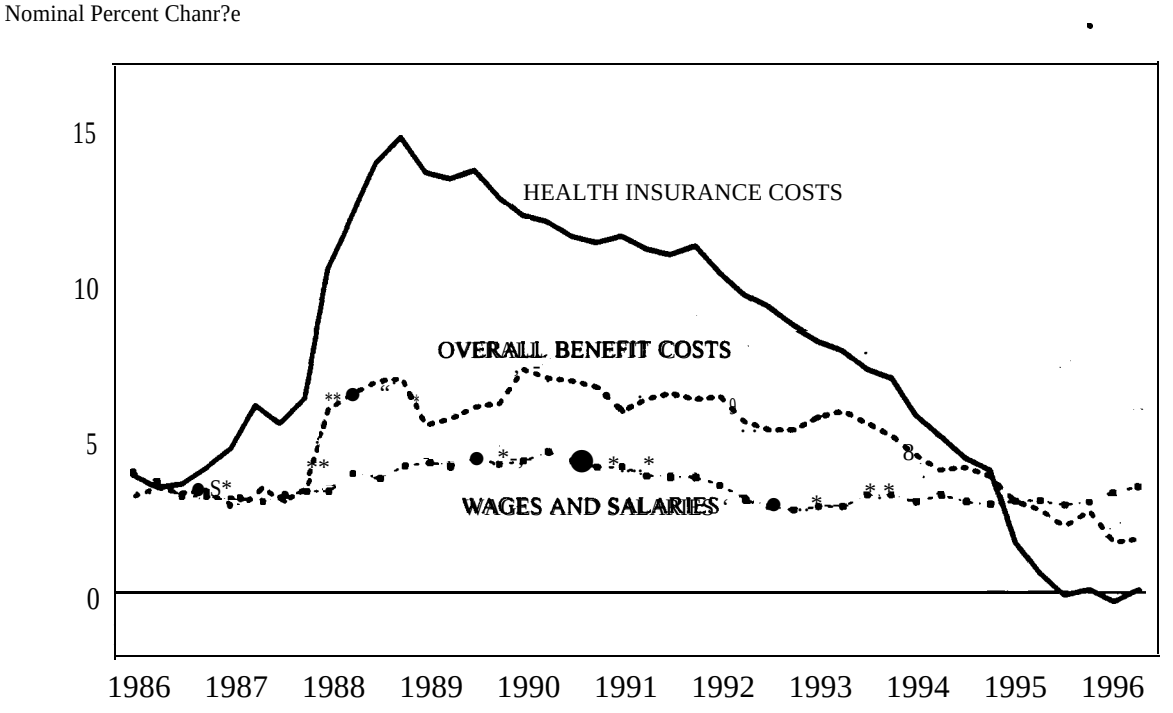
A Look at Employers' Costs of Providing Health Benefits

Handout

Office of the Chief Economist
U.S. Department of Labor

July 31, 1996

GROWTH IN EMPLOYERS' HEALTH COSTS SLOWS



Source Based on data from the Bureau of Labor Statistics, Employment Cost Index, Private Industry..
The nominal percent changes inemployer costs for health insurance per hour worked are unpublished estimates.fromBLS

GROWTH IN EMPLOYERS' HEALTH COSTS SLOWS

- The rate of growth of employer's costs for health insurance has steadily slowed since 1989, as measured by the Employment Cost Index, This slower growth of health costs has been a major factor in the deceleration in overall benefit costs for employers.

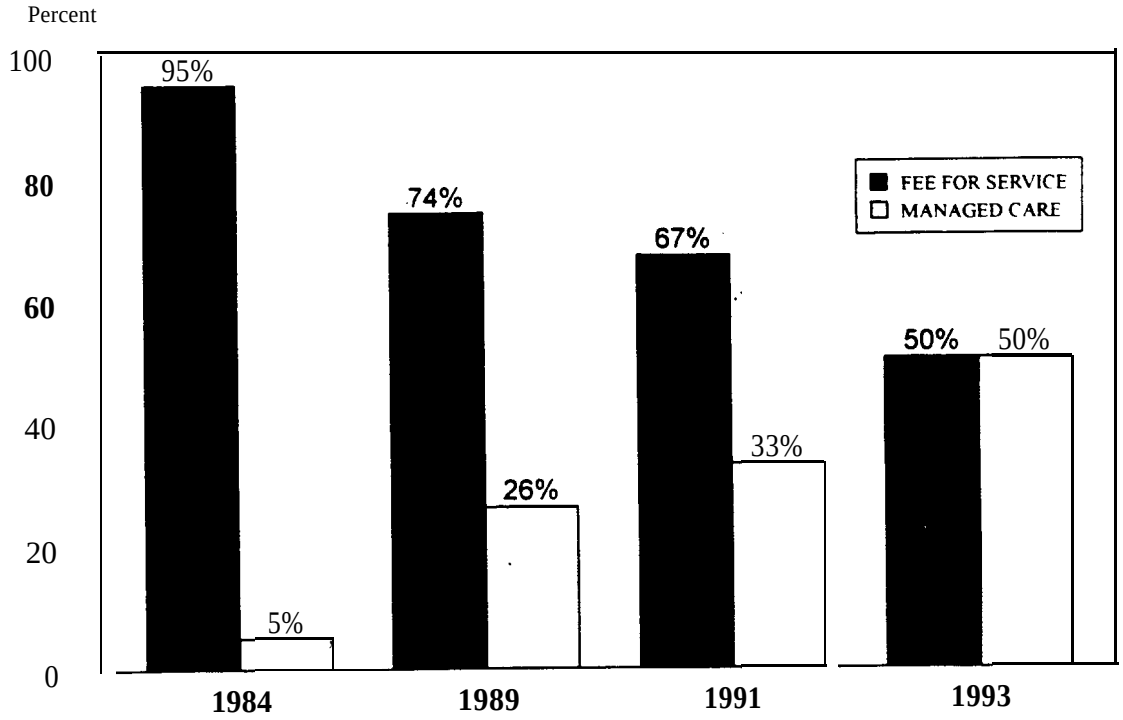
- Since 1995, employers' costs for health insurance grew more slowly than overall benefits or wages and salaries For the 12 months ending in June 1996, employer health insurance costs (not adjusting for inflation) increased by 0, 10/0 -- down from 0.6 and 5.0 percent increases during the previous 12 month periods in 1995 and 1994, respectively.

- Possible explanations for this slowdown include:
  - the rise in health care costs slowed considerably
  - employers switched to lower-cost managed-care plans

  "employees paid a larger share of the costs of employer-provided health insurance
  "the number of employees receiving employer-sponsored health insurance fell

THE SWITCH TO MANAGED-CARE HEALTH PLANS

Distribution of Enrollment by Type of Health Plan, Medium and Large Private Establishments . .



Source Based on data from the Bureau of Labor Statistics, Employee Benefits Survey.

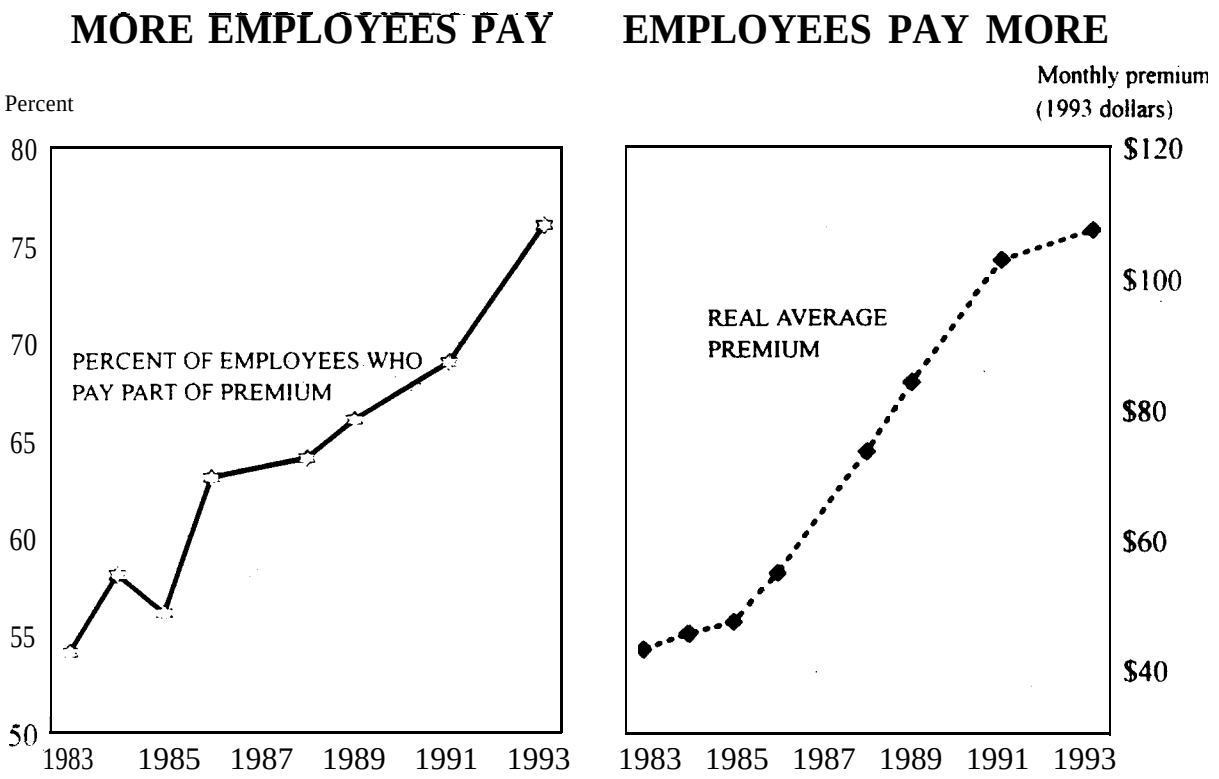
THE SWITCH TO MANAGED-CARE HEALTH PLANS

- Fee-for-service plans, which dominated employer-sponsored health care a decade ago, are no longer the norm for employees' health coverage. In 1984, fee-for-service plans covered 95% of the full-time employees who participated in employer-sponsored health insurance in medium and large private firms. By 1993, only half of employees were in traditional fee-for-service plans, with the other half roughly evenly distributed among HMO's and PPO'S

- This trend towards managed care has continued. The share of enrollment in conventional fee-for-service health plans fell an additional 10 percentage points between 1993 and 1995, according to a KPMG Peat Marwick survey of employer-sponsored health benefits.

- The cost difference for employers differs by region, by firm size, and according to the demographic composition of the workforce. However, on average, medical plan costs per employee for HMO's and PPO's were almost 20% less expensive than costs for traditional indemnity plans in 1995, according to benefits consulting firm Foster Higgins.

BURDEN SHARING



Source Based on data from Bureau of Labor Statistics, Employee Benefits Survey. Figures are for family coverage in medium and large private establishments. The CPI-U was used to convert nominal monthly premiums to 1993 dollars.

BURDEN SHARING: EMPLOYEES PAY MORE, AND MORE EMPLOYEES PAY

A growing number of employees are required to contribute toward health-care premium costs for employer-provided health insurance. In addition, growth in the average premiums paid by contributing employees has outpaced inflation.

- In 1983, slightly more than half (54%) of full-time employees in medium and large firms contributed towards employer-provided health premiums for family coverage. Ten years later, over three-quarters (76%) of these employees paid health insurance premiums.

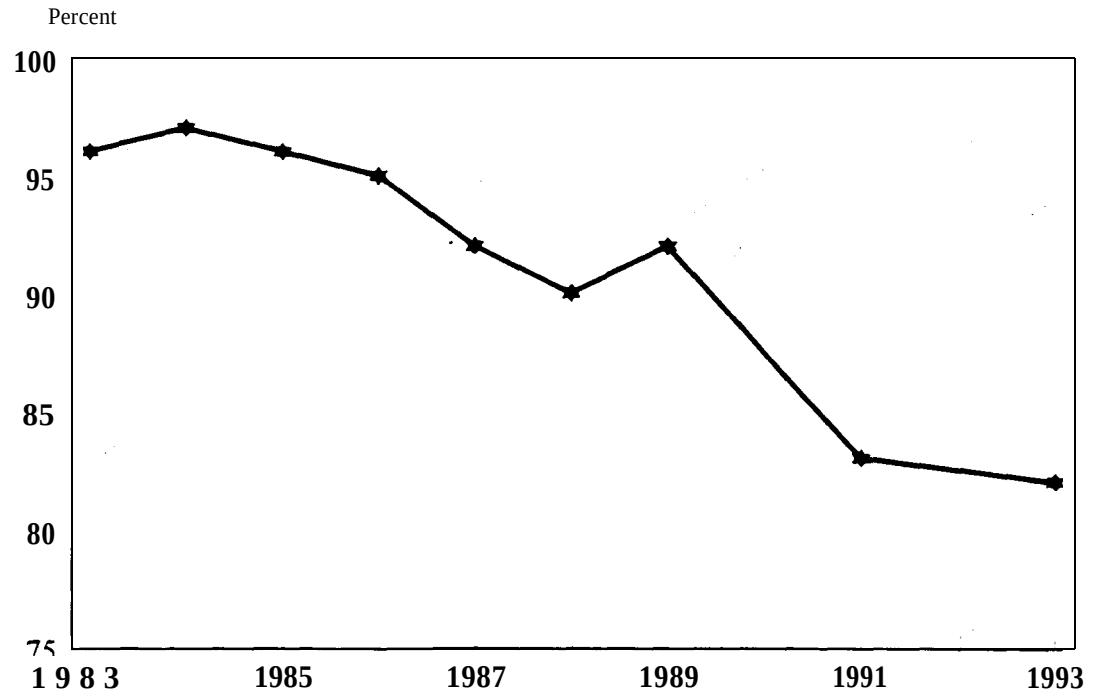
- The real average monthly contribution paid by fill-time employees for employer-provided family health coverage has more than doubled from $45 in 1983 to $107 in 1993.

- Employees' share of premiums for employer-provided health insurance continued to rise through 1994 and 1995. KPMG Peat Marwick reports that the employee share of premiums in conventional family plans increased from 23% in 1994 and 31% in 1995.

- Employees in nonfederal jobs contributed 16% of the premium costs for employer-provided health insurance in 1994, according to unpublished estimates from the Health Care Financing Agency, up from 13.7% in 1987. If the employer share of health insurance premiums had remained at its 1987 level through 1994, employees' contributions would be $5.5 billion lower.

DECLINE IN EMPLOYEE HEALTH COVERAGE

Percent of Full-time Employees Participating in Employer-Sponsored Health Plans, Medium and Large Private Establishments



Source Based on data from the Bureau of Labor Statistics. Employee Benefits Survey

. DECLINE IN EMPLOYEE HEALTH COVERAGE

- In 1993, 82% of fill-time employees in medium and large private firms participated in an employer-sponsored medical care plan, down from 96% in 1983. The percentage also fell in small private firms.

- Enrollment decline may be attributed to

  - a decline in the number of employees and their dependents participating in health plans sponsored by their employers. In particular, many employees decline coverage because they are already covered by a spouse's policy.

  - a decline in the number of employees offered employer-sponsored health benefits, either because employers have dropped or restricted coverage for their employees, or because of sectoral change in the economy.

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Technical Appendix

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TECHNICAL APPENDIX:
A LOOK AT EMPLOYERS' COSTS OF PROVIDING HEALTH BENEFITS

Overview

Employers' costs of providing benefits rose dramatically in the late 1980's. However, the growth rate in benefit costs began to slow in the 1990's, especially since 1995, as shown by the Employment Cost Index in Figure 1.

Since 1995, employer benefit costs, particularly for health insurance, have grown more slowly than wage and salary costs. This slower growth of health costs has been a major factor in the deceleration in overall benefit costs for employers. For the 12 months ending in June 1996, employer health insurance costs, not adjusting for inflation, only increased by0. 1% - down from 0.6 and 5.0 percent increases during the previous 12-month periods in 1995 and 1994, respectively.

This document summarizes the possible explanations of this deceleration in health care benefit costs for employers.

Possible explanations include

- the rise in health care costs slowed dramatically
- employers switched to lower-cost health care plans
- the number of employees receiving health benefits fell
- employees paid a larger share of the costs of employer-provided health insurance
- other reasons
  (change in usage of health care or breadth of coverage)

Possible Explanations for the Deceleration in Employers' Health Benefit Costs

1-The rise in health care costs slowed dramatically

Health care prices grew much faster than overall inflationand wages during the 1980's and early 1990's. Since 1993, the gap between medical care inflation and overall inflation has fallen.

- In 1991 and 1992, prices for medical care grew over 4% per year faster than other prices, as measured by the Consumer Price Index. By 1995, the difference in medical and nonmedical inflation narrowed to less than 2 percentage points. In the sixth months ending in June 1996, medical prices grew slower than nonmedical prices.

2-Employers switched to lower-cost plans

Over the past decade, the range of health care plans provided by employers has increased.

In recent years, many employers have expanded the range of plans they offer to include managed-care plans that have much lower average employer premiums than traditional indemnity plans and that tend to control utilization through gatekeepers. Some employers have switched entirely to managed-care health plans, while others allow the worker to choose between plans.

- The best-known managed-care plans are health maintenance organizations (HMO's) and preferred provider organizations (PPO'S). Managed-care plans tend to restrict patient choice, use primary-care physicians as gatekeepers for specialized service, and negotiate fees directly with health care providers. When offered a choice of plans, many workers choose nontraditional plans because they have lower deductibles and lower fees when services are rendered.

- The cost-controlling mechanisms for managed-care plans result in lower costs to participating employers. Foster Higgins' national survey of employer-sponsored health plans reveals that the average medical plan cost per employee (both employers' and employees' share) for HMO's was 19% lower (a $804 cost difference) than traditional indemnity plans in 1995. The average cost for PPO coverage was 18% lower ($781) than for a traditional indemnity medical plan.

- In 1984, 95% of employees in medium and large firms were in fee-for-service plans. By 1993, these employees were about equally likely to be in a managed-care health plan as in a traditional fee-for-service plan, according to the Employee Benefits Survey data shown in Figure 2. This represents a dramatic change in the type of health care plans offered over the last decade.

Distribution of Enrollment, by Type of Health Plan

Medium and Large Private Establishments	1984	1989	1991	1993
Fee for service	95%	74%	67%	50%
HMO	-	17%	17%	23%
PPO	5%	10%	16%	26%

Small Private Establishments	1990	1992	1994
Fee for service	74%	68%	55%
HMO	14%	14%	19%
PPO	13%	18%	24%

Source: Based on data from Bureau of Labor Statistics, Employee Benefits Survey
Figures are for full-time employees.

- Data fromBLS's Employee Benefits Survey are not yet available for large and medium employers after 1993, but other surveys suggest that enrollment continued to shift from conventional to managed care plans in 1994 and 1995. According to data from KPMG Peat Marwick, enrollment in traditional fee-for-service health plans fell by another 10

percentage points between 1993 and 1995.

3The number of employees receiving health benefits fell

For the majority of Americans, health insurance is still based on the employment relationship. The share of workers participating in employer-sponsored plans fell over the same period that growth in employers' costs have fallen.

•In 1993, 82% of full-time employees in medium and large firms participated in an employer-sponsored medical care plan, down from 92% in 1989, as shown in Figure 3. In small private firms, the percentage fell from 69% in 1990 to 66% in 1994, according to the Employee Benefits Survey by the BLS. Enrollment in employer-sponsored health insurance coverage is much lower for part-time workers.

•Enrollment may decline due to a fall in the number of employers offering employer-provided insurance, or because employees, especially low-wage employees, are electing to not enroll in health insurance plans. A study of 1987 data from the Employee Benefits Supplement to Current Population Survey shows that 76% of all workers age 18-64 were offered health insurance by their employer. Of these, 87% participated in the plan, 11% declined coverage because they were covered by another plan, and 2% chose to remain uninsured (Long and Marquis, 1992). Those who declined coverage entirely tend to be the lowest-wage workers, in small firms, and in agricultural and construction occupations.

•Structural change in the economy may also contribute to stagnation in enrollment. Service-sector jobs have lower percentage of workers eligible for health benefits, so that relative growth in service employment implies a slow down in the growth of the overall number of workers getting employer-sponsored health benefits.

•Another important factor in the issue of enrollment in employer-provide health insurance is the enrollment of retirees. In 1994, 34% of retirees were covered by a former employer's health plan, down from 44% in 1988, according to the Pension and Welfare Benefits Administration.

4-Employees paid a larger share of the costs of employer-provided health insurance

A growing number of employees are required to contribute towards health care premium costs for employer-provided health insurance. In addition, the average premiums paid by contributing employees have increased.

•Employees in nonfederal jobs contributed 16°/0 of the premium costs for employer-provided health insurance in 1994, according to unpublished estimates from the Health Care Financing Agency, up from 13.7% in 1987. If the employer share of health insurance premiums had remained at its 1987 level through 1994, employees' contributions would be $5.5 billion lower.

•Employees' share of premiums for employer-provided health insurance continue to rise

through 1994 and 1995. KPMG Peat Marwick reports that the employee share of premiums in conventional family plans increased from 23% in 1994 to 31% in 1995.

Wore employees paid some part of health insurance premiums

Fewer employers are offering no-cost health insurance. BLS's Employee Benefits Survey shows that an increasing number of employers are requiring that employees contribute to health care premiums, as shown on the left side of Figure 4. Information from compensation experts suggests these trends have continued into 1995.

Percent of Enrollment in Employer-Sponsored Plans Requesting Employee Contribution

Medium and Large Establishments	1989	1991	1993
Single coverage	47%	51%	61%
Family coverage	66%	69%	76%

Small Private Establishments	1990	1992	1994
Single coverage	42’?4.	46?4.	52%
Family coverage	67’%0	72%	75’%0

Source: Based on data from Bureau of Labor Statistics, Employee Benefits Survey

● *Average premiums paid by employees have increased*

Not only must more employees contribute to health insurance premiums, average premiums paid by contributing employees have increased. The real average premiums for family coverage in medium and large private establishments are shown on the right side of Figure 4. The real value of premiums has especially increased for employees in smaller establishments, and for family coverage.

Real Average Monthly Employee Premiums , 1994 dollars

Medium and Large Establishments	1989	1991	1993
Single coverage	$30.25	$28.94	$32.36
Family coverage	$86.17	$105.51	$110.17

Small Private Establishments	1990	1992	1994
Single coverage	$28.49	$38.57	$40.97
Family coverage	$123.98	$159.02	$159.63

Source: Based on data from Bureau of Labor Statistics Employee Benefits Survey, The CPI-U was used to convert nominaI figures into 1994 dollars.

ŽThe move to managed care plans has increased the share of premiums paid by employees. KPMG Peat Marwick research states that the employer share of total premium costs for individual coverage in HMO’s is 80%, versus 83% in PPO'S and 88% in traditional fee-for-service plans in 1994.

● The real average deductible paid by employees in non-HMO plans has risen 8% between 1989 and 1993, (from $202 to $218) for medium and large private establishments, according to BLS' Employee Benefits Survey.

● Despite growing deductibles for traditional insurance plans, out-of-pocket spending has not increased dramatically. Managed-care plans reduce out-of-pocket expenses with low co-pays and often no deductibles. Growth in individuals' out-of-pocket spending on health care was 3.0% in 1993 and 3.2% in 1994, according to the Health Care Financing Administration. This is still higher than inflation, but alone cannot explain the deceleration in employers' health benefits costs.

5- Other explanations: Usage of health care declined

Measures of the intensity of use of medical services show that utilization has fallen recently: community hospital admission rates are down, the average length of a hospital stay has fallen, and hours worked by physicians are stable. This is partly explained by lower coverage, but also suggests managed-care plans have reduced utilization.

6- Other explanations: Change in the breadth of service

The breadth of services covered under employer-sponsored health insurance expanded for at least a decade to include well-baby care and physical examinations. However, some firms have been carving out supplemental health services like dental and vision plans from their medical insurance plans. These benefits are still offered, but are separate from medical plans and require separate deductibles and copays. This de-bundling of services means that fewer employees are choosing to carry the insurance for supplemental health services.

Conclusions

Employer costs for health insurance have fallen for a variety of reasons: medical inflation has slowed and employers and employees are migrating towards managed-care health care plans. A larger share of employees must now pay part of the premiums for employer-provided health plans, and the average premium paid by employees has grown in recent years. In addition, the number of workers and retirees participating in employer-sponsored health insurance has declined.

One cost that is not accounted for is the opportunity cost of time spent by beneficiaries as they weave through the maze of gatekeepers and precertification required for specialized procedures in managed-care plans.

Unfortunately, the data can not tell us about the quality of health care. Surveys of consumer sentiment about the quality of their health plan do not give conclusive answers. In a nationwide survey sponsored by The Robert Wood Johnson Foundation in 1995, 46% of respondents thought the quality of the medical care they received had improved in the past three years, and 25%

thought it had worsened (Knickman and others, 1996). However, a recent survey by *Consumer Reports* of their readers showed that 10% of readers did not get the medical treatment they needed because their HMO discouraged it, while only 2% of readers in traditional fee-for-service health insurance said they did not get the necessary care ("How Good is Your Health Plan?" . August 1996).

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Figure 1

GROWTH IN EMPLOYERS' HEALTH COSTS SLOWS

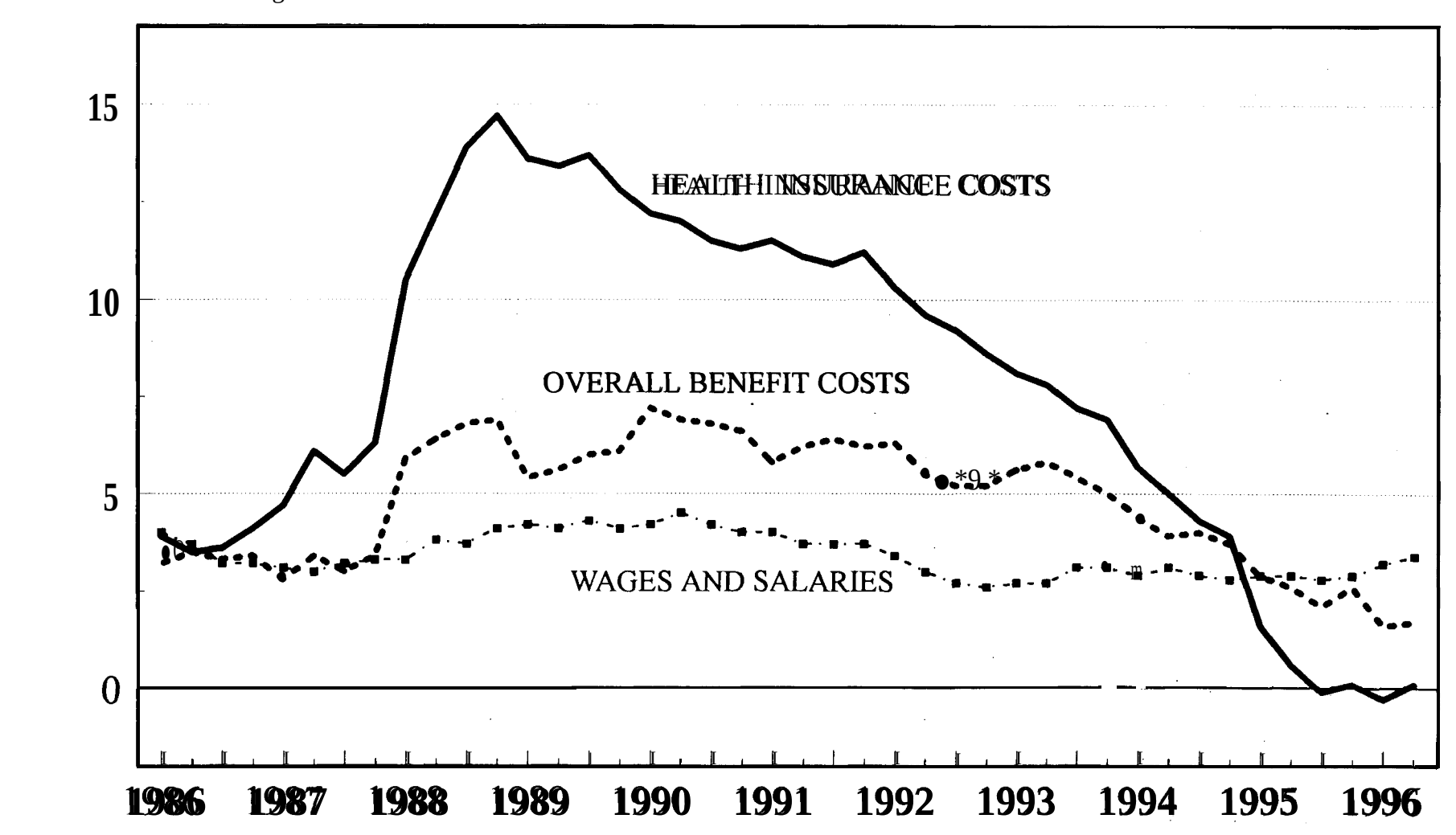

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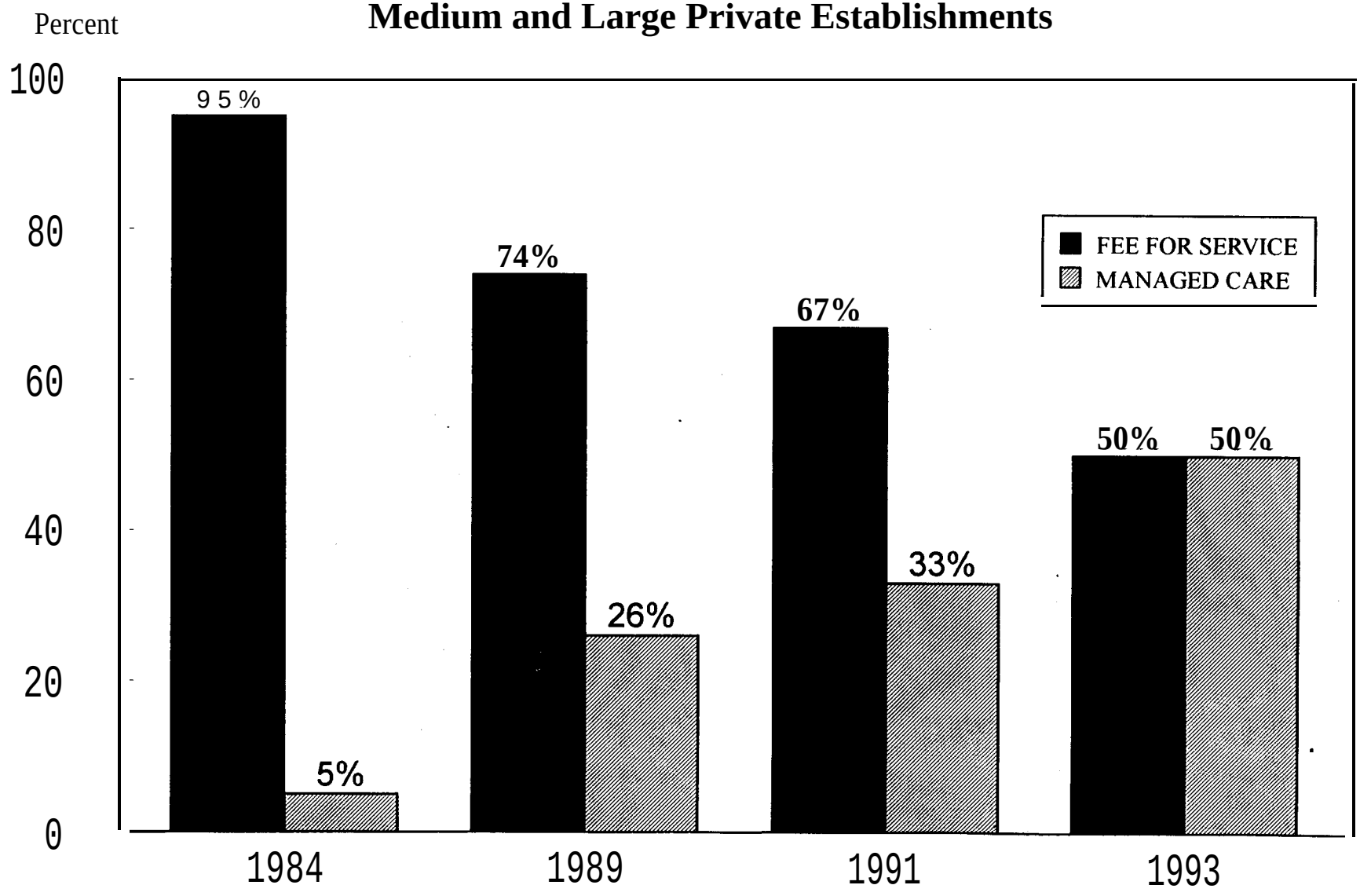
Figure 2

THE SWITCH TO MANAGED-CARE HEALTH PLANS

Distribution of Enrollment by Type of Health Plan, Medium and Large Private Establishments

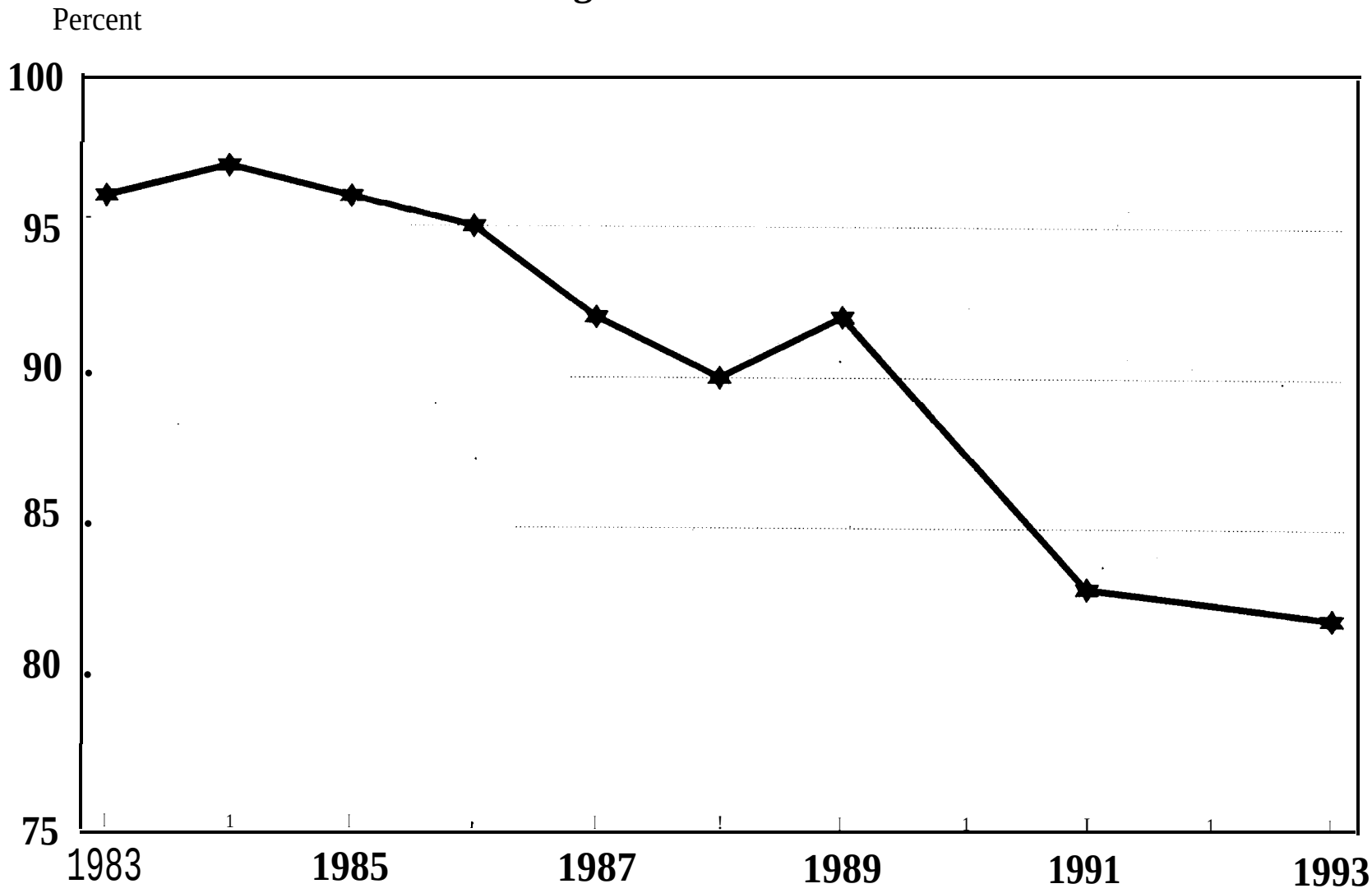


Source: Based on data from the Bureau of Labor Statistics, Employee Benefits Survey.

Figure 3

DECLINE IN EMPLOYEE HEALTH COVERAGE

Percent of Full-time Employees Participating in Employer-Sponsored Health Plans, Medium and Large Private Establishments

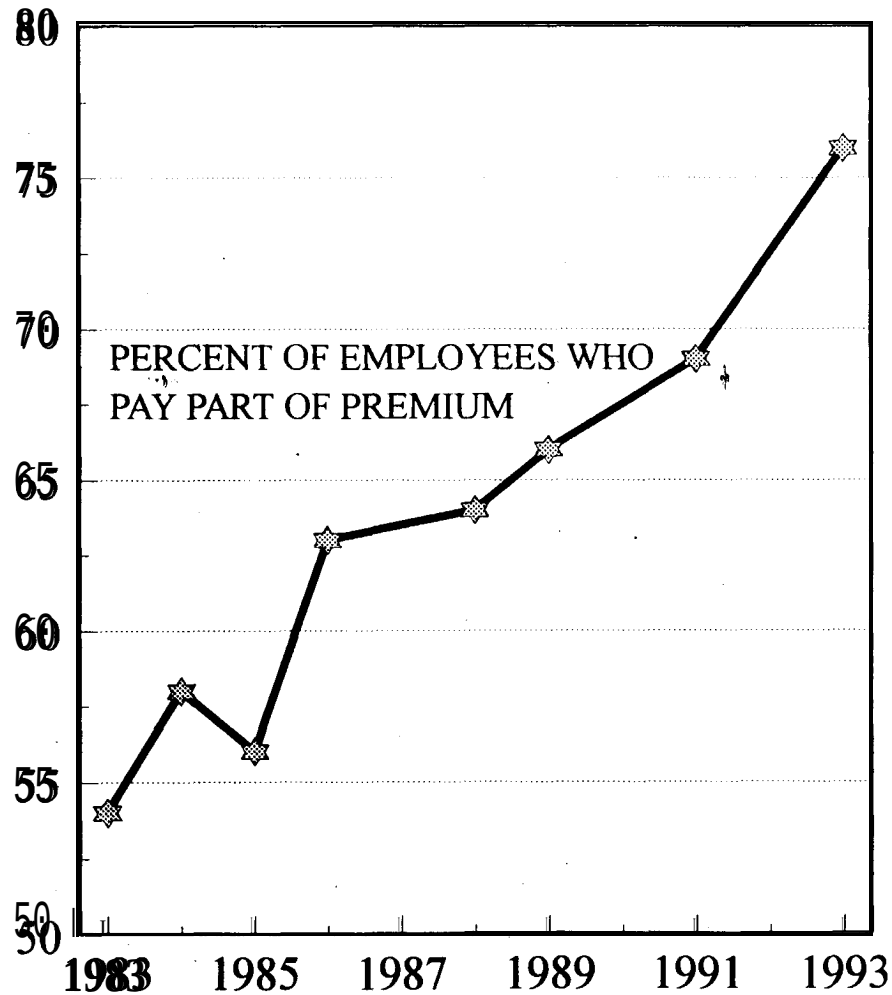


Source: Based on data from the Bureau of Labor Statistics, Employee Benefits Survey.

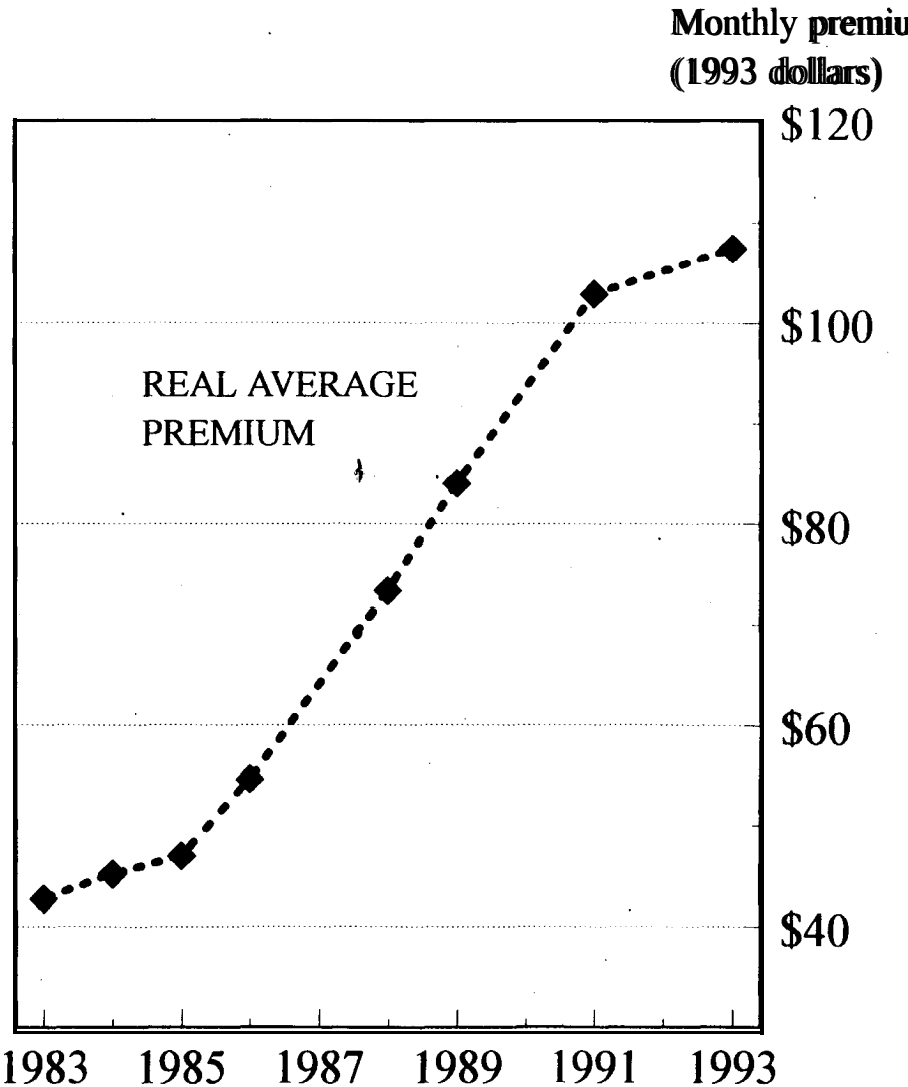
Figure 4

BURDEN SHARING

MORE EMPLOYEES PAY



EMPLOYEES PAY MORE



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