Employee Benefits Report

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Why Consumer-Driven Health Plans Are Growing in Popularity

The National Compensation Survey (NCS) found the average cost for a private employer to provide health insurance rose from $1.03 per hour worked in 1999 to $2.00 per hour in 2009, an increase from 5.4 percent to 7.3 percent of total compensation.

Employees have watched their share of healthcare costs soar as well. The NCS estimates that average monthly premiums paid by private industry workers increased from $67.57 (single coverage) and $264.59 (family coverage) in 2004 to $92.43 (single) and $349.36 (family) in 2009.

The squeeze is driving some companies to withdraw health benefits altogether and some employees to opt out of health insurance.

Consumer-driven health plans (CDHPs) have emerged to help ease the financial strain on employ-

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This Just In…

Health spending rose to a record 17.6 percent of the U.S. economy in 2009, the last year of record, as the overall economy shrank and higher federal Medicaid spending helped to push up health costs.

According to the federal government's number crunchers, the U.S.'s total health spending rose four percent in 2009 to $2.49 trillion. That was the smallest percentage increase in the last half-century, owing to the recession.

Still, health spending took a greater share of the economy— up one percentage point from 16.6 percent in 2008—because gross domestic product shrank 1.7 percent in 2009.

Feds amend grandfathered health plan regulations to permit insurer changes. The amendment permits certain changes in insurance policies, certificates or contracts for providing coverage under group health plans without the loss of grandfathered status.

Specifically, the amendment provides that a plan does not cease to be a grandfathered plan merely because the plan or plan sponsor entered into a new policy, certificate or contract of insurance after March 23, 2010. A permissible insurance change includes both a contract with a new insurer and a new policy issued with an existing insurer. For details, please see P. 4.

ers. These plans give employees more control over their health-care expenditures and incentives to control costs. One of the most popular CDHPs is the health savings account (HSA) combined with a high-deductible health plan (HDHP).

In a typical arrangement, an employer places a sum of money each year into an HSA for each employee, who can use funds to pay medical expenses. To qualify for an HSA, an individual must have a high-deductible major medical policy.

Lower premiums make CDHPs a popular choice among employers. According to a recent study published by the National Business Group on Health and Towers Watson, 2 percent of companies with 1,000 or more employees offered CDHPs in 2002, while 54 percent of these companies offered these plans in 2010.

Three advantages

A few things set this type of CDHP apart from traditional coverage. The first is the rollover. Employees can carry over any unused balance in their HSA from year to year. Over the years, savings can build to provide a substantial cushion from high medical expenses. Employees can even use savings to fund health-care in retirement.

Moreover, HSAs are portable. Individuals can take their HSA balances with them when they change employers, withdraw from the workforce or retire.

And perhaps most attractive, health savings accounts are triple tax advantaged — tax-free when contributed; tax-free as they grow (funds can be invested); and tax-free at withdrawal (whether one day after the money is deposited or 20 years later) when used to pay medical expenses.

Downturn causes uptick

The recent economic downturn may increase the prevalence of these plans. In a 2010 Mercer survey of private employers, 46 percent of respondents said they would make more cost-saving changes to their health plans in response to the economic downturn. Twenty-two percent of respondents planned to institute a CDHP to curb cost increases.

Although employers like the cost savings, CDHP enrollees report a slightly lower satisfaction rating (52 percent) than traditional plan enrollees (66 percent), according to a study by the Employee Benefit Research Institute. Furthermore, only 45 percent of enrollees in CDHPs state that they would recommend their plan to friends or coworkers, compared with 55 percent of those in traditional plans. These figures suggest that employers should weigh health-care costs against employee satisfaction before deciding to switch to a CDHP.

For more information on high-deductible health plans and HSAs, and other CDHP options, please contact us.

Type of account	Pretax employee contribution allowed	Employer contribution allowed	Rollover allowed	Can participant invest fund assets?	If yes, what investments are allowed?	Linkage to HDHP required?
Health savings account (HSA)	Yes	Yes	Yes	Yes	Fund assets can be invested in any IRA instrument.	Yes
Medical savings account (MSA)	Yes, only if employer does not contribute. None, if the employer contributes.	Yes	Yes	Yes	Fund assets can be invested in any IRA instruments.	Yes
Health reimbursement arrangement (HRA)	No employee contribution allowed.	Yes	Yes	No	Funds may only be used for qualified medical expenses.	No
Flexible spending account (FSA)	Yes	Yes	No	No	Funds may only be used for qualified medical expenses.	No

401(k) Annuities: How and When to Use Them

The economic downturn has coupled with longer lifespans and higher medical costs to make running out of retirement income a real possibility for many workers. For this reason, many employers are considering adding annuity options to their 401(k) plans.

For years, many investors avoided annuities due to high expense ratios and other factors. While annuities still have disadvantages in some situations, today's annuities designed specifically for 401(k)s offer advantages for the right type of employee.

When a plan offers an annuity option, employees can direct all or part of their 401(k) contributions into annuities rather than into mutual funds, which are today's primary 401(k) investment choice.

Some plans offer variable annuities, which combine features of a securities product and insurance. Their value fluctuates according to the performance of mutual funds and investments chosen by the owner. During the savings, or "accumulation," phase, investments grow tax-free.

In some plans, participants can elect to have a portion of each contribution go toward the purchase of fixed-deferred annuities. As the name suggests, these annuities pay a fixed monthly benefit after the participant retires. Buying annuities over time in this manner reduces the risk of locking in a low interest rate.

Annuities also have uses when participants reach retirement age. At retirement, some participants "annuitize" a portion of the funds accumulated in their 401(k). In other words, they use this money—whether invested in mutual funds, stocks, etc.— to buy an annuity, rather than rolling it over into an IRA or drawing down funds gradually. The annuity provides a steady stream of payments for a guaranteed period, perhaps 10 or 20 years, or even until death.

What's more, some annuities provide a death benefit. If the annuitant dies before retirement, his or her beneficiaries receive the original investment or accumulated value, as specified in the contract. An insurance policy covers the guaranteed death benefit plus the rates of return and expense ratios that will be used in calculating future annuity payments.

Insurers typically offer variable annuities for 401(k) plans as a group annuity product and also provide administrative services. Participants invest their funds in a selection of sub-accounts or mutual funds.

Pros and Cons

Those who invest in annuities generally pay an additional layer of fees in exchange for the income guarantee. Depending on an individual's situation, the tax advantages of annuities may be redundant, since other investment vehicles, such as IRAs and 401(k) plans, also provide investors with tax-deferred growth and tax advantages. For these reasons, most investors will want to make the maximum allowable contributions to their IRAs and 401(k) plans before investing in a variable annuity.

So why are more employers introducing annuities to their 401(k) plans?

Insurers have addressed the perceived cost of annuities in recent 401(k) annuity products. Thanks to institutional pricing, they're of-

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ten cheaper than the annuities investors can buy on their own. They're also flexible, allowing employees to stop investing at any time or to sell their accumulated holdings with no surrender charges.

And today's 401(k) annuities have to pass the scrutiny of their retirement plan's sponsor, greatly reducing the odds of any mismanaged options entering the mix.

But there's still room for improvement. Annuities' drawbacks include weak to insufficient disclosure of certain features, such as costs and investment returns, which makes it difficult for consumers to compare different products.

Who benefits?

Today's annuities may be cheaper and more flexible, but just because they're available in a 401(k) doesn't mean they are right for every employee. Experts generally do not recommended annuities for someone who's 25 or even 30—younger workers should be invested 100 percent in equities. But annuities may be an attractive option for workers in their late 30s, 40s or beyond as a portion of a total portfolio. Annuities should not make up 100 percent of anyone's portfolio, even that of a retiree.

Bottom line: Look at expense ratios and all the fine print before adding annuities to your 401(k) offerings.

Educating Employees About Retirement Annuities

Before employees decide to buy a variable annuity, they should consider the following questions:

- Will you use the variable annuity to save for retirement or a similar long-term goal?
- Are you investing in the variable annuity through a retirement plan or IRA (which would mean that you are not receiving any additional tax-deferral benefit from the variable annuity)?
- Do you understand the features of the variable annuity?
- Do you understand all of the fees and expenses involved?
- Do you intend to remain in the variable annuity long enough to avoid paying any surrender charges if you have to withdraw money?
- If a variable annuity offers a bonus credit, will the bonus outweigh any higher fees and charges that the product may charge?
- Are there features of the variable annuity, such as long-term care insurance, that you could purchase more cheaply separately?
- Have you consulted with a tax adviser and considered all the tax consequences of purchasing an annuity, including the effect of annuity payments on your tax status in retirement?

Clarification:

In our February issue, we said that the law was unclear when a health plan loses its grandfathered status.

Amendments to regulations implementing the Patient Protection and Affordable Care Act issued after our editorial deadline clarified that certain changes in insurance policies, certificates or contracts for providing coverage under group health plans would not cause a plan to lose its grandfathered status.

Specifically, the amendment provides that a plan does not cease to be a grandfathered plan merely because the plan or plan sponsor entered into a new policy, certificate or contract of insurance after March 23, 2010. A permissible insurance change includes both a contract with a new insurer and a new policy issued with an existing insurer.

A plan will lose its grandfathered status when it: 1) Significantly cuts or reduces benefits, such as no longer covering care for diabetes or HIV/AIDS. 2) Raises co-insurance charges over those in effect as of March 23, 2010. 3) Significantly raises co-payments over those in effect as of March 23, 2010. Grandfathered plans can increase co-payments by no more than the greater of $5 (adjusted annually for medical inflation) or a percentage equal to the medical inflation rate plus 15 percent. 4) Significantly raises deductibles over those in effect as of March 23, 2010. Grandfathered plans can increase deductibles only by the medical inflation rate plus 15 percent. 5) Decreases the employer contribution more than 5 percent below the rate on March 23, 2010 for any tier of coverage. 6) Tightens any annual dollar limit in place as of March 23, 2010 or imposes a new dollar limit, unless the plan replaces a lifetime dollar limit with an annual dollar limit that is at least as high as the lifetime limit.

"Cadillac" Health Plans Get a Reprieve…For Now

The federal healthcare bill passed last year included a provision to add a 40 percent excise tax on so-called "Cadillac" health plans. What does this mean for your executive benefits?

A "Cadillac" or "gold-plated" health plan is a top-of-the-line health insurance plan, usually defined by the total cost of premiums, rather than what the insurance plan covers or how much the patient has to pay for a doctor or hospital visit. For this reason, Cadillac plans are often reserved for high-level executives and valuable employees.

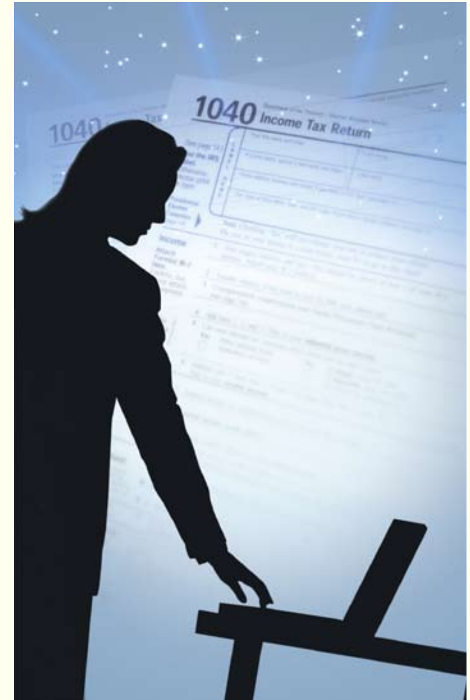
The federal healthcare bill passed last year included a provision to add a 40 percent excise tax on these high-cost plans. This provision had two goals: to generate revenue to help pay for covering the uninsured (the Congressional Budget Office estimates the tax would raise about $149 billion over the first 10 years), and to make the most expensive plans — which some argue encourage overuse of medical care — less attractive.

But the IRS has nixed the notion, at least for now. IRS Notice 2011-1, issued in January, provides that fully insured plans do not have to comply with the nondiscrimination rules until the IRS issues further guidance. Accordingly, a sponsor of a fully insured plan will not be subject to the excise tax penalty under Code Section 4980D and will not have to file IRS Form 8928 with respect to excise tax penalties for years before the IRS issues the regulations.

In providing the delay, the IRS cited the lack of comprehensive regulatory guidance. In addition, the IRS highlights the need to determine how to apply the nondiscrimination rules starting in 2014, when employees will be able to purchase health insurance under the state exchanges.

What does that mean for employers that offer Cadillac plans to certain employees? Continue as usual.

And that's good news because an analysis released by the Congressional Budget Office predicts that in 2016, 19 percent of workers who have insurance through the workplace would fall into the high-cost category. ■



Give Your Dental Plan a Checkup

There's more to selecting the "right" dental plan than just the premium. Here are some factors to consider as you evaluate a dental plan proposal.

1 How does the plan cover preventive services? Look for one that pays 100 percent for preventive maintenance. Services such as cleanings and fluoride treatments can prevent more serious and costly dental problems down the road.

2 What are the UCR reimbursements? UCR, which stands for usual, customary and reasonable, applies to your plan's reimbursement schedule. UCRs are almost invariably lower than actual fees, so look to see what your plan pays for various procedures and compare them to what dentists in your area charge.

3 Does the policy have an annual limit? Nearly all dental insurance plans put an annual limit on benefits paid; limits can vary widely.

4 Does the policy have a lifetime benefit limit? Lifetime limits are the maximum the insurance company will pay for a particular procedure over the life of the policy. Many insurers put a lifetime limit on orthodontic treatments, for example.

5 What are the deductibles and co-pays? Does the deductible apply on a per-family or per-individual basis?

6 Which dentists participate in the plan's network in your area? Consider how much your employees value choice of dentists. They may be willing to pay more in premium, coinsurance and other out-of-pocket costs if they can keep their current dentist.

7 How does the plan cover visits to out-of-network dentists? Some plans cover no charges from a dentist outside the network. Some will cover emergency care only and others may provide coverage but require higher co-payments from insureds.

8 Does the plan impose any waiting periods? Some plans have waiting periods before they will cover certain treatments. For example, employees might have to have coverage for six months before becoming eligible for orthodontic coverage.

9 What is the monthly premium? Understanding the other features of the plan can give you a better idea of whether you're getting a good value for your benefit dollars.

We can help you evaluate your dental plan. Please call us for more information. ■

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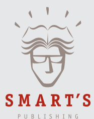

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