary models
 - One carrier offering multiple benefit choices
 - An intermediary offering a number of health plan options
 - An intermediary that contracts with or facilitates access to individual providers
- These intermediaries may provide tools to compare costs, quality of care, and the benefits offered under various options



The DC Health Plan Continuum

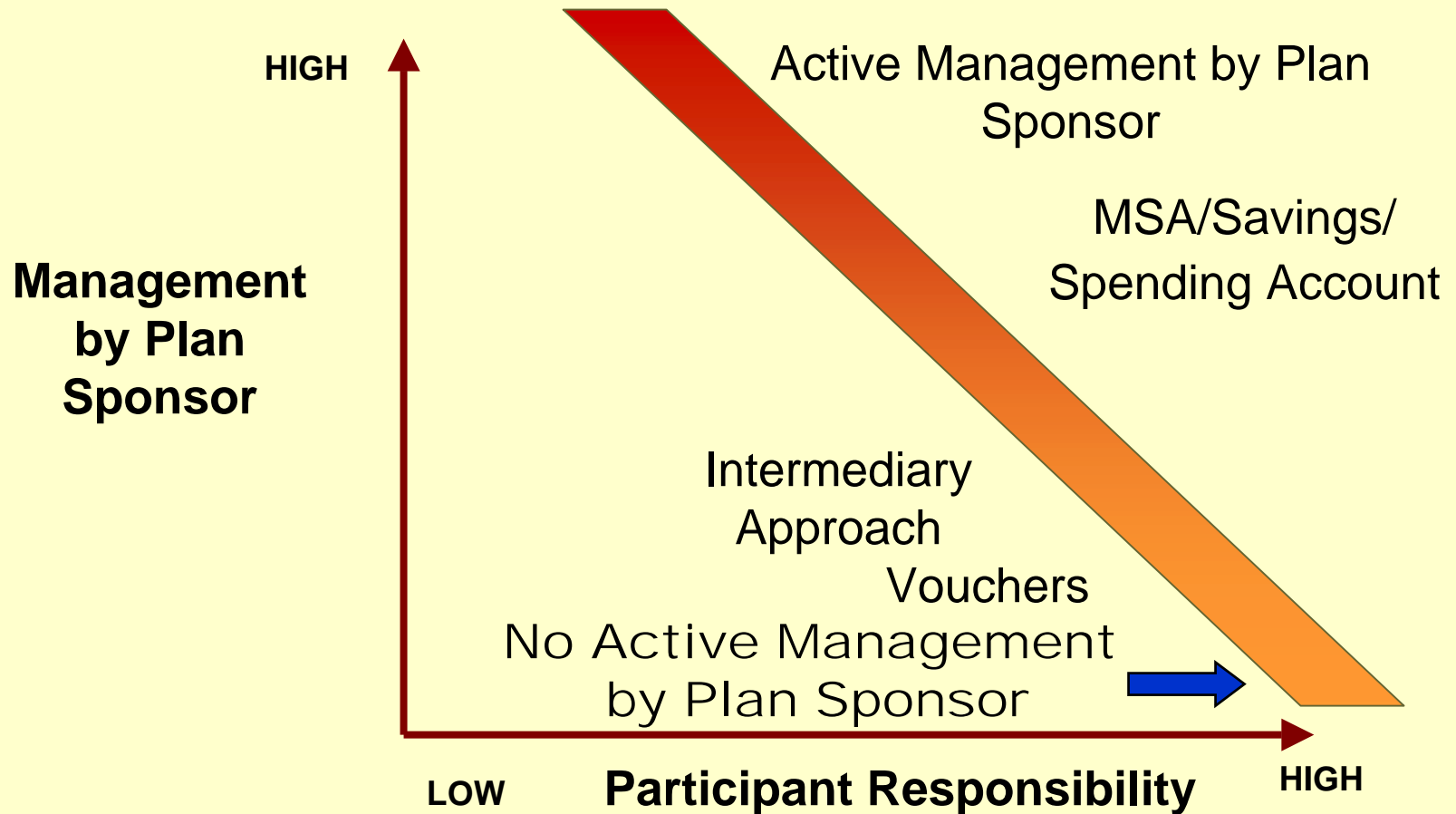


Vouchers

- The sponsor grants vouchers to participants for purchase of health care
 - Choice from among a pre-defined selection of participating benefits/plans (group or non-group)
 - The selections may be from within one health plan or from among more than one health plan
 - The participant pays the difference between the plan cost and the voucher amount
 - Unused voucher balances are forfeited



The DC Health Plan Continuum

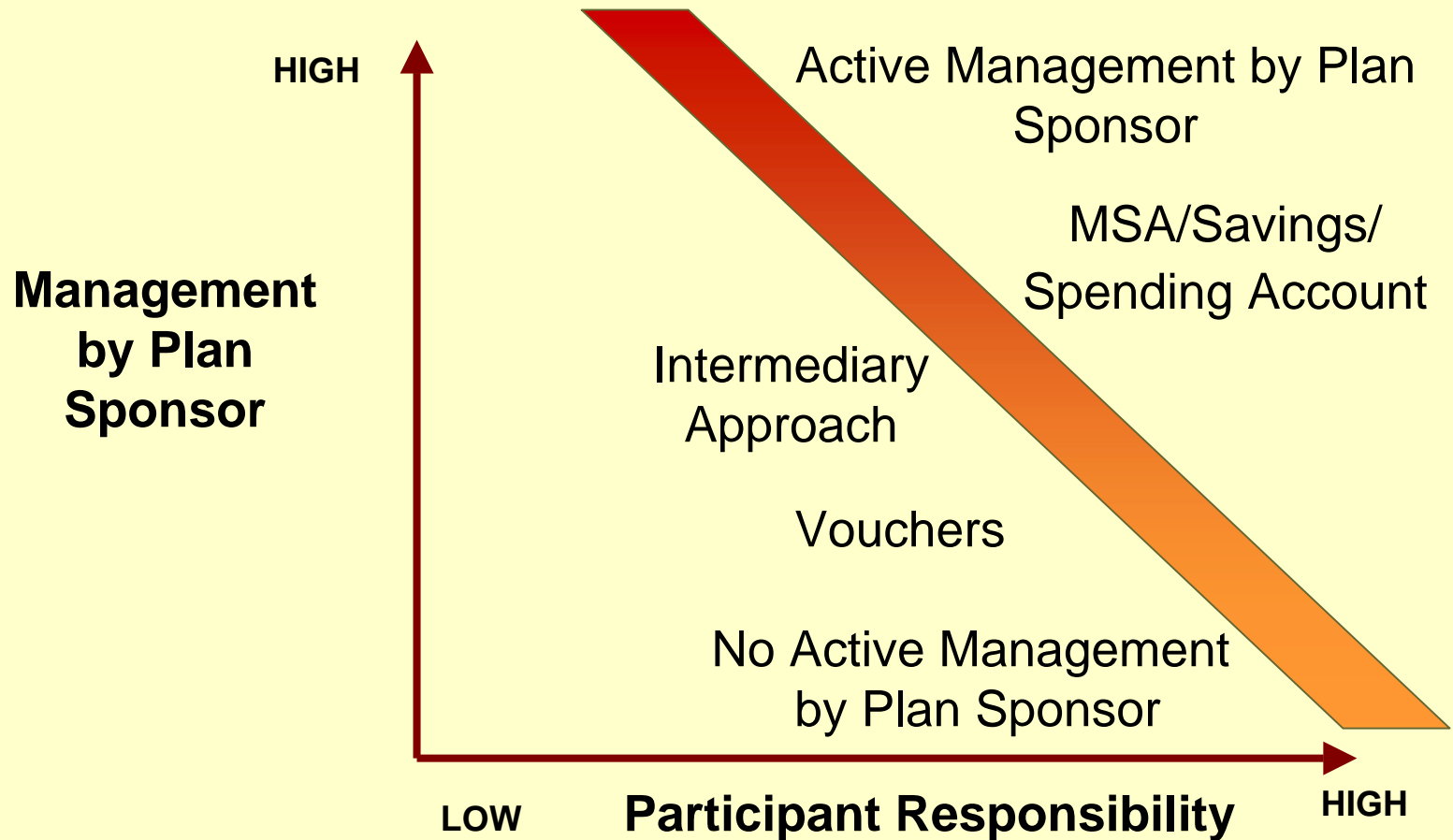


No Active Management

- The sponsor pays a pre-determined dollar amount to the participant intended to be used for health benefits
- It is then up to the participant to purchase individual health insurance in the local marketplace



The DC Health Plan Continuum



Objectives of DC plans

- Better educate employees about the true costs of health care services
- Begin to get employees more involved with the management of their own health care
- Attempt to stabilize health care costs



Issues & Challenges

- Tax treatment
- Contribution strategy
- Anti-selection
- Education



Conclusion

- What we know.
- What we don't know.



Evaluating the Cost Effectiveness of HRA Products

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Principal, Reden & Anders Ltd.

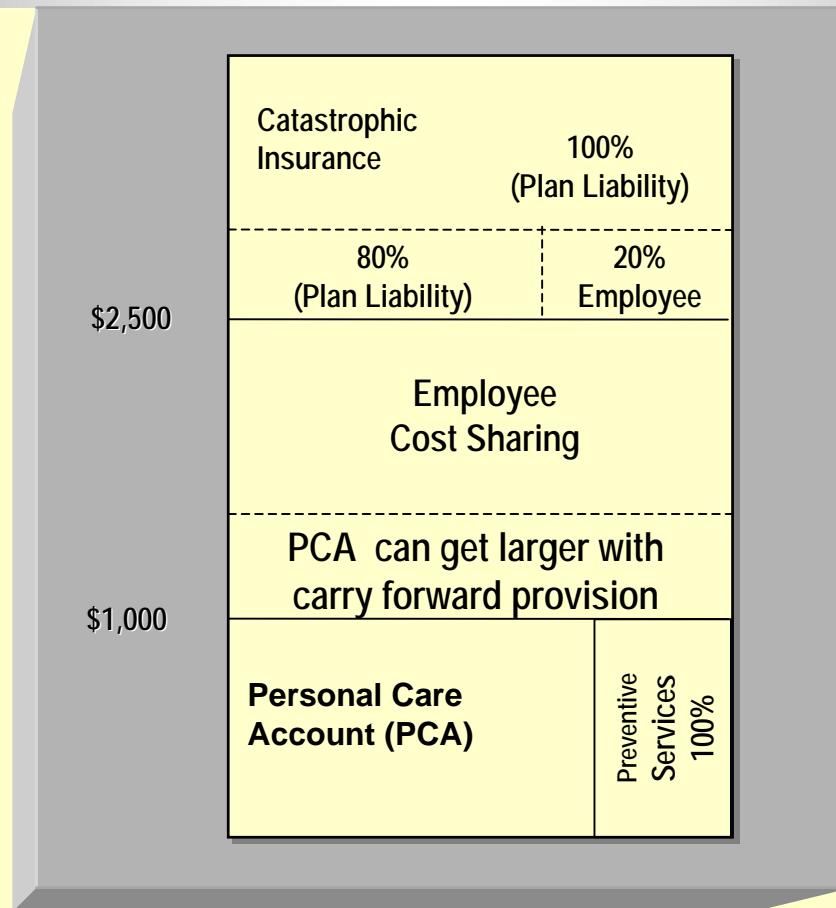


Common Business Objectives of Health Reimbursement Arrangement (HRA) Products

- Produce lower cost trends by:
 - Rewarding consumers who actively manage their medical care by creating greater benefits (but at a lower cost).
 - Offering lower benefits to those consumers who do not take an active role in managing their medical care.
- Educate the consumer through use of technology:
 - On how much health care costs.
 - Evaluate quality between providers.
 - How they can better manage their own medical care and health.



Basic Structure of HRA Product



Product Design Characteristics That Influence Costs

- Level of PCA by contract (Single, Double, Family):
 - New employees
 - Change in life status
- Level of catastrophic insurance coverage:
 - Deductible
 - Coinsurance
 - Maximum out-of-pocket
- Eligible services covered by PCA.



Product Design Characteristics That Influence Costs (cont')

- Carve-outs to PCA and insurance.
- PCA carry-over and forfeiture provisions.
 - At termination
 - At retirement
- Carrier replacement vs. multiple option offering.
- Regulatory issues/restrictions.



Other Items That Influence Costs

- Employee turn-over.
- Long-term impact of carry-over provision:
 - Incremental benefit.
- Long-term impact of high deductible
 - Leveraging of health care costs
- Paid vs. future unpaid obligation of employer from PCA.
 - At termination.
 - At retirement.
- Adverse selection in multiple option.
- Measuring potential impact of consumer decisions on utilization of services and shift in providers.



HRA Product Pricing Model

The purpose of this model is to:

- Evaluate the long-term cost impact of a HRA product.
- Determine which consumers will likely benefit from this product (versus existing coverage).
- Determine the level of PCA balances over the long-term and percentage of contracts having balances.
- Explore potential impact of selection between products.
- Analyze the impact resulting from consumer decisions.



Illustrative Benefit Design

	HRA	PPO (In-Network)
<i>PCA</i>		
Single	\$ 750	N/A
Double	1,100	N/A
Family	1,500	N/A
<i>Deductible</i>		
Single	1,500	\$200
Double	2,200	300
Family	3,000	500
<i>Coinsurance (Plan Liability)</i>	80%	80%
<i>Maximum Out-of-Pocket</i>		
Single	2,500	1,000
Double	3,500	1,500
Family	5,000	2,000

Approximately same benefit value.



Comparative Cost Analysis

Definitions

- HRA Liability – Total of claims paid from HRA and insurance plus value of remaining unused HRA balance.
- HRA Claims Paid – Total claims paid from HRA and insurance.
- PPO Standard – Representative of paid claims for employer's PPO plan currently in force.
- 3-Year Employees – Employees present for all three years of the analysis.

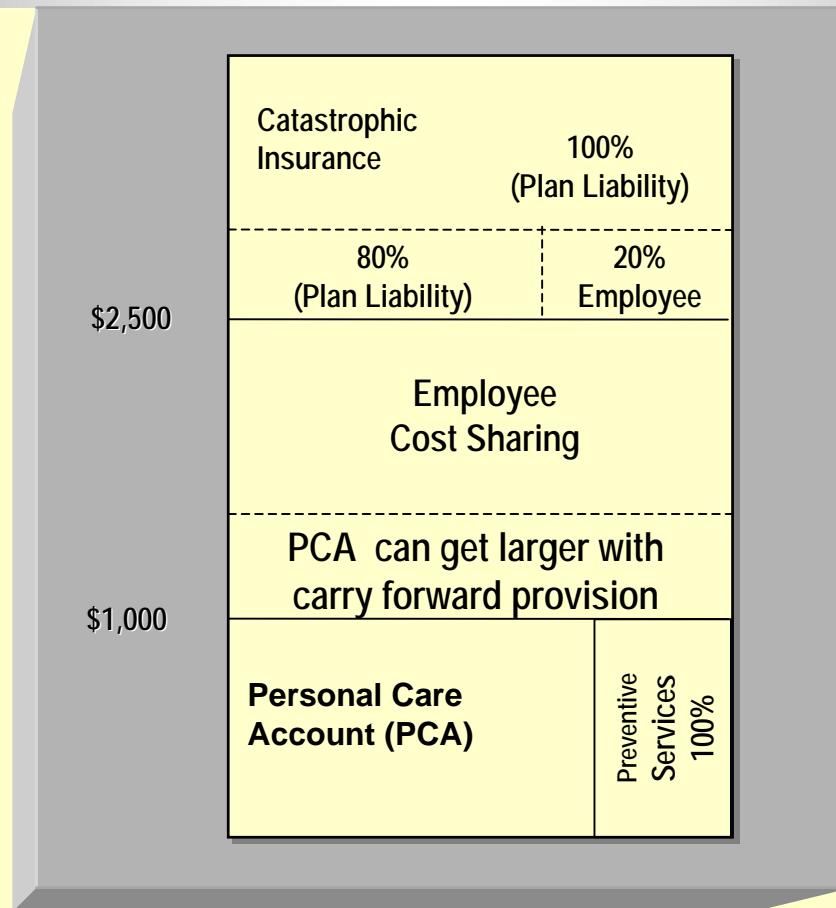


Average “Future Obligation” of HRA (Unused Balance)

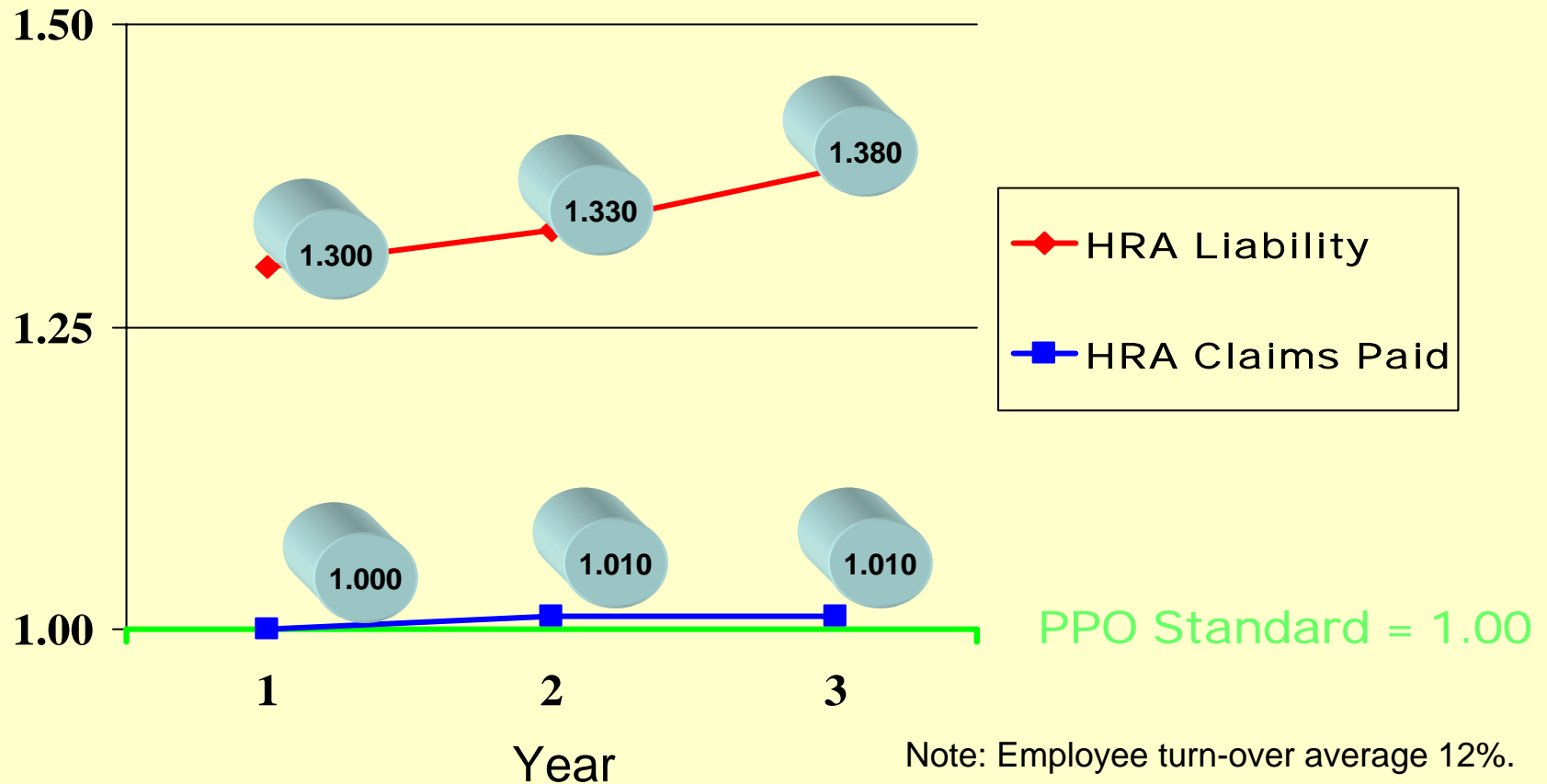
All Contracts with HRA Balance					
	Employee Cost- Sharing	Year 1	Year 2	Year 3	# Contracts
Single	\$ 750	\$ 664	\$1,089	\$1,415	73%
Double	1,100	904	1,351	1,651	56%
Family	1,500	1,189	1,718	2,132	55%



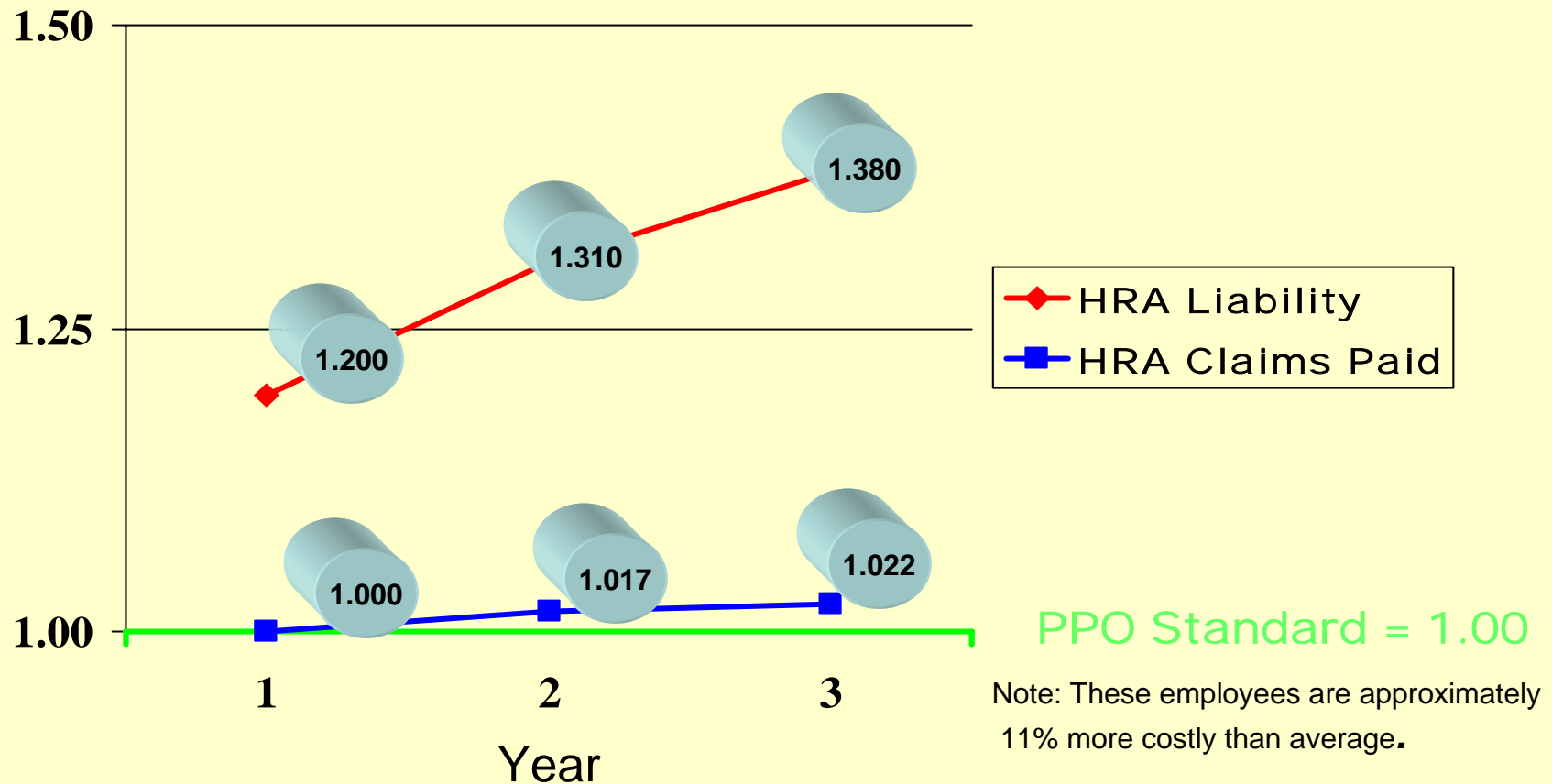
Basic Structure of HRA Product



Comparative Cost Analysis – All Employees

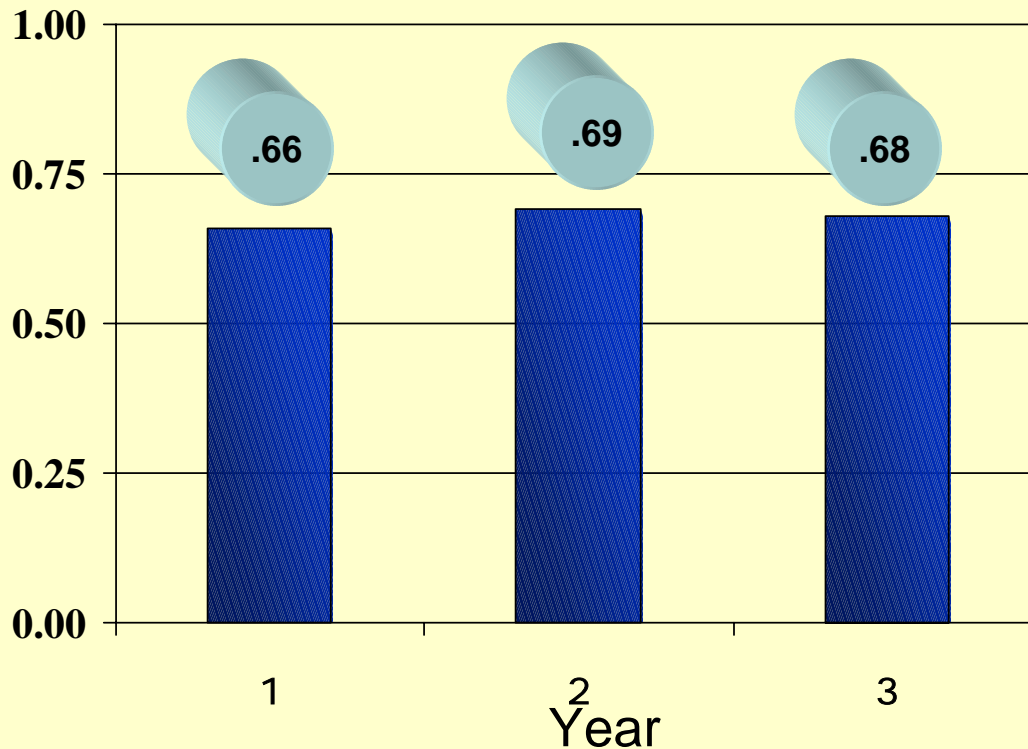


Comparative Cost Analysis – 3 Year Employees



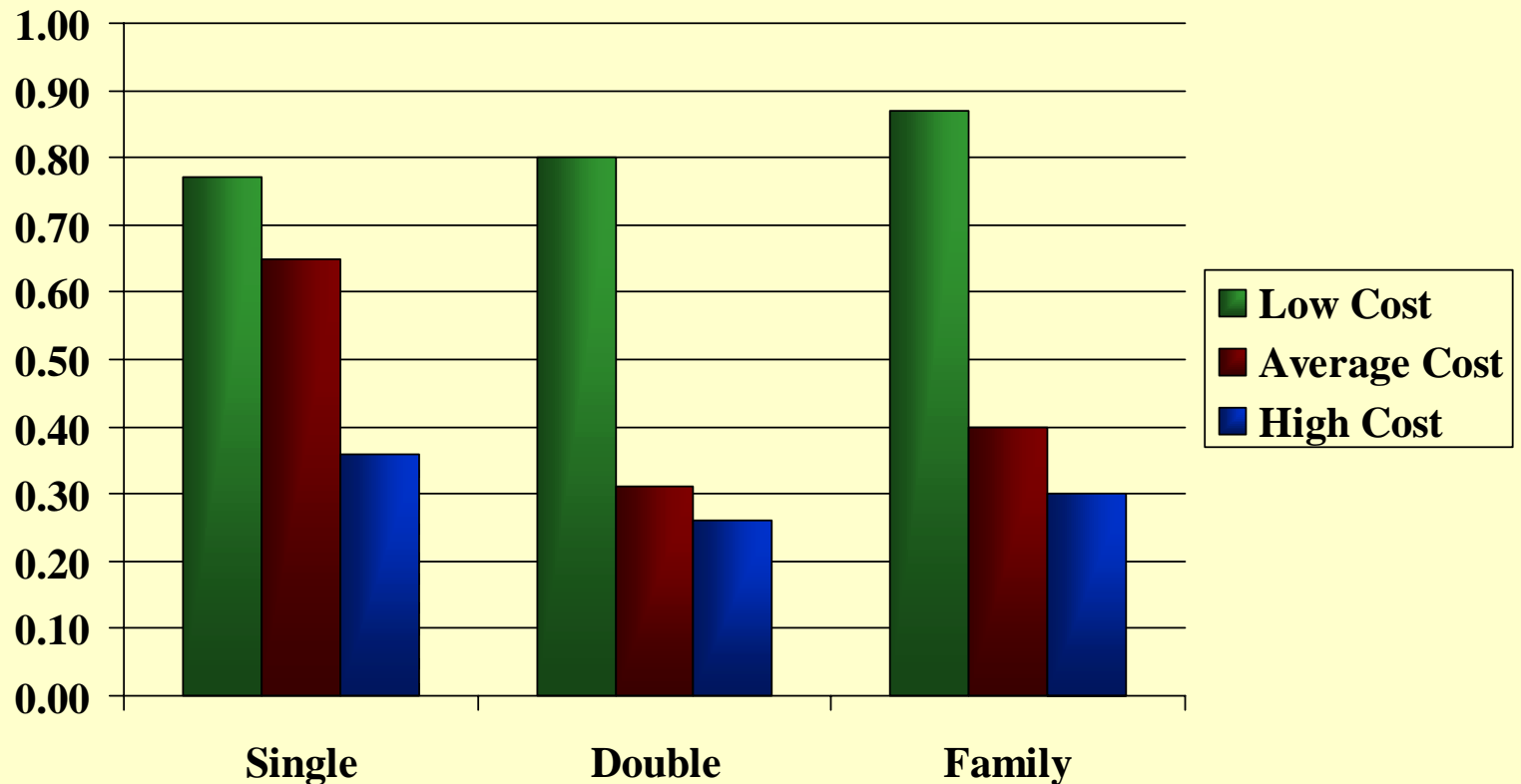
Percentage of Employees Who Are Better Off - OOP Expense Viewpoint

% Where OOP Expense Lower under HRA vs. PPO



Percentage of Employees Who Are Better Off - OOP Expense Viewpoint

% Where OOP Expense Lower under HRA vs. PPO



Average 3 years based on health status and contract type.

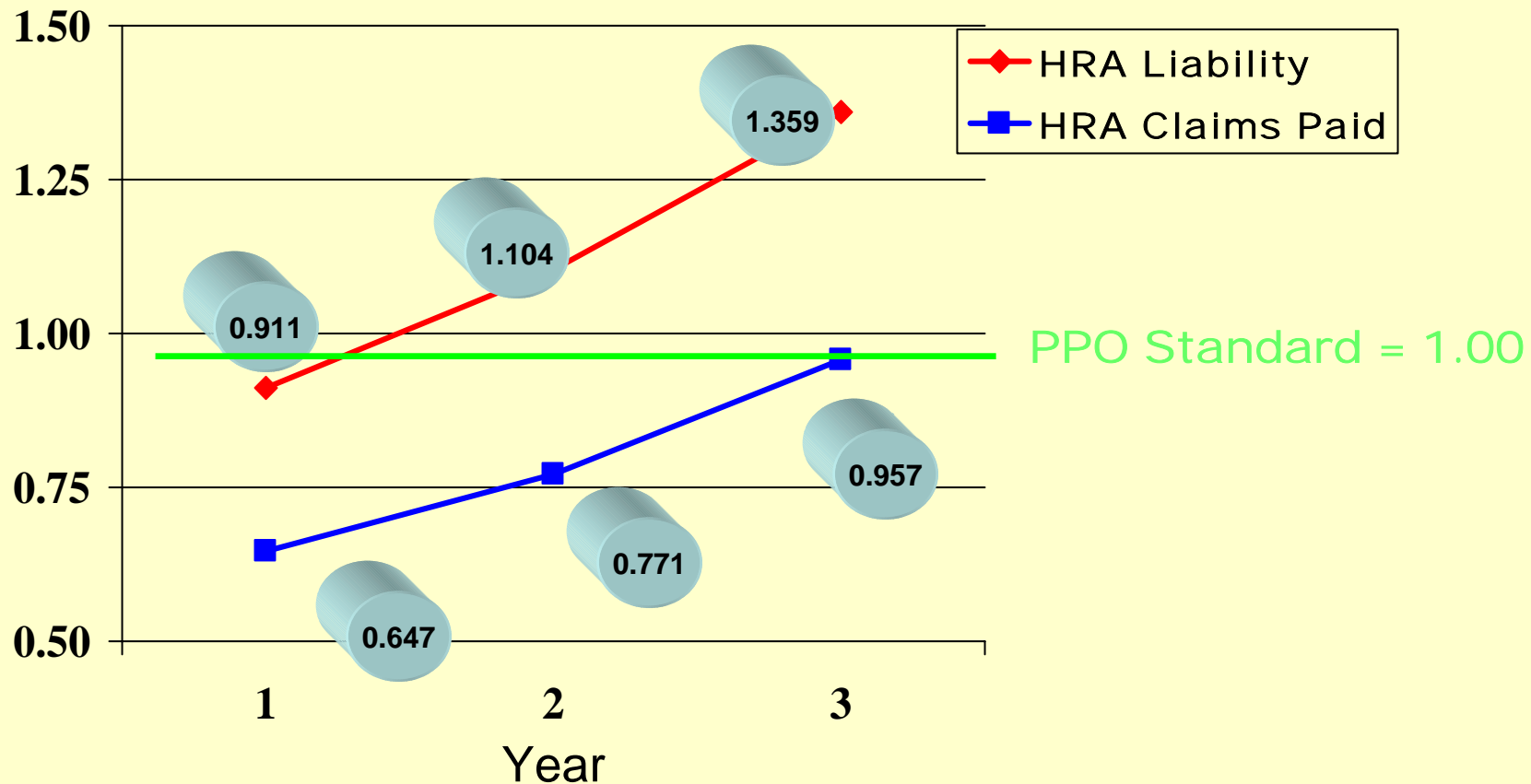


Enrollment Assumptions for Multiple Offering Scenario

<i>Percentage Enrolled:</i>		
Contract Type	PPO	HRA
Low Cost	75%	25%
Average Cost	90%	10%
High Cost	95%	5%
Overall	81%	19%



Comparative Cost Analysis with Selection



Key Observations from HRA Modeling

- If start from same equivalent benefit, over time the HRA product may have a higher trend rate due to leverage of PCA roll-over.
- The HRA should start at a benefit level 5%-10% below current PPO plan, if one of the objectives of the employer is to reduce costs.
- Employee turnover has a large impact on products' long-term cost.
- “Future obligation” of HRA pushes total potential liability significantly above PPO.
- If additional services covered by HRA, total cost to employer would increase.



Key Observations from HRA Modeling (continued)

- Those who benefit most are employees with lower medical care costs on average (equity issue).
- When offered in multiple setting, adverse selection will likely occur.
- Wild card is impact of consumer decisions on health care costs.



Early Feedback from Existing HRA Products

- Emerging experience indicates:
 - Lower frequency of routine office visits.
 - Lower frequency of Rx.
 - Greater percentage of generic Rx.
 - Minimal impact on large cost cases.
- Product design variation:
 - Multiple HRA product offerings with increasing cost-sharing.
 - Integration of employee funded FSA within HRA product (FSA used first).



Early Feedback from Existing HRA Products (continued)

- Keys to success:
 - Valid and comparable quality/cost measures (standardization).
 - Effective modes of communication.
 - Enough financial incentives for consumer to be active participant.
 - Consumer acceptance of concept and ownership in health behavior.



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