

the implications of an economic recession on health plans

Like the Incredible Hulk rampaging through a cityscape, a recession can wreak havoc on employer health-plan costs. The U.S. federal government recently released statistics showing the largest monthly increase in unemployment rates in nearly 20 years. Whatever the industry — from auto, airlines and banking to pharmaceuticals — a sustained downturn in the economy can have unforeseen consequences on health benefits budgets.

Recessions and Health-Plan Expenditures — Background

Actuaries and underwriters have long understood that unlike other forms of insurance, health-care spending is highly sensitive to manipulation by consumers and providers. While very few consumers load up on car insurance claims when tough times are expected, it's easy to schedule major dental work or stockpile long-term maintenance medications when jobs face an uncertain future.

By Edward Kaplan, The Segal Co.

QUICK LOOK

- ⇒ When jobs face an uncertain future, consumers may load up on health-care benefits like scheduling major dental work and stockpiling maintenance medicines.
- ⇒ Longer hospital stays, more expensive tests and higher medical bills may be a result of doctors trying to preserve their income levels as they see a future with fewer patients.
- ⇒ A surge in health-care spending in the private sector seems to be linked to an acceleration in unemployment during the past 30 years.



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Liberal use of benefits becomes even more likely when employees realize that their COBRA premiums could exceed \$1,000 per family per month in some parts of the country. The use of disability insurance can also escalate as employees consider, perhaps fraudulently, elevating a back injury or mental health issue into a full-blown disability.

On the provider side, pressures to preserve income levels may lead to longer hospital stays, more MRIs and higher bills. After all, providers are not immune to the forces of inflation or the impact of \$4-per-gallon gas. The one difference is that providers, unlike other industries, can dramatically influence not only the supply of, but also the demand for, services. Few patients will ignore a physician’s

recommendation for a few more images and other tests, especially if a “shadow” appeared on a prior CT scan.

A comparison of upticks in unemployment rates with spending on health care in the private sector, as shown in Table 1, reveals some interesting patterns. Looking back over 30 years, three periods show an apparent correlation between acceleration in unemployment and subsequent surges in health-care expenditures.

Preparing for the Next Recession

This time around, a recession may back employers into a corner. The challenges today would be even greater than in the past because the market has fewer countermeasures available to address health-care inflation.

In the 1980s, the countermeasure was to leverage managed-care provider networks, trading patient volume for deep provider discounts. Prior to that, most plans paid prevailing charges to hospitals, labs and physicians. These charges were not negotiated in advance, so no contracts were in place to prevent balance billing to patients. Consequently, large managed-care organizations and buyers used their leverage to gain price concessions.

In the 1990s, the Clinton administration took serious steps to threaten a tightly controlled, government-regulated purchasing cooperative approach. The market responded with a temporary display of self-control, resulting in some of the lowest medical price inflation (during the mid 1990s) in years.

Since the dawn of the new millennium, the prime response to rising health-care costs has been neatly packaged as “consumerism,” under which major costs have been shifted to employees. It is true that before managed care, under traditional indemnity plans, workers paid 20 percent to 30 percent of the cost of health care because most plans required a deductible and then indemnified typically 80 percent of the bill. With the migration to managed care, health maintenance organizations (HMOs) and preferred provider organizations (PPOs) touted the fact that huge provider discounts would eliminate the claim form and increase coverage. In some cases that was true; some HMOs were paying nearly 95 percent of the bill.

However, the return to double-digit medical trends in recent years has resulted in major plan redesigns. Typical employment-related PPOs now require substantial patient co-pays, growing annual deductibles and 20 percent or higher co-insurance. These changes, which have been adopted during the past 10 years, have helped tame health-care inflation — at least for employers.

TABLE 1: UNEMPLOYMENT AND HEALTH-CARE EXPENDITURES

	1981-1982	1990-1991	2001-2002
Percent change in the unemployment rate	From 7.6% to 9.7%	From 5.6% to 6.8%	From 4.0% to 5.8%
Increase in private health insurance expenditures	15.3%	8.9%	10.9%

Source: U.S. Bureau of Labor Statistics

Now What?

If a sustained and painful recession is around the corner or if we're already in one, what countermeasures can employers take to keep medical cost increases at levels that won't throw their balance sheets into a death spiral?

- **Seek to Control Extra Use:** Past recessions saw some people increase their use of medical services, drugs or dental work because they worried about losing their jobs and benefits. Such active use may have fueled new rounds of employer plan costs. However, the latest cost-shifting has created much higher co-pays and co-insurance costs for employees than in the past. As a result, many employees may not have the necessary disposable income to dramatically increase use, which means that this recession may not produce the same uptick in medical trends as prior recessions.
- **Watch out for Vendor Price Increases:** Since almost all employers now contract with managed care provider networks, employers should expect their networks to keep provider price increases in line with overall inflation. They must stay with those networks that can keep reimbursement rates under control and keep a close watch for possible health-care provider abuses.
- **Be Prepared for Carrier Financial Vulnerabilities:** Economic recessions can lead to a "thinning of the herd" and cause some major insurers to quickly become financially unstable. Plan sponsors should make sure they are placing their business with financially secure companies and periodically ask the insurance representative to provide data to attest to the financial stability of the organization. However, as we have seen in the past, ratings agencies cannot always


uncover hidden financial problems, so look for signs of trouble, such as ratings downgrades, increased media scrutiny and service problems.

Additional Prudent Steps

In addition to contracting with those networks that work to keep medical plan cost inflation under control, health plan sponsors can:

- Tighten health plan membership rolls through eligibility audits to make sure the company is not paying for ineligible lives.
- Monitor employee use of health-care services via data mining. Find out what diseases and treatments are driving costs up and create strategies to address them.
- Audit disability and medical provider claims for overlap, waste and inefficiency.
- Negotiate diligently with health-care providers and insurance carriers to build in multiyear cost-trend guarantees.
- Review vendor contracts and create performance guarantees tied to outcomes and avoidance of provider abuses.
- Redesign plans to promote wellness, improve population health status, and create access to and provide incentives for employees to seek out lower-cost, less-intense providers (walk-in clinics, nurse practitioners, alternative health-care providers).
- Examine the full implications of proposed cost-shifting. (Will employees forsake needed care to save out-of-pocket expenses that could, in turn, raise admissions for expensive, later-stage diseases?)
- Invest in medical decision-support tools that educate the workforce to be better consumers of care. Improving the health literacy of employees can only improve outcomes and long-term trends.

Conclusion

Even with government reform on the horizon, employers may still be on the hook for providing health-care benefits and managing costs. A recession could have wide-ranging effects on how employees use their health-care benefits. Employers that are well-prepared for a recession will likely encounter fewer financial surprises down the road. With a tight labor market, this downturn will create new challenges for employers, who generally do not want to burden their workers with more health-plan cost increases. 

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