

Managing Through Fiscal Stress: Avoiding Health Plan Side Effects During an Economic Recession

A recession can put added pressures on group health plans, if plan sponsors are unprepared. As illustrated in the table on page 2, experience from the last three decades has shown that increases in unemployment during recessions are typically accompanied by dramatic drops in the consumer price index (CPI). However, they do not always lead to comparable decreases in health care plan costs. In the current, severely distressed and rapidly changing financial services environment, there is an additional concern: the stability of insurers. This *Public Sector Letter* discusses steps to take now to ensure that plan costs stay within budgets and that coverage is not disrupted.¹

¹ This *Public Sector Letter* is part of a series on managing through fiscal stress. For more information about strategies for health plans in a recession and other key compensation and benefits topics, visit the following page of The Segal Company's Web site: <http://www.segalco.com/managing-through-fiscal-stress/>

LESSONS ABOUT UTILIZATION FROM PREVIOUS RECESSIONS

Actuaries and underwriters have long understood that spending on health care, unlike other forms of insurance, is highly sensitive to consumer and provider behavior. In tough times, the pattern becomes more pronounced.

When individuals are worried about the security of their jobs — and, if they become unemployed, their ability to afford premiums for continued health coverage under the Consolidated Omnibus Budget Reconciliation Act (COBRA) that may exceed \$1,000 per family per month — they may increase some forms of utilization of their health benefits (*e.g.*, by scheduling major dental work or elective surgery) and cut back on or delay other services that may prevent costly complications in the future. Some participants may attempt to enroll as “dependents” people who do not meet the legal definition of a dependent (*e.g.*, ex-spouses who want to avoid paying COBRA premiums following a divorce). Applications for disability benefits may also escalate if participants consider elevating a back injury or mental health issue into a disability claim.

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The Segal Company is pleased to announce that Serena G. Simons has joined Segal as Senior Vice President and National Compliance Retirement Practice Leader. Ms. Simons is an employee benefits attorney with over 20 years of experience. A graduate of the University of North Carolina and Duke University School of Law, she has worked with several leading Washington, DC law firms. Serena is currently the Chair of the Employee Benefits Committee of the DC Bar Section of Taxation and a member of the Section's Steering Committee. Ms. Simons has been recognized in *The Best Lawyers in America* for employee benefits. She can be reached at 202.833.6472 or ssimons@segalco.com

Managing Through Fiscal Stress Webinar

The Segal Company invites you to join a webinar on that will discuss key tactics and strategies for helping jurisdictions to manage human resources during these difficult economic times. The webinar will be held on two dates:

- > Thursday, April 16 at 1:00 pm EDT
- > Tuesday, April 21 at 1:00 pm EDT

To register to join the webinar on either date, visit <http://www.segalco.com/managing-through-fiscal-stress/webinar.html>

Unemployment, Inflation and Increases in Per Capita Private National Health Expenditures during Recessions

| Recession Years | Annual Unemployment Rate ¹ | Increase in Consumer Price Index for All Urban Consumers (CPI-U) ¹ | Increase in Per Capita Private National Health Expenditures ² |
|-------------------|---------------------------------------|---|--|
| 1981 | 7.6% | 10.3% | 15.2% |
| 1982 | 9.7% | 6.2% | 12.9% |
| 1990 | 5.6% | 5.4% | 10.4% |
| 1991 | 6.8% | 4.2% | 5.5% |
| 2000 | 4.0% | 3.4% | 5.6% |
| 2001 | 4.7% | 2.8% | 5.6% |
| 2008 ³ | 5.8% | 3.8% | Unavailable ⁴ |
| 2009 ⁵ | 8.5% ⁶ | Unavailable | Unavailable ⁴ |

¹ Source: U.S. Bureau of Labor Statistics.

² Source: Center for Medicare & Medicaid Services (CMS). Equivalent public sector data is not available.

³ In December 2008, the Business Cycle Dating Committee of the National Bureau of Economic Research (NBER), the research organization that makes the official determination of when the U.S. has experienced a recession, determined that a peak in economic activity occurred in the U.S. economy in December 2007. The peak marks the end of the expansion that began in November 2001 and the beginning of a recession. Economists generally consider a decline in a gross domestic product (GDP) for at least two consecutive quarters to constitute a recession. The NBER takes into account other measures, such as declines in employment, industrial production and wholesale-retail sales.

⁴ Because CMS data on per capita private national health expenditures is not available for 2008 and 2009, data from the two most recent reports of results from the annual *Segal Health Plan Cost Trend Survey* may be of interest. The 2008 survey (<http://www.segalco.com/publications/surveysandstudies/2008trendsurvey.pdf>) found that the projected trend for open-access preferred provider organizations/point-of-service plans was 10.6 percent and the 2009 survey (<http://www.segalco.com/publications/surveysandstudies/2009trendsurvey.pdf>) found that the projected trend for those plans is 10.4 percent.

⁵ Many economists anticipate the current recession will continue through 2009.

⁶ This rate is for March.

In order to preserve their income, providers can dramatically influence not only the supply of but also the *demand* for services. For example, they may request additional tests and procedures beyond what is standard medical practice.

Yet these behaviors can be offset by a recession’s influence over consumer spending and reduction in utilization rates of many health care services. A seemingly logical assumption is that use of health care services, like other services, declines dramatically in a recession as consumers cut back

on their spending. However, experience has shown that might not be the case. In fact, health expenditures remain significantly higher than increases in the CPI, even during recessions.

Plan design changes adopted over the past 10 years, such as substantial patient copayments, higher coinsurance and larger annual deductibles, may go a long way toward discouraging extra utilization. Current cost-sharing levels for both employer-based plans and Medicare reduce the natural tendency to use more medical services.

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However, two issues may emerge. First, employers that have comprehensive medical plan designs and existing or impending reductions in force (RIFs)² may be at risk for unanticipated surges in claim costs during the transition period (on a per capita basis). This may come from spikes in COBRA enrollment as well as an increased utilization of elective procedures prior to announced layoffs.

The second issue is that a severe decline in utilization of key health care treatments and preventive procedures by employees who are not laid off can lead to volatile or even catastrophic future claim costs resulting from increased complications from untreated chronic conditions.

HEALTH INFLATION COUNTERMEASURES

To mitigate increased health care utilization in tough times, plan sponsors may want to:

- **Reexamine Appropriateness of Cost-Sharing.** This determination is important. While low cost-sharing with participants may encourage higher utilization, cost-shifting that is too high could prompt participants to forsake needed care in order to save out-of-pocket expenses, a decision that could prove to be unwise for participants and their plans, if it results in the

² RIFs were discussed in the March 2009 *Public Sector Letter*: <http://www.segalco.com/publications/publicsectorletters/march2009.pdf>

need for more expensive treatment at a later date. (The graph below presents some data recently collected by Segal on cost sharing). A relatively recent claims analysis done for *The Wall Street Journal* found that people with health insurance were already curtailing their health care use before the economic downturn worsened. Between March 2007 and March 2008, dispensed prescriptions for antidepressants dropped 29 percent, knee replacements fell 18.6 percent and pap smears fell 6 percent.³ Each of these could result in increased program costs and reduced productivity in future years.

- **Tighten health plan membership rolls.** Eligibility audits can ensure that the plan is paying only for eligible participants and dependents. One Segal client that conducted an audit in 2008 discovered that approximately 8.5 percent of dependents covered by the plan were not eligible for benefits.
- **Provide incentives for participants to seek treatment from lower cost providers who offer less intensive care.** Options include development of plan incentives to use on-site or

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retail clinics, nurse practitioners and alternative health care providers, and financial disincentives to seek non-emergency care from emergency rooms and other high-cost providers.

- **Spell out expectations for managed care provider networks.** Plan sponsors should make it clear to their carriers that they are expected to keep network provider price increases in line with overall inflation and to keep a close watch for possible provider abuses. In addition, plan sponsors may find it helpful to review vendor contracts and create performance guarantees tied to outcomes and avoidance of provider abuses.

PLAN MANAGEMENT STRATEGIES

In addition to keeping health inflation in check, plan sponsors should consider the following strategies for managing their health care costs:

- **Monitor employee use of health-care services via data mining.** The more specific the data that plan sponsors have to identify the diseases and treatments that are driving up their costs, the more they are able to develop ways to address those cost factors.
- **Improve case management and health coaching services.** Plan

sponsors can flag trends in non-compliance with essential preventive diagnostic and pharmaceutical therapy and have vendors intercede more aggressively to get patients to stay on appropriate therapies that avoid complications from disease.

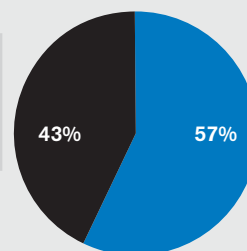
- **Audit disability and medical provider claims.** A claims audit can help identify overlap, waste and inefficiency. A growing number of plan sponsors and insurers are no longer paying for claims directly related to hospital errors.
- **Redesign plans to promote wellness.** While wellness programs do not create immediate cost savings, continued emphasis on participant and dependent wellness can help to improve the overall health status of a plan’s population with the corresponding reduction in high-cost claim events over time. Moreover, these programs can help improve productivity by reducing time off and absenteeism.
- **Invest in medical decision support tools that educate the workforce to be better consumers of care.** Improving the health literacy of employees in conjunction with promoting wellness and self-responsibility can improve outcomes and reduce long-term health plan cost trends.
- **Watch out for unintended consequences of state and federal government regulations.** Whether it is mental health parity, the new temporary COBRA subsidy⁴

³ See “Consumers Cut Health Spending, As Economic Downturn Takes Toll,” which was published in *The Wall Street Journal* on September 22, 2008: <http://online.wsj.com/article/SB122204987056661845.html> The text box on the last page of this *Public Sector Letter* includes links to other articles on personal health expenditures during the current recession.

Changes in Cost-Sharing for Health Benefits in Response to the Recession

In early February 2009, The Segal Company began collecting data through a brief online survey about how state and local governments are responding to the recession. The pie chart below shows preliminary, anecdotal responses to the following question received as of April 1, 2009: **Are you requiring employees to pay a larger portion of benefit costs (health benefit and retirement)?**

Key:
 ■ Yes
 ■ No



⁴ For information about the COBRA subsidy, which was introduced as part of the American Recovery and Reinvestment Act of 2009, see The Segal Company’s February 2009 *Bulletin*: “The Stimulus Law’s Temporary Subsidy for COBRA Premiums”: <http://www.segalco.com/publications/bulletins/feb09COBRAsubsidy.pdf>

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or changes in payments from Medicare and Medicaid, regulations often lead to unintended changes to public sector employer health plans. Employers need to evaluate their options and find administrators and vendors that can help maximize potential federal subsidies over more than just the current year.

COPING WITH INSTABILITY IN THE VENDOR MARKETPLACE

For the first time, health plan sponsors need to be prepared for broad-based carrier financial vulnerabilities. Economic recessions and undisclosed liabilities can cause some major insurers to become financially unstable. The current recession has been notable for the number of insurance and financial institutions that are being downgraded, bankrupted, acquired by a competitor or taken over by the federal government.

Health benefit plan sponsors should make sure they are placing their business with financially secure companies that continue to meet the financial qualifications outlined in the bid

process and in their contracts. Carrier ratings should be updated and reviewed periodically to check the financial stability of the organization. Plan sponsors should be on the lookout for early signs of trouble, such as ratings downgrades from multiple rating agencies, successive downgrades, increased media scrutiny, network stability problems and participant-service problems. Plan sponsors should actively monitor their vendors’ performance for both transactional processes and for customer satisfaction. Some key statistics to consider when evaluating insurers:

- Financial strength ratings (e.g., Secure ratings from sources such as AMBest, S&P, Moody’s),
- Negative ratings outlooks, and
- Rapid declines in net worth (e.g., gross changes in capital and surplus).

CONCLUSION

The current economic downturn creates new challenges for health plan sponsors. Those that are well prepared for a recession will be less

likely to burden their workers with more health plan cost increases and more likely to encounter fewer financial surprises down the road. Rigorous health plan monitoring and a willingness to apply innovative new tactics can help employers and health trust funds weather the challenges brought by a recession.



For more information about or assistance with the strategies discussed in this Public Sector Letter, contact your Segal Company consultant or one of the following experts:

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For Additional Reading on Recessionary Health Spending

Sponsors of group health plans may be interested in the following information on personal health expenditures during a recession:

- March 13, 2009 *New York Times* article, “Bad Economy Leads Patients to Put Off Surgery, or Rush It” (<http://www.nytimes.com/2009/03/14/us/14surgery.html>)
- February 25, 2009 press release on results from a 2009 survey conducted by The Kaiser Family Foundation: “More than Half of Americans Say Family Skipped on Medical Care Because of Cost in Past Year, Worries about Affordability for Health Care Rise” (<http://www.kff.org/kaiserpolls/kaiserpolls022509nr.cfm>)
- November 6, 2008 *New York Times* article, “Hospitals See Drop in Paying Patients” (<http://www.nytimes.com/2008/11/07/business/07hospital.html>)

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