

# HIU

News and Tips for America's Benefits Professionals

HEALTH INSURANCE UNDERWRITER  
MARCH 2015

## NAHU'S LEGISLATIVE PRIORITIES

Trends in Voluntary Benefits

FSAs and PPACA

The Truth about Private Exchanges

# THE TRUTH ABOUT PRIVATE EXCHANGES

Opinion by Scott M. Wood  
Principal, Benefit Commerce  
Group  
Scottsdale, AZ  
scott@benefitcommerce.com



There have been a lot of articles that make private exchanges appear to be inevitable or necessary—that they are going to solve the problems of healthcare for employers. This article will explain why that is just not so.

- Are private exchanges...
  - ...cheaper? No.
  - ...easier? No.
  - ...better for employees? No.
  - ...sustainable? No.

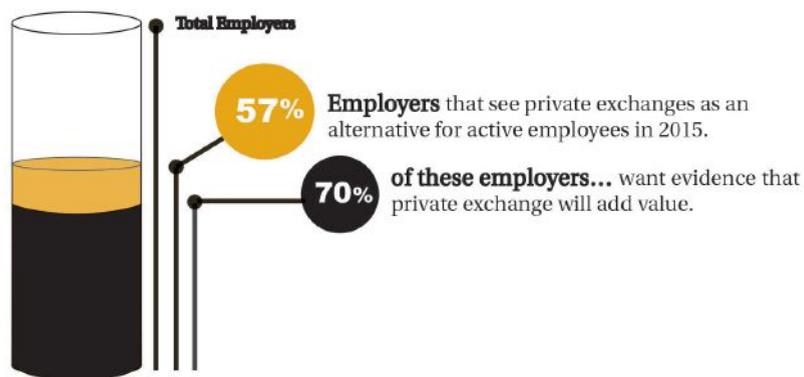
## WHO'S TALKING?

Have you noticed that all the articles that paint private exchanges in a favorable light are written by people/organizations that are selling their own private exchanges?

During the past couple of years, various “studies” have shown that a large percentage of employers “plan to” move to or are “studying” private exchanges.

Actual adoption of private exchanges is only a small fraction of what these projections would lead one to believe.

### Towers Watson 2013 Health Care Changes Ahead Survey:



### Private Exchange Evaluation Collaborative 2013 survey of 700 businesses

Reuters interviews with industry executives found no major U.S. company signed up for the first time with a private

exchange for 2015. These employers are waiting for “proof that the new exchanges will save them enough money to warrant

the switch, raising doubts about this new business model.”

Brian Marcotte, chief executive of the National Business Group on Health (NBGH), an organization that represents more than 50 million employees, said, “We have a lot of wait-and-see going on with large employers. They are not quite sure yet how they will deliver on managing costs better.”

Dan Mendelson, chief executive of research firm Avalere Health, said, “Private exchanges were over-hyped from the beginning.”

He added: “Large employers enjoy significant leverage in negotiating down the price of benefits for the many members of their workforce, an advantage that an exchange can’t match.”

Jon Loftin, MJ Insurance president and COO, said in a recent interview that his firm launched its private exchange in the spring of 2014 and had one client enrolling for January 1, 2015.

Troy Alstead, chief operating officer of Starbucks, told Reuters that the company had studied private exchanges to understand them, but has never planned to move its 136,000 employees. “What we tended to learn is that what we do is just easier and better for people,” he said.

In an October 2014 blog bswift noted that there is “most likely less than five-percent adoption for active employers for midsize and large employers.”

So when you sort through who’s saying what and what’s really happening, it’s clear that there is no groundswell for private exchanges. All the frantic activity has been on the supply side of the equation, not the demand side.

Why?

- Employers can see that there is no real case to be made for them. Private exchanges do little, if anything, to address the underlying root cause of our real healthcare problem: rising health plan costs.
- Once employers get past the buzzwords and hype, it becomes clear that private

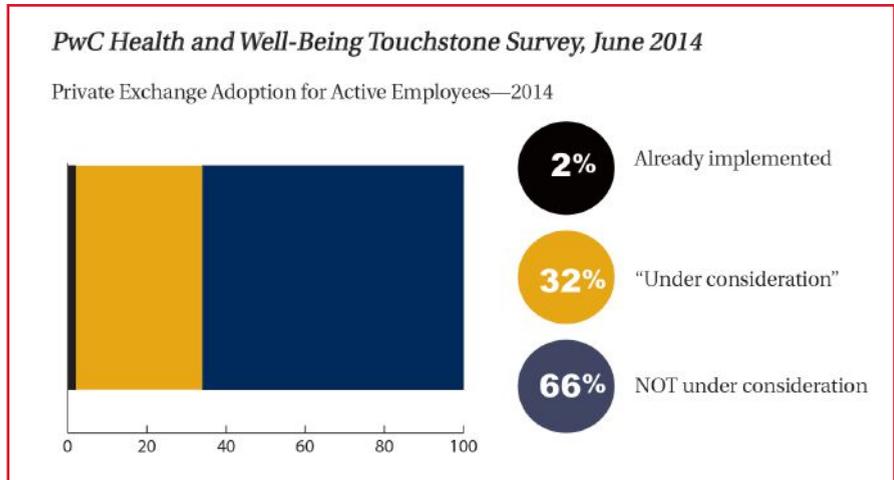
exchanges are not the cure-all that their sellers are promoting.

When you distill this down, employers are looking for their broker/benefits consultant to be an objective advocate. Many of the brokerage agencies that now have their own private exchanges have converted their brokers into product salespeople rather than consultants.

reviewing carrier offerings, shopping and comparing rates and plans, then offering choices to employees.

If consumers are not already getting this kind of program and support, they should be looking for a different benefits consultant.

At this point in time, most private exchanges have been focused on very large employers. That’s because:



**WHAT IS A PRIVATE EXCHANGE ANYWAY?**

There is a lot of confusion about what defines a private exchange. In most cases, a private exchange means:

- Setting a budget (some call this a defined-contribution)
- Plan selection and choice
- Easy enrollment

All of this is woven together through an online system that may include some decision-support tools.

If this sounds a lot like a recycled version of the cafeteria plan concept that dates back to 1978... that’s because it is.

A private exchange is merely a repackaging of the current offerings, with a big emphasis on the technology of the transaction. Employers are still engaged in the same process they were before healthcare reform:

- Most multi-carrier exchanges require 2,500-plus employees and risk-share arrangements between carriers.
- Large employers in industries such as restaurant/hospitality see private exchanges as a convenient way to offer benefits to lower-wage, lower-hour employees who had not been offered coverage before.

Single-carrier private exchanges are much the same as what employers are now offering to their employees. However, if a wide range of plan choices is offered, costs on plans can increase due to adverse selection.

**IT’S ABOUT A COMPREHENSIVE STRATEGY**

The hard truth is that there is no silver bullet for containing healthcare cost increases. However, that doesn’t stop people from trying to make it sound like it can be simple. For the last 30 years, we all have seen a long

## OPINION: PRIVATE EXCHANGES

line of “solutions” (some would call them gimmicks) that have been promoted as silver bullets.

Here are just a few:

- Capitation was going to save health insurance because it put the doctors at risk. But employees realized that their doctors were now looking at them as “expenses” instead of “patients,” so that fizzled.
- Gatekeeper plans were going to ensure that unnecessary specialist utilization would be eliminated. But employees got tired of playing “Mother may I?” with their physicians, so those fizzled.
- Community rating has been tried over and over again, as a way of pooling employers for their protection. But those in the “good half” of the pool quickly realize they are overpaying to subsidize the other half. This is once again likely to be unsuccessful under new PPACA requirements.

The list goes on and on.

Private exchanges are simply the latest version of the elusive “silver bullet” offering a false promise of a solution.

The fundamental question facing employers is: Do you want to solve your problem or do you want to ignore it?

The truth is: The employers that have been successful in controlling their health plan costs—and encouraging health and wellness among their employees—are those that use some or all of the following:

- a knowledgeable benefits consultant
- alignment of economics for the employer and employees
- running their health plan like a business by developing a strategy
- consumer-driven health plans
- wellness programs that work for their specific employee culture
- employee education throughout the year, not just at open enrollment

- incentives
- engagement of employees and their families
- Accountable Care Organizations/narrow

or theory for strong cost-reducing advantages from exchanges is not available.”

In addition, this analysis raised serious cautions about the defined-contribution concept: “. . .if total health insurance

### Private Exchanges: What They Can and Can't Do

CAN:	CAN'T:
Provide a defined contribution strategy on a benefits administration platform	Provide long term solution to rising total healthcare costs
Assist some employers with large groups of non-traditional employees: part-time, seasonal, retirees	Transfer ERISA fiduciary responsibility away from employer
Shift costs to employees, especially in future years, if employer does not substantially increase defined contribution	Hide the cost-shift to employees
Help improve employee communication channels on an integrated platform	Replace the value of face-to-face employee meetings and employer activities to promote healthcare consumerism – to reduce the underlying cost of healthcare
Offer multiple benefit plan options	Access multiple carriers in mid-market

networks

### COST SAVINGS

Although some private exchanges are being marketed to employers as a way to reduce costs, the only clear way that costs—for the employer—would be reduced is by setting a defined-contribution amount and not increasing it as costs inevitably increase. This would create a massive cost-shift to employees.

A defined-contribution funding structure “enables an employer to de-link their future cost increases from the underlying medical trend that they may experience,” said Eric Grossman, a senior partner at Mercer, in an interview with *Forbes*.

With a large cost-shift to employees, the employer’s benefit/total compensation package becomes less valuable, and the employer may begin to lose its best talent to competing employers.

In an independent economic analysis of private exchanges 10, the employer affordability feature was found to be “largely illusory.” The report also stated that “evidence

premiums fluctuate as expected, moving toward a defined-contribution model will subject the worker to much of the cost of the excess premium growth and to the consequences of unpredictable fluctuations in premiums. The benefit to the employer is therefore achieved only by imposing a cost on the workers. At a minimum, workers will probably require higher money wages to compensate. That may be larger than the expected savings and it will be taxable income for workers.”

Simply put, an employer implementing a defined-contribution approach creates a leveraged trend impact to employees and families that translates to an exponential cost-shift.

### WHO DOES BENEFIT FROM PRIVATE EXCHANGES?

It seems clear that the private exchange model may be a way for large insurance agencies and insurance companies to lower their cost of doing business and sell more

insurance, which can lead them to improved margins.

In addition, many of the insurance companies that have launched private exchanges have been focused on moving large employers from self-funded to fully insured. The fully insured model is necessary because of the increased breadth of plan choice, complexity of administration and risk-share issues.

However, it is also important to know that insurance companies' profit margins, in general, are about 4.5 times higher for fully insured lives than self-funded lives.

For insurance companies, the move to private exchanges can be a huge windfall. Even if they lose members in the transition, the higher profit margin for fully insured lives can result in a net gain.

### THE PROBLEM WITH TOO MANY CHOICES

One of the selling points of some private exchanges is that employees will have a wide choice of plans and can “right-size” their benefits.

However, there is little empirical evidence that greater choice makes for better decisions.

You only have to attend one employer open-enrollment meeting to understand that the health plan decision is a difficult one for employees. Even with ample educational materials, most employees spend very little time making their health plan decision.

One survey showed that employees believe that choosing healthcare benefits is more difficult than purchasing a car, making decisions about medical tests or treatments, parenting and selecting other forms of insurance.

As employers consider the health plan choices they want to provide to their employees, they also should determine the communication and educational information that will be needed and plan for this. New types of choices can be phased in, with communication that helps employees understand why the choices have changed

and why they may need to do more than just “keep what they had before.”

Human resources staff also will have additional burdens with private exchanges, as they must get themselves educated and up-to-speed on a larger number of plan choices. The HR responsibilities will expand as they have to help guide employees through any issues and concerns.

Insurance can be confusing, and most employees appreciate that their employers work with benefits professionals to design and select their options. In addition, when employers and benefits consultants work together, they can choose health plans designed to provide the benefits their employees need with cost-containment and consumerism aspects to control costs. Top-quality benefits consultants also can analyze data and negotiate aggressively with insurance companies for their clients.

As we all move forward, there will be more responsibility for day-to-day health and healthcare choices by individual employees, while employers are focused on establishing choices and wellness programs to promote health and well-being.

### OTHER PITFALLS

**Potential loss of self-funding savings.** When private exchanges are elected, many self-funded employers are pressured to move to a fully insured basis in multi-carrier exchanges. This eliminates for them the economic and other beneficial factors of self-funding. In most cases, self-funding saves employers 10% or more on health plan costs.

**Fiduciary responsibility.** While some employers want to believe that moving to a private exchange is akin to totally outsourcing their health benefit plan, it does not remove their fiduciary responsibility. Nor does a private exchange avoid the reporting and other compliance requirements of PPACA.

**Employer responsibility for employee health and well-being.** Employers that are the most effective with strategies for con-

taining healthcare costs and promoting the well-being of their employees also typically have healthier workforces. With a hands-on approach to plan design and by educating their employees on consumerism, these employers can reduce absenteeism, improve presenteeism and lower the other costs related to employee health. The Gallup-Healthways Well-Being Index survey of 94,000 employees found 77% with chronic health conditions that related to total annual lost productivity of \$84 billion. 13 Many of these chronic conditions can be controlled with proper health and wellness programs.

**Due diligence.** With a private exchange, it is more difficult to conduct effective due diligence on vendors. Some private exchanges will not allow third-party consultants to review proposals and compare them against others in the market.

### COST CONTROL REQUIRES RESPONSIBILITY AND BEHAVIOR CHANGE

Those who have worked for some time in employee benefits understand that many plan changes to “control costs” are simply cost-shifting techniques. Increasing a deductible or coinsurance amount shifts more of the cost of healthcare to employees; it does nothing to reduce the total cost of healthcare services.

Only consumer behavior changes and lifestyle choices can actually impact healthcare costs. Helping consumers/employees to be responsible for their own well-being and healthcare AND providing them with cost-transparency programs and education on selecting healthcare services is the only proven way to truly control costs.

That is why high-deductible plans coupled with healthcare spending accounts (HRAs or employer-funded HSAs) can have a significant impact. Although these plans have higher deductibles, the accounts provide employees with part of the deductible amount as “their own” money to spend on healthcare. When it is their own money, employees

spend more wisely. They ask questions, search for providers by price and quality, and seek alternative locations and treatments.

Along with an increased understanding of their insurance benefits and the cost of healthcare services, the gradual process of educating employees can lead to additional employer-offered choices. For example, a menu of plans could allow employees to utilize a high-deductible health plan along with supplemental coverage for accidents, critical illnesses or hospitalization—to fill in the deductible gaps. In this way, the total benefit program provides more economical comprehensive coverage for high-cost catastrophic care as well as unpredictable events (accidents and critical illness) that may still fall within the deductible amount.

### CONCLUSIONS

Private exchanges are being pitched as a method to make employee benefits easier and less costly for employers: the employer merely selects a defined-contribution amount and the exchange handles everything. That rationale is short-sighted, simplistic and simply not true.

For most employers, healthcare costs are the second or third highest expense on the income statement. Given that fact, does it make sense to adopt a private exchange “solution” that will put more distance between the employer and the costly challenge of healthcare costs, at a time when the employer needs to be more involved, not less involved, in order to achieve more control?

Everyone agrees that the problem is the overall cost of healthcare. No one can point to how private exchanges will solve this problem. Unfortunately, many health plans are on a road leading directly to the Cadillac Tax in 2018. Employers need to be more involved, not less involved, in planning and containing costs in order to avoid this high excise tax.

When private exchanges don't reduce costs (and they won't), then what? How will an employer unwind the complex web the private exchange creates and get back to a strategy that can contain costs and improve the health and well-being of employees?

How will an employer deal with the collateral damage to employees of unwinding a private exchange? These include confusion, resentment at reduced entitlement and decrease in overall employee morale.

Will employers lose some of their best talent, as employees move to competitors who have retained stronger control over their benefits program?

Consider the similarities with workers compensation costs: Employers control their workers comp costs by emphasizing safety and making sure their employees are appropriately engaged. Healthcare costs are controlled by emphasizing health improvement and driving that same sense of employee engagement. A private exchange does not replace the need for this control and engagement.

Employers that are looking for the following should work with a knowledgeable benefits consultant that will help them develop a long-term comprehensive strategy for their health benefit plan:

- Cost control
- Employee engagement
- Health improvement
- Decision support
- Transactional services

A professional benefits consultant will tailor the employer's program to utilize education, communication, benefit administration and data analysis services that are right for each employer. [HIU](#)

### References:

- 2014 bswift Benefits Study: The Private Exchange Blog, October 27, 2014
- Towers Watson 2013 Health Care Changes Ahead Survey, Executive Guide to Health Benefit Exchanges
- Private Exchange Evaluation Collaborative, 2013 study; Business Insurance magazine: June 9, 2014
- Aon Hewitt 2012 survey, Corporate Health Care Exchange—The Time is Now: Rethinking Health Care Coverage
- “U.S. Corporate Health Exchanges Find No New Blue Chip Clients,” Reuters, December 15, 2014
- “Broker Beat Video Series,” Business Insurance magazine, December 1, 2014
- Results from the 2014 Inside Benefits Communication Survey conducted by the National Business Coalition on Health (NBCH) and Benz Communications
- PwC Health and Well-Being Touchstone Survey, June 2014
- “Private Health Insurance Exchanges Unleash ‘Transformational Change,’” Forbes, January 24, 2014
- “Private Health Insurance Exchanges,” Pauly, Mark V. and Harrington, Scott E., 2013, Health Management, Policy and Innovation, 1 (4):61-72
- Jay Godla, Partner, Strategy&, at AIS Virtual Conference: Private Insurance Exchanges—Bottom-Line Strategies for Insurers, November 12, 2014
- “Healthcare Benefits Second Most Difficult Decision for Consumers,” BenefitsPro cites Aetna survey
- “The Causes and Costs of Absenteeism In the Workplace,” Forbes, July 10, 2013
- “A Simple Fix? A Look at Private Exchanges,” Woodruff-Sawyer & Co. blog, June 2014

---

## THE LEGISLATIVE FRONT

*Continued from page 51*

University of California Berkeley Labor center found that 2.3 million workers are at risk of reduced hours due to the 30-hours provision in PPACA.

The revised expected enrollment total for 2015 was reduced by the CBO from 13 million to 12 million. Next year, CBO estimates that enrollment will total 21 million, down from 24 million that it previously anticipated. The bulk of the difference is expected to go to Medicaid instead of exchanges. As of January 23, just fewer than 7.3 million Americans had enrolled in coverage through the federal marketplace, with an additional 2.4 million signed up through the 14 state-based marketplaces for a total of 9.7 million. The Administration's revised goal for this year's enrollment was 9.1 to 9.9 million consumers enrolled through the federal marketplace. There are about 30 million Americans who remain uninsured, with roughly half of them qualifying either for subsidies or Medicaid, according to a recent Kaiser Family Foundation survey. [HIU](#)