Employers Wary of Health Reform Costs and Hassles

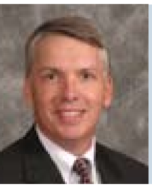
Health Reform Financial Analysis Report

Lockton Benefit Group | Revised April 5, 2011

Shannon Demaree, ASA, MAAA
Vice President
Director of Actuarial Services
Lockton Benefit Group
Telephone: 816-960-9963
sdemaree@lockton.com

Katy Curry, FSA, CERA, MAAA
Consulting Actuary
Lockton Benefit Group

Telephone: 816-960-9202
kcurry@lockton.com



Ed Fensholt, JD
Senior Vice President
Director of Compliance Services
Lockton Benefit Group
Telephone: 816-960-9775
efensholt@lockton.com

Mark Holloway, JD, CEBS
Senior Vice President
Co-Director of Compliance Services
Lockton Benefit Group
Telephone: 816-960-9567
mholloway@lockton.com

HEALTH REFORM FINANCIAL ANALYSIS REPORT

Our actuarial modeling of more than 130 employee benefit plans shows that last year's health reform law imposes additional costs on employers' health plans. The study also shows that the law will create a financial incentive for some employers to terminate health benefit plans in 2014 when new Insurance Exchanges take effect.

Lockton's actuaries have modeled the impact of health reform for hundreds of its clients and aggregated results from 136 of those analyses into a report that examines the impact of the health reform law on middle-market health plan sponsors. The report includes a variety of industry segments, including construction, government, healthcare, manufacturing, professional services, transportation and retail and entertainment. Summary charts of the research are included in this report.

The modeling project assesses the additional costs for employers and employees in their current health plans due to changes imposed this year by the health reform law *(fig. 2)*. It also evaluates the financial implications of options employers will have in 2014 when they are required to offer health coverage to full-time employees or risk penalties.

"Employers are burdened and frustrated by aspects of the health reform law that add costs to their health plans," said Mike Brewer, President of Lockton Benefit Group. "Some employers will eliminate group health coverage and full-time jobs in 2014 because of the law." Brewer said, "Our clients understand that health reform is needed. They just wish that it was making their plans less expensive, not more expensive."

KEY FINDING—"PLAY OR PAY" MANDATE CREATES INCENTIVES TO TERMINATE COVERAGE

The modeling examined the implications of choices the sponsor of a group health plan will face in 2014 under the health reform law's "Play or Pay" mandate.

Across all industry segments in Lockton's group of clients,[1] companies will have a significant financial incentive to terminate their group coverage once the Insurance Exchanges present employees with another subsidized health insurance option. The vast majority of our clients currently spend far more on health insurance per employee than the nondeductible penalty under the "Play or Pay" mandate. By 2014 this gap will be much larger still, the data shows.

[1] Except retail, hospitality and entertainment employers, whose modeling results are addressed separately.

HEALTH REFORM'S COST IMPACT—ALL INDUSTRIES *(fig. 1)*

(EXCEPT RETAIL, RESTAURANT, HOTELS, HOSPITALITY AND ENTERTAINMENT)

Reform Requirement		Description	Average Cost Adjustment	
2010/2011				
2010/2011 Mandated Benefits		+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	2.5%	
2014				
Waiting Period (WP)		+ Waiting Period cannot be greater than 90 days	From current 180-day WP	3.9%
			From current 365-day WP	19.9%
Auto Enroll *		+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	3.8%**	
Play or Pay			Plan	Employee
	Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above.	
	Pay	+ Employer terminates plan	-44%	101% - 155%[#]
2018				
Excise Tax		+ If plan value exceeds limits, excess will be taxed.	1.9%	

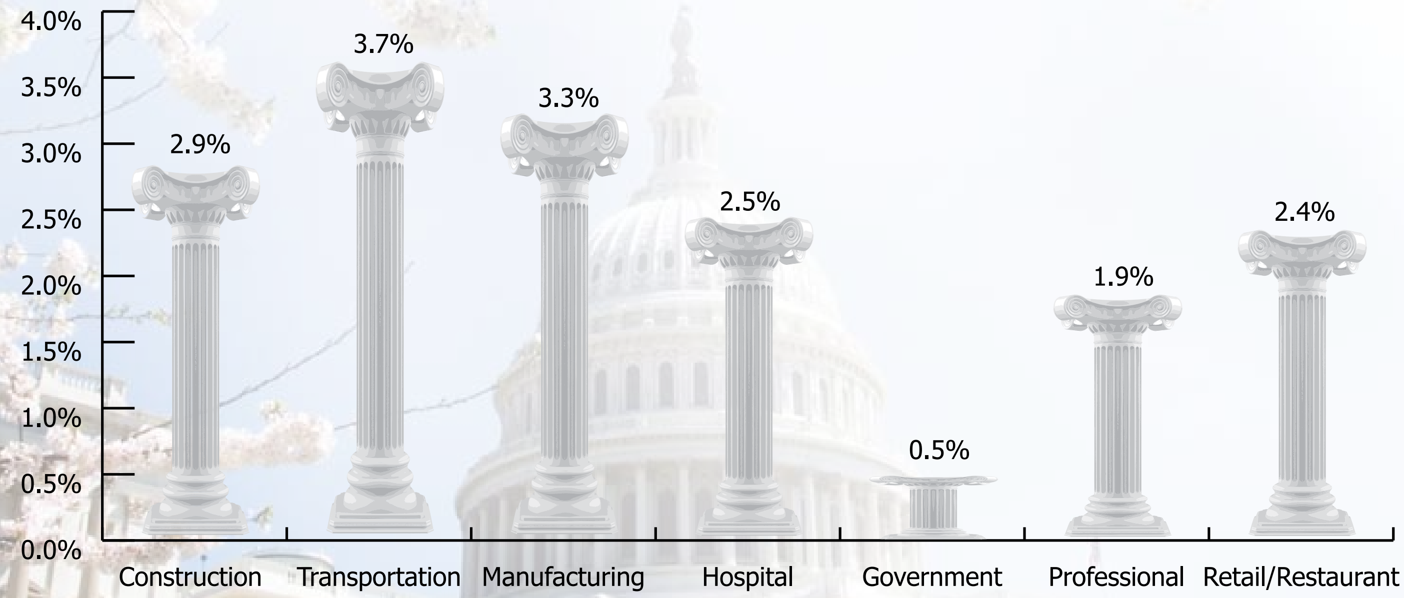
The impact to the employee varied based on salary levels and the employer's contribution.

For example, for a low-paid workforce where the employer does not contribute a significant portion of premium, the employee's increase is much smaller than a higher-paid workforce with a substantial employer contribution.

Based on analysis of 136 clients; Summary of Findings – February 2011
** Statute did not clearly indicate effective date; regulators leaning toward 2014 effective date.*
*** Employees can opt out, so the impact will depend on how many new employees remain on the plan, for how long, and the size of the employer's subsidy.*
 # First number based on employee's salary; second based on estimate of the employees household income, on which Exchange subsidies will be based.

HEALTH REFORM'S COST IMPACT—ALL INDUSTRIES *(fig. 2)*

2010-2011 MANDATED CHANGES



As a result, were they to terminate their group coverage in 2014, companies would, on average, save 44 percent of their projected 2014 health insurance costs. For clients whose health plans tend to be more expensive, savings are larger (84 percent for governmental clients, 60 percent for hospital clients in the study). *(fig. 1)*

We also modeled the impact of plan termination on clients' employees, were they compelled to seek coverage in an Insurance Exchange. On average, our clients' employees can expect to pay between 101 percent and 155 percent more for Exchange-based coverage[2] equivalent to their employer's health plan (101 percent assuming the employee is the sole wage earner in the household, 155 percent assuming there is household income in addition to the employee's salary, thus reducing the size of the subsidy the employee receives in the Exchange).

This is because companies in the Lockton study typically subsidize a larger portion of employees' health insurance costs than the Exchanges will subsidize, and employees pay their portion of employer-based coverage with pre-tax dollars. Their portion of Exchange-based coverage will be paid with after-tax dollars.

2 Estimates of Exchange coverage costs based on Kaiser Family Foundation data.

The more highly paid the employer's workforce, the more significant the expense borne by the employee in the Insurance Exchange. For example, employees of the studied professional service firms can expect to pay 113-148 percent more than they would pay for equivalent employer-based coverage.

The modeling results for Lockton clients in the restaurant, retail, hotel and entertainment (e.g., amusement park) industries are more sobering. Most of these clients do not offer group health coverage to all their full-time employees because they cannot afford to do so. A restaurant chain, for example, will typically offer coverage to its corporate staff and restaurant managers. An amusement park will typically offer coverage to its year-round staff but not to its extended seasonal workforce.

These employers are caught in a "damned if we do, damned if we don't" bind. On average, to comply with the "play or pay" mandate and offer qualifying and affordable coverage to all full-time employees, the employer's health insurance costs increase 150 percent. Maintaining the status quo will trigger penalties. *(fig. 3)*

Ironically, if the retail, hotel or entertainment employer simply terminates its group plan, it still pays 56.6 percent more than it would pay to continue its plan. These companies that employ a large number of full-time, relatively low-paid hourly workers who do not have health coverage today, tell us they have but one option: eliminate large numbers of full-time positions. By making full-time employees part-time, the employees are removed from the penalty equation.

2014 IMPACT TO RETAIL, RESTAURANT, HOTELS, ENTERTAINMENT INDUSTRIES *(fig. 3)*

CURRENTLY NOT OFFERING TRADITIONAL PLAN COVERAGE TO ALL 30+ HOUR FTEs

By 2014, when the Insurance Exchanges open and present employees another, largely subsidized option for health insurance coverage, the burden of group health insurance costs on an employer's balance sheet will create tremendous tension within many clients between cost, profitability, and appropriate compensation and benefit structures.

So far, few clients have told us they definitely intend to terminate group coverage in 2014, when Exchange-based coverage becomes available. Similarly, few clients have told us they definitely intend to maintain their group coverage. The majority of our clients tell us they will wait and see.

"What they will do in 2014 depends on their health insurance costs and budget in 2014 and their perceived need to use a health plan to gain a competitive advantage for labor," said Brewer.

Lockton's actuaries are working to expand the existing study by incorporating additional modeling results into the analysis.

ADDITIONAL FINDINGS

The Lockton actuarial modeling study shows additional impacts.

Immediate Benefit Mandates (in effect now)

Requirement to cover adult children to age 26, the elimination of lifetime dollar maximums, restrictions and ultimate elimination of annual dollar limits add 2.5 percent to our clients' health insurance costs.

+

Waiting Periods Limited to 90 Days (2014)

This mandate has little cost implication for most of our clients because most do not currently maintain waiting periods in excess of 90 days. However, for those who do, the consequences can be more dramatic. For example, a construction firm client with a six-month waiting period experiences a 3.9 percent cost increase, while another construction firm with a 12-month waiting period sees a 39.3 percent cost increase.

+

Automatic Enrollment Required (2014)

Automatic enrollment adds 3.8 percent to our clients' health insurance costs on average, assuming 25 percent of employees currently waiving coverage remain on the plan after auto enrollment.

"What they will do in 2014 depends on their health insurance costs and budget in 2014 and their perceived need to use a health plan to gain a competitive advantage for labor."

HEALTHCARE REFORM MODEL COMPILED DATA BY INDUSTRY

HEALTH REFORM'S COST IMPACT—ALL INDUSTRIES
(EXCEPT RETAIL, RESTAURANT, HOTELS, HOSPITALITY AND ENTERTAINMENT)

Reform Requirement	Description	Average Cost Adjustment	
2010/2011			
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2014			
Waiting Period (WP)	+ Waiting Period cannot be greater than 90 days	From current 180-day WP	3.9%
		From current 365-day WP	19.9%
Auto Enroll *	+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	3.8%**	
Play or Pay		Plan	Employee
Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above.	
Pay	+ Employer terminates plan	-44%	101% - 155%#
2018			
Excise Tax	+ If plan value exceeds limits, excess will be taxed.	1.9%	

The impact to the employee varied based on salary levels and the employer's contribution.

For example, for a low-paid workforce where the employer does not contribute a significant portion of premium, the employee's increase is much smaller than a higher-paid workforce with a substantial employer contribution.

CONSTRUCTION INDUSTRY

Reform Requirement	Description	Average Cost Adjustment	
2010/2011			
2010/2011 Mandated Benefits	+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	2.9%	
2014			
Waiting Period (WP)	+ Waiting Period cannot be greater than 90 days	From current 180-day WP	3.9%
		From current 365-day WP	39.3%
Auto Enroll *	+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	3.2%**	
Play or Pay		Plan	Employee
Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above.	
Pay	+ Employer terminates plan	-46%	129%-164%#
2018			
Excise Tax	+ If plan value exceeds limits, excess will be taxed.	0.4%	

The impact to the employee varied based on salary levels and the employer's contribution.

For example, for a low-paid workforce where the employer did not highly subsidize coverage, the employee's increase was 8% based on salary/80% based on est. household income. For a higher paid workforce with a high employer contribution, the impact to the Ee was 566% based on salary/877% based on household income.

Based on analysis of 136 clients; Summary of Findings – February 2011
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 # First number based on employee's salary; second based on estimate of the employees household income, on which Exchange subsidies will be based.

GOVERNMENT EMPLOYERS

Reform Requirement		Description	Average Cost Adjustment	
2010/2011				
2010/2011 Mandated Benefits		+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	0.5%	
2014				
Waiting Period (WP)		+ Waiting Period cannot be greater than 90 days	0%	
Auto Enroll *		+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	1.4%**	
			Plan	Employee
Play or Pay	Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above.	
Play or Pay	Pay	+ Employer terminates plan	-84%	108%-223%#
2018				
Excise Tax		+ If plan value exceeds limits, excess will be taxed.	4.3%	

The impact to the employee varied based on salary levels and the employer's contribution.

For example, for a low-paid workforce where the employer does not contribute a significant portion of premium, the employee's increase is much smaller than a higher-paid workforce with a substantial employer contribution.

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HOSPITAL INDUSTRY

Reform Requirement	Description	Average Cost Adjustment	
2010/2011			
2010/2011 Mandated Benefits	+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	2.5%	
2014			
Waiting Period (WP)	+ Waiting Period cannot be greater than 90 days	0%	
Auto Enroll *	+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	4.6%**	
Play or Pay		Plan	Employee
Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above.	
Pay	+ Employer terminates plan	-60%	67%-159%#
2018			
Excise Tax	+ If plan value exceeds limits, excess will be taxed.	2.5%	

The impact to the employee varied based on salary levels and the employer's contribution.

For example, for a low-paid workforce where the employer does not contribute a significant portion of premium, the employee's increase is much smaller than a higher-paid workforce with a substantial employer contribution.

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HEALTHCARE REFORM MODEL COMPILED DATA BY INDUSTRY

MANUFACTURING INDUSTRY

Reform Requirement		Description	Average Cost Adjustment	
2010/2011				
2010/2011 Mandated Benefits		+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	3.3%	
2014				
Waiting Period (WP)		+ Waiting Period cannot be greater than 90 days	From current 120 WP	1.2%
Auto Enroll *		+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	2.7%**	
			Plan	Employee
Play or Pay	Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above.	
	Pay	+ Employer terminates plan	-43%	91%-153%#
2018				
Excise Tax		+ If plan value exceeds limits, excess will be taxed.	1.0%	

The impact to the employee varied based on salary levels and the employer's contribution.

For example, for a low-paid workforce where the employer does not contribute a significant portion of premium, the employee's increase is much smaller than a higher-paid workforce with a substantial employer contribution.

PROFESSIONAL FIRMS

Reform Requirement		Description	Average Cost Adjustment	
2010/2011				
2010/2011 Mandated Benefits		+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	1.9%	
2014				
Waiting Period (WP)		+ Waiting Period cannot be greater than 90 days	From current 180-day WP	4.0%
			From current 365-day WP	0.5%
Auto Enroll *		+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	3.9%**	
			Plan	Employee
Play or Pay	Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above.	
	Pay	+ Employer terminates plan	-41%	113%-148%#
2018				
Excise Tax		+ If plan value exceeds limits, excess will be taxed.	2.9%	

The impact to the employee varied based on salary levels and the employer's contribution.

For example, for a low-paid workforce where the employer does not contribute a significant portion of premium, the employee's increase is much smaller than a higher-paid workforce with a substantial employer contribution.

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HEALTHCARE REFORM MODEL COMPILED DATA BY INDUSTRY

RETAIL, RESTAURANT, HOTELS, ENTERTAINMENT INDUSTRIES

Reform Requirement		Description	Average Cost Adjustment			
2010/2011						
2010/2011 Mandated Benefits		+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	2.4%			
2014						
Waiting Period (WP)		+ Waiting Period cannot be greater than 90 days	From current 180-day WP		N/A	
			From current 365-day WP		N/A	
Auto Enroll *		+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	Groups not offering qualifying coverage to all 30+ Hour FTEs		Groups offering qualifying coverage to all 30+ Hour FTEs	
			16.6%**		5.7%**	
Play or Pay			Plan	Employee	Plan	Employee
	Play	+ Employer continues to offer coverage	150%		14.3%	
	Pay	+ Employer terminates plan	56.6%	-4.9%-9.5%	-27.1%	6%-51%#
2018						
Excise Tax		+ If plan value exceeds limits, excess will be taxed.	3.4%			

Note: Assumes Limited Medical Plans get waiver of annual dollar maximum requirement.

The impact to the employee varied significantly based on salary levels.

For example, one client's salaried employees would see a 73% increase to purchase through the Exchange where the hourly employees would see a 40% decrease because of the governmental subsidies.

TRANSPORTATION INDUSTRY

Reform Requirement		Description	Average Cost Adjustment	
2010/2011				
2010/2011 Mandated Benefits		+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	3.7%	
2014				
Waiting Period (WP)		+ Waiting Period cannot be greater than 90 days	From current 120-day WP	6.4%
Auto Enroll *		+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	10.0%**	
Play or Pay			Plan	Employee
	Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above.	
	Pay	+ Employer terminates plan	-33%	53%-84%#
2018				
Excise Tax		+ If plan value exceeds limits, excess will be taxed.	0.0%	

The impact to the employee varied based on salary levels and the employer's contribution.

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OTHER INDUSTRIES

Reform Requirement		Description	Average Cost Adjustment	
2010/2011				
2010/2011 Mandated Benefits		+ Remove pre-existing condition restriction to 19 + Remove lifetime dollar maximums on EHB's + Minimum annual dollar maximums on EHB's + Cover children to age 26	2.8%	
2014				
Waiting Period (WP)		+ Waiting Period cannot be greater than 90 days	0%	
Auto Enroll*		+ Plans must automatically enroll newly eligible FT employees and re-enroll existing employees	2.2%**	
Play or Pay			Plan	Employee
	Play	+ Employer continues to offer coverage	~0% other than the cost impacts listed above	
	Pay	+ Employer terminates plan	-41%	255%-417%
2018				
Excise Tax		+ If plan value exceeds limits, excess will be taxed.	0.5%	

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Our Mission
To be the worldwide value and service leader in
insurance brokerage, employee benefits, and risk management

Our Goal
To be the best place to do business and to work

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