Are CDHPs Here to Stay?

An overview of CDHPs, HSAs, and HRAs; their pros and cons; and current trends

National Employee Benefits Advisory Forum (NEBAF)

Methodology

The information presented in this paper has been compiled from multiple sources, including thought leadership studies and other material offered by and available on various stakeholder and industry websites.

Sources used are listed at the end.

Executive Summary

Consumer-Directed Health Plans (CDHPs) present employers with one strategy for managing rising health care costs. These somewhat controversial health care plans offer employers lower premiums in the short term, with the hope for slower cost growth in the long term.

This report examines what CDHPs are and how they work.

- CDHPs allow employees to be consumers of their own healthcare. Employees control when they see the doctor, what doctor they see, and how much they pay.
- These plans typically include high deductibles, lower premiums, a tax-advantaged spending account, and decision-making tools.
- The associated tax-advantaged account, usually either a 'Health Savings Account (HSA)' or a 'Health Reimbursement Account (HRA)', grows tax-free and unused balances can be rolled over at the end of the year.
- Employees can contribute to HSAs, but this is not the case with HRAs.

And, this report presents early research and trends on CDHPs.

- CDHPs are a growing trend. Reports among both employers and carriers indicate increased enrollment in CDHPs in the last few years, with a significant jump seen in the past year.
- Early reports also indicate that CDHPs cost less per employee than both PPOs and HMOs, and that, cost increases are substantially lower (or there might even be cost decreases) than compared to other coverages.

A New Strategy

The state of U.S. health care has been a hot topic in recent years, and the upcoming Presidential election has brought the U.S. healthcare system even further into the spotlight. In the last decade, the cost of healthcare has grown exponentially, with premiums almost doubling. Although the growth in premiums declined last year, it still outpaced inflation.

Employers more and more are challenged to control healthcare costs. One strategy that has surfaced is Consumer-Directed Health Care, and its associated health plans, also known as CDHPs (consumer-directed health plans). This relatively new term in healthcare got its beginnings in the 1990s, but only in the past five years has it become more mainstream, more widely known and more utilized.

CDHPs Aim to Promote Consumerism

A key goal of Consumer-Directed Health Plans is to empower employees to become consumers of their own healthcare. The logic of these plans is:

- Employees pay for their services directly, and therefore will be more financially involved and responsible for their healthcare.
- They will become more cost conscious because they decide how to spend their healthcare dollars and are able to save unused funds for the future.
- This cost-consciousness will motivate them to be more cautious with treatments, make better and more informed choices, demand better service, and utilize fewer unnecessary treatments.

With employees as consumers, healthcare would function more as a 'free market' system. Supply and demand would regulate costs, slowing cost growth, while competition would regulate the quality of care.

What are CDHPs?

Although the term applies to a broad range of health plan designs, CDHPs most commonly include three components:

- A high deductible health plan (HDHP) with lower premiums and higher deductibles.
- An associated tax-advantaged account to pay for medical expenses under the deductible, such as an HRA (health reimbursement account) or an HSA (health savings account).
- Decision-support tools to help enrollees evaluate treatment options, costs, providers, etc. and make their own decisions.

How much does Healthcare cost?

According to the United Benefit Advisors' (UBA) 2008 annual health study:

The average annual health plan cost per employee is estimated to be $7,327 (medical coverage only), with employers paying an average of $4,117 and employees paying the remaining $3,210.

Small Employers are Particularly Affected...

One recent study by the Kaiser Family Foundation indicates that small employers are dropping healthcare coverage all together in the face of rising health care costs; 68% of small companies surveyed in 2000 offered health benefits to their employees, but by 2007, that number slid to 59%.

Which is More Prevalent: HSA or HRA?

From a 2006 Government Accountability Office (GAO) study: In January 2006, coverage was just about even; 50% of those enrolled in a CDHP had an HSA, and 50% had an HRA. Yet, large employers are more likely to offer HRAs, while small employers are more likely to offer HSAs.

The number of enrollees and dependents covered by HSAs appears to be growing faster than those covered by HRAs.

Did You Know.... [1]

In 2007, the average annual employer contribution received by employees enrolled in a HDHP/HRA was $915 for single coverage and $1,800 for family coverage.

For those enrolled in HDHPs/HSAs, the average contributions were $428 for single coverage and $714 for family coverage.

And, many companies offering an HSA-qualified HDHP do not make a contribution to the HSA: about two-thirds for single coverage and about half for family coverage. [1]

In a typical CDHP model, individuals pay for healthcare expenses out of a savings or spending account (HRA, HSA or other payment product). After the savings account is depleted, individuals pay directly out-of-pocket until they reach their deductible, which is higher than those of other health plans. To qualify as a HDHP, a plan must have a minimum deductible of $1,100 or greater for single coverage, and $2,200 or greater for family coverage this year. These amounts are set by the U.S. Treasury and are scheduled to increase annually.

Because the deductible is high, the premiums are usually lower. Individuals may keep or 'rollover' any unused balance in their savings or spending account at the end of the year.

HSAs vs. HRAs

Together they are known as 'account-based plans' or 'savings accounts', but there are key differences in design, legal requirements, and incentives between these two types of tax-advantaged accounts.

Characteristic	HSA	HRA
Began in…	2003	2002
Who opens the account?	Employers and individuals	Employers only
Who can contribute?	Employers and individuals	Employers only
Who administers?	Financial or insurance institution	Employer, insurance carrier, or other third party administrator
Portable?	Fully	No
Tax advantages	Contributions can be made pre-tax or claimed as deductions, accounts receive tax-free interest	Withdrawals are tax-free (excluded from Gross Income), accounts receive tax-free interest
Can be carried over from year to year	Yes	Yes

For most HSA-based CDHPs, employees are not required to open and contribute an HSA. Total contributions (by all sources) to HSAs can't exceed a certain set dollar amount which is adjusted annually. This year the maximum contributions are $2,900 for an individual and $5,800 for a family. Enrollees may use accrued balances for non-medical purposes, such as retirement income, but they are subject to tax penalties.

[1] 2007 Kaiser Family Foundation/HRET Employer Health Benefits Survey.

Positives vs. Negatives

Proponents of CDHPs cite several benefits for employees:

- Lower premiums
- More control and choices over their own care
- Ability to save money for future use
- Tax benefits

Critics argue several negatives for employees:

- High deductibles that employees may struggle to pay
- Postponed care and/or less preventative care (it is feared this will more greatly affect low-income users)
- Lack of information and good decision-support tools, making it difficult for employees to make good decisions

Challenges to Adopting CDHPs

According to a recent study by Deloitte, employers feel that employee resistance and/or entitlement to coverage is their biggest obstacle (62%) in changing their current health care model. Yet, only 13% view employee attraction and retention as a barrier.

What Will the Future Hold

CDHPs are a Growing Trend

Consumer-Directed Health Care is a trend that seems to be catching steam. In the past three years, the enrollment in CDHPs has grown, indicating that this is a strategy that may be here to stay. Many industry surveys, among both employers and carriers, report increased use of CDHPs.

Research Among Employers

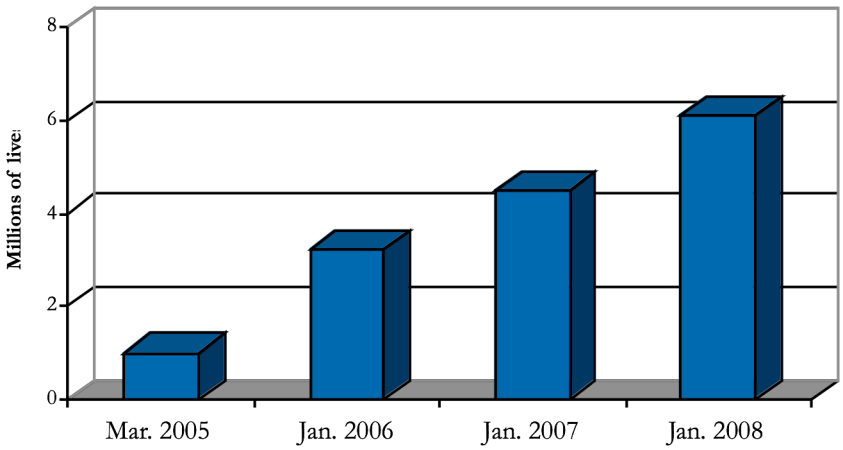
According to a Kaiser Family Foundation/HRET survey of firms offering health benefits in 2007, 10% report offering a HDHP with a HRA or HSA. This represents an increase from the 7% of employers who offered them in 2006. One in five surveyed say they are likely or very likely to offer a HDHP with an HSA in 2008, while nearly one-quarter indicate they are highly likely to offer a HDHP with an HRA in 2008.

In its annual benchmark survey of employer-sponsored health plans and plan costs, United Benefits Advisors (UBA) found that the percentage of employees enrolled in CDHPs nearly doubled from 6% in 2007 to 11.2% in 2008. The study estimates that CDHPs now comprise 13% of all plans offered by employers, an increase of 43% over the previous year. PPOs are the most common, representing 54% of plans, and HMOs seem to be on the decline with 21% of plans offered.

Research Among Carriers

America's Health Insurance Plans (AHIP), a national trade association, conducts an annual census of HSAs (only) among private health insurance carriers. This year's census reported that 6.1 million people became covered by HDHP/HSA products in January, representing an increase of 1.6 million people since January 2007 and 5.1 million since March 2005 (including both group and individual markets).

HSA/HDHP Plans Enrollment (Covered Lives)



The chart relates survey results; the chart is taken directly from AHIP's census.

What does it all mean for employers?

Since Consumer-Directed Health Plans are relatively new, it is difficult to gauge their effect on healthcare costs at this point. Some research has been conducted, but much more will be needed. Yet, early evidence is encouraging for employers.

Recent research suggests that CDHPs are cost-effective for employers. In its 2007 National Survey, Mercer reports that CDHPs tend to cost employers less per employee than either PPOs or HMOs. On average, CDHPs cost $5,970 per employee, while PPOs cost $7,352, and HMOS cost $7,120. When comparing HSA plans vs. HRA plans, HSAs are the least costly of all ($5,679 compared to $6,224 for HRAs).

Additional positive reports indicate that cost increases for CDHPs are much less than for other coverages. For instance, Deloitte found that the cost of CDHPs increased by 2.6% in 2006, whereas other coverages increased by nearly 8% (e.g. 7.4% for HMOs and 7.5% for PPOs). The United Benefit Advisors' research reported a cost decrease in premiums of 7.9% for CDHPs in 2008, while all other health plans increased premiums on average by 7.4%.

How Are Employers Informing Thier Employees

Excerpt from Deloitte's *Reducing Corporate Health Care Costs 2006 Survey*:

"To complement and enhance their CDHP plans, as well as educate their employees regardless of health plan, the survey findings indicate that there are many different approaches respondents are using to educate their employees about health care. We see close to 100 percent growth in intranet-based information in just three years. This includes employer- generated information and links to health plans and to health content sites. More than half of the participants (52 percent) are creating employee newsletters and hosting health fairs and workshops (58 percent)."

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101 Federal Street, Suite 1900
Boston, MA 02110
(617) 451-9500
nebaf@csr-bos.com

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